ANNEXURE - II

IMPORTANT RECOMMENDATIONS OF THE COMMITTEES ON THE WORKING OF REGIONAL RURAL BANKS

DANTWALA COMMITTEE'S RECOMMENDATIONS:

The Reserve Bank of India appointed in June, 1977 a "Committee to Review the Working of Regional Rural Banks" under the Chairmanship of Prof. M.L. Dantwala. After reviewing the overall progress of the business of all the Regional Rural Banks functioning in the country up to the end of June, 1977, the Dantwala Committee submitted its report in February, 1978.

The Dantwala Committee was convinced that 'within a short span of time, the Regional Rural Banks have demonstrated their capability to serve the purpose for which they were established'. The Regional Rural Banks have established their image "as a new type of institution catering to the credit needs of a class of borrowers to whom institutional credit was hitherto not available." With some modifications in their organisation and functioning, the Regional Rural Banks can become a very useful component in the totality of rural credit structure. The Committee felt that
the Regional Rural Banks can make substantial contribution towards improving the quality and quantity of credit flows to the rural credit structure.

The Committee opined that 'ideally the jurisdiction of a rural bank should be confined to one district' and 'the number of branches should be higher so as to do justice to the local people and their problems. Naturally, one Regional Rural Bank should cover a population of 10 to 15 lakhs. From the angle of financial viability and managerial efficiency, the reasonable number of branches per district should be between 50 and 60. This would mean that 'one Regional Rural Bank branch would be enough approximately for a population of about 20,000 and an area roughly equal to that covered by five recognised Primary Agricultural Credit Societies.

The Committee held the view that the establishment of Regional Rural Banks will not disturb the Cooperative Credit Structure at the base level since Regional Rural Banks function at the intermediate level. It is assured that the reorganised Primary Agricultural Cooperative Credit Societies and Farmers' Service Societies, wherever they can be effectively organised, will constitute the base of the rural credit structure. The Regional Rural Banks are to fill up the gap where the existing cooperative credit institutions at the intermediate and retail level are weak and inadequate. The Committee emphasised that "the role of Regional Rural Bank was only to supplement and not to supplant the other credit institutions in the rural areas." It was proposed that while establishing Regional Rural Banks, priority should be given to the districts having weak commercial and cooperative banking structure. The District Central Cooperative Banks are weak in as many as 182 districts. The 48 Regional Rural Banks established covered 55 of these 182 districts. All these districts were thought to be covered in the beginning.

Commercial banks operating in the command area of a Regional Rural Bank should be persuaded to progressively entrust their rural credit business which their rural branches are currently doing to Regional Rural Bank and its branches. The Committee opined that the total replacement of rural branches of commercial banks
by Regional Rural Banks and their branches over a period of time would be acceptable to commercial banks and be welcomed by the rural clientele. It is relevant to note in this regard the observation of the Committee on the Functioning of the Public Sector Banks under the Chairmanship of James Raj that the Regional Rural Banks should not only open more branches in the rural areas, but also gradually take over the existing rural branches of commercial banks. Consequently all public sector banks and large private sector banks should be allowed to open branches only upto district headquarters/mandi/block levels.

On the operational aspects, the Committee suggested that the Regional Rural Banks will have to undertake direct lending to clients not served by the cooperatives and for the purposes for which cooperative credit is either not available or inadequate.

The Review Committee did not recommend any change in the authorised and paid up capital of a Regional Rural Bank. However, it recommended certain changes in the composition of share capital. It endorsed the need for local participation by cooperatives, other local institutions and individuals in the share capital of Regional Rural Banks. This enables Regional Rural Banks to mobilise sizeable chunk of deposits, promotes local feel and familiarity and easily sorts out specific problems. In case, there is a shortfall in the share of the local participation, it may be filled up by the Sponsoring Bank or the Reserve Bank of India, with the provision that as and when local demand for subscription comes up, the shares so held may be released to the eligible institutions and individuals. It further suggested that "hereafter the Reserve Bank instead of the Central Government may contribute to the share capital." Similarly, the Committee argued the case for increasing the share of the Sponsoring Bank in the share capital of Regional Rural Banks by 5 per cent over the present level. The composition of share capital of a Regional Rural Bank recommended by the Review Committee was as follows:
Reserve Bank of India: 25 per cent
Sponsoring Bank : 40 per cent
State Government : 15 per cent
Local participation : 20 per cent

The Committee also recommended the paying of a minimum guaranteed dividend to the shareholders at the rate which was recommended earlier by the Narasimham Working Group.

