Executive Summary

Rural development vis-à-vis upliftment of rural poor has remained an abiding concern of the government both at the centre and at the state since the beginning of our planning era. One of the important factors behind the rural backwardness, poverty, and miseries of life is inadequate access to finance to utilise the productive resources available in rural areas. An easy access to institutional finance is, therefore, considered as an important vehicle to achieve the goal of rural development and a solution to the miseries that existed in rural India.

The regional rural banks (RRBs) were established to serve the banking needs of the people living in rural areas. They were expected to provide credit on easy terms and conditions for various productive purposes with a view to boost up the rural economy that comprise 72.2% of our total population. However, although these banks inherited the features of local feel of cooperatives and business acumen / professionalism of commercial banks, yet, their profitability and financial viability was not given prime importance.

Under the wave of liberalisation and global orientation of Indian economy, the banking sector reforms were introduced in 1994-95 in the line of Narashimham committee report (1991), a bit later than in commercial banks. This pioneered a new era in rural banking of the country and brought the RRBs at par with the commercial banks. The role of RRBs in economic development of rural areas was relegated and the efficacy of these banks as a separate financial institution for rural people was questioned. It was also argued that in order to serve the rural poor the financial health of these banks are to be strengthened at first. They are to become self sufficient and economically viable.

The present study was undertaken for an in-depth analysis of the performance of the RRB in Barak Valley in South Assam, with a view to highlight its present financial viability status and examine whether the reform measures have exerted any significant impact on its profitability and viability. It also intended to suggest some policy measures to solve the problems that are being encountered by the RRB of the region in particular and of the nation as a whole.

To achieve the aforesaid objectives 5 (five) null hypotheses have been formulated, on the basis of a model, especially designed for financial viability of a financial institution like RRBs [1.10, diagram-1.3].
The hypotheses are:

- $H_0^1$: ‘The operational policies and objectives of the RRBs of the country have not changed with the changing socioeconomic scenario, over time’.
- $H_0^2$: ‘The financial performance of the bank under study has not improved, in spite of the implementations of banking sector reform measures in RRBs.’
- $H_0^3$: ‘The profitability of the bank under study is independent of the measures implemented by the banking sector reform.’
- $H_0^4$: ‘The operational efficiency and viability of the RRB under consideration has not improved even after the implementation of reform measures.’
- $H_0^5$: ‘The RRB has failed to satisfy its customers’ aspirations.’

The major findings of the study are as under:

1. The Study observed a paradigm shift in the operational objectives, policies and approaches of the RRBs in the post reform era [2.9.7, Table-2.5] and therefore rejected the null hypothesis $H_0^1$: ‘The operational policies and objectives of the RRBs of the country have not changed with the changing socioeconomic scenario, over time’.

2. The geographical area of operation of the bank has remained unchanged since its inception. [3.2.1]

3. No branch expansion programme was undertaken after 1990-91. [3.2.2].

4. A total number of 20 branches were either relocated to more vibrant areas of from rural to semi-urban or converted to urban branches from semi-urban status during the period 1994-95 to 2003-04 [3.2.3, Table-3.2]

5. The average number of population per branch of the bank under study for the Region (67932) is higher than that of the state (65978) but less than that of the country as a whole (70906). [3.2.4., Table 3.3, Diagram-3.3]

6. The performance of the bank in terms of number deposits accounts, number of deposits accounts per employee, number of deposits accounts per branch, volume of deposits outstanding, volume of deposits per employee and per branch, volume of deposits per account, total number of loans and advances accounts, number of loans and advances accounts per employee and per branch, total volume of loans and advances outstanding, total income of the bank, income per employee and per branch has shown a significant improvement in absolute terms.$[p(t) < 0.05]$
However, in terms of their growth rate, the performances are not satisfactory [3.2.5a, 3.2.5b., 3.2.6a, 3.2.6b, 3.2.6c].

