OPENING UP OF THE BANKING SECTOR TO PRIVATE PLAYERSIN 1993 AND 2003 WITH SPECIAL EMPHASIS ON THE NEW BANK LICENSES OF 2014.

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Abstract

The Reserve Bank of India has been pondering over the objective of 'Financial Inclusion' since its inception. Financial Inclusion is defined by the RBI as "the process of ensuring access to financial services and timely and adequate credit where needed by vulnerable groups such as the weaker sections and low income groups at an affordable cost from mainstream financial institutions." For this objective, RBI considered the idea ofbanks' nationalization in 1969. But, since this objective remained under-fulfilled even after two decades of nationalization, RBI considered granting licenses to the private players in the early 1990s.This paper highlights the problems of nationalization, grounds on which the banking sector was liberalized in the early 1990s and early 2000s with special emphasis onthe new bank licenses of 2014& reasons why RBI has chosen private sector banks for its objective of financial inclusion.

Key Words:financial inclusion, nationalization, monetization, non-performing assets

Introduction

In the early decades of 19^{th} century, the banking sector of India was dominated by the private sector. All banks were in the hands of private giants except the State Bank of India. In this phase, major problems were faced by the Indian economy. Indians had established many small banks, most of which served particular ethnic and religious communities. The exchange banks, mostly owned by Europeans, concentrated on financing foreign trade. Indian joint stock banks were generally under-capitalized and lacked the experience and maturity to compete with the presidency and exchange banks. Due to these factors, a debate had ensued about the nationalization of the banking industry in the 1960s.

In theory, nationalization means that the government becomes majority shareholder in the banks meaning thereby that the government can pick board of directors of its choice. It implies that the bank takes decisions to suit government's Five year plan requirements.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."* The meeting received the paper with enthusiasm.An important rationale for the Indian bank nationalizations was to direct credit towards sectors the government thought were underserved, including small scale industry as well as agriculture and backward areas.

For this purpose, 14 banks were nationalized in 1969 and 6 banks were taken into govt. possession in 1980. Ownership was not the only means of directing credit: the Reserve Bank of India issued guidelines in 1974, indicating that both public and private sector banks must provide at least one-third of their aggregate advances to the priority sector by March 1979. In 1980, it was announced that this quota would be increased to 40 percent by March 1985. Sub-targets were also specified for lending to agriculture and weaker sectors within the priority sector.

The nationalization phase also faced many problems, because of which the government of India embarked upon the concept of liberalization of banks in the early 1990s, which are explained below:

Problems of Nationalization

The Indian financial system of the pre-reform period essentially catered to the needs of planned development in a mixed-economy framework where the Government sector had a predominant role in economic activity. As part of planned development, the macroeconomic policy in India moved from fiscal neutrality to fiscal activism (Reddy 2000). Such activism meant large developmental expenditures, much of it to finance long-gestation projects requiring long-term finance. The sovereign was also expected to raise funds at fine rates, and understandably at below the market rates for private sector.

In order to facilitate the large borrowing requirements of the Government, interest rates on government securities were artificially pegged at low levels, which were unrelated to market conditions. The government securities market, as a result, lost its depth.

The provision of fiscal accommodation through *ad hoc* treasury bills (issued on tap at 4.6 per cent) led to high levels of monetization of fiscal deficit during the major part of the eighties. In order to check the monetary effects of such large-scale monetization, the cash reserve ratio (CRR) was increased frequently to control liquidity.

By the end of the eighties, the financial system was considerably stretched. The directed and concessional availability of bank credit with respect to certain sectors resulted not only in distorting the interest rate mechanism, but also adversely affected the viability and profitability of banks. The lack of recognition of the importance of transparency, accountability and prudential norms in the operations of the banking system led also to a rising burden of non-performing assets.

In reality, nationalization created more problems than it solved. Some more problems of the nationalization phase were as follows:

1. Almost all the board members were politicians, retired bureaucrats and their relatives.This led to sycophancy instead of professionalism.
2. Banks were forced to give loans at throwaway prices to farmers/small enterprises. Sometimes even the cost of giving loans (i.e. staff salary, electricitybill, office rent etc.) was higher than the profit involved.
3. Local politicians interfered in operations. They would get lakhs of rupees @4% interest rate and then circulate the same money to farmers @36% interest rate.
4. RBI kept the CRR and SLR very high (15 & 38.5% respectively in 1991). This resulted in very less money left for banks to lend.
5. Businessmen could not get easy loans, therefore no business expansion could happen and as a result exports declined.

