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ECONOMIC DEVELOPMENT OF INDIA – AN ACCOMPLISHMENT BY Mrs. INDIRA GANDHI

[1,2]Chetan Gupta, [3]Dr. Madhu Vashishtha
[1]Associate Professor, [2]Research Scholar, [3]Associate Professor
[1,2,3]Department of History,
[1]Govt. College, Gharaunda (Karnal), Haryana
[2]Dr. Bhimrao Ambedkar University, Agra, U.P. (India)
[3]Srimati B.D. Jain Girls PG College, Agra, U.P.

ABSTRACT:
Economy of a country basically depends upon the strength and growth of banking sector and government policies for the same. Government control over banks has always had its fans, ranging from Lenin to Gerschenkron.While there are those who have emphasized the political importance of public control overbanking, most arguments for nationalizing banks are based on the premise that profit maximizing lenders do not necessarily deliver credit where the social returns are the highest. The Indian government lead by Mrs. Indira Gandhi when nationalizing all the larger Indian banks in 1969, argued that banking was "inspired by a larger social purpose" and must "sub-serve national priorities and objectives such as rapid growth in agriculture, small industry and exports.

INTRODUCTION:

Measured by share of deposits, 83 percent of the banking business in India is in the hands of state or nationalized banks, which are banks that are owned by the government, in some, increasingly less clear-cut way. Moreover, even the non-nationalized banks are subject to extensive regulations on who they can lend to, in addition to the more standard prudential regulations. There is now a body of direct and indirect evidence showing that credit markets in developing countries often fail to deliver credit where its social product might be the highest, and both agriculture and small industry are often mentioned as sectors that do not get their fair share of credit. If nationalization succeeds in pushing credit into these sectors, as the Indian government claimed it would, it could indeed raise both equity and efficiency (1).

This paper builds on the previous work with the aim of using that evidence and evidence from other research by ourselves and others, to come to an assessment of the appropriate role of the Indian government vis a vis the banking sector. We first provide a very brief history of banking in India.

BACKGROUND:

India has a long history of both public and private banking. Modern banking in India began in the 18th century, with the founding of the English Agency House in Calcutta and Bombay. In thefirst half of the 19th century, three Presidency banks were founded. After the 1860 introduction of limited liability, private banks began to appear, and foreign banks entered the market. The beginning of the 20th century saw the introduction of joint stock banks. In 1935, the presidency banks were merged together to form the Imperial Bank of India, which was subsequently renamed the State Bank of India. Also that year, India's central bank, the Reserve Bank of India (RBI), began operation. Following independence, the RBI was given broad regulatory authority over commercial banks in India. In 1959, the State Bank of India acquired the state-owned banks of eight former princely states. Thus, by July 1969, approximately 31 percent of scheduled bank branches throughout India were government controlled, as part of the State Bank of India (2).The post-war development strategy was in many ways a socialist one, and the Indian government felt that banks in private hands did not lend enough to those who needed it most. In July 1969, the government nationalized all banks whose nationwide deposits were greater than Rs. 500 million, resulting in the nationalization of 54 percent more of the branches in India, and bringing the total number of branches under government control to 84 percent (3).

After nationalization, the breadth and scope of the Indian banking sector expanded at a rate perhaps unmatched by any other country. Indian banking has been remarkably successful at achieving mass participation. Between the time of the 1969 nationalizations and the present, over 58,000 bank branches were opened in India; these new branches, as of March 2003, had mobilized over 9 trillion Rupees in deposits, which represent the overwhelming majority of deposits in Indian banks (5). This rapid expansion is attributable to a policy which required banks to open four branches in unbanked locations for every branch opened in banked locations. Between 1969 and 1980, the number of private branches grew more quickly than public banks, and on April 1, 1980, they accounted for approximately 17.5 percent of bank branches in India. In April of 1980, the government undertook a second round of nationalization, placing under government control the six private banks whose nationwide deposits were above Rs. 2 billion, or a further 8 percent of bank branches, leaving approximately 10 percent of bank branches in private hands. The share of private bank branches stayed fairly constant between 1980 to 2000 (7).

