# Pace and Pattern of the Banking Sector Development in India During Pre and Post- Reform Period

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**Abstract**

*1991 financial sector reforms helped the Indian banking sector to be on par with the global standards of banking. This is very much evident from the significant improvement in number of parameters like capital adequacy ratio, asset quality, profitability and productivity of banks. However, maintaining stability and robustness besides meeting the social objectives and be a part of the inclusive growth process in the wake of the rising global exposure, given the integration of world's financial and capital markets remains a great challenge today. In this context, we make an attempt to go into a critical evaluation of the pace and pattern of India's banking system during pre and post reforms period and provides policy suggestions.*

## 1. Introduction

"Money and banking is the centre around which economic science cluster" goes a dictum by an eminent economist of yester years. Banking is an important growth ingredient for a nation to not only to achieve higher economic growth, but also to facilitate the stakeholders to participate in the growth process and redistribute the growth fruits. Thus it plays a pivotal role in the inclusive growth process.

The Indian Banking system has its roots in the British era. Colonial rulers established a few banks in select pockets of the country to facilitate their trade. Presidency banks were established in Bombay, Madras and Calcutta. Later, after the independence these banks were undertaken by Government of India. They were brought under the single umbrella of State Bank of India. Till 1969, to be more particular, until 1935, banking in India was under private control and the motive of banking was confined to profit making without much emphasis on social welfare. Later in 1969, fourteen banks were nationalized, followed by other six banks in 1980. Although they were performing well in the initial stages, later their performance deteriorated due to phenomenal expansion of the new branches, which resulted in the rise of operating costs. Increase in the non performing assets also attributed to the losses of these banks.

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With the unleashing of economic reforms in early 90s, banking sector underwent a major over haul. Private and foreign players too were allowed. This resulted in rise in the competition and inflow of world class managerial practices and technology in to the Indian banking system. They enhanced the efficiency of the Indian banks and thereby increased the profitability and productivity of commercial banks. Parllely, there has been a significant decline in the non performing assets of the public sector banks.

However, maintaining stability and robustness besides meeting the social objectives and be a part of the inclusive growth process in the wake of the rising global exposure, given the integration of world's financial and capital markets remains a great challenge for Indian banking sector today. In this context, a deeper understanding of banking sector development in India is necessary.

We make an attempt to go into a critical evaluation of the pace and pattern of India's banking system. The period of study is divided into two categories viz. post nationalization phase or pre-reforms phase (1969-1991) and the post reform phase (since 1991). Empirical evidences are established on various aspects such as aggregate deposit growth, credit growth, banking business growth, credit deposit ratio etc, across three phases and an attempt is made to draw some logical conclusions from the results obtained. A brief mention of the colonial past has been made in order to capture the essence about the way in which our banking system had grown from innocence to strength today

The paper is divided in to five sections. The initial section comprises the introduction, section 2, discusses the brief history of the Indian banking sector since British period. In section 3, deals with the methodology and the data analysis and section 4 brings forward the contemporary major challenges confronted by Indian banking sector. The last section provides policy suggestions and conclusion.

## 2. Indian Banking Sector: A Brief History

The Indian banking industry has its foundation in the last decades of 18$^{th}$ century. The English Agency House that began to serve as bankers to the east India Company. In this end, the first bank in India namely Hindustan bank was started in 1770 and General Bank of India established in 1786[1], both of are now defunct. The oldest bank in existence in India is the State Bank of India which originated in 1806 by the name of Bank of Bengal which was first presidency bank in India. The other two being the Bank of Bombay (1840) and the Bank of Madras (1843). For many years, these presidency banks were acted as a quasi-central bank. Three presidency banks merged in the 1921 to become Imperial Bank of India which in transformed into the State Bank of India in

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[1]*Some banks and their starting year. Bank of Bengal 1809, Bank of Bombay 1840, Bank of Madras 1843, Allahabad Bank 1865, Pubjab National Bank Ltd 1894, Canara Bank 1906, Indian Bank 1907, Bank of Baroda 1908, Central Bank of India 1911, Bank of Mysore 1913, Union Bank of India 1922.*

1955. The first purely Indian owned bank was the Oudh Bank started in Faizabad in 1881 and later it failed in 1858. The second owned Indian bank was Punjab National Bank started in 1895 in Lahore and it is still functioning and it is the largest of old banks in India. The Allahabad Bank was established in 1865 and still functioning today is oldest bank in India. The other important banks were established then, have survived to the present such as Canara Bank (1906), Indian Bank (1907), Bank of Baroda (1908), Central Bank of India (1911), Bank of Mysore (1913) and Union Bank of India(1922).

After India's independence, significant changes have been taken place in the Indian banking industry. The entire period of Indian Banking since independence can be segregated into three distinctive phases: pre-nationalization of banks (prior to 1969), Post-Nationalization of banks (1969-1991), and Post-reforms period (since 1991)[2].

During the first phase of banking industry, two important steps have taken to establish securitized and sound banking system in India. The first step was the enhancement of banking companies act 1949 which was subsequently changed into banking regulation act 1949 to ensure sound banking through conduct and control of operation of the commercial banks in India. Another important step has been taken during this period was the transformation of Imperial Bank of India into State Bank of India in 1955 and also redefined its role in the Indian Economy. Strengthening of the co-operative credit structure and setting up in-situational institutional framework for providing long run finance to the priority sectors such as agricultural and other small scale industries. Therefore, this period can be called as foundation phase of Indian banking system. During this period, the number of banks has been declined mainly due to sharp decline in the number of non-scheduled commercial banks.

Look at the period of post nationalization of banks, this period mainly characterized by the death of private banks and birth of social banks. The Government of India has nationalized 20 major commercial banks into two phases (14 banks in 1969 and 6 banks in 1980) to control monopolies, reducing the regional imbalances and to increasing priority sector lending. Another, important steps taken in this period were the establishment of Regional Rural Banks (RRBs) in 1975, and the birth of National Bank for Agricultural and Rural Development (NABARD) in 1982 with the view of priority sectors like agriculture and small scale industries development.

