Chapter 1

INTRODUCTION

A sound financial system is essential for a healthy and vibrant economy and it will result in achieving a faster rate of economic growth. The banking sector constitutes a predominant component of the financial service and the performance of the economy, to a large extent is dependent on the performance of banks and hence the banking system occupies an important place in a nation’s economy. Banks play an important role in mobilization and allocation of resources in an economy.

In a developing country like India, where propensity to consume is high and savings of people are meager, banks play a strategic role in attracting more deposits from the people and deploying these savings for lubricating various sectors of the economy. They have to supply credit to the promotional and developmental activities of the society, at the same time restricting credit for socially undesirable and economically less beneficial purposes. Availability of adequate and timely credit can go long way in improving productive capacity of the different sectors of the economy. Modern business is certainly impossible without them and no country can achieve industrial progress in the absence of a sound banking system.

Rural development has been sine qua non in the process of accelerating the pace of economic development and significantly improving the standard and quality of living of rural house holds. Even now, majority of the rural folk in India are not able to meet their day-to day requirements from their own source of income, not to speak of other productive enterprises for improving their economic conditions.

Therefore, they have to depend on various financial agencies for arranging funds for making investments. Rural population is composed of agricultural producers, tenant cultivators, village artisans and landless
labourers. All these categories are in need of credit. In such a situation, the role of credit is dynamic and of immense importance.

**Banking in India**

A bank is an organization that mobilises deposits from the people and extends the same as facilities to people. A bank therefore has to manage work, man and resources. It aims at profits as a reward for its efforts. In the organizational structure of the Indian banking system, the central bank occupies the apex place. Below this central bank there are three categories of banks, namely, commercial banks, co-operative banks and Regional Rural Banks.

The RBI is the supreme monetary and banking authority in the country and has the responsibility of central banking system in the country. It keeps the reserves of all commercial banks and hence is known as the Reserve Bank.

Commercial banks have been in existence for many decades. They mobilise savings in urban areas and make them available to large and small industrial and trading units mostly for working capital requirements. After 1969 commercial banks are broadly classified into nationalised or public sector and private sector banks. The State Bank of India and its associate banks along with other twenty banks are public sector banks. The private sector banks include newly started hi-tech banks, a small number of Indian scheduled banks which have not been nationalised and branches of foreign banks operating in India, commonly known as foreign exchange banks.

Primary co-operative credit societies were originally set-up in villages to promote thrift and savings of the farmers and to meet the credit needs for cultivation. To support them state co-operative banks were established. The funds of the RBI meant for the agriculture sector actually pass through the state co-operative banks and central co-operative banks. Originally based in the rural sector, the co-operative movements have now spread to urban areas also,
and there are many urban co-operative banks coming under state co-operative banks.

Another set of banking institutions which have been added to the Indian Banking system since October 1975 is the Regional Rural Banks. The main objectives of RRBs are to develop the rural economy by providing for the purpose of development of agriculture and allied activities, village industries, and other productive activities, in rural areas, credit and other facilities, particularly to the small and marginal farmers, agricultural labourers, artisans, and small entrepreneurs.

**Figure 1.1**

**INDIAN BANKING SYSTEM**

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Reserve Bank of India
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Commercial Bank
  ↓
Private Sector Banks
  ↓
  Indian
  ↓
  Foreign
  ↓
Public Sector
  ↓
State Bank Group
  ↓
SBI
  ↓
Associate Banks
  ↓
Co-operative Banks
  ↓
State Co-op Bank
  ↓
Central Co-op Banks
  ↓
Primary Co-op Banks
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Rural Banking in India

In a developing country like India, the rural economy is the life breath of national economic development. When the rural sector fails, the effects on the national economy are far reaching and damaging. In the case of India, with peculiar socio-economic and geographical factors, rural sectors pose both a challenge and threat to the stability of the national development. Therefore economic development and progress of India really mean reconstruction and resurgence of the rural communities of the country.

Development of rural economy is a must for the overall development of India. Though ‘rural development’ and ‘agricultural development’ are treated as synonymous, the scope of two is different. Rural development is a wider term which includes both farm and non-farm sectors. The farm sector comprises of two parts, namely agriculture, and allied activities such as animal husbandry, forestry, etc. The non-farm sector comprises three components namely (a) traders (b) artisans and (c) rural industries. Since majority of rural folk depend on agriculture as a source of living, rural finance is basically concerned with agricultural finance.

