CHAPTER 1
INTRODUCTION

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Backdrop

Indian economy is regarded as one of the leading developing economies where 76 percent of the total population lives in rural areas and 69 percent of the total working population depends on agriculture for their livelihood (Statistics on Indian Economy, RBI, 2006). Report on human development has ranked India's development index at 126 out of 177 countries (Human Development Report, 2006). The economy in India is very much influenced by the development of its rural sector and the government has been initiating various programmes during the plan periods for its overall development. The entire planning period for rural development is divided into four phases encompassing different approaches. The first phase (1951 – 1966), the initial three plan periods, laid emphasis on restructuring agrarian relations, institution building and community development. The second phase (1966 – 1985), beginning from fourth five-year plan, focused primarily on technology-based growth for agricultural development and helped the country to become self-sufficient in food-grains. During the third phase, from late eighties to early nineties, the focus shifted to growth with equality. The various programmes initiated during this period included Integrated Rural Development Programme (IRDP), Drought Prone Area Development Programme (DPAP) and others. During the fourth phase, which began since nineties, the government started endeavouring for economic reforms not only in the financial sector but also in the banking sector.

The history of Indian banking, during post independence era, can be divided into three distinct phases. During phase I (1947 – 1969), banks under private ownership were forced to cater services to special category of clientele. The second phase (1969 – 1991) was characterised by social banking resulting in the emergence of large public sector banks with rapid expansion of branch network. The third phase (1991 onwards) portrayed a prudential higher accounting and
disclosure standards at par with the best practices of international standards.

Necessity is regarded as the mother of all inventions. In 1991, the Indian economy was facing a grave crisis in all fronts – forex reserves touched an abysmal low, increased deficit in oil pool account and severe resource crunch had a throttlehold on the economy. It was at that juncture, the new Parliament under the stewardship of Shri P.V. Narasimha Rao decided to go in for sweeping changes in the economic front and with Dr. Manmohan Singh, as Finance Minister, the government unveiled the economic reforms package. The package was framed to serve as a boost for an ailing economy. Financial and banking sector reforms were also a part of the package.

Moreover, in the wake of economic liberalisation and increased global integration, there felt a constant need for greater transparency in banking operations including supplying correct and timely data of vital parameters reflecting the strengths and weaknesses of banking institutions. Till 1991, institutions were functioning in an environment with restricted interest rates, government control and skewed development. During the post liberalisation era restriction were relaxed resulting in growing financial disintermediation, emergence of new financial products and services, greater need for professional acumen and wider use of technology.

Rural banking forms one of the significant parts in Indian banking. Many economists and policy makers opine that the future growth of banking sector in India depends to a large extent on the robust performance of the Rural Financial Institutions (RFIs). Among the factors responsible for economic development and poverty alleviation in rural sector, the role of the RFIs is considered very significant as a substantial portion of the institutional rural credit by the RFIs is used for rural development to support formation of rural capital. While increased investment generally leads to higher productivity, majority of the rural people in our country find themselves in the vicious circle, where low productivity leads to low savings resulting low capital
formation and ultimately low investment. This low-level income equilibrium (Nelson, 1956) can only be broken by what Leibenstein termed as Critical Minimum Effort (Chakravarthi, 1967). The Pre-requisites for this effort include availability of appropriate technology and adequate supply of capital.

But rural banking sector is still under penetrated in our country. According to RBI (2005), of the total branch network of scheduled commercial banks in the country (roughly 68,300), nearly 48% of the branches (approximately 32,400) are in the rural sector. But in terms of business, the rural branches have mobilized only 14% of the total deposits. Similarly, the rural advances constitute only 14% of the total advances of banking system, just prior to the introduction the concept of doubling of credit in rural India. In the year 2001, the per capita rural deposits of Rs.2150 formed only 1/10th of the per capita GDP; while the per capita deposits were 160% of per capita GDP for urban India. In the same year, the per capita credit in rural India was only Rs.900 or 4% of GDP; while it was 100% of GDP (i.e. Rs.20,600) for urban India. The number of credit accounts in rural areas was only 3.4% of the rural population as against 10% of population in urban areas. Nachiket – Mor, Deputy MD of ICICI Bank, pointed out that the credit demand in rural India expected to touch Rs.1330 billion, where it supply just about Rs.40 billion (Press release, Nov. 07, 2006).