7. The volume of priority sector lending has increased in absolute terms but its compound growth rate of the volume of priority sector lending has declined from 25.64% during the pre reform period to 16.26% in the next period. [3.2.7].

8. The significant decline C.D. ratio in the post reform period compared to that of the pre reform one (t = 11.0437, p = 0.000) demonstrates that the RRB is moving away from its rural lending activities and gradually approaching towards investment in corporate sector in order to increase the volume of profit. The decline in C.D. ratio also demonstrate the reverse flow of fund from the rural areas to the urban centers.[3.2.8].

9. No statistically significant improvement in recovery rate of the bank was observed in the post reform period (t = 0.954, p = 0.363), reflecting the need of adopting more rigorous steps for recovery of loans. [3.2.9] 

10. However, the NPA percentage is found to be declining over the years following implementation of banking sector reform measures. [3.2.10; Diagram-3.15].

11. The comparison of net NPA% of the bank with that of other RRBs of the state shows that the bank under study is in better position than two other RRBs of the state, viz., erstwhile Lakhimi Gaonlia Bank and Longpi Dehangi Rural Bank.[Table-3.6]

12. There is negligible change in the composition of income as depicted by the statistically insignificant change in the interest income to non-interest income ratio of the bank, despite the implementation of reform measures (t = 2.216, p = 0.051). [ 3.2.11]

13. Income to volume of business ratio has increased marginally from 0.065 to 0.075 over the two periods under comparison (t = 0.10, p = 0.341). [3.2.11]

14. Income to working fund ratio has however remained constant for both the periods at 0.09, delineating the fact that the performance of the bank has not improved in terms of this ratio. [3.2.11].

15. The volume of profit during the post reform period is found to increase at the positive rate (g2 >0; b>0) [3.212]
16. the increase in profit per branch, profit per employee, profit to volume of business ratio, profit to volume of expenditure, profit to income ratio are not statistically significant [3.2.12, Table-3.7]

With these findings of chapter III we have partially accepted the null hypothesis $H_0^2$: ‘the financial performance of the bank under study has not improved in spite of the implementation of banking sector reform measures in RRBs’ and concluded that the reform measures brought a mixed blessings to the bank to improve its performance. In one hand, these measures have opened up some new avenues of increasing income but at the same time introduced challenges in the form of compliance with the prudential norms of income recognition, asset classification and provisioning; and by introducing tough competition in rural banking business with other commercial banks and financial intermediaries in the field.

17. The bank has turn around from loss incurring stage to profit earning stage in 1998-99 and since then it has been earning profit. But the improvement is not statistically significant $(t=0.76885, p = 0.459755)$. Similarly, in terms of (a) Profit per branch, (b) Profit per employee, (c) Profit to the volume of business (%), (d) Profit to Working fund (%), (e) Profit to volume of expenses (%) and (f) Profit or loss to Income (%); the improvements in the performance of the bank are not statistically significant. ($P(t)>.05)$; [3.2.12; and 4.3.4a].

18. However, the bank has not yet come out from the accumulated losses of the past years. [Table-3.7]

19. The factors that contributed to the turn around of the bank from its loss incurring stage to profit making stage are:-

a) significant increase in the volume of business per branch $(t = 4.568, p = 0.001)$ [4.3.4b]

b) Decline in C.D. Ratio and moving towards the urban / affluent clients / corporate sector $(t = 11.044, p = 0.0000)$ [4.3.4c].

c) Increase in Recovery rate $(t = 4.622, p = 0.001)$ [4.3.4d].

d) Average working fund per branch [4.3.4e]

e) Decline in the share of borrowings to the working fund [4.3.4f]
f) Deliberate reduction in priority sector lending and avoidance or risk of lending [4.3.4g]

g) Reduction in transaction cost through increase in banking businesses by accommodating relatively well off clientele in semi-urban / urban areas, neglecting the poor rural people for whom the bank was actually established. [4.3.4j]

h) A reduction in manpower expenses to total expenses ratio, mainly by postponing new recruitments (t = 5.684, p = 0.000) [4.3.4l]

20. The study found a weak and negative correlation (statistically not significant) between the volume of profit and the share of priority sector lending in both the periods ($r = -0.311$ with $p = 0.352$; and $r = -0.391$ with $p = 0.235$ respectively for the two periods under study) and thus concludes that the problems are not with the priority sector lending but with their management and recovery. [4.3.4g]

21. Composition of income found to have insignificant effect on profitability of the bank. [4.3.4h].

22. There is no significant improvement in the spread to working fund ratio of the bank during post reform period [4.3.4i].

23. The decline in the burden ratio of the bank over the periods, found to be declining statistically insignificant [4.3.4k].

With these findings the null hypothesis $H_0^3$: "The profitability of the bank under study is independent of the measures implemented by the banking sector reform" is partially rejected and the chapter concluded with observations that reform measures have influenced the profitability of the RRB to some extent. However, the bank could not exploit its profit potentiality fully because of the inefficiencies, mainly, in the field of credit deployment, recovery performance and product innovation.

24. Two profit functions of the form

$$\pi_t = \alpha + \sum \beta_i X_{it} + \epsilon_{it} \quad (1), \text{ and}$$

$$\pi_t' = \alpha' + \sum \beta'_i X'_{it} + \epsilon'_{it} \quad (2)$$

have been derived for pre and post reform periods, following the multiple regression analysis [4.4].
25. The regression summary is as under:

<table>
<thead>
<tr>
<th>Predictors</th>
<th>Pre reform period</th>
<th>Post reform period</th>
</tr>
</thead>
<tbody>
<tr>
<td>(Constant) ($\alpha$)</td>
<td>-2.658</td>
<td>-24.27</td>
</tr>
<tr>
<td>Volume of Deposits per branch (Rs.'000) ($X_1$)</td>
<td>-0.041</td>
<td>0.026</td>
</tr>
<tr>
<td>Volume of outstanding Loans / Adv. per Branch (Rs.'000) ($X_2$)</td>
<td>-0.268</td>
<td>0.139</td>
</tr>
<tr>
<td>Share of priority sector lending to total loans and advances (%) ($X_3$)</td>
<td>-0.166</td>
<td>-0.143</td>
</tr>
<tr>
<td>Recovery rate (%) ($X_4$)</td>
<td>0.462</td>
<td>0.588</td>
</tr>
<tr>
<td>Volume of Interest income per branch (Rs.'000) ($X_5$)</td>
<td>-0.307</td>
<td>0.241</td>
</tr>
<tr>
<td>Volume of non-interest income per branch (Rs.'000) ($X_6$)</td>
<td>-0.026</td>
<td>0.154</td>
</tr>
<tr>
<td>Volume of Interest expenses per branch (Rs.'000) ($X_7$)</td>
<td>-0.386</td>
<td>0.067</td>
</tr>
<tr>
<td>Volume of operating expenses per branch ($X_8$)</td>
<td>-0.273</td>
<td>-0.111</td>
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</table>

<table>
<thead>
<tr>
<th></th>
<th>Coefficients</th>
<th>t</th>
<th>Sig.</th>
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<th>t</th>
<th>Sig.</th>
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<td>-0.041</td>
<td>-1.266</td>
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<td>0.815</td>
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**ANOVA**

<table>
<thead>
<tr>
<th></th>
<th>R^2</th>
<th>F(8,2)</th>
</tr>
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<tbody>
<tr>
<td></td>
<td>0.887</td>
<td>40.042 (p=0.025)</td>
</tr>
<tr>
<td></td>
<td>0.844</td>
<td>54.929 (p=0.018)</td>
</tr>
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*Dependant variable: Profit / loss per branch ($\pi$)

26. We observed that the regression is significant in both the periods ($F_{(8,2)} = 0.025$ and $54.929, p<0.05$) and explanatory variables explain more than 80% of variations in the explained variable ($R^2 = 0.887$ and $0.844$ respectively).