Finance is the life blood of modern agricultural economy. In India, the main obstacle to rural development has been the lack of credit facilities in rural areas. Broadly, there are two sources of credit available to the farmers - institutional and private. Non institutional or private includes money lenders, traders and commission agents and land lords. Institutional sources consist of the government, co-operatives and commercial banks including the Regional Rural Banks.

The role of credit institutions in augmenting production and productivity is well recognised. The main thrust of Indian public policy towards rural credit has, therefore, been to ensure that sufficient and timely credit, at reasonable rates of interest, is made available to as large a segment of the rural population as possible. The strategies followed have undoubtedly
helped to build up a broad based institutional infrastructure for the delivery and deployment of credit.

In India, four sets of co-operative credit institutions have been providing farm credit. These have been the primary agricultural societies, other primary level farm credit societies and land development banks which deal directly with farm borrowers. There are also state co-operative banks and central co-operative banks which extend only indirect finance. Both before and after independence, these institutions failed to meet the farm credit requirements. Therefore, farmers had to depend primarily on the money lenders.

The involvement of commercial banks in rural banking began with the nationalisation of Imperial Bank of India into the State Bank of India in 1955. The SBI started providing the agricultural credit through co-operative banks, land mortgage banks and co-operative processing and marketing societies in 1956.

With the adoption of the new agricultural strategy in 1968, it was felt that the co-operative institutions helped by the SBI would not be able to meet the credit requirements of the expanding farm sector by themselves. Accordingly, the Government accepted the principle of multi-agency approach to farm credit with the entry of commercial banks in the sphere of agricultural finance. This led to the nationalisation of 14 commercial banks in 1969. It was only after this that the commercial banks as a class began to enter the rural sector in a big way. There was remarkable expansion of branches of commercial banks in rural areas. But they failed to meet credit needs of the farmers except that of the rich farmers and landlords. Instead of supplementing co-operative credit, they weakened co-operative societies by mobilising the saving of rich farmers and channelising them into urban areas for ensuring profits. Moreover, commercial banks experienced that working in rural areas was very costly and not viable and secondly, the urban staff was unable to understand the needs and problems of rural finance. It was against this background that Banking Commission in its report submitted to government in Jan
1972 recommended the formation of ‘Rural banks’. It recommended that a chain of rural banks be established in addition to the regular branches of commercial banks. It appears that the Banking Commission’s idea of a rural bank was influenced by the working of People’s Bank in Srilanka which has rendered immense service to the rural Population of Srilanka. Finally on 26th September 1975, the Government promulgated in an ordinance that Regional Rural Banks would be set up from 2nd October 1975. The ordinance was replaced by an Act of Parliament known as the Regional Rural Banks Act 1976. By the promulgation of the ordinance the Central Govt. established RRBs in different states.

**Regional Rural Banks in India**

Regional Rural Banks (RRBs) which form an integral part of the rural banking system came in to existence in 1975 and have been working along with the co-operatives and commercial banks in meeting the increasing credit requirements in rural area. The uniqueness of RRBs lies in the harmonious blending of low-cost profile and local feel of co-operative credit system and modernised outlook and professional management of commercial banks. It was created exclusively for catering to the credit requirements of the rural poor.

These institutions established themselves as a strong alternative mechanism for rural credit delivery. Since their inception, RRBs have carried banking to the door steps of rural masses. They have opened branches both in remote and isolated villages which had no banking facilities before. Initially starting with 5 RRBs on 2\(^{nd}\) October 1975, the RRBs have achieved a phenomenal growth over the years. Between 1975 and 1987, 196 RRBs were established in India and no RRBs were set up there after except Pudvai Bharathiar Grama Bank established in 2008. As a part of reform measures taken by the government of India and RBI to strengthen the RRBs in India, the state level sponsor-wise amalgamation of RRBs started in September 2005 and as a result of this, the number of RRBs has come down to 82 as on March 2010.
Regional Rural Banks in Kerala

There are two Regional Rural Banks in Kerala namely South Malabar Gramin Bank sponsored by Canara Bank and North Malabar Gramin Bank sponsored by Syndicate Bank. South Malabar Gramin Bank was established in 1976 with its head office at Malappuram. Its area of operation include geographical jurisdiction of Malappuram, Kozhikode, Wynad (Except Mananthavady Taluk), Thrissur, Palakkad, Idukki, Pathanamthitta and Thiruvananthapuram districts. As on 31st March 2010, the Bank have 228 branches spread over these districts. The second RRB, North Malabar Gramin Bank was started on 12th December 1976 with its head office at Kannur. Now the operational area of NMGB is the geographical jurisdiction of Kannur, Kasargode, Ernakulam, Kottayam, Alappuzha and Kollam districts and Mananthavady taluk of Wynad district. As at the end of the financial year 2009-10 the bank had 178 branches spread over these districts.

