GOVERNMENT INITIATIVES IN BANKING SECTOR REFORMS

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Abstract:

The traditional face of banking is undergoing change from one of mere intermediator to that of provider of quick cost effective and efficient services. The Indian banking sector is an important constituent of the Indian financial system. The banking sector plays a vital role of promoting business in urban as well as in rural areas in recent years. Without it India cannot be considered as a healthy economy. Form the past three decades India's banking system has several outstanding achievements to its credit. Developing economy like India the banking sector has to face difficult challenges and issues, to overcome these challenges and issues banking sector reforms is important. The main intent of banking sector reforms was to uphold a diversified, efficient and competitive financial system with the aim of improving the allocative efficiency of resources through operational flexibility and improved financial viability. The main objective of the paper is to make a simple assessment of the banking sector reforms in India and the financial sector reform was one of the important parts of the process. The study will try to list the major reforms of the Indian baking sector and to find out the impacts of these reform and the future prospects.

Key words: intermediator, diversified, operational flexibility, allocative efficiency, financial viability

INTRODUCTION

During the decades of the 60s and the 70s in India nationalized most of its banks. This culminated with the balance of payments crisis of the Indian economy where India had to airlift gold to International Monetary Fund (IMF) to loan money to meet its financial obligations. In 1991 the country was caught into deep economic crisis. The Govt at this juncture decided to introduce comprehensive economic reforms. The Government of India (GOI), post-crisis, took several steps to remodel the country's financial system. The banking sector, handling 80% of the flow of money in the economy, needed serious reforms to make it internationally reputable, accelerate the pace of reforms and develop it into a constructive user of an efficient, vibrant and competitive economy by adequately supporting the country's financial needs.the Govt. Appointed a committee of the financial system under the chairmanship of M. Narasimham. In 1991 which deliver its report within 3 months. The Govt.Also appointed the committee the banking sector reforms under the chairmanship of M. Narasimham which submitted its report in April 1998. These reports are land mark documents and have influenced greatly the banking sectors reforms during the past few years.

OBJECTIVESOFTHESTUDY

- To have a overview the initiative taken by the Govt about banking sector reforms after 1991
- The study will try to list the major reforms of the Indian baking sector
- To find out the impacts of these reforms upon credit delivery, share market of banks, profitability and prudential regulations.

REVIEW OF LITERATURE

- Dr. NallaBalaKalyan

Banking sector is treated as to be the back bone of the Indian economy. The task of banking industry is particularly vital as one of the leading and mostly essential service sector. The banking sector, being the indicator of the economy, is reflective of the macro-economic variables. While the Indian economy is yet to catch strength, the Indian banking system continues to deal with improvement in asset quality, execution of sensible risk management practices and capital adequacy. The paper focuses on the impact of reforms and analysis in Indian banking system. The Indian banking system consists of 26 public sector banks, 25 private sector banks, 43 foreign banks, 56 regional rural banks, 1,589 urban cooperative banks and 93,550 rural cooperative banks, in addition to cooperative credit institutions. The purpose of this paper is to study the performance of banking industry in India.

- Sayuri Shirai (2002)

India and China both carried out banking sector reforms in the 1990s.Despite taking a radual approach, India's reforms have been the more comprehensive and have been implemented at a faster pace than in China. India's experience suggests that the following four issues would be relevant in China's future reform agenda: (1) privatizing the wholly state-ownedcommercial banks (WSCBs) and introducing measures to improve corporategovernance; (2) removing Government intervention to make WSCBs more commercially oriented; (3) reducing the dominance of WSCBs byrationalizing weak banks and downsizing large WSCBs; and (4) if adopted, relaxing the stringent statutory liquidity requirement, which seems todiscourage banks from lending.

RESEARCH METHODOLOGY

The sources of the secondary data are, RBI publications, published data of banks, newspaper clippings, economic survey and other reports of government of India, published and unpublished research works of various eminent scholars in the field.

Banking Sector Reforms

Autonomy in banking

Recommendation:-

• Greater autonomy was proposed for the public sector banks in order for them to function with equivalent professionalism as their international counterparts. For this panel recommended that recruitment procedures, training and remuneration policies of public sector banks be brought in line with the best-market-practices of professional bank management.

• The committee recommended GOI equity in nationalized banks be reduced to 33% for increased autonomy. It also recommended the RBI relinquish its seats on the board of directors of these banks. The committee further added that given that the government nominees to the board of banks are often members of parliament politicians, bureaucrats, etc., they often interfere in the day-to-day operations. As such the committee recommended a review of functions of banks boards with a view to make them responsible for enhancing shareholder value through formulation of corporate strategy and reduction of government equity.

