

See discussions, stats, and author profiles for this publication at: <https://www.researchgate.net/publication/343335927>

Nationalization of Commercial Banks in India

Article · December 2016

CITATIONS

0

READS

29,148

2 authors:



Anamitra Roy

Concept Research Foundation

44 PUBLICATIONS 2 CITATIONS

[SEE PROFILE](#)



Aamarpali Roy

Ana publishing private limited, India.

39 PUBLICATIONS 27 CITATIONS

[SEE PROFILE](#)

Some of the authors of this publication are also working on these related projects:



Biogas Researchers Group [View project](#)



Research Publication Sharing [View project](#)

Nationalization of Commercial Banks in India

Anamitra Roy*

***B.Com. Hons.** (University of Calcutta, India), **Certified Financial Accountant**(CMC, India),**DFA** (CMC, India), **PGDBF** (HSIS India, India), **Certified Business Case Analyst** (TASMAC, India), **Certified Financial Accountant** (GLOBSYN Skills, India), **GPBL** (TASMAC & University of Wales, U.K.).

&

Dr. Aamarpali Puri**

****MSc Chemistry & Ph.D.** from Guru Nanak Dev University, Punjab, India.
Associate Member – National Institute of Personnel Management (Kolkata, India).

In 1969, fourteen major commercial banks were nationalized in India. Foreign banks and other banks with deposits of less than Rs. 50 crores were not nationalized. Six more commercial banks were nationalized in 1980. 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.

Arguments in favor of nationalization of commercial banks in India:

Various factors were responsible for the nationalization of commercial banks in India. A discussion on these factors that helped in this, are as follows:

1) Too much concentration in the banking sector:

In 1959 there were 570 banks in India. But in 1963 the number came down to 276. However, during this period the amount of bank deposit had increased by more than two times. This shows too much concentration in the banking sector. Again, out of 276 banks just 5 banks contributed to more than 50% of the deposits. The big industrialists used the bank funds to build up their industrial empires. This implies concentration of economic power. It was thought that the nationalization of commercial banks would solve it.

2) Mobilized savings were not used for social development:

According to an estimate there were 188 directors in 20 commercial banks. These directors used to control 1,640 companies. As a result, the savings of the commercial banks were used for the promotion of the interests of a few groups of people. This was not utilized for general economic development.

3) Hoarding of essential commodities of speculation:

The speculators could get higher profits as the general price level increased. These speculators used to take loans from commercial banks. Thus, in order to check these speculative activities the nationalization of commercial banks was thought to be essential.

4) To check illegal activities:

According to Indian Companies Act, each company has to submit the estimates of profit and loss to the Registrar of Companies. However, the provision was not applicable to the banking companies. The bank could hold secret reserve funds and declared lower profits. These funds were used to purchase shares of different companies. The banks were involved in under invoicing of exports and over invoicing of imports. It was thought that these illegal activities could be checked as a result of bank nationalization.

5) Urban bias:

The banks were mostly confined to urban areas. They did not pay any attention to opening of new branches of rural areas. But in order to have all round development of the country there is need for opening up of new branches in rural areas. As a result of nationalization of commercial banks it was thought that branch expansion of banks in rural areas will be possible.

6) Discrimination against small business:

The banks lent money only to the big business units. They neglected the needs of the agricultural sector. But the development of agricultural sector is necessary for the economic development of the country. Agriculture is the priority sector. In order to ensure flow of credit to the priority sectors, bank nationalization was thought to be essential.

7) Stopping of failure of banks:

Up to early 1960s there were a large number of bank failures in our country. This hampered the interest of the depositors. It was thought that through bank nationalization the confidence of the public in commercial banks would rise. This would also check the growth of black money in our country.

8) Improvement of service conditions of bank employees:

Nationalized banks would be able to provide better service conditions to their employees. The efficiency of the banking business would rise through better training.

Arguments against nationalization of commercial banks in India:**1) Fall in efficiency:**

It was thought by many economists that nationalization would reduce the efficiency of this sector.

2) Deposit insurance corporation and bank failures:

After the establishment of Deposit Insurance Corporation, the deposits of the commercial banks were insured. Therefore, the interest of the depositors was protected. There was no need for bank nationalization.

3) Adverse effect on the private sector:

The commercial banks supplied credit mainly to the private sector. If banks were nationalized it would adversely affect the growth of the private sector.

4) Rise in political pressure and fall in efficiency:

If banks were nationalized it was thought that political pressure would rise on the banks. The politicians would force the banks to give loans on the basis of political considerations and not on economic merit.

5) Huge compensation to the shareholders:

If a large amount of money was paid as compensation to the shareholders, the fund for economic development would be reduced.

Performance of nationalized commercial banks since nationalization:

One of the major criticisms of commercial banks prior to nationalization was that they never extended their hands to the priority sectors like agriculture, small scale industries, exports etc. Before nationalization such banks operated with the profit motive only. But after nationalization the scene changed to a huge extent. Commercial banks started to consider objectives like social development and economic development of the nation. Thus, they started supporting sectors on which the growth of the then Indian economy was dependent heavily. The total credit provided by the public sector banks in 1969 was Rs. 440 crores. In 1988 it went up to a level of Rs. 29,330 crores.

Another massive change in the Indian banking scenario was observed as a result of nationalization of commercial banks. Previously, the private banks were operating with only the profit motive. So they were eager to operate and open their branches only in urban areas where scope of business was bigger and brighter than the rural areas. After nationalization of

these banks, there was a gigantic change in the motives of these commercial banks. They were operating no more with just the profit motive. As a result of this, the commercial banks started to extend their services in the rural areas also. This had a manifold effect on the Indian economy. Firstly, due to this approach of the nationalized commercial banks there were more branches being opened in rural areas. Thus, the untapped rural markets were also coming under the ambits of the Indian banking industry. Secondly, this was helping in generation of employment opportunities in the Indian job markets. Thirdly, from the point of view of consumer behavior it can be said that the vast population in the rural areas were being exposed to the banking services. In this context, it is mention worthy that since 1969 to 1989 there was 600% growth rate observed in the opening of new branches of commercial banks. Moreover, in June, 1969 on an average a branch of a bank was serving more than 65,000 customers in India. This number came down to 12,000 customers per branch in June, 1989.

Another significant impact was felt in case of deposit mobilization. The deposits of commercial banks which stood at Rs. 4,650 cores in June, 1969 grew to Rs. 1,47,000 crores in January, 1989.

However, in spite of these successes, there were also certain limitations of nationalization of commercial banks. Profitability of the commercial banks declined to a huge extent. Nationalization also made these commercial banks heavily dependent on the politicians. Thus a large part of the bank credit was still being diverted towards the big industries and corporate houses. Lastly, it can be said that nationalization brought in security in the lives of the banking employees. This established a complacent attitude thereby resulting into a sharp decline in the standard of the banking services provided to the customers.

In conclusion, it can be said that due to nationalization of commercial banks the Indian banking industry faced a steep challenge. It was the challenge of blending the profit motive with the objective of social and economic development of the nation. The game of balancing these two diagonally opposite sets of goals is still on.