The Committee expressed its discontentment over the nomination of directors staying at far off places. It observed that:

a) all the Central Government nominees come from Delhi and have to travel long distance to attend the Board meetings of Regional Rural Banks every 5 to 6 weeks;

b) though Regional Rural Banks were supposed to cater to the credit needs of rural artisans and other non-agriculturists, the Industries Department is not represented adequately on the Board of Directors; and

c) The Board Members nominated by the Central Government have remained absent from the Board Meetings frequently.

So, the Committee recommended certain changes in the composition of the Board. The Board of each Regional Rural Bank, according to the Committee, should consist of nine members including the Chairman. Of the remaining Directors, three should be nominated by the Sponsoring Bank, one by Reserve Bank, two by the State Government and two to be nominated by Reserve Bank from amongst the local shareholders.

The Committee emphasized that the Regional Rural Banks should cater to the credit needs of weaker sections of the rural clientele. Since Regional Rural Banks are supposed to be established in areas where the existing credit facilities are inadequate, the Committee suggested that a dominant share (60 per cent) of total loans be reserved by the Regional Rural Banks for the weaker sections and the remaining (upto
40 per cent) may be lent to large farmers and other borrowers not covered by these Banks at present. The Committee suggested that in respect of loans to large farmers and others, suitable ceilings be fixed on loans to a single individual and recommended the stipulation of strict penalties for misrepresentation of the borrower's status and non-adherence to the quota. The Committee also recommended that the Regional Rural Banks be allowed to offer full banking facilities especially because of its view that the rural branches of commercial banks are not to operate in the areas served by the Regional Rural Banks.

One arrangement which gives benefit to the small cultivators is the issue of pass books. The Committee urged that all the State Governments may expedite the issue of such Pattadar Pass Books especially to the small farmers. Similarly, the poor rural households may be given Identity Cards showing occupational assets to give no scope for undue delay in the sanction of loans and also to keep the costs of operation of the Bank to the minimum.

Thus, the general approach to the base level rural credit structure is that institutions at this level should be relatively simple and easy to organise. They should not be loaded with numerous and complex functions which require a level of managerial and technical competence difficult to muster at the base level. This institutional device, however perfect conceptually, there are some practical problems relating to recovery of loans and the quantum of overdues. However, the magnitude of overdues of Regional Rural Banks is very low when compared to other institutions since the overall recovery performance was good. Considering the staffing pattern and capital available, it can be said that the banks have succeeded in imparting rural orientation and local touch to their operations. An assessment of quantity of lendings of Regional Rural Banks compared to that of the rural branches of Commercial Banks shows that the credit administration of the former was in many respects better and more responsive to rural needs than the latter.
The Committee also considered another important aspect viz., for how long the Regional Rural Banks can continue to get staff on deputation from the Sponsor Banks which at present bear their expenses on the salary account. If the Regional Rural Banks have to pay fully for their staff, their expenses will rise two or three-fold and even, to break even the banks have to raise their business more substantially. So the question arises as to whether the cost should be so subsidised in the interest of rural financial institution like cooperative societies. And if the cost of running Regional Rural Banks is to be subsidised for some years to promote the cause of social welfare in rural areas, care has to be taken to see that the Regional Rural Banks provide credit - adequate, timely and productive - to right parties in right quantities.

II. KELKAR WORKING GROUP'S RECOMMENDATIONS:

The Government of India set up a Working Group in August, 1984 to go into the various aspects of the functioning of Regional Rural Banks and make suitable recommendations for future policy. The review was felt necessary in the context of a large number of Regional Rural Banks being established in the country and in view of certain weaknesses discernible in the working results of Regional Rural Banks particularly relating to their profitability aspect. The Working Group under the Chairmanship of Sri S.M. Kelkar examined the data in respect of 183 Regional Rural Banks established till June, 1985 and arrived at certain conclusions. The Group was convinced, taking into consideration the average size of deposits (Rs. 712) and loans (Rs. 1886) per account, that these banks have catered successfully to the banking requirements of small men in rural areas of the country.