INTRODUCTION OF INDIRA GANDHI:

Indira Gandhi was born Indira Nehru into a Kashmiri Pandit family on 19 November 1917 in Allahabad. Her father, Jawaharlal Nehru, was a leading figure in India's political struggle for independence from British rule, and became the first Prime Minister of the Dominion (and later Republic) of India. She was the only child (a younger brother died young), and grew up with her mother, Kamala Nehru, at the Anand Bhavan, a large family estate in Allahabad. She had a lonely and unhappy childhood. Her father was often away, directing political activities or incarcerated, while her mother was frequently bedridden with illness, and later suffered an early death from tuberculosis. She had limited contact with her father, mostly through letters

In the 1950s, Indira, now Mrs. Indira Gandhi after her marriage, served her father unofficially as a personal assistant during his tenure as the first prime minister of India. Towards the end of the 1950s, Gandhi served as the President of the Congress. In that capacity, she was instrumental in getting the Communist led Kerala State Government dismissed in 1959. That government had the distinction of being India's first-ever elected Communist Government. After her father's death in 1964 she was appointed a member of the Rajya Sabha (upper house) and served in Prime Minister Lal Bahadur Shastri's cabinet as Minister of Information and Broadcasting. In January 1966, after Shastri's death, the Congress legislative party elected her over Morarji Desai as their leader. Congress party veteran K. Kamaraj was instrumental in Gandhi achieving victory. Because she was a woman, other political leaders in India saw Gandhi as weak and hoped to use her as a puppet once elected.

NATIONALISATION IN 1969 AND 1980:

Despite the provisions, control and regulations of the Reserve Bank of India, banks in India except the State Bank of India (SBI), remain owned and operated by private persons. By the 1960s, the Indian banking industry had become an important tool to facilitate the development of the Indian economy. At the same time, it had emerged as a large employer, and a debate had ensued about the nationalization of the banking industry (4). Indira Gandhi, the then Prime Minister of India, expressed the intention of the Government of India in the annual conference of the All India Congress Meeting in a paper entitled Stray thoughts on Bank Nationalization

Thereafter, the Government of India under the leadership of Smt. Indira Gandhi issued the Banking Companies (Acquisition and Transfer of Undertakings) Ordinance, 1969 and nationalized the 14 largest commercial banks with effect from the midnight of 19 July 1969. These banks contained 85 percent of bank deposits in the country. Within two weeks of the issue of the ordinance, the Parliament passed the Banking Companies (Acquisition and Transfer of Undertaking) Bill, and it received presidential approval on 9 August 1969 (6).

The following banks were nationalized in 1969:

- Allahabad Bank (now Indian Bank)
- Bank of Baroda

- Bank of India
- Bank of Maharashtra
- Central Bank of India
- Canara Bank
- Dena Bank (now Bank of Baroda)
- Indian Bank
- Indian Overseas Bank
- Punjab National Bank
- Syndicate Bank (now Canara Bank)
- UCO Bank
- Union Bank of India
- United Bank of India(now Punjab National Bank)

A second round of nationalizations of six more commercial banks followed in 1980. The stated reason for the nationalization was to give the government more control of credit delivery. With the second round of nationalizations, the Government of India controlled around 91% of the banking business of India (7).

The following banks were nationalized in 1980:

- Punjab and Sind Bank
- Vijaya Bank (Now Bank of Baroda)
- Oriental Bank of India (now Punjab National Bank)
- Corporation Bank (now Union Bank of India)
- Andhra Bank (now Union Bank of India)

ARGUMENTS FOR NATIONALISATION

Though it was a good, bold and dare devil steps taken by Indian Government, there were some arguments (5). Some of them are discussed here in next few lines.

1. NATURAL MONOPOLY

Many key industries nationalised were natural monopolies. This means the most efficient number of firms in the industry is one. This is because fixed costs are so high in creating a network of water pipes, there is no sense in having any competition (fig.1). A private natural monopoly could easily exploit its monopoly power and set higher prices to consumers. Government ownership of a natural monopoly prevents this exploitation of monopoly power.

