A. Statement of the problem

The field of rural credit is varied and complex and the unsatisfied demand for credit is very large. Therefore new experiments and innovations for evolving new and bolder schemes for effective distribution of credit are to be made continuously. The demand for agricultural credit turned on a new and different dimension with the introduction of new agricultural strategy in the early sixties. It was felt that a single agency - the cooperatives - alone would not be in a position to tackle the problem of growing credit demands of the farmers. Cooperative finance has also often been considered inelastic, dilatory and inadequate largely owing to the inefficiency, high-handedness and selfishness of the managing committees and hence turned out to be 'closed shops' for the weaker sections. So a multi-agency approach was introduced by which commercial banks were roped in for providing credit to farmers. Subsequent to their nationalisation, these banks opened a wide network of

1. Panandhikar S.C., Banking in India, New Delhi, Orient Longman's, p.107
2. Government of India, Draft VI Five Year Plan, 1984, p.151
branches even in the remotest parts of the country with a view to extending credit to agriculturists particularly to small and marginal farmers, thereby supplementing the operations of the cooperative banks. But in actual practice, instead of supplementing the activities of cooperatives, they appeared to have supplanted cooperative credit and weakened it by taking away the good business of cooperatives, rather than providing more funds to rural areas, they channelized them to the urban and metropolitan areas. This was exactly the opposite of what was expected.

Although the cooperatives and the commercial banks did achieve significant progress in dispensing rural credit, they tended to reach the large farmers while the small and marginal farmers constituting a majority of rural population were neglected. The urban orientation of commercial banks and the domination of the affluent in the cooperative have made the institutional credit mere sour grapes for the rural poor. Evidently, it has become a plus point for the rural money-lenders to reinforce their monopolistic hold over the rural credit.

By and large, the cooperatives and commercial banks have not succeeded in 'absolute institutionalisation' of rural credit nor succeeded in meeting the credit requirements of weaker sections. It was thought at this juncture that a new agency combining the advantages of commercial banks and cooperatives—a synthesis of the best that is found operating in the cooperatives and commercial banks—should be established with the already existing financial institutions in the field of rural credit to cater to the credit needs of small and marginal farmers, landless agricultural laborers, rural artisans and rural entrepreneurs. The outcome was the advent of Regional Rural Banks in the rural credit scene in October 1975.

The Regional Rural Bank selected for the purpose of the present study was established on 9th March 1977 under the Regional Rural Banks Act, 1976. The area of operation has been confined to two districts namely, Tirunelveli and Ramanathapuram. It is sponsored by Indian Overseas Bank with the object of providing credit to small farmers, marginal farmers, landless labourers and rural artisans. Nearly

Note: At the time of selection of the present study, both Tirunelveli and Ramanathapuram Districts were undivided. But later in 1984 Ramanathapuram District was trifurcated and three districts have been created viz., Ramanathapuram, Pasumpon Thevar Thirumagan, and Kamarajar Districts. In 1986, the Tirunelveli District was bifurcated and two Districts are newly formed. They are Tirunelveli Katha-bomman and Chidambararanar Districts. Hence for purpose of analysis five district figures have been given.
one decade has passed (at the time of the study) since the establishment of Regional Rural Bank in Tamilnadu. What is the record of this new agency? Has it been serving the purpose for which it was organised? Has it been able to satisfy the credit requirements of the small and marginal farmers and thereby overcome the disadvantages of both cooperatives and commercial banks? Who are the beneficiaries of the loan? Are they benefited by bank loans? Is there employment creation and income generation out of loan activities to the beneficiaries? What about the repayment performance of borrowers of this bank? Has the bank been able to achieve viability through profitability over a period of ten years of its operation? These issues certainly call for a scientific investigation and hence this study.

B. Objectives:

The specific objectives of this study are:

i) to study the performance and progress of Regional Rural Banks in India;

ii) to assess the performance of the Pandyan Grama Bank (PGB) in Tamilnadu in terms of branch expansion, deposit mobilization, credit deployment, credit-deposit ratio, recovery and financial results;
iii) to study the operational efficiency of the branches in the two functional districts viz., Tirunelveli and Ramana-thapuram (later bifurcated and trifurcated respectively resulting in five districts);

iv) to assess employment creation and income generation among the sample borrowers through developmental credit as also to record the problems (if any) faced by them; and

v) to offer suggestions for improving the performance of the bank.