Thus, the nationalization of banks and the birth of RRBs and NABARD were resulted in rapid branch expansion, deposit mobilization and credit creation especially in rural and semi-urban areas. However, it was hardly realized that banks were used to organize with social responsibilities but not social organization. Therefore, this was

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[2] *Prof K.V Bhanu Murthy also classified Indian Banking History as four eras; Early historical and formative era: 1770-19052. Pre-independence era: 1906-19463. Post independence regulated era: 1947-19934. Post independence deregulated era from 1993 onwards.*

ultimately resulted in the high expenditure or low profitability and less earnings because the banks were used to finance to the prioritized sectors at the concessional interest rates. Moreover, the operational expenditure is increased mainly due to the rapid expansion of branch banking. This was also mainly due to rural branch expansion.

During the post-reforms period the Indian banking industry had significant changes in nature of operation and regulation environment. The less operational efficiency of banks, growing incidence of non-performing assets (NPAs) and low capital base during the post nationalization of banks resulted in weak financial health of baking system in Indian. According to Narisimhan committee, during the post-nationalization period, the banking industry suffered with system of direct credit operations in the form of subsidized credit to the priority sectors. This committee pointed out that the phenomenal expansion of bank branches, rising staff level, high unit cost administrating loan to the priority sector and poor supervision has led the tremendous increase in the operational cost of public sector banks. These changes have necessitated devise a reform agenda for the banking sector. By following recommendation of Narisimhan committee, the financial sector reforms of 1991 brought about deregulation of interest rates, increased a healthy competition by allowing private and foreign banks into domestic banking business. Besides this, Preemptive measures, cautiously undertaken by the Central Bank of India over a period of time had proved handy. Implementation of prudential norms like income recognition, asset classification and capital adequacy ratio are some such measures which helped the Indian banking industry to remain more strong and stable. This is evident from the relative stability of the Indian Banking system during the recent global crisis, while many countries across the world had a disrupted and shattered banking system.

Financial sector reforms of 1991 helped the Indian banking sector to be on par with the global standards of banking. It is very much evident from the significant improvement in number of parameters like capital adequacy ratio, asset quality, profitability and productivity of banks. look at the assets quality of schedule commercial banks during the reforms period, the gross non-performing assists of SCBs was around 15.7 in 1996, had declined to 2.3 in 2008. Similarly, net NPAs of SCBs have also been significantly declined from 8.1 per cent in 1996 to 1.1 in 2008. In regards to the average capital adequacy ratio for SCBs, this was around 10.4 per cent in 1996, later which was significantly increased to 13.2, 14.3 per cent in 2008 and 2011 respectively. The reform measures also significantly improved the profitability and productivity of schedule commercial banks.

## 3. Methodology and Data Analysis

Data used in this paper is secondary in nature. They have been collected from the report on Trend and progress of Banking in India 2010-11 and from Centre for Monitoring Indian Economy (CMIE) data base. To analyze the financial performance of banking sector, Key banking sector performance indicators have been used namely average growth rate of bank deposit, total bank credit, total banking business, bank credit to commercial sector etc[3]. For this purpose, We have taken average growth rates of all the indicators of banking performance rather taking percentages of GDP. This is because, the average growth rates could capture the changes in a particular variable over period of time. In contrast, if their values are taken as a percentage of GDP, it would create obscurity in interpretation as the variable values will be significantly affected by the changes in GDP from time to time. The average growth rates of each indicators have been calculated in the excel sheet. Since our objective is to examine the banking performance during pre and post reforms period, we have calculated all measures separately for both the two periods.

### *3.1. Average growth rate of total bank deposit*

The average growth rate of aggregate deposit during pre-reforms period that is from 1969-70 to 1991-92 was 19.0 per cent. Whereas, during post-reforms period i.e. 1992-93 to 2009-10 the average growth rate of aggregate deposit declined to 18.0 per cent (see chart-1 in appendix). Thus, the average growth rate of aggregate deposits during post-reforms period was lower than that of in pre-reforms period might be due to the rate of interest on deposits being offered by schedule commercial banks in post-reforms period was lower than the deposit rate during pre-reforms period. Therefore from the above table it is clear that although the financial reforms which have taken place in India in the year 1991-92, the performance of the banking sector in mobilizing deposits was poor in post-reforms period as compared to the pre-reforms period.

### *3.2. Average growth rate of total Bank credit*

The average growth rate of total bank credit during pre-reforms period that is from 1969-70 to 1991-92 was 17.2 per cent. Whereas, during post-reforms period i.e. 1992-93 to 2009-10 the average growth rate of total bank credit increased to 20.1 per cent (see chart-2 in appendix). Thus, it is clear that in one hand, as we discussed earlier, the average growth rate of bank aggregate deposits has declined during post-reforms period; on the other hand the average growth rate of total bank credit in post-reforms has been increased. At the same time it is evident that the share of consumer loans by banks has significantly increased (see the chart-6) during post-reforms period. Therefore, it is clear that during post-reforms period the banks in India has focused more on advancing loans rather mobilizing funds. The average credit growth in post-reforms

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[3] *All the above banking performance indicators calculated in nominal terms.*

period was higher than that of in pre-reforms period might be due to higher lending rates in post-reforms period. The lending rate of commercial banks in 1991 was around 19 per cent, latter which was continuously declined to 8 % in 2009(see Figure-A in appendix).

### *3.3. Average growth rate of banking business*

From the above figure, it is evident that the average growth rate of banking business was more or less same both in pre-reform and post-reforms period. During pre-reform period, the average growth rate of banking business was 18.3 % which slightly increased to 18.5% during the post reform period (see chart-3 in appendix). Despite the banking sector reforms in early 90s, there is no much improvement in the total banking business in India and remain stagnated at around 18% both in pre-reforms and post reforms period. This might be due to in the post-reforms period the banking industry has more concentrated on secondary functions like collecting information on different investment opportunities, issuing of bank drafts and letters of credit, providing locker facilities rather concentrate on primary functions such as accepting deposits and granting loans and advances.

### *3.4. Average growth rate of total bank investment*

It is evident from the above figure that during the period 1970-71 to 1991-92, the average growth rate of total bank investment was 20.7% and it was 16.2% for the period 1992-93 to 2009-10 (see chart-4 in appendix). Thus, the post reform average growth rate of total bank investment declined as compared to the pre-reforms period.