The government recognising the importance of a functioning rural financial system has taken several steps over the past years to build an extensive formal rural credit structure. There is a bank branch or a primary credit cooperative in every third village in India (Census 2001). Generally speaking, physical outreach of RFIs is not an issue in India, however sustainable growth of these institutions is very much in demand as less than half of the credit usage by rural households comes from the formal sources till now. So there is a need for up-gradation of the rural
banking systems in India through performance evaluation in the context of necessity of institutional rural credit.

In India, institutional rural credit is usually arranged by co-operative banks, commercial banks and regional rural banks or RRBs (popularly known as gramin banks) through their various wings. Since 1975 RRBs are being regarded as one of most important sources of institutional financing of rural credit in India. These institutions are established exclusively to meet the excess demand for institutional credit in the un-banked rural areas, particularly among the economically and socially marginalised section. In other words RRBs are emerged, as institutions that 'combine local feel and familiarity with the rural problems which the cooperatives posses and the degree of business organisation, ability to mobilize deposits, access to central money markets and modernized outlook which the commercial banks have'.

Among the 196 RRBs operating as scheduled commercial banks within the framework of multi-agency system in India, nine are functioning in West Bengal (March, 2005). These specialised institutions after much experimentation have ultimately emerged as development inducing institutions with a network of branches spread over the remote villages of the country. It has been documented from the studies on the performance of RRBs, that they are undergoing a continuous improvement of services in many areas and also have made their presence felt among the rural people in the areas of agriculture credit (Wadhva 1980; Sudhakar 1984; Mehta 1984; Singh 1985; Parmar et al 1988; Pariyan 1988; Savaraiah 1988; Bapna 1989; Kalkundrikar 1990; Krishnan 1990; Dixit et al 1994.). These institutions have emerged as an instrument to salvage the poorest among the poor from the mire of squalor. The emancipation of rural poor in India is greatly influenced by successful discharge of duties by the RRBs.

Although the performance of RRBs may be gauged from the success of poverty
alleviation programmes to which they are dedicated as catalyst, their achievements as commercial banking organization can never be ignored. The objective of social equity can not be accomplished unless the RRBs register a sustainable growth in terms of expansion of credit facilities through earning profit. There is a strong belief that the banks have social responsibility – not only to meet the credit needs of the society but also to extend the facilities at concessional rates of interest. As such, to respond to the socio economic need, there should be continuous urge to reconcile efficiency and social equity consideration and combine social banking with efficient banking.

At the end of expansion phase (the year 1987 marks the end of addition to the number of RRBs) commercial viability of the RRBs emerged as an important issues to the policy makers. It was pointed out that the RRBs to survive as a credit institution could not remain unviable for long time (Agriculture Credit Review Committee or Khusro Committee 1989; Velayudham and Sankaranarayanan 1990; Committee on Financial Systems or Narasimham Committee, 1991). Thus it was perceived that the RRBs should come out as leading financial institutions to change the rural economy and also to fulfill the objectives for which they emerged. The failures of the RRBs, it was opined, in delivering goods or proving inadequate in meeting the challenges of growing credit needs of the toiling rural masses, would lead to drain on public exchequer and consequently a burden on our economy as a whole. Since the past few years a huge public fund was with the RRBs for rural people. Therefore, it is quite necessary to examine the working of RRBs and appraise their performance, since in a demographic set up every citizen has a right to know how the public money is being used.

In view of the divergent services rendered by the RRBs, an evaluation on the performance of RRBs in West Bengal is seriously felt. The present study aspires to make an overall evaluation on region-wise performance of RRBs in India, particularly in West Bengal, in
respect to restructuring of rural banking and also in satisfying the financial needs of the poor rural folk.