The Group felt that the Regional Rural Banks as a part of multi-agency approach to rural credit are eminently suitable to do the job particularly in view of their large branch network, comparatively low cost of operation, local involvement and operations in tune with the national objectives of serving the weaker sections. They can be trusted as district level organisations to take banking closer to the rural
households and ensure effective supervision over the end-use of credit. They can co-exist alongside the Cooperatives and Commercial Banks, playing a supplementary role to each other.

At the end of June, 1985, out of 183 Regional Rural Banks established in this country, as many as 88 covered one district each and 67 covered two districts each. There were 20 Regional Rural Banks covering three districts each and five Regional Rural Banks covering four districts each. For example, one Regional Rural Bank in Nagaland covered seven districts and another in Manipur covered eight districts. The Group felt that from the point of view of manageability and better control by Head Office over the branches, there is need to bifurcate unwieldy Regional Rural Banks and also amalgamate two or more small and uneconomic Regional Rural Banks into one single viable unit. It recommended a case by case study by NABARD to take suitable action. The Committee also recommended that more attention has to be paid to the consolidation of existing Regional Rural Banks and where new Regional Rural Banks have to be set up, they be established in areas with preponderance of Scheduled Caste or Scheduled Tribe population, taking into consideration the existing banking facilities and credit gap both in qualitative and quantitative terms.

The Working Group referred to the new branch licensing policy of the Reserve Bank for the Seventh Plan period and recommended relaxation in respect of Regional Rural Banks, taking into account the need and viability aspects. The new licensing policy envisaged the 'block' as 'a unit' and that a branch would cover 200sq.km. area. Under this policy, fresh licences would be issued only in deficit blocks which do not conform to the above norms. The Group felt that once a Regional Rural Bank is required to be established in an area, viability considerations demand that sufficient number of branches should be allowed to be opened by it and so the need for Reserve Bank of India to relax the policy norms on the merits of each case. The Group also recommended that priority may be continued to be given to Regional Rural Banks while issuing licences for rural centres.
Regarding the authorised and paid up share capital of Regional Rural Banks, the Group felt that there is a case for increasing the share capital by a substantial amount in view of increasing number of branches of Regional Rural Banks and the escalation of costs over the years. While examining the question of viability of Regional Rural Banks, the Group examined the balance sheets of 173 Regional Rural Banks as at the end of December, 1984 which revealed that 130 Regional Rural Banks had incurred losses. The accumulated losses of 49 Regional Rural Banks had eroded their entire paid up share capital and another 26 had eroded half or more than half of their paid up share capital. In view of all this, the Group felt that higher issued share capital, besides strengthening the capital base of the Regional Rural Bank would also provide cost free funds to the Regional Rural Bank. So the Group recommended that the paid up share capital of each Regional Rural Bank be raised to Rs.100 lakhs and correspondingly the authorised capital to Rs.500 lakhs. The Group did not recommend any change in the composition of shareholders as also their respective shares in the paid up share capital. The Group hoped that all the three shareholders would come forward to meet this extra burden. In case the concerned State Government finds it difficult to subscribe to the increase in share capital of existing Regional Rural Banks, the Group recommended that NABARD should make available long term loans to State Governments out of its National Rural Credit (Long Term Operations) Fund for enabling the latter to subscribe to the share capital of Regional Rural Banks. The NABARD Act, 1982 may be suitably amended for this purpose, the Group recommended.

There had been a suggestion from quite a considerable period of time that Regional Rural Banks should be allowed to finance bigger borrowers upto a given percentage of their total loans so that they can increase their business, tap deposits from richer sections and improve their viability. The Group felt that such a relaxation was not likely to make any dent in improving the viability of Regional Rural Banks.
The Group desired that the Regional Rural Banks should retain their present image of small man's banks.

The Group recommended changes in the composition of Board of Directors of each Regional Rural Bank other than the Chairman as below:

- Government of India : 2 non-officials
- Reserve Bank of India : 1 official
- NABARD : 1 official
- Sponsor Bank : 2 officials
- State Government : 2 officials

It is also recommended that the respective nominating authorities be allowed to nominate their members directly without any reference to Government of India and without the Government of India following the present procedure of issuing notification nominating the various persons on the Board, representing Sponsor Bank and State Governments which is unnecessary and time consuming. Similarly, the Chairman has to be appointed directly by the Sponsor Bank in consultation with NABARD. Sufficiently Senior Officers of Sponsor Bank with organisational experience at its Head Office in management of funds, human resources, industrial relations etc., and having been imparted preferably a suitable orientation training programme should be selected by Sponsor Bank for being appointed as Chairman.