Narasimham Committee I (1991)

All the problems mentioned above contributed to the Balance of Payment (BoP) crisis in 1991.The Government of India adopted a policy of economic liberalization. Therefore, the economic and banking policies were to be reversed to suit the requirements of a liberalized economy. The banking sector reforms became inevitable to accelerate the pace of reforms to usher in a vibrant and competitive economy. An expert Committee under the Chairmanship of Sh. M. Narasimham (a former Governor of RBI) was set up for spearheading the financial sector reforms in India. The Narasimham Committee (*Committee on Financial Sector Reforms 1991*) inter alia, recommended opening up of the banking sector to the private entrepreneurs to bring in competition and efficiency, thereby paving the way for licensing of new commercial banks in the private sector.

Bank Licenses: 1st Round (1993)

Economic conditions during 1993 and 1994 demanded new banking licenses. Economic liberalization was underway, and the role of banks and other financial sector intermediaries was becoming prominent. Due to the problems faced in the nationalization phase mentioned earlier, the govt. had no other option than inviting the private sector to set up banks and take stake-holding in the public sector banks at the same time. Prior to liberalization, the PSBs held 91% of the total bank branches and accounted for85% of the total banking business in the country.

Banking sector reforms essentially consisted of a two-pronged approach. While nudging the Indian banking system to better health through the introduction of international best practices in prudential regulation and supervision early in the reform cycle, the idea was to increase competition in the system gradually.Special emphasis was placed on building up the risk management capabilities of the Indian banks. Measures were also initiated to ensure flexibility, operational autonomy and competition in the banking sector.

- In 1993, RBI invited applications for the new bank licenses.
- Total ten private banks were given licenses: 6 still running + 4 closed down.
- New private banks started operations in 1994-95.

6 running

1. Industrial Credit and Investment Corporation of India (ICICI)
2. Housing Development Finance Corporation (HDFC)
3. Unit Trust of India (UTI)- became Axis bank in 2007
4. Industrial Development Bank of India (IDBI)
5. Indus Bank
6. Development Credit Bank (DCB)

All of the above banks are running successfully giving the impression that not all private entities are reprehensible. In fact, ICICI, HDFC and Axis banks are the top banks of India. They have their presences abroad and employ lakhs of people.

4 closed down

Bank	**Merged with**
Global Trust Bank	Oriental Bank of Commerce
Bank of Punjab	Centurion bank
Centurion bank	HDFC
Times Bank	HDFC

These four banks give us the arguments against the private banks. Because they can also close down like these four, panic may arise among the clients and this may lead to the general public's loss of confidence in the whole banking system.

Some measures taken by the RBI:

- As per Basle Committee norms, the RBI introduced capital adequacy norms. It wasprescribed that banks should achieve a minimum of 4 per cent capitaladequacy ratio in relation to risk weighted assets by March 1993, of whichTier I capital should not be less than 2 per cent. The BIS standard of 8 percent should be achieved over a period of three years, that is, by March 1996.

- Since 1969, none bank had been allowed to be opened in India. That policychanged in January 1 1993 when the RBI announced guidelines for openingof private sector banks public limited companies. The criteria for setting up ofnew banks in private sector were: (a) capital of Rs. 100 crore, (b) mostmodern technologic, and (c) head office at a non-metropolitan centre, InJanuary 2001, paid-up capital of these banks was increased to Rs. 200 crorewhich has to be raised to Rs. 300 crore within a period of 3 years after thecommencement of business. The promoters share in a bank shall not be lessthan 40 per cent.

- The Banking Companies (Acquisition and Transfer of Undertaking) Actwas amended with effect from July 1994 permitting public sector banks toraise capital up to 49 per cent from the public.

