### Indian Financial System

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### Indian Financial System

#### General Overview-

- The Indian Financial System is one of the most important aspects of the economic development of our country. This system manages the flow of funds between the people (household savings) of the country and the ones who may invest it wisely (investors/businessmen) for the betterment of both the parties.
- The services that are provided to a person by the various Financial Institutions including banks, insurance companies, pensions, funds, etc. constitute the financial system.
- The financial system of a country mainly aims at managing and governing the mechanism of production, distribution, exchange and holding of financial assets or instruments of all kinds.

#### <u>Definition –</u>

The various type of services that are provided by financial institutions like banks, insurance companies, pensions, fund etc. to the people of the country makes a financial system.

### Features/Role of the Indian Financial system

- It plays a vital role in the economic development of the country as it encourages both savings and investment
- It helps in mobilizing and allocating one's savings
- It facilitates the expansion of financial institutions and markets
- ► Plays a key role in capital formation
- It helps form a link between the investor and the one saving
- It is also concerned with the Provision of funds.
- ➤ It is responsible for capital creation.
- To maintain the economic stability in the country and the markets.
- ➤ Boosting the growth of stock markets and other financial markets.
- To create markets that can judge the investment performance.
- ➤ It forges a connection between depositors and investors.

# Banking System and Origin of Banks

### Banks

- Meaning-
- ➤ Bank is a lawful organization, which accepts deposits that can be withdrawn on demand. It also lends money to individuals and business houses that need it.
- Banks give two assurances to the depositors
  - a. Safety of deposit, and
  - b. Withdrawal of deposit, whenever needed
- ➤ On deposits, banks give interest, which adds to the original amount of deposit. It is a great incentive to the depositor. It promotes saving habits among the public. On the basis of deposits banks also grant loans and advances to farmers, traders and businessmen for productive purposes. Thereby banks contribute to the economic development of the country and well being of the people in general. Banks also charge interest on loans.

 The activities carried on by banks are called banking activity. 'Banking' as an activity involves acceptance of deposits and lending or investment of money. It facilitates business activities by providing money and certain services that help in exchange of goods and services.

### Role of Banking

- ✓ It encourages savings habit amongst people and thereby makes funds available for productive use.
- ✓ It acts as an intermediary between people having surplus money and those requiring money for various business activities.
- ✓ It facilitates business transactions through receipts and payments by cheques instead of currency.
- ✓It provides loans and advances to businessmen for short term and long-term purposes
- ✓ It also facilitates import export transactions.
- ✓ It helps in national development by providing credit to farmers, small-scale industries and self-employed people as well as to large business houses which lead to balanced economic development in the country.
- ✓ It helps in raising the standard of living of people in general by providing loans for purchase of consumer durable goods, houses, automobiles, etc.

### Origin / History of Banking

Banking in India forms the base for the economic development of the country. Major changes in the banking system and management have been seen over the years with the advancement in technology, considering the needs of people.

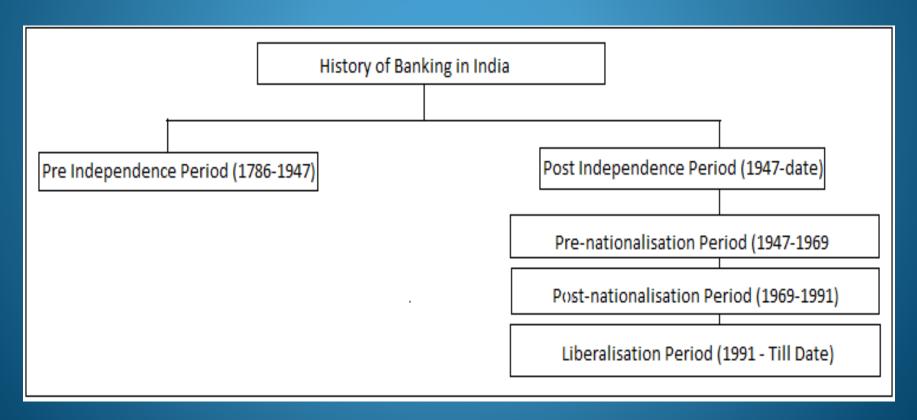
The History of Banking in India dates back to before India got independence in 1947

The banking sector development can be divided into three phases:

Phase I: The Early Phase which lasted from 1770 to 1969

Phase II: The Nationalization Phase which lasted from 1969 to 1991

Phase III: The Liberalization or the Banking Sector Reforms Phase which began in 1991 and continues to flourish till date.



