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Role of Commercial Banks in Economic Development.

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A B S T R A C T

Commercial banks play a vital role in economic development of a country like our India. Banks promote capital formation which is the most important problem of developing a country. Commercial banks are playing an active role to educate rural people and mobilize their daily savings. Commercial banks accepting deposits from general public and use this deposits to other's investment for the purpose of growth of economic in our country.
Economic development in India depends on real factors like internal trading, agricultural sectors, industrial sectors; expansion of foreign trade especially exports, etc. Commercial banks keeping the middle category population in our country in their view started giving advanced credit for purchase of durable consumer items like vehicles, televisions, refrigerators etc.

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Introduction:

Commercial banks are considered not merely as dealers in money but also the leaders in economic development. They are not only the store houses of the country's wealth but also the reservoirs of resources necessary for economic development. They play an important role in the economic development of a country. A well-developed banking system is essential for the economic development of a country. The "Industrial Revolution" in Europe in the 19th century would not have been possible without a sound system of commercial banking. In case of developing countries like India, the commercial banks are considered to be the backbone of the economy.

Commercial bank functions:

Commercial banks can contribute to a country's economic development in the following ways:

Capital formation is the most important determinant of economic development. They mobilize idle resources for production purposes. Economic development depends upon the diversion of economic resources from consumption to capital formation. Banks help in this direction by encouraging saving and mobilizing them for productive uses. Commercial banks are a very important source of finance and credit for industry and trade. Credit is a pillar of development. Credit lubricates all commerce and trade. Banks become the nerve centre of all commerce and trade. Banks are instruments for developing internal as well as external trade. Banks generally provide financial resources to the right type of industries to secure the necessary material, machines and other inputs. In this way they influence the nature and volume of industrial production. Banks in underdeveloped countries have been paying more attention to trade and commerce and have almost neglected agriculture and industry. Banks can also play an important role in achieving balanced development in different regions of the country. They transfer surplus capital from the developed regions to the less developed regions Industrial development needs finance. Commercial banks encouraged industrial development by granting long-term loans also. Loan or credit is a pillar to development. In underdeveloped countries like India, commercial banks are granting short-term and medium-term loans to industries.

Commercial banks provide banking services to businesses and consumers through a network of branches. These banks are in business to make a profit for their owners and they are usually public limited companies managed by shareholders. In India, however, most of the top commercial banks are owned by the government. But many private commercial banks have been established in the recent years.

Commercial banks are all-purpose banks that perform a wider range of functions such as accepting demand deposits, issuing cheques against saving and fixed deposits, making short-term business and consumer loans, providing brokerage services, buying and selling foreign exchange and so on.

The primary functions of commercial bank are accepting deposits from the public and granting credit to all sectors of the economy after making provisions for reserves as per the RBI regulations.

Apart from receiving and lending functions, commercial banks undertake various secondary or incidental functions such as agency services and general utility services.

Functions of Commercial Banks

The functions of commercial banks are explained below:

Primary functions

Collection of deposits

Making loans and advances

Collection of deposits: The primary function of commercial banks is to collect deposits from the public. Such deposits are of three main types: current, saving and fixed.

A current account is used to make payments. A customer can deposit and withdraw money from the current account subject to a minimum required balance. If the customer overdraws the account, he may be required to pay interest to the bank. Cash credit facility is allowed in the current account.

Savings account is an interest yielding account. Deposits in savings account are used for saving money. Savings bank account-holder is required to maintain a minimum balance in his account to avail of cheque facilities.

Fixed or term deposits are used by the customers to save money for a specific period of time, ranging from 7 days to 3 years or more. The rate of interest is related to the period of deposit. For example, a fixed deposit with a maturity period of 3 years will give a higher rate of return than a deposit with a maturity period of 1 year. But money cannot be usually withdrawn before the due date. Some banks also impose penalty if the fixed deposits are withdrawn before the due date. However, the customer can obtain a loan from the bank against the fixed deposit receipt.

Loans and advances: Commercial banks have to keep a certain portion of their deposits as legal reserves. The balance is used to make loans and advances to the borrowers. Individuals and firms can borrow this money and banks make profits by charging interest on these loans. Commercial banks make various types of loans such as:

Loan to a person or to a firm against some collateral security;

Cash credit (loan in installments against certain security);

Overdraft facilities (i.e. allowing the customers to withdraw more money than what their deposits permit); and Loan by discounting bills of exchange..