Narasimham Committee II (1998)

The Narasimham-II Committee was tasked with the progress review of the implementation of the banking reforms since 1992 with the aim of further strengthening the financial institutions of India. It focused on issues like size of banks and capital adequacy ratio among other things. M. Narasimham, Chairman, submitted the report of the *Committee on Banking Sector Reforms (Committee-II)* to the Finance MinisterYashwantSinha in April 1998.

It was observed that the new private sector banks along with the public sector banks have lagged behind in their objective of financial inclusion. To achieve this objective,the need for new banks in the system was felt.

New Bank Licenses: 2nd Round (2003)

In 2001, the applications were invited for granting licenses to the private sector. Though the performance of the New Generation Private Sector Banks was quite satisfactory, the episode of Global Trust Bank had sent alarming signs to the banking industry, thus, making the regulator cautious and judicious while allowing licenses to new players. In the above backdrop, RBI granted licenses to only two strongest contenders:

1. Kotak Mahindra, and
2. Yes Bank

In 2003-04, the winners launched banks and started operations.

Evaluating the impacts of two-phased liberalization(i.e.1993 and 2003)

Due to the liberalization of banks, the Indian economy has seen a remarkable increment in the various financial performance indicators such as savings rate, investment rate, return on assets etc. It is explained in the following table:

Financial Performance Indicators	1990-91 (pre-reform)	2007-08 (post-reform, preceding global crisis)	2011-12
Gross Domestic Saving Rate (% of GDP)	22.9	36.8	30.8
Gross Domestic Investment Rate (% of GDP)	26.0	38.1	35.0
Bank Credit / GDP (%)	20.4	47.4	50.60
Broad Money / GDP (%)	46.7	82.9	83.21
Spread (return on funds-cost of funds)		2.9	3.62
Net Interest Income To Total Assets (%)	1.95	3.0	2.9
Return On Assets (%)		1.13	1.08
BSE Market Capitalization (% of GDP)	16	103	70.2
Primary Market Resource Mobilization (Rs. Billion)	43.1	636.4	3087.5

Source: Speaking notes of Dr. DuvvuriSubbarao, Governor, RBI, at the FICCI-IBA Annual Banking Conference in Mumbai on August 13, 2013.

It is evident from the table that ever since the new private sector banks were introduced, the Indian economy has seen a considerable improvement in the economic and financialparameters.

New Bank licenses: 3rd Round (2014)

Need for New Banks

'Financial Inclusion' has been the RBI's core area of focus in the recent years. To achieve this objective, RBI has taken certain measures from time to time such as Financial Inclusion Plan,SwabhimaanCampaign,Financial Literacy Centers etc.

A snapshot of the progress made by the banksundervariousinitiativesitself speaks of the journey travelled so far:-

i. Banking outlets in villages have increased to nearly 2, 68,000 from 67,694 outlets in March 2010.
ii. About 7,400 rural branches have been opened during this 3-year period compared with a reduction of about 1300 rural branches during the last two decades.
iii. Nearly 109 million Basic Savings Bank Deposits Accounts (BSBDAs) have been added, taking the total no. of BSBDA to 182 million. The share of ICT-basedaccounts has increased substantially. The percentage of ICT accounts to total BSBDAs increased from 25% in March 2010 to 45% in March 2013.

About 490 million transactions have been carried out in ICT-based accounts through BCs during 2010-13. The no. of transactions through ICT-based BC outlets, though increasing, is still very low when compared with the manifold increase in the no. of banking outlets and no. of accounts. Due to the less than optimal performance of the various plans (explained below), RBI felt the need for new banking licenses in 2013.

- Despite the progress made over the years since nationalization of banks in 1969, the problem of financial exclusion is staggering. According to the findings of World Bank Global Findex Survey (2012), only 35 per cent of Indian adults had access to formal bank account and just 8 per cent borrowed formally in the last 12 months.

- As per Report on "Trend and Progress of Banking in India 2010-11" and "Mid-Year Economic Analysis 2012-13", metropolitan regions and semi-urban areas enjoyed 68% and 9% of total credit respectively while rural areas accounted for only 6% of credit.
- Banking service as such remains slanted in favor of the metropolis and cities as Greater Mumbai, Delhi, Chennai, Kolkata, Bangalore and Hyderabad together accounted for 46% of total deposits and 56% of total credit in 2010-11.
- The Government of India has adopted financial inclusion as a state policy. In order to achieve this objective, not only more number of branches but also some more new banks are necessary.