27. The differences in the magnitudes of coefficients and their directions (signs) as depicted in the derived function over the periods signify that marginal impact of reform measures on profitability of the bank [4.4] and thus further supports partial rejection of $H_0^3$.

Chapter V was devoted to analyse the viability problems of the bank from efficiency point of view with the hypothesis $H_0^4$: 'The operational efficiency of the RRB under consideration has not improved despite the implementation of banking sector reform measures' and the econometric analysis came out with a number of findings. The important findings are:

28. There has not been any significant change in the average business growth ratio of the bank in the post reform [5.5.1].

29. The business efficiency ration has not improved in significant manner [5.5.2]

30. Employee efficiency in terms of number of business accounts per employee has increased significantly over the periods under consideration [5.5.3]

31. There is significant increase in per employee business turnover ratio [5.5.4.]

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32. The branch level efficiency of the bank in terms of average number of business accounts per branch and business turnover ratio per branch has also increased significantly. [5.5.5 and 5.5.6]

33. The increase in income efficiency ratio is not statistically significant indicating the fact further scope of increasing income with similar expenditure. In other words, more income generating avenues are to be created within the existing set up. [5.5.7]

34. The increase in non-interest income to total income ratio is not statistically significant [5.5.8.]

35. No statistically significant decline in the business cost efficiency ratio and the employee cost efficiency ratio is observed in the post reform period in comparison to that in the earlier period [5.5.9 and 5.5.10].

36. There is marginal and statistically insignificant improvement in the operational cost efficiency ratio over two periods under study. [5.5.11].

37. The chapter identified the factors affecting the viability of the RRB with their relative significance with the application of Principal Component Analysis. It has been found that the 88.515% variance in financial viability of the RRB can be explained by the two factors, viz., Operational Activities and Efficiency factor. The operational activities are the prime factor that includes 9 components such as Total Business Growth Ratio, No. of Deposits A/C Per Employee, Volume of Deposits Per employee (Rs.'000), No. of Loans/Adv. Accounts Per Employee, Volume of Loans / Adv. Per Employee, No. of Deposit A/C Per Branch, Volume of Deposits Per Branch (Rs.'000), No. of Loans/Adv. Accounts Per Branch, and Volume of Loans / Adv. Per Branch (Rs. '000). These components taken together explain 56.887% of variance in viability.

38. The efficiency factor includes five components, viz., Business efficiency ratio, Income Efficiency Ratio, Non-interest income to interest income ratio, Business cost efficiency ratio, Employee cost efficiency ratio and they, together explain 31.683% of variance in financial viability of the bank under study.

39. With the above findings the chapter partially accepted the null hypothesis considered for this part of treatise. The chapter concluded that the viability of the bank has improved only partially with some improvement in operational factors.
but on efficiency side, the bank is performance is far from the satisfactory level and therefore, an adequate strategy is needed to improve both the operational and efficiency factors to exploit the untapped potentialities.

With the above conclusion we proceeded to analyse the aspect of customers’ satisfaction levels of the bank in Chapter VI. With the introductory framework and conceptual underpinning of the concept of customers’ satisfaction, the chapter found:

40. In terms of Customers’ Satisfaction Index (CSI \(_{C}\)), 97.14% of the customers are under dissatisfied category and thereby suggesting an urgent attention to improve the C.S. level of the bank. [6.6.2; Table-6.4]

41. In terms of satisfaction index for attributes (CSI \(_{A}\)), the number of **highly dissatisfied customers** was found to be the highest for the ‘procedural complexities in sanctioning of loans’ (44.3%), followed by inadequate ‘sitting arrangements’ (32.14%) and longer ‘waiting time for withdrawal of money’ (29.3%). [6.6.3; Table-6.5]