Secondary functions

Agency services

General utility services

Agency Services: The customers may give standing instruction to the banks to accept or make payments on their behalf. The relationship between the banker and customer is that of Principal and Agent. The following agency services are provided by the bankers:

Payment of rent, insurance premium, telephone bills, installments on hire purchase, etc. The payments are obviously made from the customer’s account. The banks may also collect such receipts on behalf of the customer.

The bank collects cheques, drafts, and bills on behalf of the customer.

The banks can exchange domestic currency for foreign currencies as per the regulations.

The banks can act as trustees / executors to their customers. For example, banks can execute the will after the death of their clients, if so instructed by the latter.

General Utility Services: The commercial banks also provide various general utility services to their customers. Some of these services are discussed below:

Safeguarding money and valuables: People feel safe and secured by depositing their money and valuables in the safe custody of commercial banks. Many banks look after valuable documents like house deeds and property, and jewellery items.

Transferring money: Money can be transferred from one place to another. In the same way, banks collect funds of their customers from other banks and credit the same in the customer’s account.

Merchant banking: Many commercial banks provide merchant banking services to the investors and the firms. The merchant banking activity covers project advisory services and loan syndication, corporate advisory services such as advice on mergers and acquisitions, equity valuation, disinvestment, identification of joint venture partners and so on.

Automatic Teller Machines (ATM): The ATMs are machines for quick withdrawal of cash. In the last 10 years, most banks have introduced ATM facilities in metropolitan and semi-urban areas. The account holders as well as credit card holders can withdraw cash from ATMs.

Traveler's cheque: A traveler's cheque is a printed cheque of a specific denomination. The cheque may be purchased by a person from the bank after making the necessary payments. The customer may carry the traveler's cheque while travelling. The traveler's cheques are accepted in banks, hotels and other establishments.

Credit Cards: Credit cards are another important means of making payments. The Visa and Master Cards are operated by the commercial banks. A person can use a credit card to withdraw cash from ATMs as well as make payments to trade establishments.

In developing countries like India commercial banks perform certain promotional (developmental) activities. For example, nationalized banks in India provide credit to the top priority sectors of the economy such as agriculture, and small-scale and cottage industries. In this way commercial banks help to promote the socio-economic development of the country.

Objectives of the study:

1. To understand meaning of the commercial banks.
2. How they helpful to achieve economic development.
3. The type of loans they give.
4. What is the impact of commercial banks on economic.

Review of literature:

The role of commercial banks in economic development is a very important topic; so many authors write the paper on the role of commercial banks in economic development. This paper is trying to give clear idea of what is the role of commercial banks in economic development, how they helpful to farmers, industrialists and general public.

Analysis:

Growth of Banking in India of Scheduled Commercial Banks

Indicators	31 March of								
	2005	2006	2007	2008	2009	2010	2011	2012	2013
Number of Commercial Banks	284	218	178	169	166	163	163	169	151
Number of Branches	70,373	72,072	74,653	78,787	82,897	88,203	94,019	102,377	109,811
Population per Banks (in thousands)	16	16	15	15	15	14	13	13	12
Aggregate Deposits	17002billion (US$260 billion)	21090 billion (US$320 billion)	26119 billion (US$390 billion)	31969 billion (US$480 billion)	38341 billion (US$580 billion)	44928 billion (US$680 billion)	52078 billion (US$790 billion)	59091 billion (US$890 billion)	67504.54 billion (US$1.0 trillion)
Bank Credit	11004 billion (US$170 billion)	15071 billion (US$230 billion)	19312 billion (US$290 billion)	23619 billion (US$360 billion)	27755 billion (US$420 billion)	32448 billion (US$490 billion)	39421 billion (US$600 billion)	46119 billion (US$700 billion)	52605 billion (US$790 billion)

Conclusion:

After nationalization of the banks our country got the success in every field. Our central bank give targets to the banks how much percentage they have to give loans to agricultural and industrial sector, howmuch percentage they have to give to export import business. In this way banks give loans to every sector.

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