Chapter–I

INTRODUCTION

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1.1 INTRODUCTION

The progress of a country involves not merely economic but also social and institutional changes. In many under-developed countries, it calls for a new set of values and new concepts of society and Government. India is a country of villages and so the development of the country mainly depends upon the all-round progress of the rural area. Mahathma Gandhi, the father of the nation, wrote long back in 1936 in Harijan, "I have believed and repeated times without number that India is to be found not in its few cities but in its 7,00,000 villages. . . .' I would say that if the villages perish, India will perish too."[1] Rural development is advocated to-day as a basic strategy for all-round development of countries like India. In this context, the importance of banking is fully realized. Without proper banking, there cannot be any economic growth or social upliftment.

Banking in India has a long history and it had flourished even in ancient Vedic times. Modern commercial banking can be said to make its beginning in India with the setting up the first Presidency Bank called the Bank of Bengal in Calcutta in 1806.

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1. Gandhiji, quoted in Radha Raman Singh and Rabindra Narayan Singh, "IRDP and Revitalisation of Rural Scena in India", **Khadigramodyog**, January, 1985, p.172.

Two other Presidency Banks were started in Bombay and Madras in 1840 and 1843 respectively. During the time of Indian Independence the banking facilities were heavily concentrated in Metropolitan centres with very high proportion of total advances going to trade.[2]

But, after Independence, things started changing and the policy markers put banking at the pivot of the whole financial structure of the economy. The first planned move to take the commercial banking system to the rural area was made in July 1955. The imperial bank was converted into the State Bank of India on the basis of the recommendation of the All India Rural Credit Survey Committee (1954).[3]

The Committee had recommended the creation of a strong integrated, State-sponsored and State-partnered commercial bank with an effective network of offices to spread banking facilities in rural areas. The State Bank of India was asked to open more branches in the interior parts of the country. The establishment of the State Bank of India was a fundamental reform in India One of the major objectives with which the State Bank was founded was to spread banking facilities in rural areas.

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2. Ramanand Pandey, **Commercial Bank and Rural Development**, Deep and Deep Publication, New Delhi, 1989, pp.67-70.
3. S.B. Gupta, **Monetary Economics**, Sultan Chand and Company, New Delhi, 1982, p.87.

However, rural banking got a boost after the nationalization of the 14 major banks in 1969. The commercial banks provided a large chunk of their funds for rural development.

However, the high cost of operation and the urban outlook of the commercial banks acted as major hurdles to achieve the social objective of rural financing.[4]

The banks have been accorded very important role in the development process of the country. The role assumes added significance due to the fact that banks provide one of the essential inputs, namely finance for the growth of various segments of the rural society. In a developing country like ours, where the scarcity of financial resources is admittedly one of the constraints, for accelerating the pace of development in the rural areas, an efficient and responsive banking system is of utmost importance.[5]

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4. Sixth Five Year Plan, **Planning Commission**, Government of India, New Delhi, 1980-85, p.179.
5. M.K. Jain, **Rural Banks and Rural Poor**, Printwell Publishers, Jaipur, 1989, p.54.

1.2 RURAL DEVELOPMENT IN INDIA

Rural development is associated with agriculture, and it remained, for a long time, coterminous with agricultural development in India. The Royal Commission on Agriculture (1928) for instance, agrees with this kind of interpretation of 'rural' development. To quote from the Report of the Commission: "We cannot too strongly state our conviction that the directorship of agricultural advance must in a very great degree depend upon the suitability of the officer appointed." Nearly half-a century later, another committee took a more or less similar view of rural development. The Planning Commission's task force on Integrated and Rural Development, observed in 1972. "After careful consideration, we have belatedly decided to take what might be considered a rather restricted view of the expression 'rural development'."[6]

1.3 RURAL DEVELOPMENT PROGRAMME IN INDIA

After independence, realizing the significance of improving the plight of rural masses and being committed constitutionally to improve their socio-economic well-being, several steps were taken by the Government of India. Various programmes like Community Development Programme (CDP), Intensive Agricultural District Programme (IADP), High Yielding Variety Programme (HYVP), Small Farmers Development and Agencies (SFDA), Marginal Farmers

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6. I.C. Dhingra, **Rural Banking in India**, Sultan Chand & Sons Publishers, New Delhi, 1987, p.47.