Significance of the Study

The Indian banking sector has been facing hectic competition since 1991 due to liberalization of the Indian economy. The economic and financial policies enunciated by the Central Government promoted foreign direct and indirect investments in the banking sector of India. In the new banking scenario of the liberalized world, especially with coming of the foreign banks, both the public and private sector banks of India are forced to make considerable changes in the method of operation and decision making processes.

In this situation, the banking sector has to survive the extreme challenges launched by the new banking policies. There emerged an atmosphere of severe competition for survival among the public and private sector banks in the country. It appears that a large number of nationalized banks eventually started moving away from their traditional objective of serving the common people, and neglected the agrarian sector of the economy.
Need less to say, in the case of private sector banks, they are only interested in serving the rich and influential categories of people. Both these groups of banks now function mainly for making profit at the expense of a certain amount of welfare motivated practices which traditionally exist in their services.

In comparison to these banks, RRBs in India play a remarkable role to promote the primary sector of the economy. Despite of the influence of liberalization and privatization policies, RRBs try to retain their traditional principles and practices to serve the common people of rural India. As majority of the Indians still depends on agriculture for their every day living, existence and success of RRBs are indispensable to the country. The banking operations in Kerala reflect the general scenario of Indian banking system. As mentioned earlier there are two RRBs in Kerala. In spite of the acute competition in the banking sector, they are the two leading RRBs in India.

The concern of this study is to examine the performance of RRBs in Kerala. The annual reports published by these banks illustrate that they have made steady progress despite the adverse economic policies, which prevail as part of liberalization and privatization. The purpose of this research is to find out the banking tactics and modus operandi used by these RRBs to survive the contemporary challenges. It is reasonable to discuss these problems in the context of two lines of thoughts. (1) Whether these RRBs deviated from their traditional paths and principles for profit and sustenance or (2) whether they attained success by retaining the basic identity and service pattern, giving emphasis on rural areas.

Performance evaluation is an important pre-requisite for sustained growth and development of any institution, particularly financial institutions. Evaluation is the method of determining how much further and in what way it would be carried to accomplish the organizational objectives. The RRBs have an important role to play in our country as they have to act as alternative
agencies to provide institutional credit in rural areas. Therefore, in the case of evaluation of performance of banks, especially RRBs, it is imperative to pursue the objectives with which RRBs were established.

The present study mainly concentrates on the performance evaluation of the two RRBs in Kerala – South Malabar Gramin Bank and North Malabar Gramin Bank- and also the comparative study of its performance with each other and with RRBs at the national level. Such a study is expected to bring to the fore the strength and weakness of the RRBs, so that appropriate corrective measures can be taken for the rectification of the weakness to make the RRBs organizationally vibrant, operationally sound, financially viable and socially relevant. The importance of the present study is that performance evaluation in this direction is a new research. The review of previous studies will further elucidate this fact.

It should also be noted that in general there is an attempt to terminate the functioning of RRBs by merging them with their mother banks. It is argued that most of the RRBs are running at a loss and recovery performance is not adequate. On the contrary, RRBs in Kerala shows a unique case of success. It constitutes the second problem of this research. A study and analysis of this issue will further question the basic objective of a bank-whether it is for profit alone or for profit of the institution and welfare of the people/customers. The emerging challenges against RRBs support the former view. Hence this research is also an attempt to explicate the social role of a banking system, an essential role to help the poor that seems to be disappearing since 1991.

**Scope and coverage**

The present study analyses the performance of the two RRBs in Kerala along with a comparative analysis with each other and with RRBs at the all India level for a period of 10 years from 2000-01 to 2009-10. The study analyses the performance of these RRBs in deposit mobilization, lending activities, profitability and recovery. It examines the job satisfaction of the
employees of the bank and satisfaction of the customers with the services provided by these banks. Impact of these banks on the life of the rural folk also forms part of this study.

