A Bird Eye View on Growth of Foreign Banks in India

T. VINILA

Assistant Professor of Commerce
Smt N.P. Savitramma Govt College (w) Chittoor.
& Research Scholar of Andhra University,
Visakhapatnam.
Ph.No: 8897799816

Abstract

The foreign banks are known as Exchange Banks and are those which have their head offices outside India. Foreign banks of real multinational character on Indian scene in the first quarter of Twentieth century. Four banks namely (1) The Mercantile Bank Ltd., (2) Grindlays Bank Ltd. (3) The Chartered Bank and (4) The Hong Kong and Shanghai Banking Corporation were established in 1914. The Mercantile Bank Ltd. and the Hong Kong and Shanghai Banking Corporation were registered in Hong Kong whereas Grindlays Bank Ltd. and the Chartered Bank were registered in London. Two more banks, namely the American Express International Banking Corporation and the Algemene Bank of Nederlands N.V. were established in 1920, the former was registered in United State of America and the latter in Netherlands.

Over a period, the Foreign Banks (FBs) have become an important internal module of the Indian Financial and Banking System. In the context of emerging financial and banking scenario of openness, economic liberalization and globalization and promotion of greater economic efficiency, the need for an expanded role and operation of foreign banks has gained further momentum in India. The policy framework of RBI in the form of a declaration of the Road Map for foreign banks in India in 2008 testified this further.

Key words: Foreign Banks, Indian central banking

Introduction:

Foreign Banks in India have been operating for more than a century and a half. Under the colonial rule, the British took the lead in establishing Foreign Banks in India. There were attempts to establish Foreign Banks as early as 1836. For instance, “the Bank of India”, to be headquartered in London, with branches spread across India. The next attempt was in 1840, to setup “The Bank of Asia”. These initiatives were however, scuttled by the agency houses and the East India Company with an apprehension, that such development might affect their business adversely, as most of the banking and other functions relating to remittance, discounting of foreign bills, etc., were the virtual monopoly of these agencies. The “Oriental Banking Corporation” was the first Anglo-Indian Commercial bank to be set up in 1842 at Bombay with a Royal charter. The Bank, however, shifted its Head Office to London within three years. This was followed by the opening up of “The Chartered Bank of India, Australia and China” and “the Chartered Bank of Asia” in 1853.

Through British initiated the process of setting up banks in India, banks from many other countries, viz., Franch, Germany, Japan, Holland and US actively followed. India offered ample scope for the banking business to flourish with a highly profitability during that time. Panandikan (1966) observed that the profits of banking in India attracted the nationals of a number of countries having important trade relations with India.

Most of the present day foreign banks were originally called as “Exchange Banks” (as the Exchange banks were foreign owned banks and engaged mainly in foreign exchange business in terms of foreign bills of exchange and foreign remittances for travel and trade).

The Indian Central Banking Enquiry Committee Report of 1931 observed that Foreign Banks engaged predominately in the financing of foreign trade and the entire foreign exchange business was a virtual monopoly of these banks. Exchange Banks, invested considerable funds in the discounting of foreign bills during the busy season.

Incidentally, references state that the term “exchange bank” was used even in western countries, mainly referring to those banks that were dealing with the financing of trade of India and China, as these countries did not adhere to the gold standard and their exchange rates were subject to wider fluctuations, Foreign banks also carried out the normal transactions, viz., financing internal trade albeit to a lesser extent, accepting deposits, lending to industry and so on. However there was no trace of these banks financing agriculture and rural activities.

Interestingly even the Indian joint stock banks (1JSBS) played a negligible role in providing agricultural finance. However there is considerable debate and disagreement in the literate regarding reference to all “Foreign Banks” as “exchange banks” as there were also foreign Banks that did not exclusively deal in trade related finance. Though foreign banks played an important role in promoting the foreign exchange business, foreign trade-related financing and bills discount etc, they were always criticized to be more favourable to European traders at the cost of the Indian business interest. For instance, the Indian traders unlike the European businessmen, were required to deposit to per cent to 15 per cent of the valve of the merchandise with foreign banks to open a confirmed letter of credit.

When the country attained independence, Indian banking was entirely in the private sector. The total number of banks in existence then was 1034 an unwidely number, not amenable for closer monitoring and control. They had 4,288 branches mostly in the urban areas. Only some banks, especially in the south were having branches in smaller towns and rural areas.

