CHAPTER- I
Introductory

1.1. Introduction:

A key objective of economic development is to work out ways to lift the people out of poverty. The broad contour of rural poverty clearly shows that the poorest sections of the rural population belong to the families of land less labourers, small and marginal farmers, agricultural labourers, rural artisans, scheduled castes and tribes. The basic causes of rural poverty, indebtedness, backwardness and miseries are interlinked with the unemployment or underemployment of available skills and resources. Therefore, the way out to the problems of rural backwardness and poverty lie with the productive deployment of both human and natural resources.

Rural poverty in India is also largely, due to an inequitable access to resources and lack of institutional backings. A developed financial system, therefore, plays a fundamental role for productive deployment of available resources and exploiting the growth opportunities. Financial assistance to the rural poor, particularly institutional assistance for the development of rural activities like agriculture, handicrafts, rural industries, etc., thus, plays decisive role to bring about an over all economic development in the rural areas. Credit, in rural areas, not only acts as one of the critical inputs in agriculture, but also as an effective means of social and economic transformation.

Easy credit with suitable terms and conditions and their productive deployment increases the scope of income generation for the people in rural areas and thus acts as an important instrument of improving their economic conditions. Agricultural and non-agricultural activities in rural areas being typically seasonal in nature, rural households need credit to smooth out seasonal fluctuations in their earnings and expenditure. Further, in the absence of adequate general social security programs in the country; rural households need credit for various consumption purposes as well as for an insurance against risk. Therefore, supply of credit to them is of crucial importance for maintaining progress at the societal level also. In the Indian context, another important purpose of borrowing is to meet expenses for a variety of social obligations and rituals. To fulfill this variety
of credit needs, rural households require an access to such a credit institutions that provide them a wide range of financial services, at reasonable cost. Further, credit being one of the most important needs for economic development of the rural poor, the role of the credit institutions has therefore to be tuned to meet the requirements of specific area and specific target groups.

However, the disbursement of rural credit was a monopoly of the money lenders, till the enactment of the Cooperative Societies Act in 1904 by the colonial Government. With a view to make cooperatives as premier institutions for providing credit to the rural people, the process of three-tier cooperative structure\(^1\) was initiated in 1915. However, these initiatives failed to make any significant dent in the rural credit supply structure of the country. The gravity of the situation was highlighted in the report of the All India Rural Credit Survey Committee (1954). The report exhibited that only about 3% of the total amount borrowed by the cultivators (in 1951-52) came from government and cooperatives, and less than 1% from commercial banks. The nationalisation of commercial banks in 1969 and subsequent rapid expansion of bank branches in un-banked and under banked areas, heralded a new era of hope of restructuring rural banking. But, still there was a growing realization that the ethos and attitude of commercial banks, even after their nationalisation, were not conducive to meet the credit needs of the rural masses. The reasons behind this were, mainly, high cost of servicing, seasonal credit requirements, geographically dispersed customers, lack of trained and motivated rural bankers and inadequate local environment.

During the early 70's, it was felt that institutional finance was not available to all sections in the rural areas, due to the inability of cooperatives and commercial banks in meeting credit requirements of the rural areas. Further, the deficiencies in rural credit system were not only on the basis of quantum of aggregate credit supplied and demanded but also on the basis of class bias.\(^2\) In pursuance with this view, the government of India set up the Banking Commission in 1972 to evaluate the various alternatives for a healthy rural banking system in the country. The Commission, in its report in 1972 for the first time proposed for the setting up of Rural Banks to accelerate the flow of institutional credit, especially to meet the needs of the weaker section of the rural community.

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\(^1\) The three tiers consisted of: Primary Agricultural Credit Societies (PACS) at the village level, at the 'Taluka' level and at the 'district' level.
\(^2\) Report of the Banking Commission (1972). Govt. of India
Following the recommendation of the Banking Commission, the government of India appointed a “Working Group on Rural Banks” under the chairmanship of Shri M. Narashimham, on July 1975, to examine the feasibility of setting up of new set of rural banks as subsidiaries of public sector banks to cater to the credit requirements of the rural people. The Group identified the inherent lacunae and inability of existing financial institutions in respect of correcting the prevalent gaps in the institutional rural credit. Consequently, the Group recommended for establishment of a new type of institution which are state-sponsored, region-based and rural-oriented financial institution, called Regional Rural Banks (RRBs). The government of India accepted the recommendations of the Working Group and accordingly the RRBs came into being on 2nd October, 1975, after the ‘Regional Rural Banks Ordinance’, promulgated by the President of India, on September 26, 1975 (which was subsequently replaced by the ‘Regional Rural Banks Act of 1976’). As per the Regional Rural Banks Act of 1976, the prime objective behind the establishment of the RRBs were providing impetus to the growth of the rural economy by mobilizing resources from the region and deploying them within the rural populace of the same region.