**Objectives of the Study**

The specific objectives set for the study are:-

1. To study the significance of a specialized bank in a rural area called Regional Rural Bank to provide banking service.
2. To study the performance of the Regional Rural Banks in Kerala on the basis of
   (i) Deposits
   (ii) Lending
   (iii) Profitability
   (iv) Recovery and overdue
   (v) Customer service and
   (vi) Job satisfaction of employees.
3. To study the comparative performance of South Malabar Gramin Bank (SMGB) and North Malabar Gramin Bank (NMGB).
4. To study the flow of institutional credit to agricultural and non agricultural sector by SMGB and NMGB.
5. To study the impact of liberalization and banking reforms on the performance of RRBs in India with its prime motive of establishment.
6. To study the impact of establishment of RRBs on the quality of life of the rural folk.
7. To provide suggestions and recommendations on the basis of analysis.
Hypotheses of the study

The major hypotheses developed for the study are:

1. There is no significant difference between CD ratio of RRBs in India and RRBs in Kerala.
2. There is no significant relationship between profitability and lending of RRBs in Kerala and RRBs at national level.
3. There is no significant difference between recovery performance of RRBs in India and RRBs in Kerala.
4. There is no significant difference in the flow of credit to agricultural and non-agricultural sector among the RRBs in India and RRBs in Kerala.
5. There is no significant difference in the level of job satisfaction of the employees of SMGB and NMGB.
6. There is no significant difference in the level of satisfaction of the customers of SMGB and NMGB with regard to the service quality of their bank.
7. Existence of RRBs in Kerala have paved the way for improving the quality of life of the bank customers.

The Design and Methodology of the Study

The study has been made as an analytical one based on primary and secondary data and is made in two parts. In the first stage the secondary data were collected from the annual reports of the two RRBs in Kerala, publications of Reserve Bank of India, NABARD, State level Bankers Committee Reports etc. In addition to this, necessary literature and data were collected from the published and unpublished Ph-D thesis on Regional Rural Banks. Further, data were also compiled from the accounts of RRBs available at the head office of the two RRBs in Kerala. Constructive comments made in the research articles have paved the way for acquiring reasonably good knowledge on the topic.
In the second stage, primary data were collected from the employees and customers of the bank to study the level of job satisfaction of the employees and customer satisfaction in the services of the bank. These respondents were personally interviewed with the help of structured questionnaires. Besides, relevant information was collected through discussion with managers and officials of the banks at the head office and branches.

For the collection of samples for customer survey, multistage sampling technique was used. As more than seventy percent of the branches of the two RRBs are located in Malabar area, higher representation was given to this region by selecting two districts each, selected at random from this area. From the so selected four districts, five bank branches were selected at random. In order to give representation to other parts of Kerala five branches of SMGB and NMGB were selected at random from the remaining districts. Thus 30 bank branches, twenty from Malabar area and ten from non Malabar area constitute the sample banks. Ten bank customers consisting of a heterogeneous group were selected at random from each of these selected branches. Deliberate random sampling by applying cluster method has applied in selecting the samples. Thus the sample size constitutes three hundred persons from 30 branches selected at random from the operational area of the RRBs. Out of the sample selected, two third is males and one third is females.

For the collection of data from employees for studying the level their job satisfaction, 152 employees working all over the state were selected at random, which constitutes around 6 per cent of the total employees of these two RRBs in Kerala. Out of these, 86 employees were from SMGB and 66 were from NMGB.

**Analysis of the Data**

The collected data were analysed with the help of computer packages namely MS excel, SPSS etc. Various mathematical and statistical tools like averages, standard deviation, percentages, compound growth rate, ratio analysis, ANOVA, t-test, chi-square test, correlation analysis etc. were used for the analysis.
### VARIABLES STUDIED