Some More Facts:

- According to Rural Finance Access Survey (2003), 59% of the population does not have a deposit account and 79% do not have access to formal credit source. Rural banking service again is tilted towards the rich as it is found that 70% of the marginal farmers do not have a bank account and 87% do not have any access to formal credit.
- As per the address of Deputy Governor of RBI, K. C. Chakrabarty on 27/11/2010, of the 6 lakh Indian villages, approximately 50,000 had access to bank finance thus leaving 145 million households untouched to banking.

Why a Bank-led Model

The most important of many questions is that why RBI has chosen a bank-led model to cater to the financing needs of the masses. There are three reasons inter alia, firstly bank deposits are guaranteed by the Deposit Insurance Guarantee Corporation and the depositor's money remains safe and secure. Secondly, Banks are regulated and well capitalized institutions subject to RBI's direct control exercised through the processes of onsite and offsite inspections and supervision. Regulation is aimed at protecting depositors' interests, orderly development and conduct of banking operations and fostering the overall health of the banking system. Thirdly we have a robust widespread banking system unlike several other countries. For these countries where the banking brick and mortar network is not present the only way forward is to leverage technology. It is simpler to build digital gateways across Africa while for us we use the banking system because it is there as we have penetrative outreach through Commercial Banks.

Why Private Sector Banks

The performance of the private sector banks since early 1990s has shown that the decision of the govt. to liberalize the banking sector was a turning point. Although the public sector banks continue to dominate the banking system with 73% of market share of assets and 83% of branches, the private sector banks have outperformed the PSBs in terms of market share of assets relative to the percentage share of number of branches.

Type of Banks	Number of Banks	Number of Branches	Percentage Share of Number of Branches	Market Share of Assets (Percentage)
Public Sector	26	67,466	83.0	72.8
Private Sector	20	13,452	**16.6**	**20.2**
Foreign Banks	41	323	0.4	7.0
Total	**87**	**81,241**	**100.0**	**100.0**

Source: Speaking notes of Dr. DuvvuriSubbarao, Governor, RBI, at the FICCI-IBA Annual Banking Conference in Mumbai on August 13, 2013.

It is evident from the above table that the private sector banks have a 16.6% share of no. of branches but controls 20.2% market share of assets.
The Private Sector Banks have also outperformed the PSBs in terms of Operating Expenses to Total Assets Ratio and Spread to Total Assets Ratio.

Bank Group	1996-97	2001-02	2002-03
Operating Expenses/Total Assets			
Scheduled commercial banks	2.9	2.2	2.2
Public sector banks	2.9	2.3	2.3
New private sector banks	1.9	1.1	2.0
Spread/Total Assets			
Scheduled commercial banks	3.2	2.6	2.8
Public sector banks	3.2	2.7	2.9
New private sector banks	2.9	1.2	1.7

Note: Spread= interest income-interest expenditure.
Source: Reserve Bank of India.

Some arguments against private sector banks and their counter-arguments:

- The critics argue that the government should launch some Rajiv Gandhi scheme to open bank accounts for everyone; there is no need to get new private banks. Besides, these two (Bandhan and IDFC) are too small to be any relevant in “financial inclusion”. This does not hold true as throwing public money, subsidies and schemes to solve every problem is a bad idea. Business should become vibrant by itself.It is true that both Bandhan and IDFC are “mosquitoes” compared to elephants like SBI and ICICI but every maestro was an amateur someday.
- It has been argued that in the first round, ten banks were given licenses; four of them were closed down. Private sector cannot compete with existing giants. They try to take ‘shortcuts’, hence all the scams happen. It has been countered by the view thatthe same licensing round gave us giants like ICICI, Axis bank and HDFC. It is wrong to assume that every private player is out there only to bully, loot and steal.
- Some argue to the RBI that as per its own table, Bandhan already has 45% of its branches in rural areas as Microfinance Company, then why do they need a banking license? They’re already doing financial inclusion. It is countered by the fact that As a Microfinance Company, Bandhan cannot open savings account / current account etc. As a result, such microfinance companies have to borrow money from other banks like NABARD etc @12-15% interest rate. But if the same Microfinance Company was given a banking license, it can accept public’s deposit money under savings account at 4% interest rate and fixed deposit at 9% interest rate and thus, can give loans to poor at reasonable rates like 10-15%.