and Agricultural Labourers Development Agencies (MFAL), Integrated Rural Development Programme (IRDP), National Scheme of Training of Rural Youth for Self-Employment (TRYSEM), Development of Women and Children in Rural Areas (DWCRA), Differential Rate of Interest Scheme (DRI), 20 Point Economic Programme, Bio-gas Programme, Scheme for providing Self-Employment to Educated Unemployed Youth (SEEVY), Prime Minister's Rozgar Yojana (PMRY), were implemented. The main object of all these programmes was to improve the socio-economic conditions of the rural people, by increasing agricultural production, developing small-scale industries, creating maximum possible employment opportunities, eradicating poverty from rural sector and providing basic amenities of life. Rural development is an important tool for bringing about the desired improvement in the life of the rural people. It is a strategy designed to improve the social and economic life of a specific group of people, namely the rural poor. It involves the extending of development benefits to the poor masses living in rural India.

Rural development is of vital importance for bringing about overall socio-economic development in the country. Moreover, the economic development and progress of India would really mean, the reconstruction and resurgence of the rural masses of the country. The real growth of Indian economy, therefore, lies in the emancipation of the rural masses from the condition of poverty in which they have been living for centuries. Keeping these objectives in view, the Government gave priority to rural development in its programmes and plans.

Traditionally due to the absence of institutional lending agencies like co-operative and commercial banks, the farmers and other ruralites used to get credit from the non-institutional agencies. Sources like money-lenders, instead of providing credit facilities to the villagers, used to exploit them for their selfish ends, through the process of charging exorbitant rates of interest. Due to this evil practice of money-lenders, the quantum of indebtedness of rural poor increased by leaps and bounds. In order to relieve the rural poor from the grip of money-lenders and to provide financial assistance to the needy villagers, co-operative banks were set up in the country in 1904 and vigorous efforts were made to strengthen them. Whole of the country was covered under the network of co-operative institutions to cater to the credit needs of the rural people. Despite this network of co-operative institutions and their wider coverage, they were not in a position to keep pace with the ever-increasing demand for agricultural and industrial credit required for improved and scientific cultivation and expansion of industry in the rural sector.

In order to ensure that agricultural production may not suffer for want of adequate and need-based credit, the introduction of other financial institutions into the rural credit scene became meaningful. It was at this stage, commercial banks, with vast resources at their disposal were directed to help in this task. With this objective in view, the Government of India nationalized 14 major commercial banks in July 1969 to provide credit facilities to the neglected rural sector. The Government made changes in their credit scheme and policies of banks so as to direct the flow of their credit to hitherto neglected sectors of rural economy. Prior to nationalization the banks were inclined to finance industries only in the urban areas. They were hesitant to enter into the field of rural development. But after nationalization, the whole situation underwent a fundamental change and now the commercial banks finance a number of rural-based activities. They extend banking services to the rural people by opening branches in rural centres to ensure adequate flow of credit. The Reserve Bank of India (RBI) has directed these banks to lend 40 per cent of their advances to the priority sector comprising agriculture, small-scale industries and small business.

Thus, in the context of planned economic development, the commercial banks with their branches in the rural centres and with huge funds are contributing to socio-economic changes in the rural sector. If the credit facilities are not made available, various development programmes being launched by the Central and State Governments would be of no use. Credit is a basic input for any development programme. This is particularly true in the case of rural development programmes which require huge sums of money for their effective implementation. Bank credit certainly is an essential condition without which the development of rural people cannot take place. Since 1969, banks have been playing a key role in the upliftment of the rural masses.

1.4 ROLE OF BANKS IN THE SOCIO-ECONOMIC DEVELOPMENT OF INDIA

Finance is a vital input for economic growth. It is, therefore, obvious that institutions like banks, which command huge financial resources, can play a decisive role in shaping the economy of a country, by judiciously deploying their funds in such important activities which lead to overall economic growth.[7] Economists have expressed a wide variety of opinions on the effectiveness of the banking system in promoting or facilitating economic development. Schumpeter, the first modern economist to study the relationship, regarded banking system as one of the two key agents (the other being entrepreneurship) in the whole process of development. Alexander Gerschenkvon looks at banks as a substitute for deficiencies in the original accumulation of liquid wealth in moderately backward economics.[8] A developing economy faces many problems like poverty, scarcity of capital, lack of entrepreneurship skills, unemployment, etc. There is dependence on agriculture and at the same time agriculture is not modernised.