### *3.5. Average growth of banking credit to commercial sector*

It is also clear from the above figure that the average growth of banking credit to commercial sector during the period 1971-72 to 1991-92 was 17.6% which slightly declined to 17.5% during the period 1992-93 to 2009-10 (see chart-5 in appendix). Thus, the average growth of banking credit to commercial sector during both the pre-reform and post reform was remained static at 17%.

### *3.6. Other banking development indicators*

The number of schedule commercial banks has been significantly increased from 89 in the year 1969 to 174 in 2008 (see table-1). At the time of banking nationalization the number of commercial banks (both scheduled and non-scheduled) was at just 89. Over a period, their number has increased to 300 in 2001. Since then, due to mergers and acquisitions of banks, the number of commercial banks (especially the number of schedule commercial banks) has been declined to 222 and 174 as on 2006 and 2008 respectively. Similarly, other indicators like number of bank offices, population per office and population per deposit of SCBs had also remarkable improvement during post-reforms period. At the time of nationalization of banks ever 64 thousand of people used to get services from one bank office then over a period, number of bank offices has been sharply increased so that population per office came down to 15 thousand. It indicates that the availability banking services for each individual were tremendously increased during pos-reforms period.

**Table-1: other banking development indicators at a glance**

| Indicators | 1969 | 2001 | 2005 | 2006 | 2007 | 2008 |
|---|---|---|---|---|---|---|
| Number of banks | 89 | 300 | 289 | 222 | 183 | 174 |
| (a) Number of SCBs | 73 | 296 | 285 | 218 | 179 | 170 |
| (b) Number of Non-SCBs | 16 | 4 | 4 | 4 | 4 | 4 |
| Number of Bank offices | 8262 | 67937 | 70373 | 71685 | 74346 | 77773 |
| Population per office (in thousands) | 64 | 15 | 16 | 16 | 15 | 15 |
| Population per deposit of SCBs (Rs) | 88 | 9770 | 16281 | 19130 | 23382 | 28610 |

Source: RBI report on Bank branches in India, SCBs-Schedule commercial banks

**Findings:**

(1) The performance of the banking sector in mobilizing deposits has been declined in post-reforms period as compared to the pre-reforms period.

(2) The average growth rate of total bank credit in post-reform period is more than the pre-reforms period.

(3) There is no much change in the average growth rate of banking business both in the pre and post reforms period.

(4) The post reform average growth rate of total bank investment has been declined as compared o the pre-reform average growth rate of total bank investment.

(5) The average growth of banking credit to commercial sector during both the pre-reform and post reform was remained static at 17%.

(6) Overall, there was greater accessibility of banking services for each individual during post-reforms period. But in case of rural areas the accessibility of banking services is not up to the mark. Because of their inefficiency and higher operational cost bank branches in rural areas have been removed.

## 4. Analysis of major challenges in banking sector development in recent period

Apart from the above changes in different categories of banking development indicators during pre and post reforms period, this paper attempted to point out some important concerns about industry wise shares of banking credit, Non-performing Assets (NPAs), credit deposit ratio and distribution of bank branches during pre and post reforms period.

### 4.1. *Schedule Commercial Bank credit – Industry wise*

Economic reforms had put Indian economy on the high growth trajectory. From the Hindu growth rate of around 3 %, India could record a stable and high average growth rates over the past two decades. There has been a paradigm shift in the structure, functioning and the very system of our economy. Banking sector too underwent a radical change and it grew from strength to strength with prudent regulations, well supervised markets and cautious regulatory authorities. It played a key role in the growth process and in ensuring sound macroeconomic fundamentals.

However, there are few trends that provide enough reason not to celebrate this success story. From the data, it seems that Indian banking system is slowly shrugging off from the primary and manufacturing sector lending in the recent period. This development is not healthy, not only for banking industry but also to Indian economy itself in the medium and long run. This is evident from the fact that there has been lending shifts away from the productive sectors like agriculture and industry to the retail sector with personal loans accounting for a rising share of the total.

As chart-6 shows (see in appendix), between the end of 1990 and December 2010, the share of agricultural in total advances of SCBs fell from 16 per cent in 1990 to 11.4 per cent in 2006 and it remained around 11 per cent till date. Similarly, the share of industrial loans in total advances fell down from 49 per cent in 1990 to 37.6 per cent in 2006 and it remained around that level till 2010. On the other hand, the share of personal loans rose from 9 per cent in 1990 to 23.3 in December 2006, though it fell to 16.7 in 2010, as part of slow down that had begun to affect the economy.

The consequences of this trend are already felt in the Indian economy. Despite institutional and structural problems, a slowdown in the industrial output and sickening agricultural sector can be partly attributed to this trend. Another concern is the quality of assets of banks. Although India may not face a crisis of magnitude of subprime crisis, there is a possibility of rising NPAs, which is not a health sign.

### 4.2. Non-Performing Assets (NPAs) of Schedule Commercial Banks

#### *Non-Performing Assets (NPAs)*

One of the key variables that reflect the well being of a financial system is the maintenance of its Non Performing Assets (NPA)[4]. Credit in adequate measure is the essential ingredient for growth. However, the NPAs beyond a tolerable level could hinder the smooth flow of credit to the targeted sectors and thereby slows down the overall

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*[4] Non-performing asset in the banking system usually refers as a loan which is not meeting its stated principal and interest payments within 90 days in case of commercial loans and 180 days in case of consumer loans. Basically in India, a loan or any asset is considered as non-performing asset based on the concept of 'Past Due'.*

growth. Hence, improving the assets quality of banking is one of the important indicator banks performance as they exploit the ample opportunities provided by liberalization and moderately regulated system.