Objective of the Study

In the wake of reforms in the financial sector reforms in 1991-92, the commercial viability of RRBs was emerged as most crucial in deciding their role during the emerging economic scenario. The proposed study, as such, makes a humble attempt to enquire the performance of the RRBs in West Bengal during 1990-91 to 2004-05. The study period of fifteen years is very much relevant in this context, as these specialised institutions have undergone various reforms and initiated critical measures in spreading diversified activities for the overall development of the rural people. The government has also taken several constructive programme for the upliftment of the rural people through these institutions. The objectives of the present study are:

➤ To give an account on the genesis and development of RRBs in India (Chapter – II).
➤ To discuss on some of the conceptual issues regarding these institutions (Chapter – III).
➤ To deliberate on the need for institutional financing for rural credit in India (Chapter – IV).
➤ To make a study on region-wise performance of RRBs in India (Chapter – V).
➤ To identify the performance of the RRBs in West Bengal (Chapter- VI).
➤ To make a comparative study of performance effectiveness of RRBs in West Bengal (Chapter – VII).
➤ To compare the performance effectiveness of RRBs in West Bengal with other Rural Financial Institutions (RFIs) located within the same areas of their operation (Chapter – VIII).
➤ To conclude the discussion and provide some suggestions for improvement in performance of
Review of Literature

Several studies were conducted on the activities of RRBs in India by the academicians, researchers and by the committees appointed by RBI and NABARD in general and also in particular areas. Sketches on the major ones are given below:

• A.B. Kalkundrikar (Performance of Regional Rural Banks, 1992, Ed.1) evaluates the performance of RRBs in Karnataka in terms of deposit mobilization, credit deployment, branch expansion, recovery performance, profitability, contribution to economic development, manpower planning and employee welfare and also examines the comparative role of RRBs with respect to branches of scheduled commercial banks and cooperatives.


• A.M. Khusro (Agricultural Credit Review Committee, 1989, RBI, Bombay) found that the major factors responsible for erosion of profitability were exclusively due to lending to weaker sections, low interest margins and high operating cost and also proposed for merger of regional rural banks with their sponsored bank.

• A.K. Pariyan (RRBs and Rural Development, Ed.1) points out the rationale behind setting up RRBs, evaluates the performance of the RRBs in the country in general and examines the role of SheKhawati Gramin Bank for the rural development at Rajasthan.
• B. Ramesh and D. N. Thakur (Management of Regional Rural banks resources Fund management: A Key to Viability, Financing Agriculture, 1984, p-40-42) assessed the sources of funds of RRBs and their effective management for viability. They stressed the need for examining the scope of cross subsidisation for earning profit of RRBs and suggested that the investment in fixed assets, which failed to fetch any return, should be minimum. In respect to deployment of resources, the RRBs should keep in mind the prospect of earning profit along with socio-economic objectives, which led to their development.

• C. Krishnan (Regional Rural Bank and Rural Development, Yojana, 1990, p-32-34) finds that the regional rural banks have played a vital role in sustaining and rejuvenating rural economy despite several odds.

• G. D. Parmar, R. L. Shiyani and D. B. Kuchhadiya (Performance of Banaskantha Mehsana Grameena Bank in Gujarat State, Agricultural Banker, 1988, p-24) evaluated the performance of Banaskantha Mehsana Gramin Bank in Gujarat and found positive trend in the number of branches, deposits, advances per branch and advances per capita of the said bank.

• G. Savaraiah and N. Nirmalamani (Rural Banking for the Rural Milieu, Indian Cooperative Review, 1988, P-204-213) assessed the performance of Chaitanya Gramin Bank in Andhra Pradesh and found that investment in agriculture received a lion share especially crop loan, which led to a good sign for the development of banking sector in that area.