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7. S.D. Tripathi and K.K. Uppal, **The Role of Banking and New Economic Programme**, Publication Bureau, Punjab University, Chandigarh, 1984, p.19.
8. A.C. Shah, Banking for Economic Growth, **Journal of India Institute of Bankers,** Vol.45, No.1, (January-March, 1947), p.33.

Means of transport and communications are under-developed.[9] There are inter-regional disparities. There is unequal distribution of wealth. Banks can work as catalysts of growth by following the right kind of policies in their working depending upon the socio-economic conditions prevailing in a country.[10]

Banks can play a crucial role in bringing about planned growth in under-developed economies. As these economies are usually short of capital, the task of mobilisation of resources and their channelisation to the priority sectors belong to such institutions.[11] Broadly speaking, banks have been assigned the task of accelerating the economic growth and bringing about revolution in industrial and agricultural sectors of the economy for better redistribution of income and wealth, reducing unemployment and ameliorating the economic lot of the vast majority of people living in substandard economic conditions.[12]

Banks play an important role in the process of socio-economic development. They are both the repositories of the community's savings and purveyors of credit for economic activities. They provide to the saver a

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9. M.L. Jingan, **Money, Banking and International Trade,** Konark Publication, New Delhi, 1986, p.252.
10. S. Singh, **Performance Budgeting for Commercial Banks in India,** The Macmillan Company of India Ltd., p.21.
11. S.D. Tripathi and K.K. Uppal (ed.), **Banking and New Economic Programme,** Publication Bureau, Punjab University, Chandigarh, 1984, p.63.
12. R.S. Sayers, **Modern Banking,** Oxford University Press, 1951, p.10.

convenient avenue for investment of surplus funds and to the investor a source of finance. Recently, the need for regulation of credit flows via the banking system has come into prominence and banks have been urged to devote more attention to the 'purpose' for which they provide loans rather than to 'security' in the customary sense, to view themselves as development agencies rather as mere disbursers of funds, to pick out promising new entrepreneurs and in general, to restructure both their organisational arrangements and their working rules of practices to the new requirements.[13]

An increasing rate of saving is essential for the increasing requirements of capital formation for a developing economy. The savings can be put to direct productive use or can be invested in bank deposits, Government securities, equities on bonds. The scope for direct productive use of voluntary saving is, however, limited in a developing economy in which there exists a very large number of persons whose saving potential is low, because their incomes are very low. But the saving potential of rural people, belonging to high income group, is high. Such income earners tend to hold their savings mainly in currency and to some extent in jewellery, in land or in the form of loans and advances given to unorganised market, that is in forms which are infructuous or socially wasteful. Often they do so because of such factors as their ignorance of the availability of

13. Banking and Development–Report of an International Seminar, Reserve Bank of India, 1970, p.36.

different types of financial assets in which they can hold their saving.[14] In these situations, banks can help in the mobilisation of savings through branch expansion in unbanked and under-banked areas and by introducing a variety of deposit schemes to suit the needs of individual depositors. Thus, they are capable of stimulating savings by providing a framework of institutionalised savings and facilitate their investment in the fields of greatest urgency and productivity of the economy.[15]

Basic infrastructure is necessary for removing market imperfections for the maximum utilisation of scarce productive resources. Financial infrastructure is a part of it. The financial infrastructure is a necessary medium for effecting transfer of funds from savers to investors and thereby facilitate the process of economic development through capital creation, income generation and structure change. Banks, being the major part of financial infrastructure, provide 'savings intermediation'. According to Hyman P. Minsky,[16] savings intermediation is a process by which the flow of savings of a community is allocated to finance investment in the economy. This process brings about consistency between the

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14. Report of the Banking Commission, 1972, pp.85-86.
15. International Book for Reconstruction and Development Memorandum on Financing of Economic Development, 1958, p.82.
16. Subhash Garg, **Social Banking**, Arihant Publishing House, Jaipur, 1994, p.42.

asset preferences of households, the ultimate savings units, and the liability preferences of business firms, the fundamental investing units.

The banks by encouraging entrepreneurship, help to generate more employment opportunities, ensure better and fuller utilisation of productive resources of the community and help improve the income levels of the people for their socio-economic well-being. The availability of bank credit enables entrepreneurs to harness innovation by bridging about new combinations of productive resources, drawing resources away from their existing comparatively low yielding employment and employing unemployed resources. This, in turn, helps the economic system to get on a higher plane of economic activity.[17] They provide loans for the education of young persons studying in engineering, medical and other vocational institutions of higher learning. They advance loans to young entrepreneurs for establishing their own business. Thus, the banks not only help in human capital formation but also in increasing entrepreneurial activities in developing economies.