C. Hypothesis for testing;

The hypotheses formulated for the purpose of this study are:

i) The Pandyan Grama Bank in Tamil Nadu has recorded a higher growth rate in (a) number of branches; (b) deposits; (c) advances; (d) Credit-Deposit Ratio; (e) Recovery and (f) Profit over a period of time;

ii) The bank has attained its viability through profitability; and

iii) The higher the age of the bank the higher is the performance.
D. Operational definition of the concepts used in the study

**Credit:** In this study credit is defined as temporary transfer of funds which forms a contract for the future delivery of money by borrower to the lender.

**Financial Institutions:** (FIS) For the purpose of present study, the term 'financial institutions' refers to institutions like commercial banks, cooperative credit societies and Regional Rural Banks. They may also refer to apex bodies including refinance agencies.

**Weaker sections:** The Regional Rural Banks included the small farmers, marginal farmers, agricultural labourers, rural artisans and other persons of small means whose annual family income does not exceed Rs.4000, in the category of weaker sections.

In the present study also, the same criteria as adopted by the Regional Rural Bank has been considered for identifying weaker sections. A small farmer is one who possesses a land holding of 1.25 acres to 2.50 acres of class I irrigated land or 2.50 acres to 5.00 acres of dry land. The study considered persons whose land holdings are less than 2.50 acres of dry land or less than 1.25 acres of wet land as marginal farmers.
The landless agricultural labourer is defined as one who is employed in the field of others for wages in kind or cash and do not possess land of his own. The persons of smaller means like petty traders, hawkers, tea stall owners, transport operators, tailors, weavers, dhobies and other small traders are categorized as "small loanees".

Operational efficiency of Bank/Branch. Since the present study is confined to banking, operational efficiency of banks/branches refer to their ability to increase the operations in relation to i) productivity, ii) Cost efficiency and iii) profitability.

Productivity: The evaluation of efficiency or productivity in an industry where the output cannot be subjected to quantification, is met with many difficulties. The difficulties are particularly marked in a service industry like banking, whose 'output' consists not of a single type of service but a variety or 'bundle' of services. While evaluating the operational efficiency, productivity and profitability of public sector banks Divatia et.al developed and used the following indicators. They were (i) Total of advances and deposits per employee, (ii) Number of

deposit accounts per employee, iii) Total income per employee, (iv) Net income per employee, (v) Ratio of working funds to establishment expenses and (vi) Ratio of deposits to cash balances. Since the present study is confined to Regional Rural Bank and its branches and for assessing their operational efficiency in terms of productivity, six indicators have been identified and used on the basis of the indicators mentioned earlier. They are: (i) Number of deposit and advance accounts per employee; (ii) Deposits and advances amount per employee; (iii) Total income per employee; (iv) Net income per employee, (v) Volume of business per rupee of expenses on manpower and (vi) Percentage of cash balance to deposit.

Cost Efficiency; The working group on Regional Rural Bank has pointed out that the appraisal of the bank's working should be based both on the fulfillment of objectives and control of cost. The present study also aims at assessing the performance of the bank/branches in terms of cost efficiency. Cost efficiency refers to the ability of the bank and branches in controlling their operating cost. Operating cost is the cost incurred in order to provide services to different customers including borrowers and depositors. Operating cost includes wage, salary, cost and

all other expenses (printing, stationery, postage, rent, telephone etc.) excluding interest cost. Interest cost is an indicator of volume of business itself, it is more or less in proportion to deposits and borrowings. Therefore, it is rightly argued that it is the operating cost, instead of total cost, which might exhibit economies/diseconomies of scale in banking. Thus, it would be more appropriate to analyze the cost efficiency with respect to operating cost. Percentage of operating cost to volume of business is the indicator used for measuring the cost efficiency of the bank/branches.

**Profitability**: Profit is different from profitability. The profitability performance of bank/branches refers to the ability of the bank to earn profit. Varde et.al.\(^8\) developed a frame work for comparing the profitability performance of Regional Rural banks. It required working out of ten key indicators derived by relating various components of profit and loss account statement to a common denominator, volume of business (defined as balance sheet total less contra items). In the present study also, the profitability per-

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8 Granely Lyle E, A Study of Scale Economies in Banking, Federal Reserve Bank of Kansas City, 1962, p.3
formance of the bank/branch is assessed with the help of the same 10 key indicators. These indicators are listed as follows:

1. Interest Earned Ratio \( r = \frac{\text{Total Interest Earned}}{\text{Volume of Business}} \)
2. Interest Paid Ratio \( k = \frac{\text{Total Interest Paid}}{\text{Volume of Business}} \)
3. Manpower Expense Ratio \( m = \frac{\text{Total Manpower expenses}}{\text{Volume of Business}} \)
4. Other Expense Ratio \( o = \frac{\text{Other Establishment Expenses}}{\text{Volume of Business}} \)
5. Other Income Ratio \( c = \frac{\text{Non-Interest Income}}{\text{Volume of Business}} \)
6. Payout per employee Ratio \( m_1 = \frac{\text{Total Manpower Expenses}}{\text{Total Number of Employees}} \)
7. Volume of Business per Employee Ratio \( m_2 = \frac{\text{Volume of Business}}{\text{Total Number of Employees}} \)
8. Profitability Ratio \( p = \frac{\text{Profit Before Tax}}{\text{Volume of Business}} \)

Further, \( (r-k) \) is defined as spread ratio (9), \( (m+o-c) \) as burden ratio (10), and, spread ratio minus burden ratio which is \( p \), as the profitability ratio.

It is apparent from the definitions cited that for improving profitability performance, a bank has to aim at
increasing the magnitude of 'spread ratio' and lowering the magnitude of 'burden ratio'.

Increasing the magnitude of spread ratio can be achieved by increasing interest earned ratio 'r' faster than interest paid ratio 'k'.

Lowering the burden ratio can be achieved by lowering manpower expenses ratio 'm' other expense ratio 'o' and increasing other income ratio 'c'.

Lowering 'm' ratio can be achieved by increasing volume of business per employee ratio 'm2' faster than payout per employee ratio 'ml'.

Viability: Viability could be achieved through profitability. A bank is said to be viable if it attains a level of loan business giving it an income level which would enable it to meet not only all the expenses but also help it build a minimum reserve over a period of time. Specific criteria have been formulated and used by different groups and committees to measure the viability of Regional Rural Banks. They are:

i) The working group on Rural Banks had talked of four
dimensions for judging the viability of a rural bank. They are (a) Area Dimension - the areas which promise potential development; (b) financial dimension - this depends upon the variables, namely expenditure ratio and the level of income earned by the institutions (by expenditure ratio, the committee meant working of a rural bank on a low cost budget relating to staffing patterns, salary scales and other establishment expenses); (c) Time dimension - losses are likely to occur in the initial stages of banking operation and so viability could be achieved after some years, and (d) Task dimension - Regional Rural Banks have the social objective of 'widening the area of credit coverage'. Indeed the success of these banks should be judged as much by their efforts at expanding and extending the area of rural credit as by the conventional yardsticks of profitability. In short, viability should aim at securing a favorable cost-benefit ratio.

ii) The Review committee¹² viewed that a typical Regional Rural Bank (with 50 branches) would be able to become financially viable and generate profits beyond the Rs.3 crore level of annual loan business and that this could very well be achieved within a period of three to four years.

¹¹ Government of India, Report of the Working Group on Rural Banks, op.cit., p.15
¹² "Report of the Committee to Review the Working of Regional Rural Banks op.cit., p.6 7
iii) With the above factors in the background, the Reserve Bank of India Committee\(^3\) considered the following factors to ensure financial viability. On an average, a Regional Rural Bank would require about six years and a net work of 70 branches to become viable. For this, it is necessary that it reaches an outstanding loan business level of Rs.8 crores and also enjoys a margin of about 5 percent as between its average borrowing and lending rates.

For the purpose of the present study, the viability criteria laid down by the Reserve Bank of India Committee has been considered and used for assessing the viability performance of the selected bank.

Pre and Post Loan period. The evaluation and monitoring cell of the State Bank of India while evaluating the impact of its credit on weaker sections, followed 'before and after approach'. Under this approach, two reference periods were provided for which data were collected from the sample households or units. One of the two reference period was the 'post-loan' year, which was a complete year (financial, agricultural or calendar) immedi-

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ately preceding the data of survey, whereas the other reference period was the 'pre-loan year, i.e., the year immediately preceding availment of loan. It is also customary to select agricultural year (July to June) as the reference period for collecting data relating to agricultural schemes and calendar year/financial year for other schemes.

In the present study also, the approach as adopted by the State Bank of India has been considered for measuring the employment creation and income generation to the sample borrowers of the Bank. Two reference periods were also considered under this study, i.e., the 'Post-loan and 'Pre-loan' periods. The 'Post-loan' year, was a complete year (financial, agriculture, or calendar) immediately preceding the data of survey, whereas the pre-loan year, was the year immediately preceding availment of loan. For collecting data relating to agricultural loan schemes agricultural year (July to June) was adopted. For other loan schemes financial/calendar year was followed for collecting the data.

**Employment Creation**; For the purpose of present study, employment was measured in man-days of eight hours of work per day for men and two female or two juvenile labour days of eight hours of work were reckoned as one day. Employment created due to the loan activity in the family and the hired labour was considered. In the case of both family and hired labour, the hours of work turned out daily
was taken and converted into man-day units during the pre and post loan periods. It was assessed on per day basis. The difference between the man-days during the pre-loan and post-loan period is taken as employment created days in the post loan period over the pre-loan period.

Income generation: Income is an important variable which determines the pattern of consumption, savings and investments in households. In analysing income and income distribution, various concepts and measurements have been used by researchers and planners. In the study of functional income distribution, the meaning of income would be gross income or the value of total output which is the result of the combination of different factors employed. However, in the present study, family gross income is taken for consideration. The income of a household from all sources is the earnings - gross income - both in terms of cash and kind that accrued to and was realized by the members of the household during the pre and post loan periods as the case may be. This includes income from real property, business, profession and service, animal husbandry, fishing, hunting, wages, salary, bonus, commission, shop-keeping, financial assets, interest dividends and also transfer income such as...

pensions, social assistance and regular contributions from households and institutions other than Government. Since the present study also aims at assessing the impact of bank loan in terms of income generation to the sample borrowers, net income from the loan activity is also taken into account. For the purpose of our study, net income is calculated as follows:

\[
\begin{align*}
\text{Pre-loan net income} & = \text{Pre Loan Gross Income from the activity} - \text{Expenses} \\
\text{Post-loan net income} & = \text{Post Loan Gross Income from the activity} - \text{Expenses}
\end{align*}
\]

The difference between the pre and post loan net income is taken as income generation from the loan activities in the post loan period over the pre loan period.

E. Methodology:

This is an analytical as well as empirical study based on both secondary and primary data collected from the records of the selected banks/branches and sample borrowers.

i) Sampling Method Adopted:

Selection of the Bank: The study is confined to
Pandyan Grama Bank in Tamilnadu in the backdrop of Indian RRB experience. At the time of commencement of the research i.e., 1984, there was only one Regional Rural Bank (PGB) functioning in the State of Tamilnadu. The selection of the bank is based on the following considerations: The Pandyan Grama Bank is the first Regional Rural Bank established in Tamilnadu. For proper assessment of the performance of a Regional Rural Bank, it is necessary that it should have at least five years of sustained life. The selected Regional Rural Bank had more than five years of life at the beginning of the study.

**Selection of the Branches**: The universe of the study constitutes the Pandyan Grama Bank and its branches. All the branches of the Pandyan Grama Bank (158) functioning at the end of March 1989 were selected for the study.

The sample of the study thus includes one Regional Rural Bank with all its 158 branches.

**Selection of the Borrowers**: For selection of borrowers, five branches were randomly selected from the five operational districts of the bank. A list of borrowers who have availed loans is obtained from the respective branches. The list consisted of 3580 borrowers who borrowed in the year 1984. Out of the 3580 borrowers a sample of 358 borrowers (i.e. 10 percent of the universe) were randomly selected for the purpose of the present study, to ascertain
the impact of bank finance on them. A partially structured and pretested schedule was administered during the period between April to August 1988. The name of the districts with selected branches, the total number of borrowers who availed loans in the year 1984 and the sample size and the number of borrowers selected are given in the following table:

Table 2.1
Selection of the Borrowers.

<table>
<thead>
<tr>
<th>S.No.</th>
<th>Name of the Districts</th>
<th>Branch</th>
<th>No. of borrowers</th>
<th>Total</th>
<th>Sample size</th>
<th>Number of sample borrowers</th>
</tr>
</thead>
<tbody>
<tr>
<td>1.</td>
<td>T.K.District</td>
<td>A</td>
<td>840</td>
<td>10</td>
<td>84</td>
<td></td>
</tr>
<tr>
<td>2.</td>
<td>C.District</td>
<td>B</td>
<td>389</td>
<td>10</td>
<td>39</td>
<td></td>
</tr>
<tr>
<td>3.</td>
<td>R.District</td>
<td>C</td>
<td>803</td>
<td>10</td>
<td>80</td>
<td></td>
</tr>
<tr>
<td>4.</td>
<td>PMT District</td>
<td>D</td>
<td>768</td>
<td>10</td>
<td>77</td>
<td></td>
</tr>
<tr>
<td>5.</td>
<td>K.District</td>
<td>E</td>
<td>780</td>
<td>10</td>
<td>78</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td></td>
<td></td>
<td>3,580</td>
<td>10</td>
<td>358</td>
<td></td>
</tr>
</tbody>
</table>

Note: TK - Tirunelveli Kattabomman? C - Chidambaranar R - Ramanathapuram; PMT - Pasumpon Thevar Thirumagan; K - Kamarajar District

ii) Tools for Data Collection:

Bearing on the objectives of the study, two schedules have been drafted; one for the bank and its branches and another for the borrowers. The schedules were finalised after pretest. The first schedule for the bank aimed at seeking data on the origin of the bank, branch expansion,
deposit mobilization, credit deployment, credit-deposit ratio, recovery of loan, volume of business, income, expenditure, profit and loss and related matters. The second interview schedule for the selected (sample) borrowers was broadly divided into three parts: The first part contained questions relating to borrower's personal data, viz., religion, caste, sex, age, education, occupation, marital status, land holding, income, expenditure, savings etc., The questions in the second part were confined to various aspects relating to loan particulars. The third part comprised questions on the impact of loan and borrower's views on the bank. While the data on the first and the third parts were collected directly from the respondents, the data on the second part were elicited directly from the branches from where the respondents had raised their loans.

iii) Sources of Data:

Data were collected from both secondary and primary sources. Secondary published sources includes reports of currency and finance. Reserve Bank of India bulletins and statistical statements relating to banking and Regional Rural Banks published by the Reserve Bank of India and National Bank of Agriculture and Rural Development, Annual Reports of the financial institutions concerned, Credit plans and in-depth studies on various Districts, Report of the Banking Commission, various committee reports of the
Reserve Bank of India, Plan documents of Government of India etc., Besides, information from individual research works, the Reserve Bank of India Officers – Madras, the NABARD office – Madras, the Head Offices of various lead bank functioning in the districts, the District Collector's office of the concerned districts were also collected.

Relevant information has also been elicited by holding discussions with officials of the Regional Rural Bank, Commercial and Cooperative banks in the operational districts of the bank.

The primary data was collected from the sample units by interviewing them.

IV) Reference period:

Data regarding branch expansion, deposits, advances, credit-deposit ratio, recovery, over-dues, income, expenditure, profit and loss and staff were collected from the Pandyan Grama Bank for a period of 12 years (1977 – 1989). Data and particulars on various aspects of branch performance were gathered for five years from 1984 to 1989. Survey of the borrowers was carried out during the period between April to August 1988. For studying the performance and progress of the Regional Rural Banks in India, data and information were gathered from the secondary source for a period of 13 years i.e. from December 1975 to June 1988.
Plan of analysis:

The plan of analysis includes adoption of techniques like ratios, percentages, averages, compound growth rate, simple correlation and regression. Average and percentages were used to present the profile and performance of the bank with reference to branch expansion, deposits, advances, funds, recovery, over-dues, income, expenditure and profit/loss. The percentages, averages, indices were also computed for all the branches as a whole and compared with branches in each district.

Operational efficiency of the bank and its branches in terms of productivity, cost efficiency and profitability performance were analysed by computing 'ratios'. Correlation technique was employed to find out the relationship between the age and performance of the bank. The same statistical technique was employed to study the relationship among the independent variables like, age, branch, deposits, advances, borrowings, reserves, volume of business, income, expenditure, profit, staff and overdues.

For studying the influence of factors on profitability, co-efficient of correlation between the dependent variable and the independent variables was calculated. The co-efficient of correlation between profitability and measured independent variables were put to regression analysis to
explain the extent of variance of the dependent variable by the independent variables combined. The 't' test was applied to test the level of significance of correlation.

Compound Growth Rate was computed for measuring the growth of independent variables like branch expansion, deposit, advances, income, expenditure staff and so on in the case of Pandyan Grama Bank during 1977 - 1989.

(F) Limitations:

Though the study is mainly confined to a Regional Rural Bank and that too in the state of Tamilnadu, it also reviews the performance and progress of Regional Rural Banks all over the country for a period of thirteen years. The study attempts an analysis of the performance and the operational efficiency of the Pandyan Grama Bank and its branches at the micro level, in terms of productivity, cost efficiency, profitability and viability. In addition a micro level study of the sample borrowers has been undertaken. All these aspects of the present study would bring out the level of achievements of the goaIn of Pandyan Grama Bank as specified in the scheme of Regional Rural Bank. Due to constraints on time and resources, only 358 borrowers from the five operational districts representing five branches have been selected for the study. In the case of certain branches, required data relating to one or two aspects for the
earlier period could not be secured. However, this did not come in the way of overall framework of the study.

The micro level study of assessment of the performance and operational efficiency of the Regional Rural Banks has brought out certain deficiencies in the functioning of Regional Rural Banks. As such, the findings and the suggestions based on them would provide certain guidelines for future planning and implementation of the Regional Rural Bank' schemes at the district level not only in the study area but also in other parts of the country.
CHAPTER III