• H.R. Sudhakar, J.V. Venkataram and G. Nagaraj (An Evaluation of Performance of Regional Rural bank in Mysore District, Karnataka, Financing Agriculture, 1984, p-28-30) evaluated the performance of Cauvery Gramin Bank in Mysore district and compared the performance with Primary Agriculture Cooperative Societies (PACSs). It was found in their study that the performance of RRBs was comparatively better off than PACSs with respect to deposit
mobilisation, credit deployment, timely sanction of loan and adequacy of loan amount. The branches of RRBs were earning profit as compared to PACSs which were running on no loss no profit basis.

- K. Satyasundaram (*Capital Adequacy Gaps for Banks – Problems and Prospects*, Economic and Political Weekly, 1994, p-37-42), R. Sahaya and M. Sharma (*Functioning of the Regional Rural Banks of India*, Agricultural banker, 1986, p-14-18), Y. Dongre (*For Rural Growth*, Yojana, p-11-13), B. Devendra (*Regional Rural Bank Need Structural Change*, Kurukshetra, 1988, p-4-7) found that the performance of RRBs in terms of branch expansion, deposit mobilisation and credit disbursement was remarkable. However, the RRBs continued to face the similar problems like mounting overdue, lack of profitability etc.

- K. Singha (*Restructuring Regional Rural Bank*, Kurukshetra, 1990, p-9-11) calls for changes in the structural and strategic policies to correct the imbalances in functioning of the RRBs.

- M. Narasimham (*Report of the Committee on Financial System*, 1991, RBI, Bombay) opined that to impart viability in the operations of the RRBs they may be permitted to engage in all types of banking business and also to invest their funds in NABARD or other agency to enjoy more interest for augmentation of their income. However, he left the option of merger open to these institutions and their respective sponsored banks.

- M. C. Naidu and R. R. Naidu (*Impact of Credit on Income and Employment – Case Study of a Regional Rural Bank*, Agricultural Banker, 1988, p-24-25) assessed the accomplishment of the Rayalaseema Grameena Bank on income, profits and employment on different categories of beneficiaries. It was found in their study that the income had increased for paddy, jowar and groundnut crops between pre-loan and post-loan periods. Same trends were also noticed in case of dyeing and weaving where the income was more in case of latter due to well
established market. It was also observed that there was increase in man days of employment to 40, 36.84 and 28.57 percent for small, marginal farmers and land less labourers respectively and the improvement was comparatively lower in case of agricultural labourers as they could not afford to employ them outside.

- M. R. Vyas’s (Evolution and Management of RRBs, 1991, Ed.1) study on RRBs is an attempt to bring into limelight the role and contributions of the RRBs in Indian rural development, particularly in Rajasthan and examines the evolution, functioning, management and workings of RRBs. Dr. Vyas (Financial performance of Rural Banks, 1991, Ed.1) also evaluates the financial performance of RRBs in Rajasthan in terms of credit deployment, recovery performance, profitability and customer reaction.

- K. Fujita (Credit flowing from the poor to the rich: the financial market and the role of the Grameen Bank in Rural Bangladesh, Developing Economics, 2000 p- 343-373) analyzes the utilization of loans from Grameen banks (GBs) and illustrates in detail the mechanism used by GBs to alleviate poverty and sheds light on possible limitations on their functioning. An existence of reversed credit flow from the poor to the rich in the rural informal financial market is also discussed in this study.

- L. K. Naidu (Bank Finance for Rural Development, 1992, Ed.1) points out how far the credit gap can be minimized by the RRBs in rural India.

- P. Bhattacharyya (Problems and Prospect of Regional Rural Banks – A Case Study of Mayurakshi Grameena Bank, West Bengal. Agricultural Banker, p- 28-34) examined the problems of RRBs in West Bengal with particular reference to Mayrakshi GB and recommended some measures to improve the performance of RRBs in West Bengal.
• R. Dasgupta (*Rural banking and credit - Tale of many committees*, Economic and Political Weekly, 2001, p-733-737) presented a review of the recommendations of four financial committees on rural banking and credit in India.

• R. Singh and V. K. Jain (*Rural Banking and Its Challenges*, Yojana, 1985, p-6-8) assessed the rural banking activities in India and the challenges faced by them and found that many of the rural branches were becoming economic dead weights with ever-mounting overdues. The situation could be averted if there were appropriate policies for expansion and functioning before opening of the branches and later for efficient supervision of the use of credit.