The banks help the agricultural sector in a number of ways. They open a network of branches in rural areas to provide agricultural credit. They provide finance directly to the farmers for raising crops, for marketing their produce, for

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17. K.L. Pande, **Development of Banking in India Since 1949**, Scientific Book Agency, Calcutta, 1961, p.2.

the modernization and mechanization of farms, for providing irrigation facilities, for developing land, and the like. They also provide financial assistance for animal husbandry, dairy farming, sheep rearing, poultry farming and horticulture. Various schemes have been formulated by banks for financing agriculture. The small and marginal farmers, landless labourers, artisans and petty, shopkeepers in rural areas are financed by commercial banks thus, banks meet the credit requirements of all types of rural people.[18]

Price stability is necessary for the steady and rapid economic development of the economy. If the price of goods and services remain stable, the country will march forward on the road of economic progress. The commercial banking system, through decisions to provide or not to provide credit, has also an important role to play in this field. The direction of the flow of credit has an important bearing in price stability. Credit for production affects the economy differently than credit for consumption purposes. Even the credit which goes to production purposes can have different repercussions depending on the time lag between the increase in demand and increase in supply which the credit brings about. If too much credit goes to longer gestation uses, it can have adverse effect on the price level. Cheap and timely credit, assuming adequate availability of material, helps producers produce things at lower cost, which is one of the important

18. Report of the Banking Commission, 1972, p.64.

considerations for fixing the prices.[19] A growing economy needs increasing supply of money but its supply should be elastic only to the extent that it is geared to the seasonal demands of business, as otherwise, it would have adverse effects on the general price line.[20] Thus it has been rightly observed that commercial banks may serve as shock absorbers and effective feelers on the one hand, and circulators of funds in the arteries and veins of the money market on the other.[21]

1.5 LEAD BANK SCHEME

The concept of the Lead Bank Scheme was first mooted by the Gadgil Study Group under the Chairmanship of R.D. Gadgil which submitted its report in October 1969. The study group recommended the adoption of an 'Area Approach' to evolve plans and programmes for the development of an adequate banking and credit structure in the rural areas. This idea was accepted by the committee of bankers on Branch Expansion Programme of public sector banks and the Committee recommended that in order to enable the public sector banks to discharge their social responsibilities, each bank should concentrate an certain districts where it should act as a 'Lead Bank'. On the basis of the

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19. Report on International Seminar, Banking and Development, RBI, 1970 p.33.
20. Edward W. Reed, **Commercial Bank Management,** Harper and Row Publihsers, New York, p.67.
21. A.G. Sharma, **State in Relation to Commercial Banking in the Development Economy of India,** Sterling Publishers (P) Ltd., 1968, p.4.

recommendations of the Committee, the Reserve Bank of India introduced the 'Lead Bank Scheme' towards the end of 1969. Accordingly, the whole country was divided into 338 districts (as in the end of 1969) which were allotted among the public sector banks including the State Bank of India and its group.

The Lead Bank acted as a consortium leader for co-ordinating the efforts of all credit institutions in each of the allotted districts in expanding branch banking facilities and in meeting the credit needs of the rural economy.

The Lead Banks had first fulfilled the primary task of expanding branches, the expansion of commercial banks in unbanked and under-banked rural areas in the early 1970s. The next important development was the constitution of District Consultative Committees for Banking Development in all the districts in the country, followed by the formulation and implementation of Area Development Programmes covering the activities in the priority sectors. This gave birth to the concept of District Credit Plans and Annual Action Plans.

The objectives of the Lead Bank Scheme are:

1. To launch a programme of rapid branch expansion particularly in unbanked and under-banked areas so as to provide banking facilities to large segments of the population in rural and semi-urban areas and

2. To ensure adequate flow of institutional credit on reasonable terms to the neglected and weaker sections of the community and thus fill the spatial and sectoral credit gap.[22]

1.6 SERVICE AREA APPROACH

A seminar on 'Rural Lending' was organised by RBI in January 1988. There it was decided to implement the Service Area Approach (SAA). The service area approach was to be adopted by all the rural and semi-urban branches. SAA further envisaged each bank branch to concentrate on a specified area and to develop productive lending, thereby avoiding the diffusion of banks and the efforts over a wider area, harmonizing them in the task of rural development through credit, by the preparation of the annual action plan.