#### Pre Independence Period (1786-1947)

The first bank of India was the "*Bank of Hindustan*", established in **1770** and located in the then Indian capital, Calcutta. However, this bank failed to work and ceased operations in 1832. During the Pre Independence period over 600 banks had been registered in the country, but only a few managed to survive.

Following the path of Bank of Hindustan, various other banks were established in India. They were:

- 1.The General Bank of India (1786-1791)
- 2.Oudh Commercial Bank (1881-1958)
- 3.Bank of Bengal (1809)
- 4.Bank of Bombay (1840)
- 5.Bank of Madras (1843)

During the British rule in India, The East India Company had established three banks: Bank of Bengal, Bank of Bombay and Bank of Madras and called them the Presidential Banks. These three banks were later merged into one single bank in 1921, which was called the "*Imperial Bank of India*."

The Imperial Bank of India was later nationalized in 1955 and was named The State Bank of India, which is currently the largest Public sector Bank.

### Post Independence Period (1947-1991)

At the time when India got independence, all the major banks of the country were led privately which was a cause of concern as the people belonging to rural areas were still dependent on money lenders for financial assistance.

With an aim to solve this problem, the then Government decided to nationalize the Banks. These banks were nationalised under the Banking Regulation Act, 1949. Whereas, the Reserve Bank of India was nationalised in 1949.

Following it was the formation of State Bank of India in 1955 and the other 14 banks were nationalised between the time duration of 1969 to 1991. These were the banks whose national deposits were more than 50 crores..

#### **Impact of Nationalization**

There were various reasons why the Government chose to nationalize the banks. Given below is the impact of Nationalizing Banks in India:

- •This lead to an increase in funds and thereby increasing the economic condition of the country
- •Increased efficiency
- •Helped in boosting the rural and agricultural sector of the country
- •It opened up a major employment opportunity for the people
- •The Government used profit gained by Banks for the betterment of the people
- •The competition decreased, which resulted in increased work efficiency

#### Liberalization Period (1991-Till Date)

Once the banks were established in the country, regular monitoring and regulations need to be followed to continue the profits provided by the banking sector. The last phase or the ongoing phase of the banking sector development plays a hugely significant role.

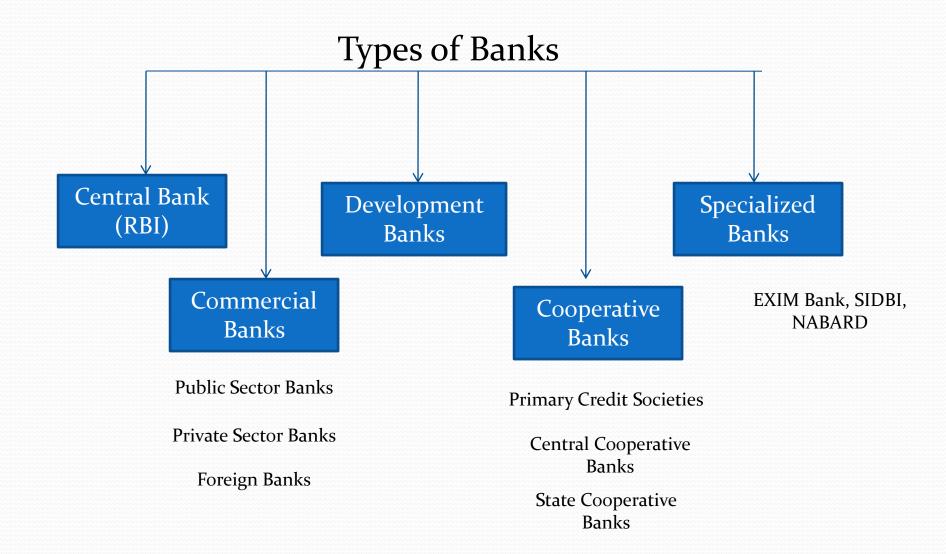
To provide stability and profitability to the Nationalised Public sector Banks, the Government decided to set up a committee under the leadership of Shri. M Narasimham to manage the various reforms in the Indian banking industry.

The biggest development was the introduction of Private sector banks in India. RBI gave license to 10 Private sector banks to establish themselves in the country.

#### The other measures taken include:

- 1. Setting up of branches of the various Foreign Banks in India
- 2. No more nationalization of Banks could be done
- 3. The committee announced that RBI and Government would treat both public and private sector banks equally
- 4. Any Foreign Bank could start joint ventures with Indian Banks
- 5. Payments banks were introduced with the development in the field of banking and technology
- 6.Small Finance Banks were allowed to set their branches across India
- 7. A major part of Indian banking moved online with internet banking and apps available for fund transfer

### Types of Banks



## Thank you