It was very much evident from table 5.1 that, there was significant improvement in the assets quality of Schedule commercial bank during post-reforms period. The gross non-performing assets as a percentage of total advances fell from 15.7% in 1996 to 2.4% by 2010. As ratio of total bank advances, net Non-performing assets too significantly declined from 8.1 per cent in 1996-97 to 1.1 per cent in 2009-10. ***However, since 2008-09, non-performing assets of the schedule commercial banks are on rise. High interest rates and moderate economic activity during that period might be the possible reason behind this.***

A group wise analysis of the data for various banks falling under the category of public sector banks, old private banks, new private banks and foreign banks gives the following results. It is found that NPAs have been on a declining trend since the initial stages to till date in all categories. In the case of Public and old private banks, both gross and net non-performing assets had sharply declined. It is evident from the table 5.2 and table 5.3 that the gross non-performing assets of public sector banks fell from 17.8 % in 1996 to 2.3 percentage in 2010. Whereas the gross NPAs of old private banks too significantly declined to 2 % in 2010 from 10.7 per cent in 1996. Similarly, Net NPAs of public sector banks was 9.2 % in 1996 and later it declined to 1.1 per cent in 2010. In case of old private banks also the net NPAs significantly fell from 6.6 percentages in 1996 to 0.5 % in 2010.

***However, the recent trend in Public sector banks performance in managing its NPA s is slightly an aspect to be worried. Gross Non-performing Assets as a percentage of Gross Advances have increased from 2.3 % in 2010-11 to 3.2% in 2011-12***

**Table- 2: Gross Non-performing Assets as % of Gross Advances**

| Year | Gross NPAs | Net NPAs | Year | Gross NPAs | Net NPAs |
|---|---|---|---|---|---|
| 1996-97 | 15.7 | 8.1 | 2004-05 | 5.2 | 2.0 |
| 1997-98 | 14.4 | 7.3 | 2005-06 | 3.3 | 1.2 |
| 1998-99 | 14.7 | 7.6 | 2006-07 | 2.5 | 1.0 |
| 1999-00 | 12.7 | 6.8 | 2007-08 | 2.3 | 1.0 |
| 2000-01 | 11.4 | 6.2 | 2008-09 | 2.3 | 1.1 |
| 2001-02 | 10.4 | 5.5 | 2009-10 | 2.4 | 1.1 |
| 2002-03 | 8.8 | 4.0 | 2010-11 | 2.4 | 1.0 |
| 2003-04 | 7.2 | 2.8 | 2011-12 | 2.9 | 1.4 |

*Source: RBI report on Trend and Progress of Banking in India*

**Table 3: Gross Non-performing Assets as % of Gross Advances**

| Year | PSBs | OPRBs | NPRBs | FBs | Year | PSBs | OPRBs | NPRBs | FBs |
|---|---|---|---|---|---|---|---|---|---|
| 1996-97 | 17.8 | 10.7 | 2.6 | 4.3 | 2004-05 | 5.5 | 6.0 | 3.6 | 2.8 |
| 1997-98 | 16.0 | 10.9 | 3.5 | 6.4 | 2005-06 | 3.6 | 4.4 | 1.7 | 1.9 |
| 1998-99 | 15.9 | 13.1 | 6.2 | 7.6 | 2006-07 | 2.7 | 3.1 | 1.9 | 1.8 |
| 1999-00 | 14.0 | 10.8 | 4.1 | 7.0 | 2007-08 | 2.2 | 2.3 | 2.5 | 1.8 |
| 2000-01 | 12.4 | 10.9 | 5.1 | 6.8 | 2008-09 | 2.0 | 2.4 | 3.1 | 3.8 |
| 2001-02 | 11.1 | 11.9 | 8.9 | 5.4 | 2009-10 | 2.2 | 2.3 | 2.9 | 4.3 |
| 2002-03 | 9.4 | 8.9 | 7.6 | 5.3 | 2010-11 | 2.3 | 2.0 | 2.3 | 2.5 |
| 2003-04 | 7.8 | 7.6 | 5.0 | 4.6 | 2011-12 | 3.2 | 1.8 | 2.2 | 2.7 |

*Source: RBI report on Trend and Progress of Banking in India,*
*Note: PSBs – Public Sector Banks, OPRBs – Old Private banks, NPRBs – New Private Banks, FBs –Foreign Banks*

**Table 4: Net Non-performing Assets % of Gross Advances**

| Year | PSBs | OPRBs | NPRBs | FBs | Year | PSBs | OPRBs | NPRBs | FBs |
|---|---|---|---|---|---|---|---|---|---|
| 1996-97 | 9.2 | 6.6 | 2.0 | 1.9 | 2004-05 | 2.1 | 2.7 | 1.9 | 0.8 |
| 1997-98 | 8.2 | 6.5 | 2.6 | 2.2 | 2005-06 | 1.3 | 1.7 | 0.8 | 0.8 |
| 1998-99 | 8.1 | 9.0 | 4.5 | 2.9 | 2006-07 | 1.1 | 1.0 | 1.0 | 0.7 |
| 1999-00 | 7.4 | 7.1 | 2.9 | 2.4 | 2007-08 | 1.0 | 0.7 | 1.2 | 0.8 |
| 2000-01 | 6.7 | 7.3 | 3.1 | 1.8 | 2008-09 | 0.9 | 0.9 | 1.4 | 1.8 |
| 2001-02 | 5.8 | 7.1 | 4.9 | 1.9 | 2009-10 | 1.1 | 0.8 | 1.1 | 1.8 |
| 2002-03 | 4.5 | 5.2 | 1.5 | 1.7 | 2010-11 | 1.1 | 0.5 | 0.6 | 0.7 |
| 2003-04 | 3.1 | 3.8 | 1.7 | 1.5 | 2011-12 | 1.7 | 0.6 | 0.5 | 0.6 |

*Source: RBI report on Trend and Progress of Banking in India*

### 4.3. Credit-Deposit Ratio

The credit deposit ratio is one of the key indicators of baking performance, which refers to the proportion of loan assets created by a bank from the deposit received, that indicates mobilization of financial resources in the form of credit disbursement out of their total deposits. The credit deposit ratio of a bank affects by many factors like the rate of interest, repayable capacity of borrower and different policy rates. The country like India, financial intermediation especially commercial banks play a key role in the economy through huge credit creation.