<table>
<thead>
<tr>
<th>Main Variables</th>
<th>Sub variables</th>
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| Deposit Mobilisation    | 1) Growth in Total deposits  
                            | 2) Growth in per branch deposits  
                            | 3) Growth in per Employee deposits  
                            | 4) Share of low cost deposit to total deposit |
| Lending                 | 1) Growth in loans and advance outstanding  
                            | 2) Growth in per branch loans and advance outstanding  
                            | 3) Growth in per employee loans and advance outstanding  
                            | 4) Share of Agricultural and non agricultural lending to total  
                            | 5) C D Ratio |
| Profitability           | 1) Growth in net profit earned  
                            | 2) Growth in Interest earned  
                            | 3) Growth in interest paid  
                            | 4) Growth in operating expenses  
                            | 5) Growth in per branch operating expenses  
                            | 6) Growth in per employee operating expenses |
| Recovery performance    | 1) Recovery ratio  
                            | 2) Ratio of NPA to total loans and advances outstanding |
| Employees’ Job satisfaction | 1) Satisfaction with Job content  
                                | 2) Satisfaction with occupational level  
                                | 3) Satisfaction with work environment  
                                | 4) Satisfaction with wages or salaries  
                                | 5) Satisfaction with Supervision  
                                | 6) Satisfaction with promotion prospects |
| Influencing factors in Bank dealings | 1) Personal relations with bank officials  
                                             | 2) Friends/ relatives/ colleagues  
                                             | 3) Nearness to residence/ working place  
                                             | 4) Motivated by advertisement  
                                             | 5) Motivated by collection agents  
                                             | 6) Statutory compulsion  
                                             | 7) Government Bank |
| Default in repayment of loans | 1) Uneasy installment  
                                         | 2) Delay in generating income  
                                         | 3) High rate of interest  
                                         | 4) Low income  
                                         | 5) Will full default  
<pre><code>                                     | 6) Expecting a write off in future |
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<table>
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<tr>
<th><strong>Service quality</strong></th>
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<tr>
<td><strong>Regularity</strong></td>
<td>1) Regularity of service</td>
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<td>2) Awareness made by bank</td>
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<td>3) Procedures</td>
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<td>4) Timeliness</td>
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<td><strong>Responsiveness</strong></td>
<td>1) Promptness</td>
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<td>2) Speed and efficiency</td>
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<td>3) Attitude and responsiveness</td>
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<td>4) Punctuality and presence</td>
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<td>5) Complaint redressal system</td>
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<td><strong>Assurance</strong></td>
<td>1) Professional commitment</td>
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<td>2) Behaviour of employees</td>
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<td>3) Job knowledge and skill</td>
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<td>4) Courtesy of employees</td>
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<td>5) Security</td>
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<td><strong>Empathy</strong></td>
<td>1) Variety of service</td>
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<td></td>
<td>2) Individual attention</td>
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<td>3) Personalised service</td>
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<td><strong>Tangibility</strong></td>
<td>1) Technology</td>
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<td>2) Infrastructure facilities</td>
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<td>3) Quality of forms and books</td>
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| **Impact of RRBs on the rural folk** | 1) Income                                                      |
|                                     | 2) Dependency on money lenders                                  |
|                                     | 3) Domestic appliance possessed                                 |
|                                     | 4) Socio-economic upliftment on the customer                   |
|                                     | 5) Socio-economic upliftment of the village                    |
Summary of chapters

The first chapter deals with the introduction, nature and importance of the study. The objectives of the study, hypotheses of the study, the methodology and the survey design are mentioned in this chapter.

The second chapter gives a brief review of the earlier studies on banking in general and RRBs in particular. Studies on customer satisfaction and employees’ job satisfaction in banks were also reviewed.

The third chapter explains the genesis and rationale of the Regional Rural Banks and also its growth and progress in India since its inception and during the last decade in particular. An analysis of the impact of globalization and liberalization policies and the resultant reform measures on the functioning of the RRBs in India have also been made in this chapter.

The fourth chapter analyses the performance of RRBs in Kerala which is presented in three sections. The first section evaluates the performance of South Malabar Gramin Bank and the second section deals with the performance evaluation of North Malabar Gramin Bank. The third section makes a comparative analysis of the performance of these two gramin banks in Kerala as well as RRBs in Kerala as whole and RRBs at the all India level.

The fifth chapter analyses the employees’ job satisfaction based on the data collected from the employees of both the RRBs in Kerala.

The sixth chapter analyses customer satisfaction and the impact of Regional Rural Banks on the life of the rural folk. It also makes a comparative analysis of the service quality of the two RRBs in Kerala.

The final chapter “Findings, Conclusions and Recommendations” is divided in to three sections. Section A contains the summary and findings of
the study, section B contains the conclusions of the study and section C includes the recommendations of the study.

Limitations of the study

Even though the study is extensive, innovative and unique in certain aspects, it suffers from the following limitations.

1. In order to get accurate results, the entire population must be studied. In the present study, the researcher tried to analyse the job satisfaction of employees by taking a sample of 152 employees. Further, to study the customer satisfaction and impact of RRBs on rural folk only 300 sample customers were selected.

2. Sample was selected by applying sampling techniques, hence it has its own limitations.

3. The present study is based on the assumption that the data given by the sample beneficiaries are correct.

4. Respondents were reluctant to spare their time to fill the interview schedule either due to their busy schedule or due to their willingness to co-operate due to some of their personal reasons.

5. Owing to security and confidentiality reasons banks were reluctant to give the name list of customers and this created some difficulty during the sample selection.