42. 62.1% of the sample customers are **simply dissatisfied** with the décor of the bank, followed by inefficiency of staffs (56.4%) and waiting time for withdrawal of money (55%). [6.6.3; Table-6.5]

43. When the entire dissatisfied category of customers are considered (simply dissatisfied + highly dissatisfied), the study observed that more than 50% of the customers are dissatisfied with 15 attributes out of 21 considered attributes. ₵. [6.6.3; Table-6.5]

44. A considerable section of customers are indifferent with the attributes like ‘parking facilities’ (45.7%), ‘location of the bank’ (42.1%), ‘interest rate on deposits’ (41.4%), ‘service charges’ (40.0%) and so on. [6.6.3; Table-6.5].

45. Value of overall satisfaction index of the bank (CSI \(_{O}\)) turned out to be 2.479, indicating the fact that on average, the customers’ perception about the service quality of the bank is not satisfactory. [6.6.4; Table-6.5]

These findings clearly suggest us, to conclude that taking all the selected attributes under consideration, the customers of the bank are not satisfied with the services rendered by the bank and thereby, we safely accept our **null hypothesis** \(H_0\): “*The RRB has failed to satisfy its customers’ aspirations.*”
With the application of Principal component analysis, the factors influencing C.S. have been identified and their relative significance in determining C.S. is derived following factor analysis. It is observed that

46. More than 60% of the variations in C.S. can be explained by 6 components, viz., (i) Work culture and timeliness, (ii) Efficiency, (iii) Furnishing and basic amenities provided by the branch to the customers, (iv) Product variety, accessibility and friendliness, (v) Procedural complexities and (vi) Locational factor [6.7.5; Table-6.13].

47. The prime factor affecting the C.S is found to be the ‘Work Culture and timeliness’ which determines 12.464% of variance in C.S. followed by ‘Efficiency factor’ (11.366%). The other factors influence around 9% of variance in C.S. [6.7.5; Table 6.13]

48. Chapter-VII is the Epilogue, wherein the summary of the findings of the study, suggestions and conclusion are incorporated.

The study concludes with the following views:

a. The bank has achieved its current viability but it can not be considered a sustainable one as the accumulated losses are not yet covered up and the bank’s performance in respect of efficiency parameters are not satisfactory.

b. The reform measures bestowed mixed blessings on the RRBs. In one hand it opened up new vistas for increasing income with a radical change in the approaches of rural banking and on the other placed the challenges and threat before for their existence in the face of competition with the modern commercial banks.

c. Although the reform measures have brought the RRBs at par with the other commercial banks, but the competitive strength of the RRBs is relatively much lower than that of the nationalized and modern private commercial banks in urban banking business. Therefore, the RRBs have to concentrate on their rural banking business to achieve financial viability where it has some comparative advantage of experience and knowledge

d. The deliberate move to cut down the C.D. ratio ignoring the rural clientele to avoid the risk of lending and preference to the corporate sector are not the way out
of the viability threat of RRBs. The real problem lies with the efficient fund management, recovery management and asset management and hence they are to concentrate on improving these vital aspects of banking.

e. The bank has to explore its new areas of business in rural areas to achieve its viability.

f. The present move of amalgamation of 4 RRBs of the state (sponsored by the UBI) and formation of Assam Gramin Vikash Bank to enhance the capital base, expand the operational area and bring the RRBs under a unified control would become futile unless the RRB concentrates on the building up of the credit portfolio, reengineer its products, and restructure its' operational policies keeping an eye to the needs of their clienteles.

g. In the present day competitive banking environment, the RRB is to devise ways and means to attract new customers and retain the existing ones. One important way to achieve this goal is to enhance the customers' satisfaction levels by improving its work culture, timeliness, efficiency of the staffs, and provision of basic amenities to the customers and so on.

h. Further the bank has to adopt the technological innovations in order to keep pace with the time and reduce the unit cost of business.