The Working Group also envisaged a greater role for both the Sponsor Bank and the concerned State Government apart from what they have been doing at present. For example, the State Governments have to assist the Regional Rural Banks in the recovery of overdues, in providing adequate security arrangements especially for branches in vulnerable rural centres, in preparing area-specific bankable schemes for being financed by Regional Rural Banks and in providing adequate infrastructural support. Similarly, the Sponsor Banks should
i) advise their Regional Rural Banks in the management of funds;
ii) monitor the progress of their Regional Rural Banks;
iii) provide staff for internal audit of Regional Rural Banks;
iv) undertake periodical inspections of their Regional Rural Banks;
v) help Regional Rural Banks in appraisal of bankable schemes;
vi) invest deposits kept by Regional Rural Banks in their current accounts in Government securities; and
vii) periodically place before their Board the progress made by the Regional Rural Banks sponsored by them.

The Group analysed the various reasons for the non-viability of many Regional Rural Banks and made certain recommendations to remedy the situation. Important among them being:

i) lowering the involvement of Sponsor Banks in Regional Rural Banks' loans by reducing their refinancing of short term loans from 30 to 20 per cent, accompanied by a reduction in the rate of interest from 8.5 per cent to 7 per cent per annum;

ii) over and above the Statutory Liquidity Ratio requirement, the Regional Rural Banks may be permitted to keep additional 10 per cent of their funds with Sponsor Banks which may be termed as 'permissible excess liquidity' and the Sponsor Banks may pay the maximum permissible rate of interest on inter-bank transactions;

iii) a relaxation by NABARD to Regional Rural Banks from its recent instruction that Credit Deposit Ratio be kept down to 100 per cent since this would lead to overall shrinkage of loans by Regional Rural Banks;

iv) a judicious readjustment of their loan portfolios so as to correct the mis-match between investment credit and working capital loans.

To tackle the problem of accumulated losses of Regional Rural Banks, the Group recommended that an exercise may be made by NABARD and Government of India to determine that portion of accumulated losses which could not have arisen, had the benefits of measures suggested by the Group been available to Regional Rural Banks from the beginning. Such portion of losses should be borne by the three shareholders in proportion to their equity in the form of grants to the respective
Regional Rural Banks. Then Regional Rural Banks will be left to bear the losses that arose due to mismanagement. They should endeavour to wipe out such losses over a period of years.

Regarding the growing overdues of Regional Rural Banks, the Group recommended that concerted action should be taken by all the concerned to reduce the overdues and thereby get the locked funds released for recycling them. The State Governments have to play a major role in helping the Regional Rural Banks in the recovery of their dues.

In respect of staff matters, the Group felt that reasonable promotional opportunities will have to be provided to the staff in their career path. The creation of the posts of Area Managers was regarded as a welcome step as it would relieve the Chairman from some of his burden besides giving promotional opportunities to some officers. The Group also recommended that the Sponsor Banks should make available some posts in the officer cadre to the Regional Rural Bank officers with requisite experience and qualifications. The staff should also be imparted rural orientation in any training programme apart from regular familiarisation with banking practice and books of accounts. Any training of the Regional Rural Bank staff should be on a different footing than the one given to commercial bank staff. The Group did not make any further recommendations since the matter was under a detailed study by a Working Group headed by Smt. Kamala Choudhary and appointed by NABARD.

In conclusion, the Group observed that the various measures suggested by them have to be accepted and implemented as a package and not in isolation. The Group felt that the recommendations if properly implemented would make Regional Rural Banks more effective and better equipped institutions to subserve the rural weak which was the primary objective for their establishment.
NARASIMHAM COMMITTEE'S RECOMMENDATIONS:

The Government of India set up a High Level Committee under the Chairmanship of Sri M. Narasimham in August, 1991, to examine all aspects relating to the structure, organisation, functions and procedures of the financial system and its various components and to make recommendations for improving the efficiency and effectiveness of the system. The Committee was, among other things, asked to review the relative roles of the different types of financial systems and to make recommendations for their balanced growth. The Committee submitted its report to the Government on November 16, 1991.

