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Role of Commercial Bank in the Economic Development of INDIA

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ABSTRACT

Banks play a vital role in the economic development of a country. They accumulate the idle savings of the people and make them available for investment. They also create new demand deposits in the process of granting loans and purchasing investment securities. They facilitate trade both inside and outside the country by accepting and discounting of bills of exchange. Banks also increase the mobility of capital. All commercial banks in India excluding Regional Rural Banks and Local Area Banks have become Basel II compliant as on March31,2009.In a country like India which is still in the initial stages of economic development. A well organized banking system is the need of the day. Commercial banks are the most effective way to generate the credit flow of money in markets. There is acute shortage of capital in India. The banks can play an important role in promoting capital formation, in controlling speculation in maintaining a balance between requirements and availabilities and in direct physical resources into desired channels.Commercial banks play an important and active role in the economic development of a country, if the banking system in a country is effective, efficient and disciplined; it brings about a rapid growth in the various sectors of the economy. As we know that the Agriculture is the backbone of economy of any country like India. Research is based upon the secondary date which provide the findings on commercial banks and how it helpful in economic development. So this research will helpful in finding out that how commercial banks are helpful in credit flowing, employment generations in rural areas and how it will contribute in development of Indian economy.

***Keywords**:* Agriculture Credit, Economic Development, Poverty.

I. INTRODUCTION

With the introduction of liberalization, privatization and globalization the role of banking sector changed dramatically. Credit is one of the critical inputs for agricultural development. It capitalizes farmers to undertake new investments and/or adopt new technologies. The importance of agricultural credit is further reinforced by the unique role of Indian agriculture in the macroeconomic framework along with its significant role in poverty alleviation. Realizing the importance of agricultural credit in fostering agricultural growth and development, the emphasis on the institutional framework for agricultural credit is being emphasized since the beginning of planned development era in India. India is home to 22 per cent of the world's poor. Such a high incidence of poverty is a matter of concern in view of the fact that poverty eradication has been one of the major objectives of the development planning process. Indeed, poverty is a global issue. Its eradication is considered integral to humanity's quest for sustainable development. Reduction of poverty in India is, therefore, vital for the attainment of international goals.

A commercial bank is a type of bank that provides services such as accepting deposits, making business loans, and offering basic investment products. Commercial bank can also refer to a bank or a division of a bank that mostly deals with deposits and loans from corporations or large businesses, as opposed to individual members of the public. The share of commercial banks in total institutional credit to agriculture is almost 48 percent followed by co-operative banks with a share of 46 percent and RRBs about 6 percent. But studies have shown that many of the ordinary people have no access to institutional credit. The growth rate of deposits in commercial banks in India is around 16 percent As per the announcement made in the Annual Policy statement for the year 2008-09, RBI advised banks in May 2008 to classify overdrafts up to Rs.25,000 (per account) against „no-frills" accounts in the rural and semi-urban areas as indirect finance to the agriculture sector under the priority sector advances with immediate effect.

A large number of formal institutional agencies like Co-operatives, Regional Rural Banks (RRBs), Scheduled Commercial Banks (SCBs), Non– Banking Financial Institutions (NBFIs), and Self-help Groups (SHGs), etc. are involved in meeting the short- and long-term needs of the farmers. Several initiatives have been taken to strengthen the institutional mechanism of rural credit system. The main objective of these initiatives was to improve farmers' access to institutional credit.

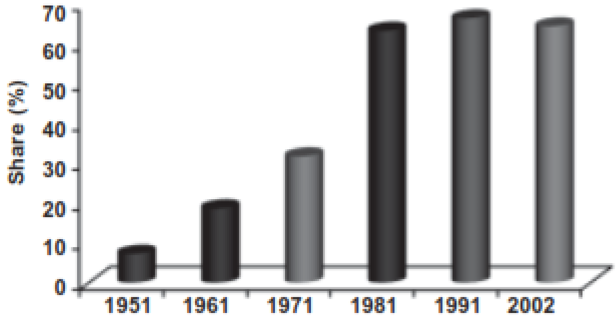
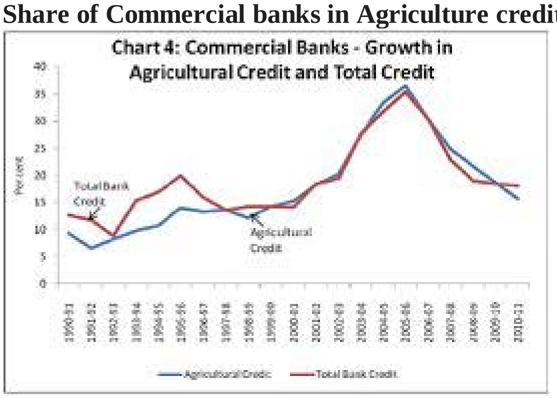


Figure 1. Share of institutional credit in total borrowing of farm households in India

Source: Mohan (2004); NSSO 59th Round (2003)

Share of Commercial banks in Agriculture credit



II. FUNCTIONS OF COMMERCIAL BANKS

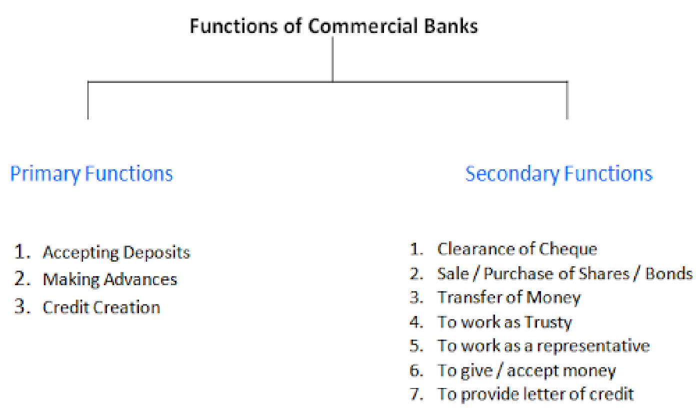
Commercial banks perform many functions. They satisfy the financial needs of the sectors such as agriculture, industry, trade, communication, so they play very significant role in a process of economic social needs. The functions performed by banks, since recently, are becoming customer-centered and are widening their functions. Generally, the functions of commercial banks are divided into two categories: primary functions and the secondary functions. The following chart simplifies the functions of commercial banks. Commercial banks perform various primary functions, some of them are given below. Commercial banks accept various types of deposits from public especially from its clients, including saving account deposits, recurring account deposits, and fixed deposits. These deposits are payable after a certain time period. Commercial banks provide loans and advances of various forms, including an overdraft facility, cash credit, bill discounting, money at call etc. They also give demand and demand and term loans to all types of clients against proper security. Credit creation is most significant function of commercial banks. While sanctioning a loan to a customer, they do not provide cash to the borrower. Instead, they open a deposit account from which the borrower can withdraw. In other words, while sanctioning a loan, they automatically create deposits, known as a credit creation from commercial banks. Along with primary functions, commercial banks perform several secondary functions, including many agency functions or general utility functions. The secondary functions of commercial banks can be divided into agency functions and utility functions.

The agency functions are the following:

To collect and clear cheque, dividends and interest warrant and to make payments of rent, insurance premium, etc. and deal in foreign exchange transaction and to purchase and sell securities and to act as trustee, attorney, correspondent and executor and to accept tax proceeds and tax returns.

The utility functions are the following:

To provide safety locker facility to customers and to provide money transfer facility and to issue traveller's cheque and to act as referees and to accept various bills for payment: phone bills, gas bills, water bills, etc. and to provide merchant banking facility and to provide various cards: credit cards, debit cards, smart cards, etc.



III. LITERATURE REVIEW

Reforms in the commercial banking sector had two distinct phases. The first phase of reforms, introduced subsequent to the release of the Report of the Committee on Financial System, 1992 (Chairman: Shri M. Narasimham), focused mainly on enabling and strengthening measures. Two major developments occurred; the first was the green revolution in the wake of adoption of the new agricultural technology. The second was the nationalization of 14 major commercial banks in

July 1969(six more commercial banks was nationalize in April 1980) .Multi agency Approach (MAA) was started regarding agricultural and rural credit. Commercial banks begin to participate with full heart in agriculture finance. Two new institutions known as regional rural banks and the farmers service societies were also establish during this period.

The following table shows the share of commercial banks and cooperatives in India.

Year	Commercial Banks
1970-71	-
1980-81	38.4
1990-91	47.6
2000-01	52.4
2001-02	54.1
2002-03	57.2
2003-04	60.3
2004-05	65.0
2005-06	69.7
2009-10	71.8

Source: Economic survey of India

The second phase of reforms, introduced subsequent to the recommendations of the Committee on Banking Sector Reforms, 1998 (Chairman: Shri M. Narasimham) placed greater emphasis on structural measures and improvement in standards of disclosure and levels of transparency in order to align the Indian standards with international best practices. During the last four decades, particularly after the first phase of nationalization of banks in 1969, there have been distinct improvements in the banking activities which strengthened the financial intermediation process. The total number of offices of public sector banks which was merely at 8262 in June 1969 increased to 62,607 as of June 2011. There was a sharp fall in the share of agricultural credit supplied by rural and semi-urban branches from 83.7 per cent in 1995 to 69.3 per cent in 2005. In 2008, the share of rural and semi-urban branches in total agricultural credit was 66 per cent.

In Table shown below, it may be observed that credit provided by the banking sector as a percentage of GDP has increased steadily over the years from 37.0 percent in 1980 to 75.1percent in 2011. On the other hand, stock market capitalization as a percentage of GDP increased from 11.8 percent in 1990 to 54.9 percent in 2011. It may also be noticed that stock market capitalization as a percentage of GDP increased sharply in 2009 and 2010. These sharp gains in market capitalization to GDP ratio in 2009 could be attributed to valuation gains due to steep rise in share prices from a very low level in 2008 as the global financial crisis heightened. Furthermore, year-wise comparison of ratios in data reveals that barring a few years, credit to GDP ratio was higher than market capitalization to GDP ratio implying that financial system in India is more biased towards bank-based.