- Regarding Bandhan and IDFC, it is argued that these two small players cannot even afford to launch all India ATM network, forget about opening "branch" offices. This does not hold true asthey donot need to open ATMs anyways, because of the "White label" ATM Scheme*
- One more argument is that the public sector banks are already bleeding because of the heavy marketing and teaser rates offered by the private banks. Two more such banks will increase the misery of the public sector banks. The counter-argument is that in the end, business is all about the survival of the fittest. Public sector banks and their trade unions should learn to perform or perish. Customers deserve better services. Just to make life easier for public sector, we must not prevent the entry of private sector.

***White Label ATM (WLA) Scheme**

A White Label ATM is similar to a normal bank ATM but is not owned by a bank, instead by a private ATM service provider. Customers can withdraw or deposit money, change pin and even withdraw mini statements from these ATMs. For consumers, similar to other ATMs, the first five transactions are free even at these WLAs. In a bid to grow the distribution network while keeping costs under check, smaller private sector banks are looking at reducing the dependence on their own automated teller machines (ATMs) and instead relying on white-label ATM (WLA) network.

Objectives of New Bank Licenses

In the past, the apex bank's stated objective behind giving licenses to new banks had been to introduce competition in the banking sector, largely dominated by government-owned banks. This time, its objective is financing higher growth, providing specialized financial services, increasing competition in the sector and bringing about greater financial inclusion in India- a country of 1.2 billion people- where around half of households remain untouched to the banking system.

RBI's intent can be broadly attributed to three objectives:

i. **Financial inclusion** — Providing affordable banking services to the lowest strata of the population is one of the primary goals. RBI has mandated that commercial banks achieve financial inclusion by offering "no-frills" savings-bank accounts and easy access to credit facilities through general-purpose credit cards (GCCs). KYC (Know Your Customer) norms have also been relaxed to achieve greater financial inclusion. Additionally, CRISIL Inclusix provides a comprehensive index for measuring financial inclusion in the country. CRISIL Inclusix measures financial inclusion on three parameters: branch penetration, deposit penetration and credit penetration.
According to CRISIL Inclusix, financial inclusion has improved from 2009 (score of 35.4) to 2011 (score of 40.1) but is still low, and reflects under-penetration of banking services in the country. To rectify this situation, RBI has mandated that new banks would have to open at least 25% of their branches in unbanked rural areas. This would result in:

ii. **A wider reach of financial services** — For banking to be truly inclusive, banking and financial services must reach a large section of the general population. Consumers can then benefit from access to a wide variety of banking products and services; banks win by bringing more people into the banking fold, which reduces the cost of offering such services.

iii. **Rural banking** — Penetration of banking services in rural areas is RBI's third objective regarding issuing new banking licenses. During 1993 and 1994, new banks were obligated to open branches in rural areas; between 2003 and 2004 they were required to have 25% of

their branches in rural and semi-urban centers. This time around, RBI has specified that new banks must set up 25% of their branches in unbanked rural centers (having a population of up to 9,999). This guideline emphasizes RBI's focus on rural banking.
Out of a total of 102,343 branches of scheduled commercial banks in India (as of March 31, 2013), 37,953 (37%) are located in rural areas. Of these, private sector banks account for just 1,937 branches (only 5.1%).
Clearly, private sector banks have lagged behind in terms of providing banking services to ruralareas. By issuing guidelines for setting up branches in those parts of the country, RBI hopes to correct this situation.

- In 2010, Finance Minister observed that there was a need to give more licenses.
- In 2013, February, RBI invited applications with the following guidelines:

Major Guidelines

(A) Eligible Promoters

(i) Entities / groups in the private sector that are 'owned and controlled by residents' [defined as per in FEMA Regulations] and entities in public sector shall be eligible to promote a bank through a wholly-owned Non-Operative Financial Holding Company (NOFHC).