An addition to the Imperial bank, there were five big banks, each holding public deposits aggregating Rs, 100 crore and more, viz., Central Bank of India Ltd., Punjab National Bank Ltd., Bank of India Ltd., Bank of Baroda Ltd., and United Commercial Bank Ltd., All other Commercial banks were also in the private sector and had a regional character; most of them held deposits of less than Rs 50 crore. Interestingly, the Reserve Bank was also not completely state-owned until it was nationalized in terms of the Reserve Bank of India transfer to Public (ownerships) Act 1948.

---

2 Panandikah, S.G. (1966): Banking in India, Longman Green and company, Delhi
3 Ram , Ramchandra(1930):Present day in Banking in India, University of Calcutta, Calcutta.
6 Ram , Ramchandra(1930):Present day in Banking in India, University of Calcutta, Calcutta
Multilateral Banking originated in the country in the second quarter of Nineteenth century. In the year 1842, the Oriental Banking Corporation established the first Anglo-Indian Commercial Bank at Bombay through a Royal Charter. Within three years of its establishments at Bombay, its Head Office was shifted to London in 1845 to provide a real multinational character. After some time, two other banks appeared on Indian scene, they were (1) The Chartered Bank of India, Australia & China and (2) The Chartered Bank of Asia, later known as Mercantile Bank of India, England & China, which were registered under Royal Charters in England. These banks commenced business in Calcutta in the year 1857. By 1870, only three Multinational Banks operated in India with their depositists of Rs. 52.31 laid’s. The number of banks increased to 8 towards the close of the Nineteenth Century.

Independent India witnessed “Land mark events” in the financial system in general and the banking system in particular, which affected the functioning of Foreign Banks in India both directly and indirectly. Some of the key policy and legislative measures such as the nationalization of the Reserve Bank of India, the passing of the Banking Companies Act, 1949, introduction of five year economic plans, conversion of the Imperial Bank of India into the State Bank of India, takeover of the Princely State Owned Banks and their conversion into subsidiaries of SBI, introduction of deposit insurance, etc., left an indelible mark on the banking scene in India. Among these, the passing of Banking Companies Act, 1949 (Presently Banking Regulation Act) was considered to be the “single most vital legislative initiative”, as this was very instrumental to repaint the whole banking canvas including the position and functioning of the Foreign Banks operating in India during the successive years of free India.

In May 1991 Indian economy faced economic crises in the form of an unprecedented balance of payment problem coupled with high rate of inflation caused by high fiscal defect. To overcome economic crisis, government undertook an extensive economic reforms ushering in an ERA of deregulation, liberalization, privatization and globalization. Along with reforms in the real sector, government also initiation reforms in the financial sector of the Indian an economy. In fact the roadmap of FSRS India can be traced largely by two committees order chairmanship the airmanship of M. Narasimham the committee on financial system and the committee on the banking sector reform popularly known as Narasimham committee I and II Narasimham committee I pointed out that objective of FSRS should be not only to correct the present financial weaknesses but seek to eliminate the causes which have been brought about this situation Narasimham committee defined its approach to ensure that the financial service industry operates on the basis of operational flexibility and financial autonomy with a view to enhancing efficiency productivity and profitability Narasimham committee II was entrusted with the task of evaluating the extent of implementation of reforms recommended by the Narasimham Committee I in 1991 and mandates to that out of the course of future reforms required to further string them the banking Sector in India and to bring the efficiencies of the system up to the international standards.

**Reforms in foreign banks:**

In order to allay the concerns as well as take fullest advantage of foreign banks, RBI has set up a regulatory framework based on recommendation given by Narasimham Committee Report of 1991, Narasimham committee Report of 1998. Narasimham Committee report of 1991 recommended a structural reorganization of the Banking System in India to improve the efficiency of operations.
of banks here was a clear push for the foreign banks as they indicated an improvement in efficiency.

The CFS recommended a liberal approval in permitting foreign banks to open their branches or subsidiaries, as the reserve bank considered appropriate, subject to minimum assign capital and reciprocity. Joint ventures between foreign banks and local banks would also be permitted. The RBI has allowed entry of as branches subject to reciprocity and other prudential considerations are also permitted to invent up to foreign banks finance companies 20.0 per cent as a technical collaborator (with in the overall 40% per cent ceiling) in a new private sector Bank subject to the government approval, provided the foreign bank did not have presence in India. Foreign equity in new Indian private banks also been allowed. Joint ventures between foreign and local banks in non-banking financial services also allowed in accordance with the foreign investment policy. In January 1991, 19 new foreign banks with total of 47 branches were allowed to operate in India.