• The committee recommended that the RBI withdraw from the 91-day treasury bills market and interbank call money and term money markets be restricted to banks and primary dealers.

• The Committee proposed a segregation of the roles of RBI as a regulator of banks and owner of bank. It highlighted that RBI's role of effective supervision was not adequate and wanted it to divest its holdings in banks and financial institutions.

Implementation:-

• To implement this, criteria for autonomous status March 1999, 17 banks were considered eligible for autonomy. But some recommendations like reduction in Government's equity to 33%, the issue of greater professionalism and independence of the board of directors of public sector banks is still awaiting.

• The RBI introduced a Liquidity Adjustment Facility (LAF) operated through repo and reverse repos to set a corridor for money market interest rates. In April 1999, an Interim Liquidity Adjustment Facility (ILAF) was introduced for further upgradation in technology and legal/procedural changes to facilitate electronic transfer.

• The RBI decided to transfer its respective shareholdings of public banks like State Bank of India (SBI), National Housing Bank (NHB) and National Bank for Agriculture and Rural Development (NABARD) to GOI. Subsequently, in 2007–08, GOI decided to acquire entire stake of RBI in SBI, NHB and NABARD.

• The Committee recommended for merger of large Indian banks to make them strong enough for supporting international trade. It recommended a three tier banking structure in India through establishment of three large banks with international presence, eight to ten national banks and a large number of regional and local banks.

• The Committee recommended the use of mergers to build the size and strength of operations for each bank. It cautioned that large banks should merge only with banks of equivalent size and not with weaker banks.

Non-performing assets

Non-performing assets had been the single largest cause of irritation of the banking sector of India.

Recommendation:-

1. The committee had highlighted that 'priority sector lending' was leading to the buildup of non-performing assets of the banks and thus it recommended it to be phased out.
2. Narasimham Committee-II also highlighted the need for 'zero' non-performing assets for all Indian banks with International presence.

3. The 1998 report further blamed poor credit decisions, behest-lending and cyclical economic factors among other reasons for the buildup of the non-performing assets of these banks to uncomfortably high levels.
4. The Committee recommended creation of Asset Reconstruction Funds or Asset Reconstruction Companies to take over the bad debts of banks, allowing them to start on a clean-slate.
5. The option of recapitalization through budgetary provisions was ruled out. Overall the committee wanted a proper system to identify and classify NPAs,NPAs to be brought down to 3% by 2002and for an independent loan review mechanism for improved management of loan portfolios.

Implementation:-

Introduction of a new legislation which was subsequently implemented as the Securitization and Reconstruction of Financial Assets and Enforcement of Security Interest Act, 2002 and came into force with effect from 21 June 2002.

Entry of foreign banks

The committee suggested that the foreign banks seeking to set up business in India should have a minimum start-up capital of $25 million as against the existing requirement of $10 million. It said that foreign banks can be allowed to set up subsidiaries and joint ventures that should be treated on a par with private banks.

Impact of Banking Sector Reforms of 1991

- Enhancing competition in the banking sector 10 new private sector banks were set up since 1993, RBI had granted license to one more new private sector bank as per the revised policy of January, 2001.
- The average CRAR of all banks increased from 9.23% as on March 31, 1994 to 12.78% as on March 31, 2003, out of the 23 banks in the public sector, 22 had CRAR of more than 10%.
- The gross NPAs, as a proportion of gross advances, have been declining steadily and distinctly over the years. The percentage of gross NPAs to gross advances for all banks, which was 14.4% in 1997-98, decreased to 8.8% as on March 2003. The percentage of Net NPAs to net Advances declined from 7.3% to 4.4% indicating the increasing emphasis by banks on adequate provisioning.
- The reform measures have also resulted in the improvement in the profitability of banks. The Return on Assets (ROAs) of all banks rose from 0.39 in 1991-92 to 1.0 in 2002-03.The profitability of public sector banks were hit in the initial years of reforms.
- Various steps had been taken by the banks, including the Voluntary Retirement Scheme, which was introduced in consultation with the Government of India, has resulted in significant improvement in the Business Per Employee of Public sector banks.

Conclusion

Due to the level of competition was gradually increased. The technology taken place in banking sector. The Indian banking industry had made sufficient progress during the reforms period. The Indian Banking sector reform started with the nationalization of banks, but it speed up after liberalization. After liberalization bank are free from unnecessary restriction. The private bank and foreign banks entered. The progress of the industry can be judged in terms of branch expansion and growth of credit and deposits. Though the branch expansion of the SCBs has slowed down during the post 1991 era but population per bank branch has not changed much. Therefore, banking sector has maintained the gains in terms of branch network in the phase of social banking during the reform period. We have remarkable reforms in banking sector after the 1991.

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