The Narasimham Committee felt that the growth of agriculture and small scale industry in India had reached a point where the legitimate production requirements of these sectors or large part of them could be met by banks on the basis of their commercial judgement. The Committee has therefore suggested that the system of directed credit programme should be gradually phased out. At the same time, it should be recognised that for some time it would be necessary to have directed credit programmes for some sectors such as a redefined priority sector consisting of the small and marginal farmers, tiny sector of industry, small business and transport operators, village and cottage industries, rural artisans and other weaker sections. The credit target for this redefined priority sector should hence forth be fixed at 10 per cent of aggregate credit which would broadly be in line with the credit flows to these sectors at present.

The Narasimham Committee is of the view that easy and timely access to credit is far more important than its cost and hence, has recommended that concessional rate of interest for priority sector loans of small size should be phased out. This would remove a major disincentive for banks to seek clients in the neglected sectors. It, however, adds that the medium term objective could be to move towards market determined interest rates but has advocated a cautious approach to deregulation, lest, in the absence of a reasonable macro economic balance and control of inflation, total
deregulation should pose the danger of excessive lending at high nominal rates to borrowers of dubious credit worthiness. The Reserve Bank, in its view, should be the ultimate authority to determine the level and structure of interest rates, with bank rate as the anchor rate and spreads between the bank rate and Government borrowing rates, bank deposit and prime lending rates being indicated by the Reserve Bank of India in accordance with the criteria suggested by the Chakravarthy Committee. The Committee has further suggested that along with the review of directed lending programmes at the end of three years, the concessional rate policy should also be reviewed with a view to its eventual elimination in about three years.\(^7\)

The Narasimham Committee has expressed a strong view that "the pursuit of distributive justice should use the instrumentality of the fiscal rather than the credit system." In its view, interest subsidy should be phased out and even capital subsidy in some developmental programmes e.g. IRDP should also be withdrawn, 'as they have distorted the pattern of lending'.\(^8\)

The Committee proposed that the interest rate paid to banks on their SLR investments and on Cash Reserve Ratio (CRR) in respect of impounded deposits above the basic minimum should be increased.

Banks, at present, experience considerable difficulties in recoveries of loans and enforcement of security charged to them. The delays that characterise our legal system have resulted in the blocking of a significant portion of the funds of banks. The Committee therefore considers that there is urgent need to work out a suitable mechanism through which the dues to respective credit institutions could be realised without delay and strongly recommended that special tribunals on the pattern recommended by the Tiwari Committee on the subject be set up. The introduction of legislation for this purpose is long overdue and should be proceeded with, immediately.
In order to enable the banks and financial institutions to recycle a part of their bad and doubtful debts, the Committee proposed the establishment of Assets Reconstruction Fund (ARF). This would take over a portion of bad and doubtful debts at a discount and would issue bonds to the concerned institution (to be guaranteed by the Government) and carrying an interest rate equal to the Government bond rate and repayable over a period of 5 years.

The Committee recommended restructuring the banking system in the country and recommended a new rural banking structure. It felt, "Given the credit gap, which exists in the rural community and the distance still required to be covered before the rural banking needs are fully taken care of, the need is to establish a viable banking structure which could effectively meet the rural credit needs." The Committee has, therefore, expressed itself in favour of a rural banking structure, which can combine effectively 'the advantages of the local character of the Regional Rural Banks and the financial strength and organisational and managerial skills of Commercial Banks.' The Committee has suggested that the Sponsor Banks should segregate the operations of their rural branches through the formation of one or more subsidiaries depending on the size, administrative convenience and business assessment of each Sponsor Bank. Each subsidiary should have a compact area of operation, to facilitate recruitment and deployment of man power, apart from providing the needed thrust to business operations and effective improvement in control, supervision and information system. It should be possible to evolve through this process a rational structure of subsidiaries of national banks which could handle rural banking in a more efficient and cost effective manner. Such rural banking subsidiaries should be treated on par with Regional Rural Banks in regard to CRR/SLR requirements and refinance facilities from NABARD and Sponsor Banks.

The Committee proposes that while Regional Rural Banks should be allowed to engage in all types of banking business, their focus should continue to be to lend to the target groups to maintain at a minimum the present level of their lending to
these groups. With a view to improving the viability of their operations, the Committee proposes that the interest structure of Regional Rural Banks should be in line with those of the Commercial Banks.

The Committee also left the option open to the Regional Rural Banks and their Sponsor Banks as to whether the Regional Rural Banks should retain their identity so that their focus on lending to the target groups is not diffused or where both the Regional Rural Banks and their Sponsor Banks wish to do so, they could be merged with the Sponsor Banks and the Sponsor Banks in such cases should take them over as 100 per cent subsidiaries by buying out the shares from other agencies at a token price and eventually merge them with the rural banking subsidiaries.

The Committee recommends that instead of having a common recruitment system for officers, individual banks should be free to make their own recruitment. As regards clerical grades, the present system of recruitment through Banking Service Recruitment Boards may continue.

The Committee believed that the Indian Banking system was over-regulated and over-administered. The Committee placed grater emphasis on internal audit and internal inspection systems of banks. And the inspection by the supervisory authorities should be based essentially on the internal audit and inspection reports.

KHUSRO COMMITTEE RECOMMENDATIONS:

The Agricultural Credit Review Committee (ACRC) chaired by Prof. A.M. Khusro, appointed by Reserve Bank of India in August 1986 studied exhaustively the problem of rural credit. There is a strong identity of approach between the Khusro Committee and the Narasimham Committee on such matters as interest rate policy, credit to agriculture and weaker sections of the society, subsidies, autonomy of financial institutions etc., though the Narasimham Committee has advocated a faster pace of reforms.
The Khusro Committee reviewed the achievements of the multi-agency system in rural credit. It pointed out in its Report (1990) that between 1969 and 1986, the number of rural branches of commercial banks increased from 1832 to 18286 and between 1976 and 1986, short term loans and advances of commercial banks to the agricultural sector rose from Rs.212 crores to Rs.1252 crores and term loans from Rs.192 crores to Rs.1476 crores. Between 1975 and 1986, Regional Rural Banks increased in number from 6 to 194 and their branches from 17 to 12838. In 1986, their deposits and advances had risen to Rs.1714 crores and Rs.672 crores respectively from negligible levels in 1975. Short and medium term credit issued by Primary Agricultural Cooperative Societies rose from Rs.203 crores in 1961 to Rs.3140 crores in 1986. Long term loans issued by Land Development Banks directly to farmers grew from Rs.56 crores in 1966 to Rs.533 crores in 1986.

The Committee felt that in the process, the frontiers of institutional rural credit widened and interest rates in the rural areas came down. The non-institutional sources, no doubt, continue to purvey credit at higher interest rates but these are now significantly lower than in the past. Some of the credit needs of the rural population like consumption credit are, in the main, met by these sources.\(^{11}\)

In its view, however, the multi-agency system has not made much dent in the rural economy as is evident by the fact that "only about 30 per cent of the rural families have demanded or obtained access to the institutional credit system..... All in all, in the aggregate as well as for the middle farmers, the credit system has a long way to go before it can be said to be extensively used or begin to change the weak structures of the agricultural economy and of the rural credit institutions."\(^{12}\)

The Committee has pointed out several weaknesses in the system such as weak recycling of credit, poor deposit mobilisation, ineffective lending, poor loan recovery etc. The basic weakness common to all the rural credit institutions, however, has been the poor viability. As a cumulative effect of the high transaction costs, administered interest rates particularly concessionality in interest rates on rural
lending, the net margin on loan was negative -3.21 per cent in the case of Primary Agricultural Credit Societies, -1.00 per cent in the case of Primary Land Development Banks, -1.85 per cent in the case of rural branches of commercial banks and -3.70 per cent in the case of Regional Rural Banks.\textsuperscript{13}

The Committee felt that Commercial Banks and Regional Rural Banks also suffered from deficiencies similar to those experienced by Cooperatives. It has observed, "Experience stretching over nearly two decades now of the performance of Commercial Banks and a decade and a half of Regional Rural Banks has, however, shown that weaknesses which were considered as endemic to the Cooperative System have, in fact, not been the weaknesses of the Cooperative System itself but the ones associated with the clientele they had been extensively serving in the past and a host of other factors. That the causes lie elsewhere has been amply borne out by the performance of the Commercial Banks and Regional Rural Banks since their entry in this area. The weaknesses, in fact, arise from such deficiencies as those relating to the structure of agricultural production itself.\textsuperscript{14}

The Khusro Committee also did not favour the charging of concessional rate of interest on priority sector advances of small sizes. It recommended the phasing out of this concession over a long time frame of 10 to 15 years "with a great deal of attention to the market conditions of supply and demand, with little pampering and spoon-feeding, no populist subsidies, concessional interest rates, writes off of the interest and loan amounts and overdues etc.", and developing an "autonomous, self-reliant, robust and cost effective system which does not work on crutches and concessions nor on tactics to please the populace temporarily."\textsuperscript{15}