The post-independence era witnessed banking industry attaining several milestones. The late sixties were marked by fundamental changes in Commercial Banking in India. After nationalization, banks effected several diversifications, modifications and innovations in their structure and functioning. These innovations were with a view to expand and extend the reach and range of commercial banks in accordance with the changing needs of the economy.

A foreign bank is a bank organized under foreign law & located outside the country of its origin. A foreign bank includes offices, branches & agencies of com/banks as trust companies, private banks, national banks, thrift institutions, credit unions, & other organizations chartered under banking laws & supervised by banking supervisors of country of operation. A “foreign bank” does not include any foreign central back as monetary authority that functions as a central bank, as any international financial institution or regional development bank formed by treaty or international agreements. On the basis of purpose to operate, there are two main types of foreign banks – those that come into developing countries primarily to serve thus home cheats, the so called traditional or classical banks, & the opportunist, who come looking for profit opportunities in developing countries. On the basis of channel to operate/ Mode of presence, there are 3 types of foreign banks- first branches, second a wholly owned subsidiary (WOS) of a subsidiary with maximum foreign investment of 74% in a private banks.

Subsidiary Bank is a type of foreign bank that is incorporated in the host country but considered to be owned by a foreign parent bank. The subsidiary bank only needs to operate under the host country’s regulations. Need for the study:

Though a number of studies have focused on the different aspects of foreign banks operations, majority of these studies were conducted during the period prior to 1995. In view of the importance attached to the foreign banks in India by the RBI since late 90’s with its positive approach, there have been pertinent policy developments taken place. As a result there is an imperative need to study the contemporary policies of the Government of India and RBI aiming at the aggressive expansion of FBs’ presence in the present context and its likely implications for the Indian domestic banking system. Objectives of the study:
The objectives of the proposed study are to:

- Present an overview of the genesis and origin of foreign banks in India.
- To examine the trends of foreign banks in India.
- To offer a meaningful and feasible suggestive framework to promote the performance of foreign banks in India.

**Methodology:**
Research methodology is a way to systematically solve the research problem. The study is primarily based on the secondary data. The information is gathered by visiting the premier banking research institutions like Indian Institute of Banking and Finance, Mumbai; National Institute of Bank Management, Pune; Institute of Banking Personnel selection, Mumbai; Bankers Institute of Rural Development, Lucknow; Institute for Development and Research in Banking Technology, Hyderabad; RBI, Mumbai; NABARD, Mumbai; Banking and Insurance Division, Ministry of Finance, Government of India.

**Review of literature:**

Niels Hermes and Robert Lensink (2012) explained the foreign bank presence, domestic bank performance, and financial development. This paper analyses the relationship between foreign bank presence and the performance of the domestic banking sector and takes into account the role of the level of development of the financial sector of the recipient country. We use bank level data of 982 banks in 48 countries for the period 1990-1996. Our results show that in general we find support for the hypothesis that financial development does matter. In particular, we show that foreign bank presence is associated with higher costs and margins of domestic banks at low levels of financial development while it is associated with falling costs and margins of domestic banks at higher levels of financial development.

Ghosh (2012) discusses how foreign banks have an impact on domestic profitability. The paper concludes that foreign banks presence improves profitability and asset quality of domestic banks.

Gaurav Saradha, Namrathaswamy, Charan Singh (2014) further discusses the various opinions towards the foreign bank operations in the host country, with India as the example. The paper looks at the regulatory framework in India to understand the attitude of RBI towards foreign banks. It also discusses what several foreign banks feel about the Indian regulatory setup and how these banks have adapted themselves to deal with the changes. To look at the impact of foreign banks the paper analyses various parameters like the rural presence, contribution towards priority sector, technological development and financial ratios like return on asset and equity. Two case studies have been discussed – one, about The Hong Kong and Shanghai Banking Corporation’s (HSBC) journey in India and the other, about BCCI in India. The paper ends by discussing various challenges which are faced by foreign banks when they set-up their shop in the country.

