Mains Practice Quesstions

Q. The bank nationalization in 1969 did India more harm than good. Critically examine. (250 words)

08 Oct, 2021 GS Paper 1 History

Approach

- Write about the history of bank nationalization in the introduction.
- Mention its objectives and benefits for the Indian economy.
- Mention the negative fallouts of the move.
- Conclude by giving its relevance for the ongoing banking reforms today.

Introduction

On 19 July 1969, Indira Gandhi government decided to nationalize fourteen of India's major private sector banks. It is considered as the most radical change in the history of the banking sector in India.

The decade of 1960-70 was marked with major events like two wars in 1962 with China and in 1965 with Pakistan, and two successive years of drought. The overall economy was in bad shape. In this backdrop, the decision of bank nationalization was taken.

Body

The major **causes and objectives of bank nationalization** were:

- **Financial inclusion:** Indian rural financial system was dominated by rich landlords, moneylenders and traders. 93% of household debt came from non-institutional sources.
- **Social welfare:** Lack of social protection like insurance facilities, investment options for old age, etc. in the rural areas.
- **Controlling private monopolies:** Private Banks were owned by a limited number of people who dominated the credit market.

It had a significant impact on the lives of people of lower strata of society. Major benefits of the bank nationalization move are:

- **Branches of the public sector bank India rose** to approximately 800% in deposits and advances took a huge jump by 11,000%.
- Government ownership gave the **public implicit faith and immense confidence** about the sustainability of the banks.
- Indian **banking system reached the remotest corners** of the country with the advent of Lead Bank Scheme where major banks were allowed to expand and lead a district.
- It had **multiplier effects** and even led to the **success of the Green Revolution.** It also promoted rapid growth in agriculture, small industries and export, encouraged new entrepreneurs in backward areas.

However, many political analysts argue that the move was suited for political gains of the government to show India's socialistic leanings with 'Garibi Hatao' as a household slogan at that time. It had many negative fallouts for the already crisis stricken economy at that time:

- It **sowed the seed of the NPA crisis** that emerged in 2012. The credit bubble that grew under political patronage emerged out of government's control over Banks.
- It led to an **incredibly complex interest rate structure** with hundreds of interest rates for different types of loans.

    It increased **corruption, bureaucratic inertia and license raj** so that loans never reached the needy ones.
- The move was **against market fundamentals.** It **reduced competition** among the banks as they were forced to extend loans as per priority sector lending norms.
- Dampened growth in other sectors due to lack of credit to core industries.

Conclusion

Former RBI governors M Narasimham (as early as the 1990s) and more recently Raghuram Rajan and Urjit Patel have called for governance reforms and asked that the government let go control of some banks, if not all. So the government should consider a couple of stateowned banks to meet social objectives while the rest slowly getting out of government control.

India’s goal of becoming a $5 trillion economy by 2024 can only be achieved by resolving the ongoing crisis like non-performing assets, the inherent deficiency of public sector banking, the structure of non-banking financial companies and small- and medium-enterprises.