Regarding banks' assistance to Priority Sectors, the Khusro Committee had taken a "two category" view of the credit system, "the larger category functioning with a developmental logic, cost-effectiveness, efficiency, rising productivity, surplus generation and market orientation, while the relatively smaller category of well-specified, low income segments and socially weaker sections of the community and
they alone should qualify for an anti-poverty treatment and only until they graduate away from the poverty-zone to the realm of non-poverty." There should be, in its view, no vaguely, described intermediate categories."16

The Committee examined the viability aspect and felt that the negative net margin was the lowest (-1.00 per cent) in the case of Primary Land Development Banks and highest (-3.70 per cent) in the case of Regional Rural Banks. Low transaction costs gave some advantage to Primary Agricultural Cooperative Societies (5.40 per cent) and Primary Land Development Banks (3.39 per cent) but these were higher at 6.00 per cent for commercial banks and 6.90 per cent for Regional Rural Banks. Cost of funds was the lowest in the case of Commercial Banks (7.48 per cent) followed by Primary Land Development Banks (7.78 per cent), Regional Rural Banks (7.80 per cent) and Primary Agricultural Cooperative Societies (9.90 per cent). Average gross income was comparatively low at 10.17 per cent for Primary Land Development Banks followed by 11.00 per cent for Regional Rural Banks, 11.62 per cent for Commercial Banks and 12.09 per cent for Primary Agricultural Cooperative Societies."17

Regional Rural Banks which were fashioned as low cost institutional set-up to look after mainly the credit needs of the weaker sections of the rural society have degenerated into the 'sickman' of the Indian Rural Credit Structure. The Committee observed that an analysis of various factors show that the weaknesses of Regional Rural Banks are endemic to the system and non-viability is built into it. Referring to the need for strengthening the credit institutions, the Committee felt that the objective of serving the weaker sections effectively could be achieved only by self sustaining credit institutions and that the Regional Rural Banks, as they are, are not institutions which could fulfil this role.

The logic and rationale which justified or perhaps necessitated the setting up of the Regional Rural Banks do not any longer exist. There have been near-parity in pay scales between Commercial Banks and Regional Rural Banks and this and other
factors have made the loan transaction costs in Regional Rural Banks at times even higher than in rural branches of Commercial Banks. The local feel thought to be brought in by Regional Rural Banks through their staff was not found to be the same as in Cooperatives. Besides, the public sector commercial banks are involved in a much larger way in lending to the rural areas as well as to the weaker sections. The share of Regional Rural Banks (which account for 32 per cent of the total number of rural and semi-urban branches of the banking system) in rural lending is barely 9 per cent and in total business 6.4 per cent whereas the commercial banks (which accounted for the balance of 68 per cent of the branches) have as much as 91 per cent of the share of rural and 94 per cent of the total business. Under these circumstances, the Committee observed that the only feasible alternative to achieve this end would be to merge the Regional Rural Banks and their branches with the concerned Sponsor Banks by making necessary amendments to the existing law.

The merger, the Committee opined, would not only leave no void but, on the other hand, the Commercial Banks which are stronger institutions, may be in a position to step up their share in rural lending so far taken care of by the branches of Regional Rural Banks. More important than this, the scope for internal cross subsidisation would be widened and losses on account of having to serve the weaker sections could be offset by the earnings from the higher interest yielding loan portfolio of Sponsor Banks. While this proposal does not mean any dilution of the concern for the poor, the intention is to give the small man a stronger institution to serve his needs best. To guard against any possible slackness, the Committee suggested enhancement in current stipulation of lending to weaker sections by Commercial Banks at 10 per cent to 15 per cent of the net bank credit.

As regards the absorption of the accumulated losses of the Regional Rural Banks, the Committee offered in-built suggestions. The net loss of each Regional Rural Bank should be shared between the Government of India, the Sponsor Bank and the State Government in the same proportion as their share holdings. The current
profit position of the Sponsoring Commercial Banks is felt adequate to absorb their share in such losses.

Looking to the accumulated losses of Regional Rural Banks which are steeply increasing year by year, the Committee felt a need of urgency for the proposed merger if the objective is to ensure service to the poor and not 'poor services'.


NOTES AND REFERENCES

3. *Ibid*, p.40