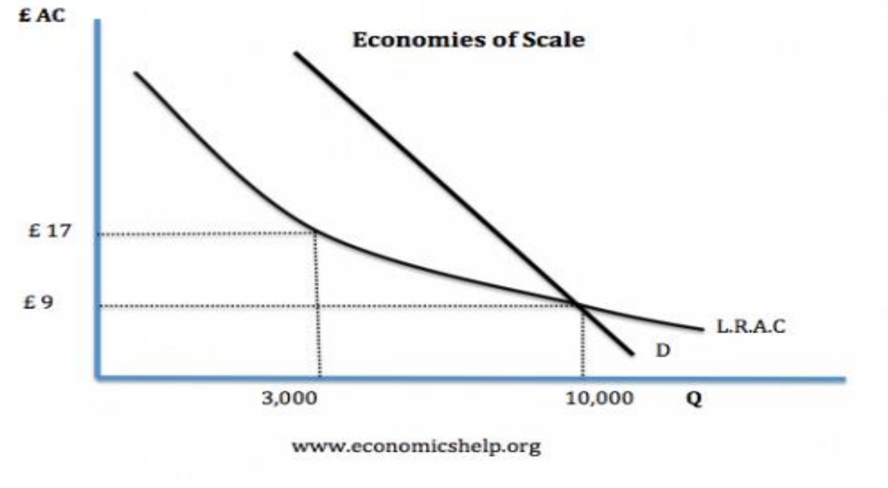

Fig.1 Economy of sale

If industry demand is 10,000 – then the most efficient number of firms is one.

2. PROFIT SHARED WITH TAXPAYER

If Virgin Trains set high ticket prices, you know the profit margin will go to a small number of wealthy shareholders. If the same service was run by a nationalised British Rail, any profit from profitable train services would go to government revenues and enable lower tax rates.

2. EXTERNALITIES

Some of the nationalised industries had significant positive externalities. For example, public transport plays a key role in reducing pollution and congestion. A private firm would ignore the positive externalities, but a government run public transport system could invest in public transport to help improve the economic infrastructure.

3. WELFARE ISSUES

Some industries play a key role in the welfare of consumers and citizens. For example, gas and water could be considered necessities for basic living standards and not luxuries. Government provision means that needy groups can be looked after and provided with basic necessities.

4. INDUSTRIAL RELATIONS

Labour unions often favour nationalisation because they feel they may be better treated by the government – rather than a profit maximising monopoly.

5. GOVERNMENT INVESTMENT

Some industries require long-term investment to improve services over time. This long-term investment may not be profitable in the short-term, so without government intervention, they may suffer from lack of long-term investment.

6. FREE MARKET FAILURE

With train franchises, two private train franchise of East Coast Mainline has failed, with the government having to step in. The third franchise Stagecoach/Virgin has also admitted difficulties, stating it overpaid for the franchise. When the government managed the service, the company made a decent profit – showing that nationalised industries can be successful in running profitable services.

7. SAVED BANKING SYSTEM

Two large banks would have gone bankrupt (Lloyds, Royal Bank of Scotland) without government intervention. Since the crisis, the government has owned shares in these two banks – showing that government ownership can provide greater stability than free-market forces.

EVALUATION OF BENEFITS OF NATIONALISATION:

- Ownership is only one factor. Shifting ownership from the private sector to the public sector is only one factor in whether it will be successful. It also depends on how the nationalised firm is managed. For example, is it possible to give workers in nationalised industries effective incentives to work hard, increase productivity and increase efficiency? This would combine the best of both worlds (7)
- Do workers feel a sense of ownership with nationalised industries? In the 1930s, workers in the Soviet Union were genuinely enthused by the "Soviet System' (with high degrees of political repression) and output rose faster than capitalist economies. But, by 1960s and 70s, workers in the Communist Soviet Union were completely demoralised. The joke went amongst Soviet workers "They pretend to employ us, we pretend to work (6).
- Does nationalisation mean increased centralisation to committee's in Westminster or can effective control be delegated to local bodies that have a closer relationship with industries?
- In the UK coal mining industry, the initial enthusiasm for nationalisation wore off because the industry faced serious challenges – declining demand, increased in-competitiveness and desire for coal mines. Also, are the funds for investing in nationalised industries there?
- It depends on the industry.

CONCLUSION

The main motive for nationalisation during the post-war period was to ensure a co-ordinated approach to production and supply to ensure economic survival and efficiency in the face of war, and post-war reconstruction. For example, the advantage of a nationalised rail network, as with other natural monopolies, was that central planning could help create a more organised and co-ordinated service. Banking sector is the backbone of country's economy and for India Smt. Indira Gandhi did a lot for the improvement in the said sector.

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