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# Colonial Legacy and the Evolution of Modern Banking Institutions in India: A Historical and Analytical Perspective

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## ABSTRACT:

The foundation of India's modern banking system was laid during British colonial rule. Introduced primarily to facilitate imperial trade, revenue collection, and financial control, colonial banking institutions neglected indigenous financial needs and shaped an unequal financial structure that continued even after independence. This paper explores how the British colonial administration institutionalized Western banking models in India, how these systems marginalized native banking, and how post-independence reforms attempted to "decolonize" the financial system. Using statistical data from the Reserve Bank of India, historical archives, and scholarly sources, the paper highlights the structural continuities and policy responses that define India's banking evolution.

## KEYWORDS:

Colonial Legacy, Financial Inclusion, Reserve Bank of India, Bank Nationalization, Indigenous Banking.

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## Introduction

Banking is a key pillar of any modern economy. In India, however, its development was neither organic nor indigenous—it was a by-product of colonial economic needs. The British East India Company and later the British Crown introduced banking primarily to manage the financial flows of trade, military expenditures, and administrative revenues.

Before British intervention, India had a well-developed indigenous banking system with shroffs, Chettiars, Marwaris, and Multanis acting as financiers and moneylenders across regions. These traditional systems were gradually sidelined as British-controlled institutions monopolized modern financial functions.

Thus, the Indian banking system evolved not as a service to the domestic economy, but as an instrument of colonial extraction and economic control.

### **Objectives of the Study**

1. To trace the historical origins of modern banking in colonial India.
2. To analyse how colonial banking structures were designed to serve British economic interests.
3. To assess the social and economic impact of colonial banking on indigenous financial systems.
4. To examine the persistence of colonial legacies in post-independence Indian banking.
5. To study the statistical trends reflecting continuity and reform in Indian banking.

### **Methodology**

This paper employs a historical-analytical and descriptive research approach.

#### **Data are drawn from:**

- RBI publications such as Report on Trend and Progress of Banking in India (various years).
- Statistical Abstracts of British India (1930–1947).
- Secondary sources including books by Tirthankar Roy, D. Rothermund, and RBI archives.
- Comparative analysis of pre- and post-independence financial indicators.

### **Evolution of Banking under British Rule**

#### **Early Phase (1770–1850): Agency Houses and Presidency Banks**

- The first bank, Bank of Hindustan, was established in 1770 by Alexander & Co. in Calcutta.
- It primarily served the East India Company's commercial transactions.
- Presidency Banks were later set up in:
  - » Calcutta (1806) – Bank of Bengal
  - » Bombay (1840) – Bank of Bombay

» Madras (1843) – Bank of Madras

These banks issued currency notes and managed government accounts, marking the birth of a dual-purpose banking model – commercial and governmental.

### **Mid Phase (1850–1920): Institutional Expansion and European Monopoly**

- The Industrial Revolution in Britain increased demand for raw materials and export finance.
- Colonial banks such as the Chartered Bank of India, Australia and China (1853) and Grindlays Bank (1864) entered Indian markets.
- These banks focused on European clients and export-oriented sectors like jute, tea, coffee, and indigo.
- Indigenous traders had limited access to credit; their activities remained confined to informal networks.

### **Late Colonial Phase (1920–1947): Regulatory Framework and RBI Formation**

- The merger of the three Presidency Banks in 1921 created the Imperial Bank of India, precursor to the State Bank of India (1955).
- The Reserve Bank of India (RBI) was established in 1935 under the RBI Act of 1934, modelled after the Bank of England, primarily to regulate currency and credit for imperial stability.
- The Banking Companies Act, 1913, and Cooperative Societies Act, 1904, were introduced to regulate native banking but mainly favoured British institutions.

### **Colonial Banking Objectives**

#### **Colonial banking in India had clear imperial goals:**

1. Facilitation of Colonial Trade: Financing exports of raw materials and imports of British goods.
2. Revenue and Treasury Management: Efficient handling of tax revenues, remittances, and military payments.
3. Exchange and Currency Control: Maintaining stable exchange rates to protect sterling reserves.
4. Financial Control and Dependence: Centralizing control through institutions like the Imperial Bank and RBI.

## Marginalization of Indigenous Banking

Before British domination, indigenous bankers played a central role in India's credit and trade finance system. However:

- Colonial banks refused to lend to them or recognize their promissory instruments.
- Traditional systems of hundis and baniyas were deemed “unscientific.”
- Indigenous institutions were denied legal protection under the British contract law system.

This led to a financial dualism – modern banks for colonial elites, and informal credit for the masses.

## Statistical Overview of Colonial Banking (1850–1947)

Year	Total Banks	Foreign Banks	Deposits (₹ crore)	Share of Indian Ownership	Remarks
1870	27	18	8.4	10%	Dominated by British banks
1913	57	36	62.5	25%	Indian joint-stock banks emerge
1939	94	42	185.6	35%	Imperial Bank monopoly continues
1947	95	45	230.1	40%	Negligible rural presence

Sources: RBI, British Statistical Abstracts 1940, Imperial Bank Reports

## Colonial Legacy in Post-Independence Banking

### Institutional Legacy

- The RBI, although nationalized in 1949, retained the same structure and mandate as under the 1934 Act.
- The State Bank of India (1955) emerged from the colonial Imperial Bank, indicating continuity.

### Structural Legacy

- Urban bias in branch location and credit distribution persisted.
- Large industrial and trading houses received major bank finance, while rural areas remained underserved.

## Legal and Policy Legacy

- The Banking Regulation Act, 1949, was an extension of colonial-era legislation, continuing British-style prudential norms and licensing procedures.

## Banking Reforms and Decolonization Efforts

### Bank Nationalization (1969 & 1980)

- Aimed to end private and foreign dominance.
- 14 banks were nationalized in 1969 and 6 more in 1980.
- Rural branch expansion increased from 22% (1969) to 37% (1991).

### Social and Development Banking

- Establishment of Regional Rural Banks (RRBs) in 1975.
- Lead Bank Scheme (1969) and Priority Sector Lending to support agriculture and small enterprises.

### Financial Inclusion Initiatives

- Post-2000: Jan Dhan Yojana (2014) aimed to close the access gap created by colonial exclusion.
- As of 2023, over 50 crore bank accounts were opened under financial inclusion schemes.

## Comparative Analysis: Colonial vs. Modern Banking

Feature	Colonial Period	Post-Independence Period
Ownership	Foreign & Private	Nationalized & Public
Objective	Trade Facilitation for Empire	Development & Inclusion
Regulation	British Government & Bank of England	RBI (Nationalized 1949)
Credit Flow	Urban & Export-Oriented	Agriculture & MSMEs

## Conclusion

Colonial rule left an indelible imprint on India's financial architecture. While the British introduced modern banking systems, they did so with the primary intent of furthering imperial interests, not national development.

After independence, India's policymakers had to reform and reorient these inherited institutions toward nation-building. The nationalization of banks, rural credit programs, and financial inclusion drives reflect

conscious efforts to correct historical imbalances.

Today, India's banking sector stands as a blend of colonial institutional structures and indigenous developmental aspirations – a testament to the country's journey from imperial finance to inclusive finance.

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