During pre-nationalization period (prior to 1969) the average annual credit deposit ratio of schedule commercial banks was higher than the later two periods. It doesn't mean that well resource mobilization has taken place during the pre nationalization phase. This was manly driven by the low deposit growth. Despite the average growth rate of bank credit during the post nationalization period has significantly increased, the average credit deposit ratio stood at only around 69 per cent which is less than that of in pre-nationalization phase. This was due to a sharp increase in the aggregate deposits of schedule commercial bank during nationalization period.

Similarly, during the post- reforms period the credit deposit ratio has significantly declined (see chart-7 in appendix) as compared to the post nationalization period. During post nationalization period, the average credit deposit ratio was around 68.8 per cent, whereas in the reform period this ratio stood at 60.7 per cent. However, in recent years this ratio is increasing due to a slight decline in the total deposit growth.

***Thus, the average credit deposit ratio during post-reforms period was less than that of in nationalization period. Therefore it is obvious, during the reforms phase financial resources have not been greatly mobilized unlike post-nationalization period.***

## 4.4. Distribution of Scheduled Commercial Banks' offices

Banking nationalization in India was planned to change the attention from class banking to mass banking. The principal aim of creating Regional Rural Banks (RRBs) was to take the banking services to unbanked population in rural areas. Especially in rural areas the branches of commercial banks and RRBs have tremendously increased during the nationalization period (See Table-5). At the time of nationalization of banks the number of rural branches was around 3063 after their number has considerably increased to 33014 as at the end of March 1990. Similarly, the branches of commercial banks and the RRBs in urban areas have also been significantly increased from 7068 in the year 1970 to 24865 branches as at the end of March 1990. ***However, during the post-reforms period the number of commercial bank offices are continuously declining both in absolute and growth terms in rural areas, since bank branches in rural areas have been closed due to their inefficiency and higher operation costs.***

The number of rural branches in 1995 was around 35329 and latter which declined to 30551 in the end of 2007, whereas, the number of commercial bank branches in urban areas has continuously increased. Thus, despite, the bank branches in rural areas have declined, the number of total bank branches in India during pre and post reforms period has been increased. Especially in post-reforms period the number of total bank branches increased mainly due to increase in unban branches. ***Declining banking branches in rural areas will reduce the banking habit of the rural people and thereby small savings generation will be obstructed. This leads to, less accessibility of formal***

***credit or getting credit from informal source even at unreasonable price, increased unemployment and general decline in investment and thereby low economic growth.***

**Table -5: Distribution of Scheduled Commercial Banks' Offices**

| Year | Rural Branches | Urban Branches | Total Branches |
|---|---|---|---|
| **1970-71** | 3063 (67.1) | 7068 (9.4) | 10131 (22.6) |
| **1980-81** | 15105 (13.3) | 17314 (2.7) | 32419 (7.3) |
| **1990-91** | 34791 (5.38) | 24961 (1.1) | 59752 (3.6) |
| **1994-95** | 35329 (-0.17) | 26474 (2.7) | 61803 (1.0) |
| **1995-96** | 33004 (-6.58) | 29363 (10.9) | 62367 (0.9) |
| **1996-97** | 32995 (-0.03) | 30031 (2.3) | 63026 (1.1) |
| **1997-98** | 32915 (-0.24) | 30635 (2.0) | 63550 (0.8) |
| **1998-99** | 32878 (-0.11) | 31340 (2.3) | 64218 (1.1) |
| **1999-00** | 32857 (-0.06) | 32082 (2.4) | 64939 (1.1) |
| **2000-01** | 32734 (-0.37) | 32678 (1.9) | 65412 (0.7) |
| **2001-02** | 32562 (-0.53) | 33357 (2.1) | 65919 (0.8) |
| **2002-03** | 32380 (-0.56) | 33810 (1.4) | 66190 (0.4) |
| **2003-04** | 32303 (-0.24) | 34232 (1.2) | 66535 (0.5) |
| **2004-05** | 32121 (-0.56) | 35067 (2.4) | 67188 (1.0) |
| **2005-06** | 32082 (-0.12) | 36273 (3.4) | 68355 (1.7) |
| **2006-07** | 30579 (-4.68) | 38892 (7.2) | 69471 (1.6) |
| **2007-08** | 30551 (-0.1) | 41288 (6.2) | 71839 (3.4) |

*Source: RBI report on Trend and Progress of Banking in India*

## 5. Summary and Conclusion

The present study is an attempt to evaluate the pace and pattern of banking sector development in India during pre and post reforms period. In order to mitigate the hindrances on the way of successful functioning of the public sector banks and to make the Indian banking system more sound and efficient, the government of India has introduced financial reforms as a part of economic reforms in the early 90s. During post-reforms period the implementation of prudential norms such as income recognition, asset classification and capital adequacy ratio are some such measures which helped the Indian banking industry to remain more strong and stable. This is evident from the relative stability of the Indian Banking system during the recent global crisis, while many countries across the world had a disrupted and shattered banking system. The average capital adequacy ratio for SCBs, this was around 10.4 per cent in 1996, later which was significantly increased to 13.2, 14.3 per cent in 2008 and 2011 respectively. The reform measures also significantly improved the profitability and productivity of schedule commercial banks.

However, the empirical analysis of the study reveals that during pre and post-reforms period there is no much improvement or decline in their performance with respect to the selected parameters such as average growth rate of aggregate deposits, average growth rate of banking credit, total banking business, the average growth rate of bank investment (including investment in government securities and other securities) and average growth of banking credit to commercial sector. Similarly, other parameters such as number of banks, number of bank offices, population per office (in thousands), population per deposit of SCBs (Rs); population per office (in thousands) was also found to be stagnant during post-reforms period. Apart from this there are certain challenges before us such as shifting of bank loans from the productive sectors like agriculture and industry to unproductive sector like retail sector with personal loans etc., retreating asset quality of public sector banks, less mobilization of financial resource and bring the rural masses into the financial inclusion and inclusive growth process. The flowing suggestions could help to improve the Banking sector performance in India.

***Suggestions***

- Shifting loans from productive sectors to unproductive sector indicates that banking sector development in India seems to help from the demand side not from the supply side of the economy. The economic growth, driven by savings is generally more sustainable than the consumption driven growth. Therefore, utmost care should be taken while advancing loans to see whether the loans are disposed up in productive sector or not.