Table : Domestic Credit Provided by Banking Sector

(% of GDP)

Country/ Region	1980	1990	2000	2005	2008	2009	2010	2011
Brazil	43.0	87.6	71.9	74.5	96.9	95.8	95.2	98.3
China	53.3	89.4	119.7	134.3	120.8	145.1	146.3	145.5
Euro area	93.6	97.0	119.4	127.3	142.8	152.6	156.0	153.6
India	37.0	50.0	51.4	58.4	67.7	70.4	73.0	75.1
Japan	185.7	255.3	304.7	317.6	302.4	329.8	329.0	340.9
Russia	-	-	24.9	22.1	23.9	33.7	38.4	39.6
South Africa	76.4	97.8	152.5	178.5	173.8	184.2	182.4	167.0
South Korea	43.4	51.9	74.7	88.3	109.4	109.4	103.1	102.3
UK	36.2	118.2	130.2	161.9	213.5	229.2	222.6	213.8
US	120.2	151.0	198.4	225.4	222.0	234.9	232.9	233.3
World	93.5	130.6	158.9	162.1	154.7	169.1	167.4	165.3

Source: World Bank Data Base.

On February 10, 2005, the Government of India announced the setting up of the National Spot Exchange for Agriculture Produce (NSEAP), which will link all agri-produce marketing committees with consumers and producers. The electronic exchange will enable agro-based industries to sell farm produce more effectively. This will help farmers sell their produce at better rates and directly to corporates. The Indian Agriculture Ministry has signed an MoU with Financial Technologies (India) and Multi Commodity Exchange (MCX) with NAFED. In this case, SBI will be the principal clearing and settlement backup for NSEAP to ensure that money can be transmitted from one center to another across the country.

IV. RESEARCH QUESTIONS

- To know that how agriculture sector will create the Employment opportunities in rural areas
- To find out that how Commercial banks increase the credit flow in agriculture sector
- To know how Commercial banks help in alleviated of poverty
- To know how Commercial banks are helpful in economic development of any country.

V. METHODOLOGY

The research article is based upon descriptive analysis and it is an empirical research on which we have taken the secondary data by analyzing the various research articles related to the same field.

VI. FINDINGS AND POLICY IMPLICATIONS

RBI and Government are taking their full steps in modifying the present conditions of the agriculture sector in India. There is a sigh of relief for the rural poor from the dreaded clutches of money lenders. NABARD as apex institution of indirect financing to agriculture is providing patronage as philosopher, guide and friend. The progress achieved by NABARD in refinancing is praiseworthy .Study reveal that 66% people are still not getting the banking facilities and cheaper credit. Poor farmers are not able to survive in this kind of scenario. There are various studies which show that in India 40% farmers are committing suicide because of not able to fulfill the loan amount of banks. Commercial banks are providing credit to the poor farmers but this is not free from the other problems. Commercial Banks are providing 43.1% of total Agriculture credit (Economic Survey 2011). These are the still privileged problems in India faced by the farmer to get agriculture credit:

- High rate of interest on loan
- Lack of financial knowledge
- Cumbersome process of getting loan
- Bank staff is not cooperative
- Lack of security of collateral
- Fear factor about recovery process

The no of banks branches in RRBS area has been increased from 1833(1969) to 35850 (2012). This is the one of finest policy of RBI . with the increasing of branches in Rural area farmers are now able to get the loan and able to understand the process of it. The present challenge in front of the banks is to cover the 70,000 villages in rural are up to 2013. This process will increase the agriculture credit in India in effective ways.

According to reddy's report agriculture credit flow is only 18% in rural ares. So that the government should take some prime steps to increase the credit flow in agriculture sectoe. Because as we know that most of the 78% population of India is dependent upon agriculture sector if agriculture sector will grow then all associated factors like Employment Opportunities and Development of country is possible. The last Agriculture sector Contributions in GPD of Indian economy was 3.4%. (Economic survey if India).

VII. CONCLUSION

According to the Confederation of Indian Industry, Indian agriculture suffers mainly because of expensive credit, a distorted market, intermediaries (who increase cost rather than add value), controlled prices and poor infrastructure. It has also suffered because of poor irrigation facilities, use of traditional technology and practices, farmers' poor economic status, fragmented landholdings, lack of post harvest infrastructure and lack of farm extension. Banks should consider these facts to invest more in infrastructure facilities like irrigation facilities, processing, storage and marketing activities. Such agricultural infrastructure can be improved by banks, as there are ample prospects for banks to invest in the above activities. The above study reveals that how commercial banks are helpful in development of country. If we make the comparison between Rural area and urban area then it always come si n our mind that Urban area are more developd. This is because of low credit flow and less contribution of agriculture sectir in GDP of India. If agriculture sector grow then only Economic development is possible in india

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