• R. K. Das (*Performance Budgeting, Monitoring and Review System in RRBs with particular reference to UttarBanga Kshetriya Gramin Bank*, Management Accountant, May, 2001,) analyses the performance budgeting, monitoring and reviewing system adopted by banks with an object to highlight in detail the various constraints in the system and also makes an attempt to assess the level of participation of the employees at different hierarchical levels. The author, in another study (*Financial Viability and Profitability Problems of RRBs – with Particular Reference UBKGB*, Finance India, February 2001, p-9-11), also highlights the factors affecting the financial viability and profitability of UBKGB in comparison to other RRBs in the country.

• R. K. Singh and S. Babu (*Performance of Regional Rural banks in India*, Financing Agriculture, 1996, p- 13-17) observed a divergent picture among the states in respect of deposit mobilisation and advances outstanding while studying a comparative analysis of performance and prospects of RRBs among the states in India. Haryana ranked first with an average deposit of nearly 0.76 crore per branch. However, mobilization of deposit per account varied from Rs.1000 to Rs.3000 across the states. In respect of advances outstanding per branch, Kerala ranked first with Rs.0.8126 crore followed by Tripura and Andhra Pradesh. The
volume of business per branch was the highest in Tripura (Rs.1.41 crore) followed by Kerala and Haryana. There was a wide variation among the RRBs in different states in respect to overdue per branch and it was found to be highest in Manipur (Re.0.7241 crore) followed by Tripura.

- R. K. Singh and K. M. Upadhayay (*A Study of Loan Recovery of Regional Rural Banks in Bihar*, Financing Agriculture, 1984, p-37-39) conducted a study on the system of loan recovery of RRBs in Bihar and found that the performance declined sharply. The major reason behind poor recovery performance was due to inefficient strategies adopted for loan recovery, as was experienced by the bank officials. The various reasons for non-payment of loans are – inadequate production of crops, social ceremonies, non-persuasion by the bank, anticipated declaration of moratorium and remission of loans by the Government. The bank officials, however, suggested some measures for better recovery e.g., lending in cluster, timely reminders, tie-up arrangements with marketing agencies and lastly stringent legal action against wilful defaulters.

- R. K. P Sinha and J. N. Choudhary (*Financial Viability of Central Cooperative Bank and Regional Rural Banks in Bihar – A Case Study*, Indian Journal of Agricultural Economics, 1994, p-515-516), while studying the comparative performance of central cooperative banks (CCBs) and RRBs in Bihar, observed that CCBs, operating above BEP, earned profit while the RRBs incurred losses.

- S. C. Srivastava and B. Subramanian (*Regional Rural Bank Operation: An Evaluation*, Eastern Economist, 1982, p-28-30) observed a steady growth in the number of RRBs in India. In 1975 there were six RRBs with 17 branches and by 1979, the number was rose to 57 with 1990 branches, indicating increased by 9.5 times and 117 times in banks and branches respectively.
They pointed out that the coverage by the RRBs was uneven and the bulk of the assistance by them were distributed disproportionately among the small and marginal farmers and agricultural labourers.

- S. Mehta (*Jhabua Dhar Kshetriya Grameena Bank: An Experience*, Financing Agriculture, 1984, p-51-53) found that Jhabua Dhar Kshetriya Grameena Bank in Madhya Pradesh introduced the performance budget in which the targets and achievements of deposits were compared each year; on the basis of which a corporate plan for the bank was prepared. Further, he suggested that cheaper funds and advances to non target group may improve the income position of the bank.

- S. S. Sinha (*Funds Management in Regional Rural Banks*, National Bank News Review, 1991, p-23-27) recommended that, the RRBs could mobilise higher deposits by offering extra margin of interest, availing maximum refinance, investment in approved securities, reduction in non productive assets and improving recovery position.