(ii) Promoters / Promoter Groups with an existing non-banking financial company (NBFC) will be eligible to apply for a bank license.

(B) 'Fit and Proper' criteria

Promoters/ Promoter Groups as defined in these guidelines should be 'fit and proper' in order to be eligible to promote banks through a wholly owned NOFHC. RBI would assess the 'fit and proper' status of the applicants on the basis of following criteria:

(a) Promoters/ Promoter Groups should have a past record of sound credentials and integrity;

(b) Promoters/ Promoter Groups should be financially sound and have a successful track record of running their business for at least 10 years.

(C) Minimum voting equity capital requirements for banks and shareholding by NOFHC

(i) The initial minimum paid-up voting equity capital for a bank shall be Rs.5 billion.

(ii) The NOFHC shall hold a minimum of 40 per cent of the paid-up voting equity capital of the bank which shall be locked in for a period of five years from the date of commencement of business of the bank.

(iii) The shareholding by NOFHC shall be brought down to 20 per cent of the paid-up voting equity capital of the bank within a period of 10 years, and to 15 per cent within 12 years from the date of commencement of business of the bank.

The bank shall be required to maintain a minimum capital adequacy ratio of 13 per cent of its risk weighted assets (RWA) for a minimum period of 3 years after the commencement of its operations subject to any higher percentage as may be prescribed by RBI from time to time.

(iv) The bank shall get its shares listed on the stock exchanges within three years of the commencement of business by the bank.

(F) Foreign shareholding in the bank

The aggregate non-resident shareholding from FDI, NRIs and FIIs in the new private sector banks shall not exceed 49 per cent of the paid-up voting equity capital for the first 5 years from the date of licensing of the bank.

(G) Corporate governance of NOFHC

(i) No NOFHC shall have as a Director in its Board of Directors, any person who is a Director in any other NOFHC or a bank other than a banking company under it.

(ii) No NOFHC shall be managed by any person-

(a) Who is a Director in any other company not being

- a subsidiary of the NOFHC or
- a company registered under Section 25 of the Companies Act, 1956 (1 of 1956) or

(b) Who is engaged in any other business or vocation.

(iii) At least 50 per cent of the Directors of NOFHC shall be totally independent of the Promoter or Promoter Group entities and their major customers and major suppliers.

(iv) Ownership and management shall be separate and distinct in the NOFHC, the banks and entities regulated by RBI.

(J) Business Plan for the bank

Applicants for new bank licenses will be required to furnish their business plans for the banks along with their applications. The business plan will have to address how the bank proposes to achieve financial inclusion.

(K) Other conditions for the bank

(i) The Board of the bank should have a majority of independent Directors.

(ii) Any acquisition of shares which will take the aggregate holding of an individual / entity / group to the equivalent of 5 per cent or more of the paid-up voting equity capital of the bank, will require prior approval of RBI.

(iii) The bank shall open at least 25 per cent of its branches in unbanked rural areas (population up to 9,999 as per the latest census) to avoid over-concentration of their branches in metropolitan areas.

RBI will consider allowing the bank to take over and convert the existing NBFC branches into bank branches only in the Tier 2 to 6 centers. Existing branches of the NBFC in Tier 1 centers may be allowed to convert into bank branches only with the prior approval of RBI.

Source: RBI Website

Who are the major applicants?

The list of various applicants includes corporate houses such asAditya Birla Nuvo Ltd. And Reliance Capital Ltd; financial intermediaries like Edelweiss Financial Services Ltd, IFCI Ltd, Indiabulls Housing Finance Ltd, India Infoline Ltd, JM Financial Ltd, Magma Fincorp Ltd, Muthoot Finance Ltd, Religare Enterprises Ltd, Shriram Capital Ltd and SREI Infrastructure Finance Ltd; microfinance institutions like Janalakshmi Financial Services Pvt. Ltd; and public sector undertaking like Tourism Finance Corp. of India Ltd. The Tatas opted out.

BimalJalan Committee

- Now,RBI had to decide winners among those 25 applicants.
- Sep 2013: RBI sets up RBI High Level Advisory Committee to process those applications.