This nationalisation of 20 commercial banks and the introduction of the lead bank scheme had both economic and social relevance. The extent to which the different objectives had been fulfilled is worth considering.[23]

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22. P. Arumugam, "Lead Bank Scheme", **Indian Banking Today and Tomorrow**, Vol.14, No.7, July, 1989, pp.12-16.
23. Debasish Banerjee, "Service Area–A Dynamic Approach for Purposive Rural Credit", **Indian Banking Today and Tomorrow**, Vol.15, No.12, December, 1990, pp.17-20.

1.7 NEED FOR THE STUDY

This study is confined to Pudukkottai district. This kind of indepth study relating to one district will definitely benefit the promotion of rural banking in that district. The study is undertaken in Pudukkottai district because of its backwardness. This district has more number of villages and rural centres than its urban counterparts. A study of the rural banking in this district can reflect a picture of rural banking in the entire state.

The study deals with the nationalized commercial banks, private sector banks and SBI Group of Banks. The focused areas are deposit mobilisation, disbursal of credit in priority and non-priority sectors.

A comparative analysis of the performance of Nationalised Commercial Banks, Private Sector Banks and SBI groups of Banks functioning under the Lead Bank Scheme in the district is done for the period from 1995-96 to 2002-03.

1.8 SCOPE OF THE STUDY

The scope of the study is confined only to the Pudukkottai district. The study includes only the rural branches randomly selected in the district. The performance of the rural branches in the district covers only the branches coming under the service area approach programme and Lead Bank Scheme in Pudukkottai district. The period of the study covers only eight years from 1995-96 to 2002-2003. The field survey was conducted among the selected respondents with the reference of the year ending March 31, 2003. The performance variables focused in the studies are identified and confined with the help of reviews. The main focus on performance is classified into deposit mobilisation and loan disbursement.

1.9 STATEMENT OF THE PROBLEM

The purpose of bank nationalisation was to promote a rapid growth in agriculture, small industries and exports, to encourage new entrepreneurs and to develop backward areas. After nationalisation, public sector banks got increasingly motivated towards helping various priority sectors in general and neglected sectors in particular. Several institutions have been established to uplift the weaker sections, particularly the poorest among the poor. Yet, there was a large gap in the flow of rural credit. The priority sector did not receive much attention from the banking side. It is confirmed with the statement mentioned by J.Ramanaidu (1987).[24] He revealed that about 40 per cent of the total credit was provided to priority sectors. Out of the 40 per cent advances, 25 per cent of the credit was given to the weaker sections and the remaining 15 per cent of the credit was given directly to agriculture. But the rural poor have not been benefited to the

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24. J. Ramanaidu, "How Banks Can Finance Rural Development", **Yojana,** New Delhi, July 16-31, 1987, p.9.

expected level. Inspite of many rural development schemes, the poor communities have not improved their status. This is due to the mismanagement of credit utilisation.

1.10 OBJECTIVES OF THE STUDY

The major objectives of the present study are the following:

i) To describe the rural banking activities in Pudukkottai district.

ii) To reveal the profile of the customers.

iii) To analyse the factors influencing loan borrowed and loan utilised.

iv) To identify the attitude of the customers to rural banking and examine the discriminatory variables of defaulters and non-defaulters and wilful defaulters and non-wilful defaulters.

v) To explain the profile of the bank employees working in rural branches at Pudukkottai district.

vi) To measure the attitude of bank employees to rural banking and

vii) To summarise findings and present suggestions.

1.11 CHAPTERISATION

The present study is in eight chapters. The first chapter introduces the topic, and presents the need for the study, scope of the study, objectives of the study and the chapter scheme.

Chapter II discusses the concepts and presents a review of past literature.

Chapter III deals with Research Methodology, employed for this study.

Chapter IV discusses Rural Banking in India and Tamilnadu.

Chapter V evaluates Rural Banking in Pudukkottai District.

Chapter VI focuses on the customers Attitude to Rural Banking.

Chapter VII discusses profiles of Bank Employees in Rural Banking and their attitudes.

Chapter VIII presents a Summary of Findings, Conclusion and Suggestions.