- Assets quality shows the soundness of financial institutions. Public Sector Banks should disburse their funds in quality assets to reduce NPA level and banks also must establish proper credit assessment and risk management mechanism to ensure appropriate assessment of credit prior to the sanctioning of loans. Further, the apex bank also should mandate that banks must fallow income recognition norms, i.e. banks must only recognize income when it is received as payment from the customer. Banks are also advised to set up realistic payment schedules based on the barrower's actual paying capability. Finally, banks also should fallow diversified revenue policy to retain their financial viability. Because Indian banks mostly dependent on interest income. For instance, in 2011-12 the ratio of interest income to total income of PSBs was 90.6.

- In other hand, instead of shutting down the bank branches in rural areas, it would be better to increase their efficiency by focusing on reducing operational costs and other controllable expenses, besides creating awareness and promoting banking literacy among the rural folk so that not only the small savings will be generated but also the rural people's banking habit canbe fostered and the rural people can be a part of the inclusive growth process. Moreover, this would also help in achieving inclusive financial growth i.e., providing an opportunity to participate and also enabling them to reap the benefits too. All that needed is a strong political will and an effective implementation.

## Appendix

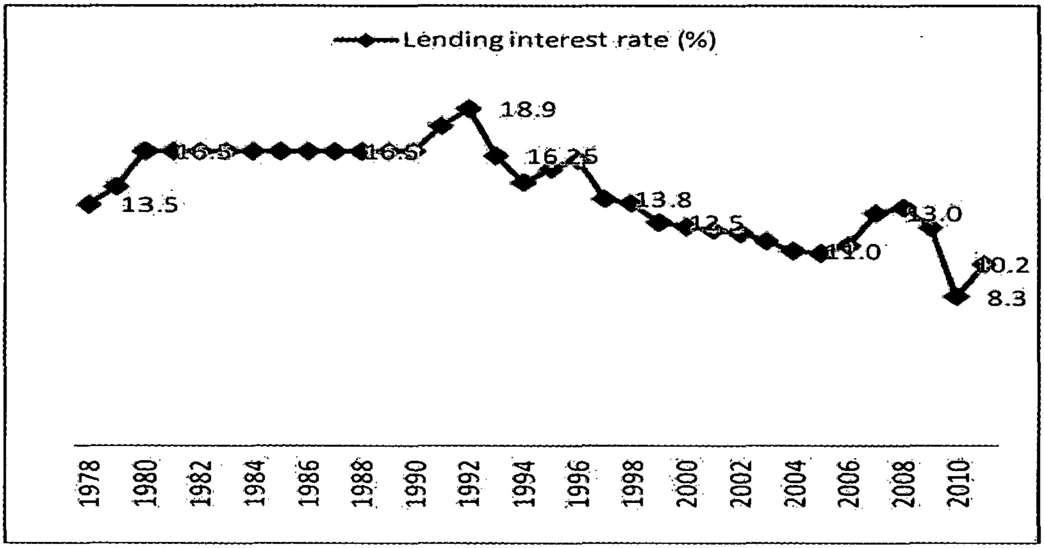
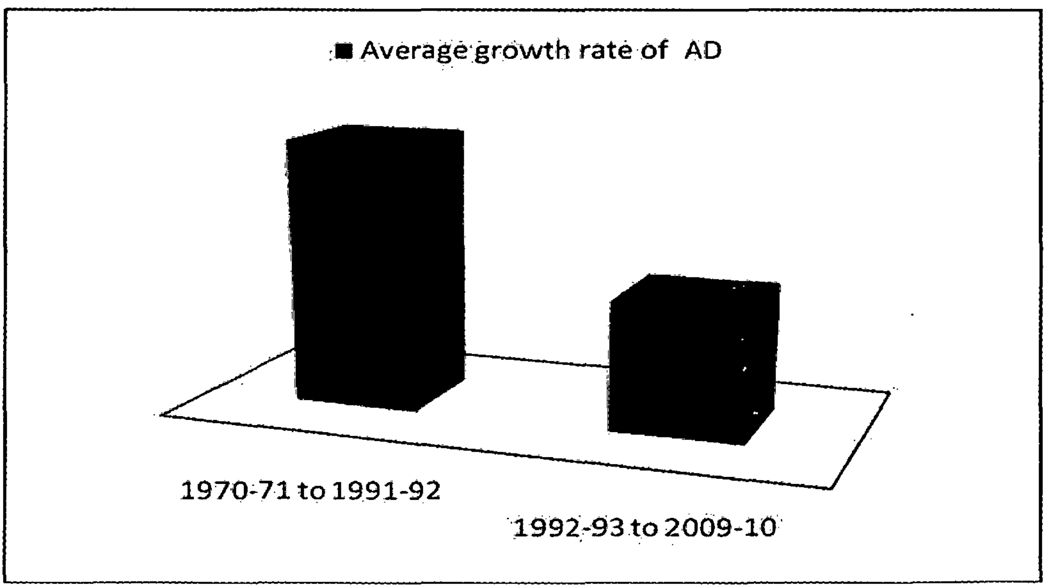
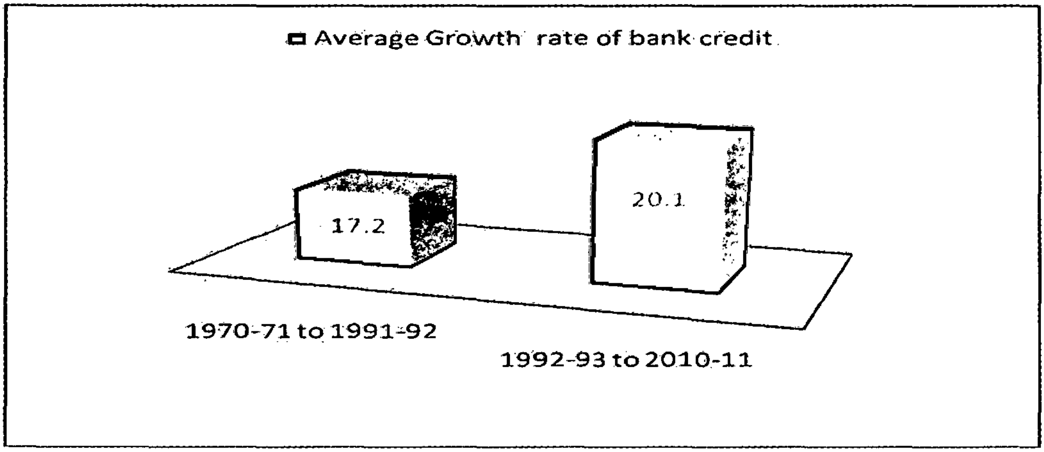