---

7 Niels Hermes is at the Faculty of Management and Organisation of the University of Groningen. Robert Lensink is at the Faculty of Economics, University of Groningen, PO Box 800, 9700 AV Groningen, The Netherlands and external CREDIT fellow, University of Nottingham, United Kingdom.
9 Gaurav Saradha, Namrathaswamy, Charan Singh, [working papers No 451 February, 2014].
Ankush Bhargava, Dr. Manisha Verma (2014) Post Liberalisation Era paved the path for the great reforms in the banking sector; this led to a great deal of efficiency and profitability in the banking institutions. The foreign banking system is diverged and contains tremendous potential to impact the outcome of the Indian banking scenario. The present study thus focuses on ten banks out of the forty three foreign banks on grounds of comparative performance, profitability and growth rate. The study gives suggestive measures for the banks regarding operational inefficiencies. The study also reveals different areas where they can improve their financial performance. The study further put some light on the banks which are professionally managed and able to attract more customers and have grown much faster than other banks in the competition.

**Growth of Foreign Banks**

- The number of foreign banks branches has increased to by March 1999-2000 from 186 to 353. Number of banks has jumped to during the year. There are 43 foreign banks operating in the country as on 31st March, 2014.
- The staff of the foreign banks moved up from 14602 in March 1990 to 2000 to 25468 in 2014.
- The ATMs of the foreign banks moved up in March 1999- 2000 to 179 to 11179.

**Category wise number of employees of foreign banks in India during 1999-2000 to 2013-14**

<table>
<thead>
<tr>
<th>YEAR</th>
<th>OFFICERS</th>
<th>CLERKS</th>
<th>SUB ORDINATES</th>
<th>TOTAL</th>
</tr>
</thead>
<tbody>
<tr>
<td>1999-00</td>
<td>8877</td>
<td>4459</td>
<td>1266</td>
<td>14602</td>
</tr>
<tr>
<td>2000-01</td>
<td>8199</td>
<td>3888</td>
<td>1145</td>
<td>13223</td>
</tr>
<tr>
<td>2001-02</td>
<td>8227</td>
<td>2838</td>
<td>894</td>
<td>11959</td>
</tr>
<tr>
<td>2002-03</td>
<td>9074</td>
<td>2056</td>
<td>655</td>
<td>11785</td>
</tr>
<tr>
<td>2003-04</td>
<td>8754</td>
<td>1914</td>
<td>505</td>
<td>11053</td>
</tr>
<tr>
<td>2004-05</td>
<td>11333</td>
<td>1428</td>
<td>460</td>
<td>13221</td>
</tr>
<tr>
<td>2005-06</td>
<td>14558</td>
<td>1620</td>
<td>618</td>
<td>16796</td>
</tr>
<tr>
<td>2006-07</td>
<td>16902</td>
<td>1637</td>
<td>570</td>
<td>19109</td>
</tr>
<tr>
<td>2007-08</td>
<td>17441</td>
<td>491</td>
<td>295</td>
<td>18227</td>
</tr>
<tr>
<td>2008-09</td>
<td>15321</td>
<td>965</td>
<td>338</td>
<td>16624</td>
</tr>
<tr>
<td>2009-10</td>
<td>19080</td>
<td>1261</td>
<td>466</td>
<td>20807</td>
</tr>
<tr>
<td>2010-11</td>
<td>22207</td>
<td>1543</td>
<td>490</td>
<td>24240</td>
</tr>
<tr>
<td>2011-12</td>
<td>19761</td>
<td>1438</td>
<td>423</td>
<td>21622</td>
</tr>
<tr>
<td>2012-13</td>
<td>19086</td>
<td>1343</td>
<td>407</td>
<td>20836</td>
</tr>
<tr>
<td>2013-14</td>
<td>23,028</td>
<td>1361</td>
<td>420</td>
<td>24809</td>
</tr>
</tbody>
</table>

*Source: RBI: Basic statistics returns of commercial bank, IBA: Performance highlights of foreign banks in India relevant issue*

**Total number of branches of foreign banks and branches in India during the period 1999-2000 to 2013-2014**

<table>
<thead>
<tr>
<th>YEAR</th>
<th>NO. OF BANKS</th>
<th>RURAL</th>
<th>SEMI URBAN</th>
<th>URBAN</th>
<th>METROPOLITEN</th>
<th>TOTAL NO. OF BRANCHES</th>
</tr>
</thead>
</table>

source: 1. Performance highlights of foreign banks in India relevant issues

Conclusions:

- The number of foreign banks is increasing day by day in number.
- The branch licensing policy has been liberalized by roadmap in 2005.
- Foreign banks are mainly concentrated on urban and metropolitan cities.

References: