Chapter-1

The Design and Execution of the Study

1.1 Introduction

Cooperative banking institutions in India have made a substantial progress in dissemination of banking services based on cooperative principles \((RBI: 2006-07, p.118)\). Since the network of cooperative banks was widespread across different parts of the country these institutions are considered as a potential instrument to bring people from far-flung areas under the formal banking network. Urban Cooperative Banks are an integral part of the cooperative banking system operating in the country. They have an important role to play in the financial system in channeling resources and bridging the financing gaps for small scale industries, small and medium enterprises and other small borrowers. UCBs have made rapid strides in resource mobilization and deployment. During the period, between 1991 and 2004, the UCB sector witnessed substantial growth possibly encouraged by the liberalized policy environment in post reform period \((RBI: 2010-11, p.107)\). However, the financial health of most of the UCBs has been a cause for concern and has so far proved to be a serious handicap in reaching out to the larger population. Keeping in view the heterogeneity of this sector, the Reserve Bank of India proposed a multilayered regulatory and supervisory approach specifically aimed at revival and strengthening of UCBs in its Vision Document for UCB sector, 2005. In the Vision Document the Reserve Bank of India proposed merger/amalgamation of viable entities within the sector and non-disruptive exit of the unviable ones.

As a result of the new initiatives and sustained efforts by RBI, the number of financially weak UCBs has declined drastically. Further, due to consolidation in the sector, on account of closures and mergers, the number of UCBs came down from 1813 as on 2006-07 to 1579 as on 2014-15 and further to 1574 UCBs as on 2015-16. The sector has recorded growth and
financial strength after consolidation. The deposit position of UCBs had been increased from Rs.1209.83 billion in 2006-07 to Rs. 3921.79 billion in the year 2015-16 alongside the loans and advances which increased from Rs 786.60 billion in 2006-07 to Rs. 2450 billion as on 2015-16. The Gross Non-Performing Assets (NPAs) has decreased from 15.5 per cent to 5.7 per cent in the same period. However, this growth was not uniform across the country as a few UCBs grew exponentially during the period. In the process, some UCBs acquired the size of smaller commercial banks (RBI, 2015, p.1).

1.2 UCBs in Tamil Nadu

As far as Tamil Nadu is concerned, there are 120 UCBs functioning as on 2016-17. All the UCBs provide banking facilities to urban and semi-urban population. They mobilize deposit from the public and extend credit facilities to small traders, artisans and persons belonging to middle-income group for purposes like housing, business, education, consumer and other non-farm sector activities. During 2016-17, the loans extent of Rs. 4391.72 crore has been disbursed. The deposit in the UCBs improved from Rs 8244.76 crore as on 2015-16 to Rs 8444.31 crore as on 2016-17. In 2016-17, the UCBs formed 1617 Joint Liability Groups (JLGs) of petty traders in urban areas and issued loans to the tune of Rs. 59.91 crore. This has prevented many small vendors from falling prey to money lenders, who charge exorbitant interest rates (Government of Tamil Nadu 2016-17, p. 40). The UCBs are advised to issue not less than 40 per cent of their total lending to priority sector. Besides it is to be ensured that at least 10 per cent of the priority sector allocation shall be issued to the weaker sections of the community.

The State Government has also signed a Memorandum of Understanding with the Reserve Bank of India to improve the functioning of UCBs. Accordingly, all the UCBs and their branches have been computerized. Establishment of Core Banking Solution for all the UCBs and
their branches is under implementation in order to improve their operational efficiency and to provide better services to the customers. ([www.tn.gov.in]).

1.3 Statement of the Problem

UCBs play an important role as financial intermediaries in urban and semi-urban areas in Tamil Nadu. These banks were traditionally centered around communities, localities, workplace groups who essentially lend to small borrowers. As UCBs are primarily cooperative societies, they are subject to dual control. While there has been an improvement in the financial performance of the UCBs in recent times, the high level of NPAs continues to pose a threat to the financial health and viability of certain UCBs. These trends slowly erode public confidence posing a systematic risk, which affects UCBs adversely with regard to liquidity and impair their ability to render banking services to weaker sections. The weaker sections of the community who depend on UCBs alone for their credit requirements in urban areas are pushed to open market, wherein the usurious practices of money lenders dragged them into the valley of indebtedness. Further, they could not come out of the clutches of money lenders easily. The street vendors, petty traders, daily wage earners etc., who depend on UCBs are severely and severally affected due to the problem of the poor financial health of UCBs. If these UCBs are financially sound they can easily protect the interest of weaker sections by providing them with needed banking services. However, certain UCBs are financially sound and they are competitive amidst the existence of public and private banking industry. These UCBs are able to render better services to their members and justify their existence. In this context this study attempts to find answers to certain questions viz., how do UCBs perform in Tamil Nadu? What are the factors that contribute to making the UCBs financially viable? What are factors that made certain UCBs financially weak banks? There are certain other related questions needed to be addressed through micro-level studies. Hence this
The present study is undertaken entitled “A Study on the Financial Viability of Urban Cooperative Banks in Tamil Nadu”.

1.4 Review of Literature

UCBs occupy a significant place in Indian banking system in general and cooperative banking, in particular. Hence, the performance of UCBs attracts studies from RBI, other development institutions and social scientists. As UCBs was brought under prudential norms since 1992-93, several studies were conducted on the financial adequacy and NPA in UCBs. Here an attempt has been made to review the studies conducted on the performances of UCBs in India and Tamil Nadu, so as to establish the scope for the present study.

The RBI survey on urban banks (1957-58) has pointed out the importance of owned funds as, the liability of urban banks being limited; they find it necessary to build up substantial owned funds which provide the base for outside borrowing. The maximum borrowing power of an urban bank, which is the limit for its deposits and other borrowings, is fixed as a multiple of its owned funds under the rules framed under the cooperative societies Act or in its own bye-laws.

*The Varde Committee* (1963) has also pointed out that the liability of members of urban banks is generally limited which is necessary in view of the fact that the membership is large, dispersed and diversified and mutual knowledge and cohesion cannot exist to the same extent as in villages. They, therefore, find it necessary to build up substantially own funds which provided chief security for outside borrowings.

Shirish and Kulkami, R. (1996) while studying the performance of UCBs in Vadodora, Gujarat found that women and people from weaker sections were less attracted by the urban banks for membership, borrowings and deposits.
Dash, N.K. (1997) studied income recognition, asset classification norms and reduction of NPA's in UCBs. The study found that an insight into the complexities of recovery management and the role of recovery as a key performance area in order to prevent the blockage of huge finds in non-performing assets.

Mahadevappa, B and Girisha, B.N. (2001) in their study found that the main contributing factors for the sound profitability position of the Sri Kannikaparameshwari UCB was an increase in total income, decrease in operating expenses, increase in the marginal level of income through interest on loans and advances and other income, etc.

Veerkumaran, G. and Subash, B. (2001) in their study found that rising percentage of overdue indicates the bank's slackness in collection policy and this trend has thus become a warning signal for the bank to strengthen its recovery machinery.

Subburaj and Karunakaran (2002) in their study mentioned that the viability of a UCBs depended on the volume of business, a good service mix cost efficiency and a sound system of NPAs reduction.

Samwel Kakukolopoytum (2003) found that there had been a steady growth in membership, share capital, reserve fund, loans and advances over the study period. There were fluctuations in loan recovery. Further it was also found that the success of bank was due to better quality of service and efficient management.

Contrary to the above trend, Vinash, A. and Raikar, V. (2004) in their study concluded that the reforms have slowed down the growth rate of trends in share capital, owned fund, deposit, investment, loans and advances and net profit. In recent years, competitions between the banks have intensified but this has not adequately affected the capacity of the Goa UCBs to grow and make profits. Masali (2004) conducted a study on the performance of UCBs in Belgum. The study found that the average cost of
funds, the average yield on assets and the net margin were lower than normal and exhibited their poor recovery performance, high cost of management and high cost of funds.

Raikar, V. and Vinash, A. (2005) attempted to evaluate the impact of reforms on the growth, functioning and performance of UCBs in India. The performance of UCBs was compared with other cooperative and commercial banks and it was found that the performance of UCBs was better as compared to that of other banks. But due to application of Prudential Norms, their performance deteriorated since 2001-02. But since the performance was improving and it was found that the imposition of norms by Reserve Bank of India (RBI) has improved the confidence among people.

Teli, R.B. (2005) attempted to evaluate the performance of UCBs in Kolhapur District of Maharashtra State for a time period of 1991-2004. The performance was evaluated from different angles and it was found that UCBs in Kohlapur District showed a considerable growth in deposits, loans and net profits. At the same time the amount of overdue was also increasing.

Namasivayam (2006) study found that the performance of the bank had been quite impressive in terms of deposit mobilization and credit deployment. It was also found that the success of the cooperative bank depends on effective manpower, planning and management.

Ramu, N. (2007) analyzed that SriLakshminarayana UCBs have shown a considerable increase in their numerical strength of membership, share capital, reserves, deposits, and working capital. The study found that the deposit was the major sources of resources for this bank. The share of fixed deposits in the total deposits was 83.12 per cent. These banks do not depend on borrowings for mobilizing resources. The accumulated reserves were 3.39 times of the share capital. Working capital of the bank showed an average growth rate of 11.66 per cent during the study period.
Ramu, N. (2008) analyzed the business performance of selected UCBs in India and Tamil Nadu. It was found that the UCBs in Tamil Nadu have not succeeded in achieving the all-India average in terms of share capital, reserve fund, borrowings, deposits, loans and advances. It is to be noted that the number of UCBs in Tamil Nadu showed a decreasing trend whereas it showed an increasing trend in India during the nine-year period.

Vasanthi, S. (2008) found that the performance with regard to coverage of membership, mobilization of share capital, allocation of reserves, and collection of deposits, lending and recovery of loans showed a fair performance in Coonoor UCB. This UCB had a vast potential for generating self-employment opportunities in the non-institutional segments of the economy in its area of operation.

Ramesh, R.P, et al., (2009) analyzed the performance of UCBs by using CAMEL model. The study found out that Pattukkottai UCB has succeeded in maintaining CRAR, at a higher level, than the prescribed level. The dependence of debt capital had decreased in case of all the three banks during the study period. The Nicholson UCB outperformed in terms of liquidity position than other UCBs. The earning capacity, measured in terms of the ratios showed that PUCB has outperformed NTCB and KDCUB except in the ratio of interest income to total income.

Alok Goyal and Harvinder Kaur (2011) found in their study that the situation of NPA in UCBs had improved over the period of study. But in 2007-08, the NPA in these banks grew in comparison to the previous year. In general, it was concluded that the position of NPA had improved considerably. Most of the UCBs had CRAR ratio of more than 9 percent. It was also found in the study that ROA exhibited in the years 2008-09 and 2009-10 and actual ROA deviated from its potential throughout the decade.
Jyoti Gupta and Suman Jain (2012) in their study found that the financial performances of UCBs improved in 2010-11 though there were some concerns with regard to some of the UCBs reporting negative CRAR.

Vilas Bhikaji Khandare (2012) study found that the owned capital, working capital, deposits, loans and advances, reserves and paid up share capital of UCBs in Beed District showed on average positive growth rates during the study period. The increasing share of reserves and decreasing share of paid up share capital in total owned funds indicated the increasing self-reliance. Jawahar Babu (2012) found that the UCBs were a key sector in the Indian Banking scene, which in the recent years has gone through a lot of turmoil. Though some UCBs have shown credible performance in the recent years, a large number of banks have shown discernible signs of weakness. The operational efficiency was unsatisfactory and characterized by low profitability, ever growing Non-Performing Assets (NPA) and relatively low capital base. Also UCBs had not been able to service the growing credit requirements of clients or the newer demands for loans in the field of personal finance.

Padmaja, B. and Bhanu Kiran (2013) analyzed and found that there was significant growth in the Deposit Mobilization, Loans and Advances, working capital, reserves and owned funds. It was also found that there was no significant growth in membership but there was significant growth in share capital per member with CGR of 9.43. There was significant increase in the total cash with the bank. There were significant differences in the growth and composition of income. Even though there was an increasing trend in the Net Profits earned during the study period, except in the year 2006-07 it was statistically insignificant. However the performance of Aanathapur UCB was satisfactory.

Shreekar Acharya (2013) found that, in terms of Capital Adequacy, Mahila Cooperative Bank has the top position. In the case of Earning
Quality, Asset Quality and Liquidity aspects Sri Matha Cooperative Bank has held the top position. In the case of Managerial Efficiency, it is Sri Lakshmi Mahaila Sahakari Bank Niyamitha which holds the top position.

Jawhar and Kabar (2014) found that the lack of professional attitude in the management as well as employees and the political interference were the main causes of the problem faced by NPA in this study. It was also found that a high amount of NPA had resulted in low profitability.

Reena (2014) found that the Noida UCB was the least efficient bank. The reasons for inefficient of Uttar Pradesh banks were less number of bank branches, high cost of doing business and low capital base. UCBs need a combination of new technologies and better processes of credit and risk appraisal, treasury management, product diversification and infusion of professionalism.

Bharati, R. and Hiremath (2014) in their study on selected UCBs in North Gujarat, found that the UCBs were facing problems of high cost of business operations, low capital base, inadequate loan appraisal and credit planning, poor recovery performance, dual control, mounting overdue, high level of nonperforming assets, political influence, lack of professional skills and relatively low level of customer satisfaction, etc. But some of the new challenges were external; for example, the phenomenal growth in the volume of the financial institution. These were a big hurdle in the development of the UCBs.

Krupa and Trivedi, R. (2014) analyzed the performance of UCBs by using CAMEL model. This study found out that overall state of capital adequacy of Surat People Cooperative Banks was satisfactory. As far as loan portfolio was concerned, the overall state of assets quality was also good. The management efficiency was also satisfactory. Though the overall earning capacity of the bank was not bad the overall state of liquidity was not satisfactory.
Anitha, N. and Karthikeyan, M. (2015) in their study found that the Namakkal UCBs performed successfully by satisfying the customers in their area. The management of liquidity of the UCBs was successful throughout the study periods. Among the liquidity funds, owned funds were less than the borrowed funds.

Vinatikumar, E. and Veerakumaran, G. (2015) conducted a study based on the efficiency in mobilization, efficiency in deployment, efficiency in operations and liquidity management.

As far as sources of funds were concerned the Vilvattam Bank mobilized more through high cost deposits and gave less importance for low cost deposit. The banks failed to deploy funds efficiently. This inefficiency was reflected in the profitability where spread was low and burden was comparatively high, leading to loss for the bank. Hence, the bank should leave no stones unturned in professionalizing its management.

Kale, K. and Chobe, C. N. (2016) attempted to identify the financial performance of Devgiri UCBs Ltd. Aurangabad. It was found that the growth trend of the DUCBs was satisfactory. The share Capital, reserves and borrowings increased almost double during the study period, with a nominal percentage of variation. Overall performance of the DUCBs was satisfactory and employment generation of the bank was increasing year by year.

Mayilvaganan, S. (2016) found that there was a significant increase in actual advances disbursed as well as the proportion of advances disbursed by Sirkali UCB relative to its total assets during the period under study. The study revealed that Mayuram UCB had gradually and significantly increased disbursement of loan to the customers during the period of study. The disbursement of loan to the customers by Sirkali UCB was significantly higher compared to that of Mayuram UCB.
Pramendra and Karwasra, J.C (2017) in a study found that the position of membership, borrowings, working capital, loan outstanding and overdue increased over the study period. It was also found that the unit transaction cost increased over time due to increase in cost of management.

Kannan Unnithan, V. and Somasundaram, M. (2017) conducted a study on the key problems faced by UCBs in Kollam District. The study found that the UCBs bear the problems of a limited area of operations, violation of prudential norms, poor management, poor quality services and lack of modernization, increasing overdue and political interference.

The above studies analyzed various financial and non-financial performances of UCBs in India including Tamil Nadu. Much of the studies concentrated on the financial aspects than the non-financial aspects. The outcome of these studies showed that though some UCBs showed better performance but majority of the UCBs were in doldrums. These studies also outlined the causes for the poor performance of UCBs.

The RBI has classified the banks on the basis of certain norms as Grade I, Grade II, Grade III, Grade IV (the norms for classification of UCBs are discussed in subsequent chapters).

While reviewing the existing literature on the performance of UCBs in India and more particularly in Tamil Nadu it was found that no attempt has been made on analyzing the performance of UCBs of different Grades. This study is an attempt to fill this research gap.

1.5 Objectives of the Study

The general objective of this study was to analyse the financial viability of UCBs in Tamil Nadu. Keeping this in mind the specific objectives of this study were:

1) to analyse the business performance of the sample UCBs in Tamil Nadu,
2) to analyse the factors that led to the financially viability of Grade I sample UCBs in Tamil Nadu,
3) to analyse the factors that led to the financial weakness of the Grade IV sample UCBs of Tamil Nadu, and
4) to suggest suitable measures to improve the financial efficiency of sample UCBs in Tamil Nadu.

1.6 Methodology

As the study is both analytical and quantitative in nature, field survey method was adopted. Both quantitative and qualitative approach was adopted for collection and analyzing of data. Both primary and secondary sources of data were collected and used for the study. Data were collected from the annual and audited reports of sample UCBs, RBI Inspection Reports, Bylaws of sample UCBs, and Trend and Progress Reports of Banks published by RBI.

1.7 Sampling

Multi stage sampling method was adopted to select sample UCBs. At the first stage UCBs in Tamil Nadu were classified as per the norms of RBI as Grade I, II, III and IV. At the second stage the sample UCBs were selected from Grade I and Grade IV UCBs. As the UCBs in Grade II and Grade III were moving towards Grade I, during the pilot study it was found that there were no much variations in their functional performance. It was justified that no study has been attempted so far by considering the classification of UCBs as per the norms of RBI in Tamil Nadu. Moreover, a comparative study on the performance of Grade I and Grade IV UCBs was also found to be absent. Thus, by banking into account the knowledge gap, it is quite pertinent to study the performance of UCBs by considering the best performing and poor performing UCBs to have an indepth insight. From each Grade 3 UCBs were selected purposively for an indepth analysis. Hence six UCBs in Tamil Nadu have been chosen as sample units for this study (Chart-1.1 and Map-1.1).
Chart-1.1

Sampling Framework

UCBs Tamil Nadu

Grade I (27UCBs)

Coimbatore UCB
Namakkal UCB
Tuticorin Melur UCB

Grade IV (14UCBs)

Madurai Sowrastra UCB
Periyakulam UCB
Valparai UCB
1.8 Period Covered by the Study

The study covered the period between 2006-07 and 2015-16.

1.9 Tools and techniques used for data collection

Data sheet was prepared for collection of data from the sample UCBs. Data on membership, share capital, reserve funds, deposits, borrowings, working capital, investments, profit/loss, loans and advances, and NPAs were collected from the annual and audited reports of sample UCBs. Personal interaction was held with the officials of sample UCBs to understand various issues involved in the financial viability of sample UCBs.

1.10 Statistical tools used for analysis

As to data analysis, the data collected from the annual and audited reports of the sample banks was entered into SPSS. Both descriptive and inferential statistical tools were used for analyzing and interpretation of data collected. Descriptive tools such as percentage, Average, Compound Growth Rates were used to analyse the trend in the business performance of sample UCBs. Interpretational statistical tools such as ANOVA, Duncon Post Hoc test and Multiple Linear Regression (MLR) analysis were employed to study the variations and relationship between dependent and independent variables. Ratio analysis was used to analyse the financial performance of sample UCBs.

Compound Growth Rate was used to know the growth rate of each component in all the sample UCBs. To estimate the growth rate, logarithm of the corresponding variables were linearly regressed over time and antilogarithm of the regression coefficient was computed and then after the subtracting one from the other, it was multiplied by 100 to get the percentage.

A one-way ANOVA was used to compare two means from two independent (unrelated) groups. It was based on the comparison of the average
value of the variance among groups related to variance within groups. In this study the Grade I and Grade IV sample banks were taken to analyze within and among the groups.

Ratio analysis was used to evaluate various aspects of banking operation and financial performance such as solvency ratio, profitability ratio, productivity ratio and asset quality ratio. The trend of these ratios over time was studied to check whether the UCBs financial performance were improving or deteriorating. Regression was used to find out the cause and effect relationship. It can be linear or non-linear. The differences between two or more number of independent variables were used to predict the value of a dependent variable. The dependent and independent variables used for the study is given table-1.1 and 1.2.

Table 1.1

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Table 1.2

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1.11 Definitions of the concepts used

1.11.1) Cash Reserve Ratio

   Cash Reserve Ratio (CRR) is a specified minimum fraction of the total deposits of customers, which the banks have to hold as reserves either in cash or as deposits with the Reserve Bank of India.

1.11.2) Current Viability

   The ability of the Cooperative Institutions to meet the cost of management and the incremental bad debts out for the gross financial margin available in a position to earn reasonable profit

1.11.3) Non-Performing Assets

   If a credit facility in respect of which interest and/or installment of principal has remained overdue for a period of more than 90 days, it’s called Non-Performing Assets (NPAs).

1.11.4) Profit

   The excess of total revenue over total cost during a specific period of time, normally a year, is called profit. In the context of UCBs, it refers to the excess of income over expenditure and Provisions in a given period of time.

1.11.5) Profitability

   ‘Profitability’ may be defined as the ability of a given investment to earn a return from its use. The word ‘profitability’ is composed of two words ‘profit’ and ‘ability’. ‘Ability’ refers to the earning capacity or power of an enterprise to earn profit.
1.11.6) Sustainable Viability

The ability to completely wipe off accumulated losses, unrealizable assets and to provide for a bad debt/assets adequately, etc., and to start on a clean and transparent balance sheet.

1.11.7) Statutory Liquidity Ratio (SLR)

Banking Regulation Act 1949 (AACS) says that every Bank (Scheduled and non Scheduled) is required to maintain, on daily liquid assets, the amount of which shall not be less than 25 per cent or such other percentage not exceeding 40 per cent, as many as notified by RBI, of its demand and time liabilities in India as on the 1st Friday of the second preceding fortnight [Section 24 2(A) (a)].

1.11.8) Urban Cooperative Banks

The Primary (Urban) Cooperative Banks popularly known as Urban Cooperative Banks (UCBs) were brought under the regulatory ambit of RBI by extending certain provisions of the Banking Regulation Act, 1949 (BR Act) effective from March 1, 1966.

UCBs are at the base level of the banking system in India providing basic banking facilities to people of small means particularly urban poor. The UCB sector is unique in the sense that there is a significant degree of heterogeneity among the banks in this sector in terms of size, geographical distribution, performance and financial strength.

1.11.9) Viability

An institution is described as viable if it can generate surplus over its expenses after providing for loss / likely to be loss assets.
1.11.10) Working Capital

Working Capital refers to the funds required for enabling a bank to carry on its operations, without break at the expected level. With respect to Cooperative Banking purview, working capital is the accumulation of owned funds and borrowed funds. The owned funds include share capital and reserves whereas borrowed funds include deposits and borrowings.

1.12 Scope of the Study

Geographically, the study has confined in to the UCBs operating in Tamil Nadu. Although there are 120 banks operating in Tamil Nadu, only six UCBs falls under two categories viz., Grade I and Grade IV alone were selected as sample units. Further, as the main focus of the study was to analyze the financial viability of sample UCBs, the study covered the performance of sample UCBs in forms of mobilization and deployment of resources, management of NPAs, and best practices adopted which contributed to the financial viability of sample UCBs.

1.13 Limitation of the study

The present study is not far from limitations. As far as Tamil Nadu is concerned, 120 UCBs are functioning. These UCBs have been segregated into four grades (Grade I, Grade II, Grade III and Grade IV). The study is limited to analyzing the performance of Grade I and Grade IV UCBs. Each Grade, 3 UCBs purposively selected totally six UCBs of Tamil Nadu were considered to analyze the financial health and viability of UCBs. The analysis made in this study is based on the data / information collected from the reports and records of sample UCBs, pertaining to financial health and viability of sample UCBs in Tamil Nadu. Sincere effort has been made, wherever necessary, to ascertain the
accuracy of the data / information provided. Through personal interview with the employees and Government officials, the various factors affecting the loss making banks and factors influencing the financially viability of UCBs were obtained and used for the purpose of analysis and interpretation of the data. Due to paucity of time, the perceptions of others stakeholders used for the study were not obtained. However, these have not affected the purpose of this study and its logical presentation.

1.14 Chapter Schemes

Chapter-I - The Design and Execution of the study

Chapter-2- Business Performance of Urban Cooperative Banks in India

Chapter-3- Business Performance of Sample Urban Cooperative Banks in Tamil Nadu

Chapter-4- Financial Viability of Sample Urban Cooperative Banks in Tamil Nadu

Chapter-5- Findings, Conclusion and Suggestions

1.15 References


40. (www.rbi.org.in).

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