**Chart-1: Average growth rate of aggregate deposit**



## Chart-2: Average growth rate of total Bank credit




## Chart-3: Average growth rate of banking business

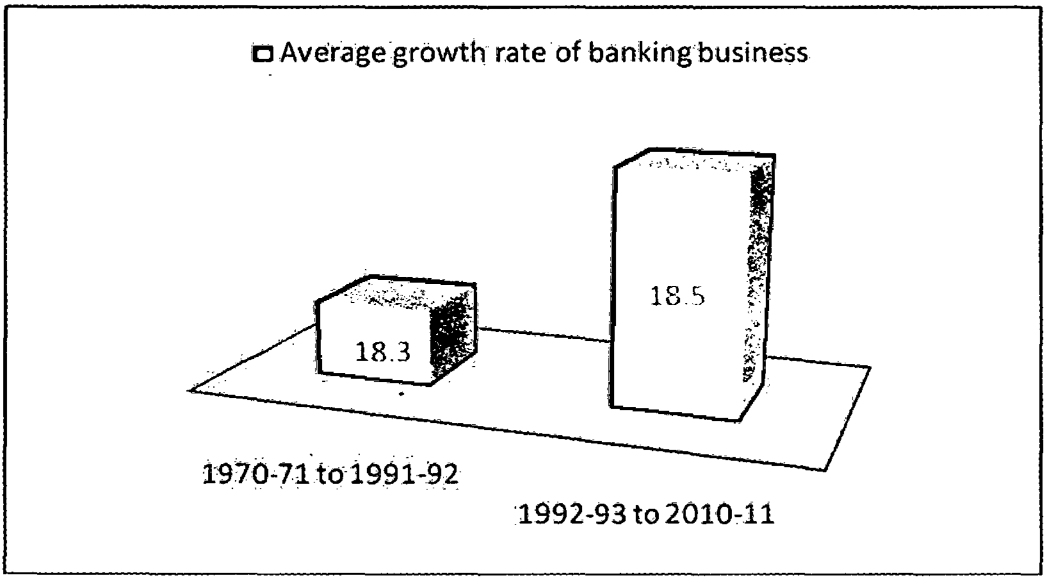


**Chart-4: Average growth rate of total bank investment**

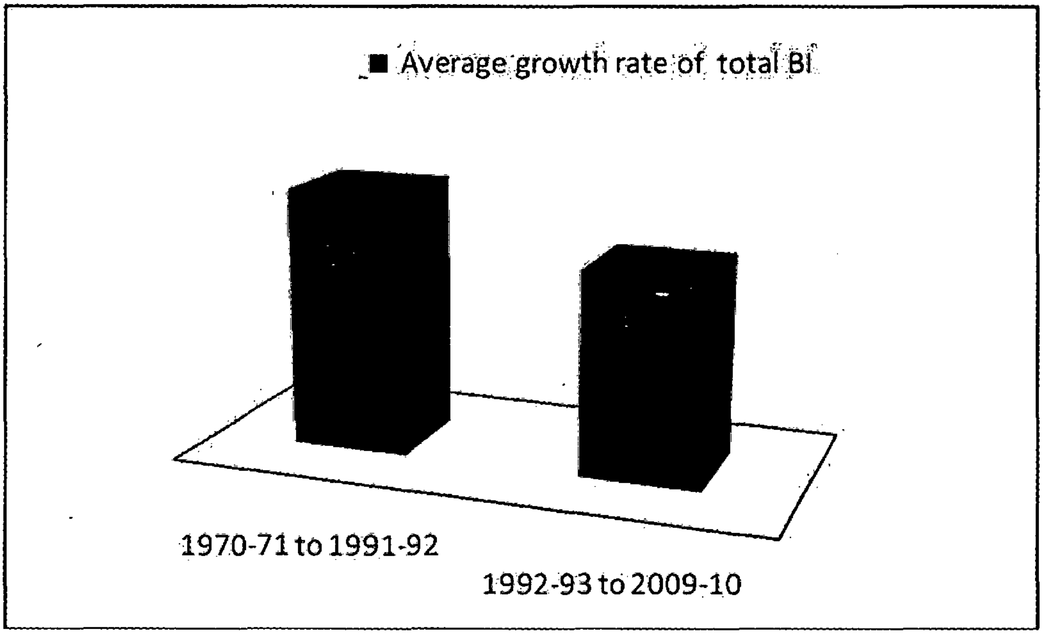
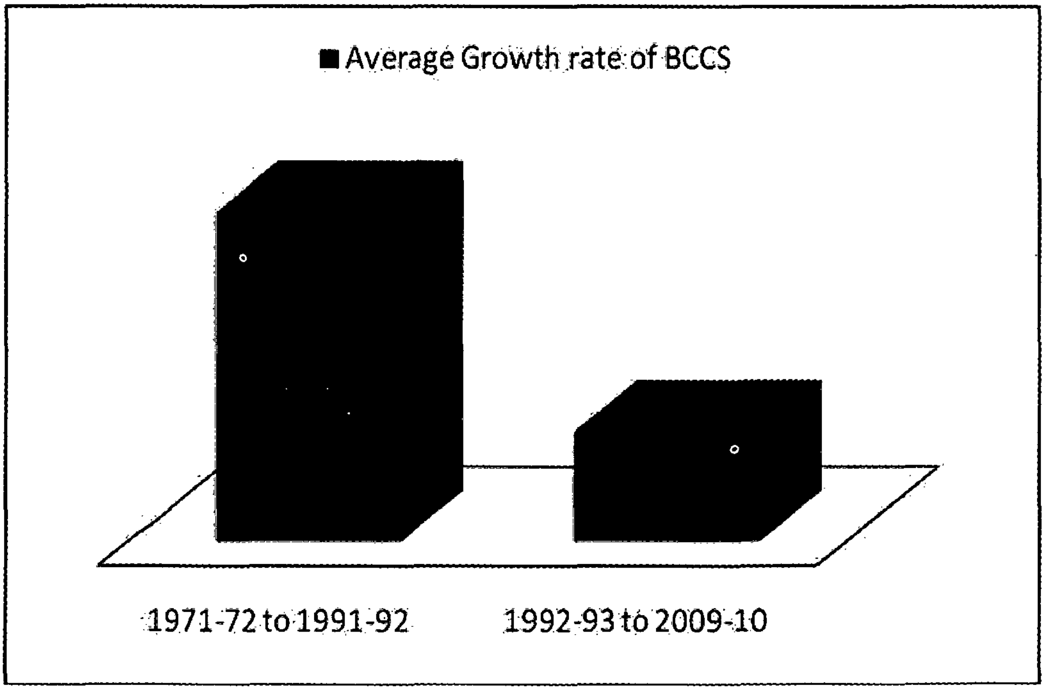
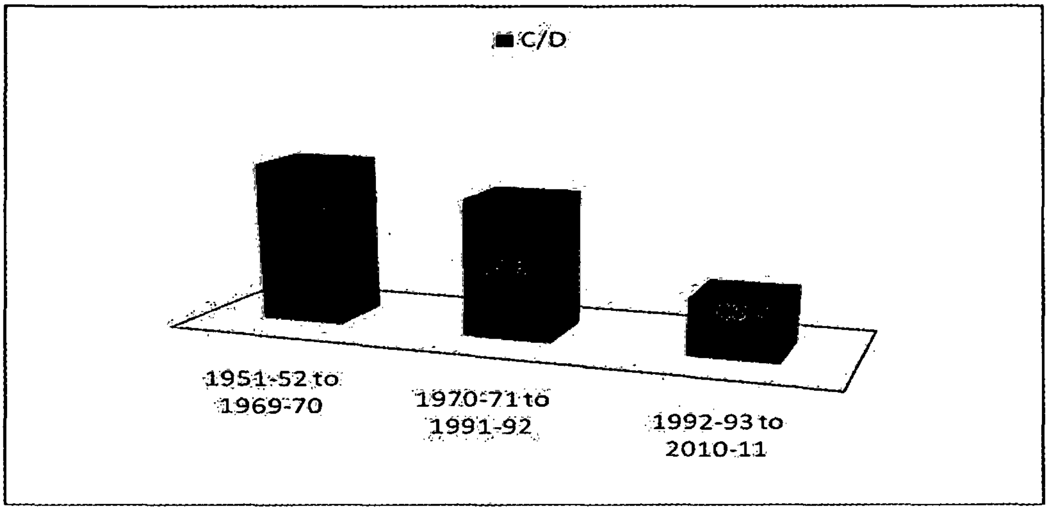


