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IMPACT OF PRIVATIZATION ON INDIAN BANKING SECTOR

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Abstract:

Privatization is transfer of ownership from the public to the private sector as well as the control over assets. In broader terms, it involves greater influence on demand and supply force, make sure that there is higher competition, it brings greater involvement in government activities. It brings liberalization in different regulations to release forces of competition and to implement demand and supply forces into the economy. Privatization is contemplate to bring up competition, making sure greater capital investment, competitiveness and modernization, resulting in development of employment and providing improved quality of products and services to the consumers and reduction in the tax burden.As part of improvement process in the financial services sector, in January 1993 RBI issued certain guidelines for getting license of new banks in the private sector. It has been revised after 8 years in January 2001. Some of the important conditions in the private sector as per revised guidelines by the RBI are Paid Up Capital, Promoters Contribution, Foreign Investment etc.The study involves the benefits how the number of branches increased after privatization, increase of credit facilities for agriculture and increase of job opportunities, and adverse impacts of privatization on Indian Banking like high interest rates, less job securities, interference of politician and Industrialist, less control of government over private banks, private sector use private recovering agents to recover bad loans these agencies uses wrong means to recover loans from people.

Index Terms: Privatization, Interest Rate, Job Opportunities & NPVs

1. Introduction:

Privatization is transfer of ownership as well as the control over assets from Public sector to Private sector. It involves greater influence in market forces, greater competition and high involvement in government activities. In Indian Banking system, the most of the banking aspects are characterized by the coexistence of private and public ownership groups. There were 27 Public sector banks, 23 Private sector banks and 23 foreign banks operating in India in the year 1990-91. Banking industry in India has always moved around the deposit and credit functions. Their main role is to assist the overall economic growth where majority of shares being controlled by the government of India. But when the liberalization takes place, the banking industry undergone tremendous change in the last 5years. The RBI introduced a new norms to adopt new practices and to make banks more accountable followed worldwide.

2. RBI Guidelines for New Private Sector Banks:

As a part of reforming sector in financial services, in January 1993, the RBI issued certain guidelines for providing license for new banks in the private sector. It has revised his guidelines after 8years in January 2001. Some of the important guidelines by the RBI to new Private Sector Banks are:

Paid-Up Capital: The new banks should maintain initial minimum paid up capital Rs.100crores. within 3years of commencement of business banks should raise initial capital to 300crores. The overall capital structure of the banks would have to be approved by the Reserve Bank of India.

- ✓ **Promoters Contribution:** The maximum contribution of promoters will be 40% of paid up capital at any point of time. The initial capital can be raised through public issue other than promoters contribution. The contribution of 40%will be locked for 5years from the date of licensing of the bank.
- ✓ **Foreign Investment:** The participation of non-resident Indian in the equity of new bank will be a maximum extension up to 40%. In case of foreign banking, co-promoter equity participation will be restricted to 20% within the upper limit of 40%. In case of shortage of equity participation by foreign contributors then multilateral institutions would be allowed to contribute foreign equity to cover the shortfalls of the equity. The necessary approval by the Foreign Investment Promotion Board(FIPB) should be obtained.

Banks Promoted by Large Industrial Houses: Individual companies are allowed to participate in the equity of bank up to 10% limit because they are directly or indirectly connected with new banks and this applies to all large business house who are interconnected companies.

- ✓ Capital Adequacy Requirements: The minimum requirement of the bank to maintain capital of 10% on a commencement of its operation

Constitutional Obligation: The constitutional method in India helps to remove the unequal opportunities and rewards for different social positions or statuses within a group of society. The main intention of framers of Indian Constitution is citizens should be safe and secure.

Recommendations of First & Second Narasimham Committee and Verma Committee: Narasimham Committee has not directly supported to banks in privatization, it suggested certain recommendations for market strategy and profit seeking banks. According to Narasimham Committee: Committee believes that there is consistency in foreign investment policy with other aspects of government policy. We believe that the entry of foreign banks to the domestic country brings more beneficial to the country from the point of view of competitive efficiency improvement of Indian banking system. And also upgradation of work technology.

In April 1998, The Committee on Banking Sector Reforms (BSR) recommended the second stage of banking reforms. The chairman of this committee is Narasimham. The main theme is making strong of the banking system to the growth of the economy and this will bring efficiency in capital adequacy, generation of income and providing related norms over the period of next four years. On the other hand, The Verma Committee report of 1998 recommended to closing down weak banks. According to the committee, weak banks means the banks which have high non-performing assets. As per the view of Verma committee rural branches have high non-performing assets and considering those banks are weak banks. If weak banks are allowed to perform in the society it affects the efficiency of other banks as well. The Verma Committee report of 1998 on the other hand recommends closing down weak banks. According to the Verma Committee, weak banks are those banks, which have high non-performing assets. The Committee found that many of the rural branches have high non-performing assets and considered those banks as weak banks. If the weak banks are allowed to function in the economy it will affect the efficiency of other banks also. Thus it is clear that as per the recommendations of all these committees banking sector should restructure to bring efficiency in it. The government has taken many measures to implement the recommendations of the committee.

Effect of Norms: The new banking culture protected by reforms, is reflected in ignoring the priority sectors, fully unfair treatment of opportunities offered by capital market related activities. As the chairman of Sate Bank of India correctly pointed out, “this approach Breaks faith of an innocence of realities of Indian economy” These brings following changes in activities:

- ✓ **Priority Sector Lending:** The general perception of the priority sectors are that prescription of 40% of net bank credit, which have lead to the higher level of Non Performing Assets (NPAs). The accepted fact that increase in Non Performing Assets will definitely affect the Indian Banking System.
- ✓ **No More Subsidized Interest:** the main aim of Narasimham committee is that the real interest rate always should be positive it should not create any concession in the aspect of interest rate.
- ✓ **Impact on Agriculture:** As far as India is concerned, agriculture is backbone of Indian economy. 59.4% of the population is engaged in agriculture, but this suffers from lower productivity compared to per hectare and per worker. One of the main reason for lack of productivity is inadequate service like finance and marketing. Credit requirement for agriculture sector is so large to meet their requirements. RBI improved the policies of agricultural advances from 54.1% in 1992 to 59.6% in 1995.
- ✓ **Regional Imbalances**: As per the Verma committee such banks should be closed who involve in lack of non-fund business, augmentation of non-interest income, establishment cost is highand non capability to improve the sustainability of business levels. Licensing policy liberalization also one of the reason for regional imbalances. As per the section 22 of the Banking Regulation Act, 1949, before commencing business in India every company should obtain license from the RBI.

3. Arguments for Privatization of Banks in India:

- ✓ By privatization government will lose ownership and there will be a existence of private ownership.
- ✓ Monopoly system will arise due to privatization this will lead to a decrease in quality of services of the banks and customers will suffer.
- ✓ State ownership reduces the competition and inefficiency.
- ✓ There is no proper evidence to say that state ownership reduces the profitability.
- ✓ The rationale behind the privatization is develops the productivity through the proper management and control and it brings efficiency.
- ✓ Privatization helps the private sector banks and foreign banks from local government pressure.

4. Arguments Against Privatization:

- ✓ The main directive principle is that privatization banks will go away from government restrictions.
- ✓ Public sector banks already foster their technological advancement due to competition. It is favour to privatization and foreign ownership.
- ✓ Privatization would remove thickness of the economy from the critical examination of public and social accountability.
- ✓ Social accountability is not so important but it becomes absolutely necessary when comes to function of Profit-Making.
- ✓ Over last 5 decades India have been planned economy, but due to absence of effective control over the commercial banks planning was incomplete and failed to achieve the goal.

5. Objectives of the Study:

- ✓ To study about the privatization how it brings advantages to the Banking Sectors.

- ✓ To know the development factor of Private Sector Banks.
- ✓ To gather information how privatization leads to a success of the banks.
- ✓ To know whether privatization leads to benefit or harmful to the Customers.

6. Findings:

- ✓ In the process of privatization banks should maintain a minimum paid up capital of Rs.100crores within 3years of commencement should raise to 300crores. Here there should be a involvement of promoters and foreign investments as well. All the capital structure format should be approved by Reserve Bank of India.
- ✓ As per the RBI rules individual companies were allowed to participate in a equity of the banks up to 10% limit.
- ✓ Narasimham Committee decided to bring efficiency in capital of Private sector banks and in up gradation of technology.
- ✓ Verma committee recommended that those banks have non-performing assets are weak banks. If these banks were allowed to function it will affect the efficiency of other banks as well.
- ✓ As for as agriculture is concerned 59.4% of population is engaged in agriculture, their main problem is less productivity due to insufficient credit finance.
- ✓ By privatization private ownership will come into existence and they lead to all the decisions with regards to business concerned.
- ✓ Privatization lead to a monopoly system, this will reduce the quality of efficiency and public will suffer.
- ✓ Public sector banks already foster their technological advancement due to competition. It is favour to privatization and foreign ownership.

7. Conclusion:

Bank plays an important role in economic progression of the country. Public fund are involved in insurance and banking sectors. It collects surplus money from the society and uses it in desired directions. As per the Indian Constitution, main economic activity is to satisfy the public interest, but in the process of privatization, it harms the public interest. This was the reason created improper behavior in human beings. India as whole are affected by privatization in Banking and insurance sectors. Because argument says that, government will not protect the public money and win the public confidence. Another point is that profit will not be revealed by such companies. It is doubtful obligation to the society. But this cannot be considered as failure of banking sectors. Only a part of the weaker section will affect the success of the sectors. There is one possible solution to retain their success is that make a working of Debt Recovery Concept effective and powerful. In the case of Privatization, Banking Industry will be dominated by other big industries. Such industry to the society ownership pattern of big industries are not consistent in banking industries. Finally what government suggests is not just disturbing but clearly developing and beneficial to the society. This will bring new culture in banking not only for small borrower but also for small saver.

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