- Sankaraiah and B.B. Reddy (*Recovery Performance of Rayalaseema Grameena Bank*, Agricultural Banker, 1994, p-38-48) observed that the recovery rate was good in the case of short-term loans, priority sector advances and rural industries. The recovery was quite encouraging, as well, in piggery in Rayalaseema Grameena Bank in Andhra Pradesh. They found that by and large, recoveries were poor in poverty alleviation programmes and declining trend was noticed for the bank as a whole.

From the detailed studies of above literature, it is perceived that most of the studies were conducted to examine the evolution, functioning, management and financial performance of the RRBs in the country in general and Rajasthan, Punjab, Uttar Pradesh and Karnataka, in particular. In West Bengal, studies were made only on Uttarbanga Kshetriya Gramin Bank and
Mayrakshi Gramin Bank in respect to credit disbursement and recovery performance. As such, no in-depth study has been performed for all the RRBs operating in West Bengal considering some major parameters and also their comparative performance with other rural financial institutions operating within the same areas of operation. The research gap in this area has motivated us to take up the current venture. The present study, as such, makes a humble endeavour to make an evaluation on the overall performance of all the RRBs operating in West Bengal.

**Limitations of the Study**

The study, in its present form is, however, subject to certain limitations. They are:

- Various issues on financial aspect are considered for the present study. The other aspects, like socio-political approach, economic approach, individual interest approach etc. are not considered here because of paucity of information in these regards.

- For comparative analysis of RRBs with respect to other rural financial institutions, the performance of RRBs is compared with the central cooperative banks and the commercial banks located in the same areas of operation of the respective RRBs. Irrespective of paucity of relevant information on various aspects of these entities relating to their performance, all out efforts are made to collect the same to derive some concrete conclusion.

**Research Methodology:**

The present study is basically exploratory in nature and depends exclusively on secondary data. Secondary data are collected from various reports on RRBs published by NABARD and the RBI bulletin, annual reports of RRBs, economic review of West Bengal, report of annual general meeting of West Bengal State Co-operative Banks, (WBSCB), report of state level bankers...
committee meeting (SLBC report) as published by UBI (the SLBC convener bank of West Bengal), reports of the various committees set up by the government on RRBs and the publications of Banker Institute of Rural Development (BIRD). Extensive discussions with official and managers of RRBs along with structure interviews have also been conducted. Direct interviews are also conducted with the customers to get some real life experience in general. Parameters like ratios, percentage of growth and others are considered for some meaningful comparison and analysis to evaluate performance of the RRBs and also to derive some concrete conclusion.

**Plan of Work**

The whole work is proposed to be completed in nine chapters, as are outlined below:

**Chapter I: Introduction** - Makes an introductory approach on the subjects.

**Chapter II: Genesis and Development of Regional Rural Banks (RRBs)** - Discusses on the genesis and development of RRBs.

**Chapter III: Conceptual Issues on Regional Rural Banks (RRBs)** - Deals with the basic and primary issues to have an overall concept about these institutions.

**Chapter IV: Need of institutional finance for rural development in India** - Examines the need of institutional finance for rural development and analyses the different sources of rural credit (both institutional and non-institutional) available during the pre and post-independence era.

**Chapter V: Performance of Regional Rural Banks in India - A region wise Analysis** - Highlights the region-wise role of RRBs in India with respect to structural growth, deposits, advances, recovery performance, profitability performance, NPA analysis etc.
Chapter VI: Performance Analysis of RRBs in West Bengal - Makes an in-depth study on the role of RRBs in West Bengal and evaluates their overall performance.

Chapter VII: Comparative Study on the Performance Effectiveness of RRBs in West Bengal - Makes a comparative analysis on the performance effectiveness of nine RRBs in West Bengal.

Chapter VIII: Performance Effectiveness of RRBs in West Bengal and Rural Financial Institutions (RFIs): A Comparative Study - Makes a comparative analysis on the performance effectiveness of nine RRBs in West Bengal with the other Rural Financial Institutions (RFIs) operating within the same periphery.

Chapter IX: Conclusion - Presents a summary of the major findings and makes some conclusions.