Chairman	**BimalJalan**	Former RBI Governor
Members	**UshaThorat**	Ex-RBI Deputy Governor
	C B Bhave	Ex-Sebi Chairman
	NachiketMor	RBI board member

On 2nd April, 2014, RBI announced two winners:

1. **Bandhan Microfinance, and**
2. **IDFC**

According to RBI's Deputy Governor, K.C Chakrabarty, RBI favored NBFCs over banking institutionsas they have good customer base and they can convert themselves into banks easily.

Moreover, YashwantSinha led Parliamentary Standing Committee on Finance had strongly argued against granting licenses to the corporate houses. Stating that industrial houses may not be geared to achieve the national objective of financial inclusion, it has recommended that banking and industry be kept separate.

1. **Bandhan Microfinance**

   Bandhan Microfinance, situated in West Bengal, was established in 2000.It started its operations in 2002. Chandra ShekharGhosh is the chairman and managing director of Bandhan Microfinance. Its asset size is Rs. 6200 cr. and capital base is Rs. 1100 cr. It has 13000 employees and provides benefits to around 54 lakh borrowers. It has 2016 branches in 22 states out of which 45% are in rural areas. It is the largest micro finance intuition in India with 22% market share. Now it would address all the four dimensions of financial inclusion i.e. savings, credit, insurance and remittances. Currently it is catering only to the credit side. Bandhan Microfinance is the first microfinance firm to get a baking license.

2. **IDFC**

Infrastructure Development and Financial Corporation (IDFC), situated in Mumbai, Maharashtra, was established in 1997.Rajiv Lal is the managing director and chairman of IDFC. It registered itself with RBI as NBFC in 1998. In 1999, it was notified as Public Financial Institution. In 2000, it got registered with SEBI as merchant banker and as an underwriter. In 2005, it got listed on BSE and NSE. It deals in project finance, corporate finance, asset mgt., mutual fund, investment banking and advisory services for infra projects. Its net worth is Rs. 21000 cr. but its rural presence is quite low.

These two are given only **"in-principle"** approval.

In principle approval

The two winners were required to fulfill the following conditions:

Within 18 months

- Must get net worth of Rs.1000 crore.
- Must open 25% branches in unbanked rural areas.

Once they fulfill the above conditions, RBI will give them license under the Banking Regulation Act, 1949 [Sec.22 (1)].

RBI has also prohibited the promoters (Ghosh and Lall) to hold CEO position in their respective banks. This is meant to prevent conflict of interest. Because in past, Global Trust bank's CEO Ramesh Gelli was accused of involved in Ketan Parekh scam.

Curiously though Yes Bank's promoter RanaKapoor enjoys both MD and CEO position in his bank.

India post

- RBI did not consider Post Bank of India (PBI) application as it did not have mandatory clearance from the government.
- For Indian postal department, BimalJalan said "RBI should consult separately with government and give license if necessary."
- PBI would use 1.3 lakh post offices as business correspondents. 90% of post offices are in rural areas. These can help in financial inclusion including deposits, loans, insurance, remittances, pensions and govt. subsidies.
- PBI will run on a unique model where just 150 branches would be opened over the next 5 years, these would be linked to 800 head post offices which will be further connected to 25000 sub-post offices and these to 1.3 lakh branch post offices in remote and rural areas.

The Road Ahead

The banking sector reforms, which were implemented as a part of overall economic reforms, witnessed the most effective and impressive changes, resulting in significant improvements within a short span. The Indian financial system has made impressive strides in resource mobilization, geographical and functional reach, financial viability, profitability and competitiveness since nationalization of banks in 1969 and liberalization of economic policies since early 1990s.

India's banking sector has the potential to become the fifth largest banking sector globally by 2020 and the third largest by 2025. The industry has witnessed discernable development, with deposits growing at a CAGR of 21.2 per cent (in terms of INR) in the period FY 06–13; in FY 13 total deposits stood at US$ 1,274.3 billion.

From now on, issuance of banking license will not be a once-in-a-decade affair. RBI will fine-tune the guidelines and licenses will be given on tap. There will also be differentiated licensing for entities such as Payment Banks, which are very different from Universal Banks.

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