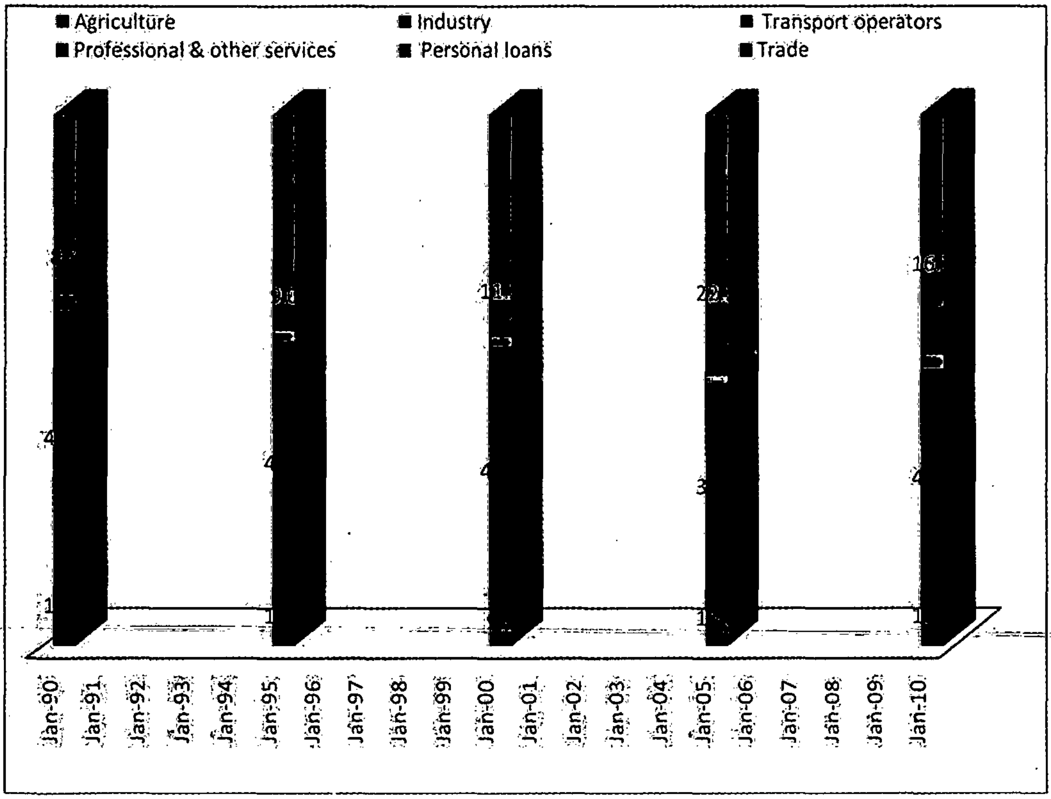

**Chart-5: Average growth rate of bank credit to commercial sector**



## Chart 7: Credit deposit ratio




## Chart-6: Schedule Commercial Bank credit – Industry wise



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