CHAPTER – III

REGIONAL RURAL BANKS:

GENESIS AND RATIONALE OF THE SCHEME
3.1 **Historical Background:**

The Banking Commission\(^1\) (1972) made the recommendation that a chain of Rural Banks be established in addition to the regular branches of commercial banks already operating or to be opened in rural areas. It was of the opinion that in a country like India where diversities abound, any single type of financial institution to meet the financial needs of people in rural areas, would not be an appropriate method of dealing with the problem of rural credit. The Commission therefore, recommended a multi-pronged programme where co-operative credit societies, branches of commercial banks and specially sponsored Rural Banks were to play their role. It was clearly felt that co-operative societies would not succeed in every region of the country, whereas opening of branches of commercial banks in rural areas had its own limitations. Hence emphasis is on specially sponsored Rural Banks. In its report it was observed that the primary credit societies neither provided credit for all productive activities of cultivators, nor met their credit needs.

The salient recommendations of the Banking Commission can be summarised as follows:

1. S.S.M. Desai, *Rural Banking in India.*
A rural bank has to act as a primary banking institution which should serve a population ranging from 5000 to 20000.

It is expected to mobilise the savings lying idle in the villages by accepting deposits in different forms. It shall act as an agent of development by providing short and medium term credit. It shall provide other banking services to the local people. It shall extend a helping hand to small and marginal farmers by supplying them inputs and providing them marketing assistance. Thus the rural banks shall act as instrument for all round and multifarious development of villages.

It is painful to note that the recommendations of the Banking Commission went unheeded for three years i.e. upto June, 1975, when long-felt need was fulfilled by the establishment of Regional Rural Banks to provide rural credit through an ordinance, which became an act after the Parliament passed in on 9th February, 1976. In the mean time, on the recommendation of the Banking Commission made in 1972, to establish a chain of rural banks, working Group on Rural Banks was set-up, under the Chairmanship of Shri M.Narasimham, to study the possibilities of establishing such banks. The Committee submitted its report in a record time of one month, on 30th July, 1975.
The Working Group headed by Shri M.Narasimham had observed that "the existing institutions, as they are presently structured would not be able to fill the regional and functional gaps in the rural credit institutional system, within a reasonable period of time, even with adoptations, reorganization and restructuring as may be considered". It further observed, "In a country of the size and regional diversity as ours, no single pattern, be it commercial banking or co-operative credit, can be expected to meet all the emerging requirements in all areas. A degree of adaptation and improvisation is called for and the range of institutional alternatives widened. It is in this context that we have come to the conclusion that a new type of institution is necessary".\(^2\)

"What is needed", observed the Narasimham Committee, is "an institution which combines the local feel and familiarity with rural problems which the co-operatives possess and the degree of business organisation, ability to mobilise deposits, access to central money market and a modernised outlook which the commercial banks have".\(^3\)

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2. Quoted in the report of the working Group on Regional Rural Banks, 1986.

3.2 **Genesis of RRBs:**

Acting upon the recommendations, the Government of India promulgated an ordinance on the 6th September, 1975 and thereunder the first five Regional Rural Banks (RRBs) were set up on the 2nd October, 1975. Names of sponsor banks and the first five R.R.Bs opened in the country are as follows:

<table>
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<tr>
<th>Sl. No.</th>
<th>Sponsor Bank</th>
<th>R.R.B.</th>
<th>H.O.</th>
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<tbody>
<tr>
<td>1</td>
<td>Syndicate Bank</td>
<td>Prathama Bank</td>
<td>Moradabad (U.P.)</td>
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<tr>
<td>2</td>
<td>State Bank of India</td>
<td>Gorakhpur Kshetriya Gramin Bank</td>
<td>Gorakhpur (U.P.)</td>
</tr>
<tr>
<td>3</td>
<td>United Bank of India</td>
<td>Gaur Gramin Bank</td>
<td>Malda (W.B.)</td>
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<tr>
<td>4</td>
<td>Punjab National Bank</td>
<td>Haryana Kshetriya Gramin Bank</td>
<td>Bhiwani (Haryana)</td>
</tr>
<tr>
<td>5</td>
<td>United Commercial Bank</td>
<td>Jaipur Nagaur Anchalik Gramin Bank</td>
<td>Jaipur (Rajasthan)</td>
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</table>

The following objectives were visualised for the establishment of RRBs:

1. to develop rural economy;
2. to provide credit for agriculture and allied activities;
3. to encourage village industries, artisans, blacksmiths, carpenters etc.;
4. to reduce dependence of rural people on money-lenders;
5. to fill the gap created by moratorium on borrowings from money-lenders;
6. to help the poor financially for their consumption needs;
7. to reach those far-flung areas, particularly backward and tribal areas and to make these areas economically better by opening branches or agencies at any place in the area.

The sponsor bank will aid and assist the RRB sponsored by it in several ways. The sponsor Bank shall subscribe to the share capital of RRB; it will assist the RRB in its establishment, recruitment, training of personnel and in general such managerial and financial assistance as may be mutually agreed upon between sponsor Bank and the RRB.

A Regional Rural Bank shall have its head office at such in the notified areas as the Central Government may specify by notification in the official gazette. The Government shall consult Reserve Bank and Sponsor Bank in the matter.

In fine, the conditions which necessitated the establishment of RRBs in the country were weaknesses of the co-operative credit structure, poor coverage by commercial bank branches and adequate potential for agricultural development.

3.3 **Main Features of RRBs:**

As stated earlier, the Regional Rural Bank Ordinance, 1975 was later on replaced by the Regional Rural Bank Act 1976. The Act has made various provisions regarding the incorporation, regulation and working of the Regional Rural Banks.
(A) **Capital Structure**:

As provided in Chapter II, "Incorporation and Capital of Regional Rural Banks" (the RRB Act 1976, Section 5), "The authorised capital of each RRB shall be one crore rupees, divided into one lakh of fully paid-up shares of one hundred rupees each". The issued capital is fixed at twenty five lakhs of rupees. The issued capital shall be subscribed in the following manner:

- Central Government: 50%
- Concerned State Government: 15%
- Sponsor Bank: 35%

The shares of RRB are deemed to be securities enumerated in section 20 of the Indian Trust Act, 1982 and approved securities for the purpose of Banking Regulation Act, 1949.

(B) **Management**:

The management of RRBs is, at present vested in the 9 member Board of Directors, headed by a Chairman, who is appointed by the Central Government. The Central Government and the 'Sponsor Bank' nominate not more than two members each while State Government nominates not more than two members on the board. The Central Government nominates one of its officers as nominee of the Government of India on the Board of each RRB.
(C) **Functions:**

The activities of RRB comprise the following:

(i) To receive from the rural areas current Deposits, Saving Bank Deposits, etc.;

(ii) to provide financial assistance to the priority sector;

(iii) to extend necessary banking facilities to remote areas;

(iv) to act as vital instrument in the implementation of Government sponsored schemes for rural development namely, the Integrated Rural Development Programme (IRDP), Twenty-Point Economic Programme, District Credit Plans (DCP), Differential Rate of Interest Scheme (DRI), NABARD Scheme, District Annual Action Plan;

(v) to adopt villages in the areas of operation and bring about overall economic development of such villages.

(D) **Special Concession to RRBs:**

To achieve viability of the RRBs, the Reserve Bank of India has granted the following concessions:

(i) Statutory Liquidity Ratio (SLR) to be maintained 25 per cent as against 35 per cent by commercial banks (Section 24 of BR Act 1949).
(ii) RRBs are allowed to pay half a per cent higher interest to its depositors than the interest rate offered by commercial banks to their depositors.

(iii) Cash reserve requirement of 3 per cent to be maintained with the Reserve Bank of India as against 9.5 per cent by commercial Banks (Section 42 of RBI Act, 1934).

(iv) They are allowed to charge interest on their direct loans at par with the rate charged by the primary agricultural co-operative societies (PACS) to its clients.

(v) They are allowed to draw refinance from RBI, now from NABARD, to the extent of 50 per cent or more depending on the type of advance of the eligible outstanding loan at a concessional rate of interest at 7 per cent per annum.

(vi) Similarly, refinance to the extent of 30 per cent of eligible outstanding loans can be drawn from the sponsoring bank at a concessional rate of 8.5 per cent per annum.

(vii) They are entitled to get 9 per cent interest on the balance maintained in the current account by them with the sponsor bank.
(viii) Sponsor bank deputes its own staff to manage the RRB branches till the time RRB is able to recruit its own staff.

(ix) All the salary, allowance, etc. of such deputed staff are borne by the sponsor bank.

(x) Free remittance is to be allowed in the multiple of Rs.5000 between the Head Office of RRB and its different branches through the office of the Public Sector Banks.

(xi) Salary, allowance, etc. of the Chairman of RRB is also borne by the sponsor bank.

(xii) Sponsor Bank arranges for training of RRB staff in its training establishment at its own cost. Further, sponsor bank also bears the expenses for training RRB branch managers at the College of Agricultural Banking, RBI, Pune.

(E) **Insured Status**:

The Regional Rural Banks are registered as insured banks with the Deposit Insurance Corporation. All deposits upto Rs.30,000 per depositor in the same right and capacity in each bank are accordingly with the Deposit Insurance Corporation of India, thus providing protection to depositors.
(F) **Refinance Facilities from NABARD**

At present Regional Rural Banks are provided refinance facilities on a composite basis. With effect from July 1984, NABARD has revised its refinance policy whereby Regional Rural Banks, which have completed five years of operation (as on 1.7.84), will be provided two separate refinance limits for short-term and medium term (non-schematic) lendings. Similarly, sanctioning limits for Regional Rural Banks, which have not completed 5 years, has been discontinued from 1986-87.

All RRBs, irrespective of their age, are eligible for refinance under Section 21 of the NABARD Act, for short-term (ST) credit limits. The proportion of involvement amongst NABARD, sponsor bank and RRB in ST advances is given in Table 1.

The short-term credit limit is operative for a period of one year, i.e. co-operative year (July to June). This is a revolving credit limit in the sense that drawal and refinance will be made any number of times during the period. The refinance will be available at 3 per cent below the bank rate.

### Table 3.1

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<th>Advances as on 31.3.86</th>
<th>Rate of involvement (%)</th>
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<tr>
<td></td>
<td>NABARD</td>
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<td>Below Rs. 800 lakhs</td>
<td>50</td>
</tr>
<tr>
<td>Above Rs. 800 lakhs</td>
<td>40</td>
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Similarly, medium-term credit (MT) limit will be sanctioned under section 24 of the NABARD Act, 1981 for investment purpose for agricultural and allied activities and Rural Development including term or composite limits for artisans or village/cottage/tiny industrial units. Refinance would be limited to the extent of 60 per cent of the RRBs eligible MT (non-schematic) loans. The involvement of the RRB in such loans shall at no time be less than 10 per cent. The balance of 30 per cent is exempted to be met by the concerned sponsor bank.

The MT credit limit is sanctioned for a period of one year and is repayable to RRBs at 3 per cent below the bank rate.

(G) Training Facilities:

It has been decided that the recruitment of managerial, supervisory and clerical staff of the RRBs should be from within the area of operation of each bank concerned on the scales of pay and allowances as are admissible to the employees of the State Government concerned. Help is given to the RRBs to undertake the task of providing training to the Chairmen and Branch Managers of the RRBs to be conducted at the College of Agricultural Banking, Pune. The training of accountants, field officers and clerks will be conducted at the training centres of the respective sponsor banks under the overall supervision of the College of Agricultural Banking.
Steering Committee for Co-operation:

The Government of India has set up a Steering Committee at the national level to work out details of the working of RRBs, to monitor their programme/progress and to provide suitable guidance to them.

At the state level, there are state level Co-ordination Committee to monitor the progress of RRBs in the state and to work plans for their progress. The Committee co-ordinates the work of RRBs in the state and provide necessary guidance to them.

Rationale of the Scheme:

The working of the RRBs was reviewed and evaluated by the Dantwala Committee in 1977. The Committee in its report submitted on February 16, 1978 observed that "the performance of the Regional Rural Banks has proved that they can become a very useful component in the totality of rural credit structure. In fact, such an institution is needed to make good some of the inadequacies in the existing rural credit system". The Committee recommended, that over a period of time, the rural branches of the Commercial Banks to be totally replaced by the RRBs and their branches so as to make the RRBs an integral part of the rural credit structure.

The Committee was of the opinion that, "ideally, the jurisdiction of a rural bank (RRB) should be confined to one
district. Since the size and the state of economic development of district vary a great deal, it is advisable to retain some flexibility in this and other related matters. The contention of the Committee was that one RRB should cover a population of 10 to 20 lakhs. From the angle of financial viability and managerial efficiency, the reasonable number of branches of each RRB should be between 50 to 60. Each RRB branch would cover approximately a population of 20,000. The Committee expressed satisfaction over the locational planning of the RRBs and their recovery performance. It hoped that RRBs would be able to attain financial viability in 3 to 4 years.

One more study was conducted by the Rural Planning and Credit Cell of the Reserve Bank of India on the 'viability of Regional Rural Bank's' in April 1980. This study has pointed out that three-year period is generally not sufficient period for a credit agency to achieve financial viability, particularly for a rural credit agency like that of RRB with its unique characteristics such as:

(i) lend only to the weaker sections,
(ii) charge lower rate of interest,
(iii) open branches in remote rural areas, and
(iv) keep up low cost profile.

The RRBs have a number of teething troubles including the staff orientation for rural lending work. Notwithstanding these limitations, the findings of the study have shown that the performance of the RRBs have been encouraging.
Before the advent of RRBs in 1975, it is the Commercial Banks and Co-operatives which were functioning in rural areas. The Commercial Banks have made a considerable progress by establishing 52 per cent of their branches in the rural areas. Similarly, Co-operatives have been in existence in the rural areas since long. It is the RRBs which are comparatively new in this field.

Some people consider the establishment of the Regional Rural Banks as a duplication of banking services in the rural areas and is a prodigal waste of time and resources. They contend that it would have been possible for us to obtain the same results by restructuring the then banking system. But we should note here that the role of RRBs is complementary and not competitive. India being a very vast country in size, there is a lot of scope for different agencies to co-exist without affecting much the working of others. Since the RRBs are sponsored by the Commercial Banks and supported by the Government, there hardly arises any question of their competing with Co-operatives.

The report of the National Commission of Agriculture throws more light on justification of establishing RRBs. It has estimated the gross credit requirements of agriculture to be met from institutional sources at Rs.16,480 crores by 1985. With increasing emphasis on rural development under plans, this estimate is likely to go up further. When we consider the
magnitude of the task and the area to be covered, it is clear that no single agency would be able to meet the entire credit needs in the rural sector. The vast and growing gaps in agricultural credit make it necessary for us to try all possible alternatives and accept multi-agency approach to the credit delivery system. According to the report of the "Working Group on Multi Agency Approach in Agricultural Finance", with different credit institutions functioning in the field agricultural credit certain problems crop up. But they could be overcome by introducing certain measures. For example, it suggested that the area of operation of each agency could be demarcated. It emphasised on geographical demarcation rather than functional jurisdiction. It advocated the regulation of unnecessary proliferation of branches where the network of co-operatives is fairly adequate. Thus, the establishment of RRBs is justified on the ground that we have accepted multi-agency approach to the credit delivery system and in a vast country of our size there is a scope for co-existence of different agencies.

Thus the Regional Rural Banks occupy a pivotal place in the credit delivery system of India. They have been regarded the potent instrument of rural development. They have been catering to the needs of the weaker sections of the community. Rural development is the major theme of their working. Though there are a large number of agencies functioning in the rural India, the RRBs have a distinct role to play. They are established to develop the rural economy by eradicating poverty.
through the provision of credit and generation of adequate employment in the villages. RRBs provide credit to that section of rural community which has suffered for centuries at the hands of landed aristocracy. This section of people has been living below poverty line for ages. It consists of small and marginal farmers, landless labourers, small traders and rural artisans. To make their living better, RRBs have a special role to play. The other agencies in the rural credit market have been providing credit to the non-target population. The potential target population remained totally neglected till recently. Hence, the RRBs have now been considered active agents of economic development in the rural India.