However, the present Indian rural credit system includes a number of agencies like the co-operatives, regional rural banks, commercial banks, non-banking financial institutions, self help groups and, of course, a large network of informal credit outlets, together constitute the present institutional structure of agricultural and rural credit system is shown through a chart presented in Diagram-1.

1.2. Present Status of RRBs in Rural Banking:

Over the years, the RRBs, considered as Poor Man’s Bank, have taken deep roots and have become an inseparable part of the rural credit structure. They are playing a key role in rural institutional finance in terms of geographical coverage, clientele outreach, business volume and contribution to the development of the rural economy. From a modest beginning of 6 RRBs with 17 branches covering 12 districts in December 1975, the numbers have grown into 196 RRBs with 14,484 branches working in 522 districts across the country (as on 31st March, 2005). Their large branch network in the rural areas constitutes around 43

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3 Statistics on Regional Rural Banks: as on 31 March, 2005, NABARD, Mumbai
per cent of the total rural branches of commercial banks. The rural orientation of RRBs is formidable with rural and semi-urban branches constituting over 97 per cent of their branch network.\(^4\)

With this rapid expansion in outreach, the RRBs had become the principal agency to finance the government sponsored rural development and anti-poverty programmes like Integrated Rural Development Programme (IRDP), Jawahar Rozgar Yojana (JRY), Prime Minister's Rozgar Yojana (PMRY) and others. During the financial year 2004-05, the RRBs of the country as a whole, mobilized Rs. 62283.71 crore of deposits and disbursed credit worth Rs. 26068.57 crore (with C.D. ratio 41.85).\(^5\) The RRBs alone have organised roughly 12 lakh self-help groups (45% of the total self-help groups) in the country. RRBs have also issued over 40 lakh Kisan Credit Cards to the farmers and organised over 5,000 out of 11,000 farmers’ clubs under NABARD scheme.\(^6\)

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Diagram-1.1

Institutional Structure - Agriculture & Rural Credit in India

\[ \text{RBI} \]

\[ \text{NABARD} \]

\[ \text{GOI} \]

- Cooperative Banks
- Scheduled Comm. Banks (100)
- Regional Rural Banks (196)
- Short Term Structure
- Long Term Structure
- Metropolitan Branches (8507)
- Metropolitan Branches (6)
- SCBs (29)
- SCARDBs (19)
- Urban Branches (10006)
- Urban Branches (348)
- Branches (823)
- Branches (1219)
- PCARDBs (755)
- Semi-Urban Branches (12633)
- Semi-Urban Branches (1875)
- DCCBs (367) (branches 12407)
- Branches (689)
- PACS (92000 approx)
- Rural Branches (20449)
- Rural Branches (12084)

*Position as on 31 March, 2001
**Source: www.nabard.org.in

Note: In addition to the above agencies, Urban Cooperative Banks and Local Area Banks also provide credit for Agricultural and Rural Development.

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\(^4\) Debate in the XV Lok Sabha on Regional Rural Bank (Amendment Bill, 2004)
\(^5\) Trends and Progress of Banking in India, 2004-05, RBI
\(^6\) Debate in the XV Lok Sabha on Regional Rural Bank (Amendment Bill, 2004)
1.3. Statement of the problem

Over the years, operation under the dictate of easy credit policy towards agriculture, politically motivated decision-making, subsidised lending, emphasis on certain quantitative targets, inadequate attention to qualitative aspects of lending, etc., led to mounting overdues and enormous losses of RRBs. Even so, by virtue of their social banking episode towards rural clienteles and the socio-economic development of weaker sections living in rural areas; the Regional Rural Banks (RRBs) also largely escaped serious evaluation of their performance in commercial or financial terms and until 1991.

However, there was a radical change concept of development banking after publication of the Report of Committee on Financial System in 1991 (Chairman, M. Narashimham). The RRBs came under the scanner with gradual realisation that a catalytic role in rural economic development through providing required banking services can not be expected from a financial institution that suffers from operational and financial inefficiency or which is financially nonviable. As a result, they could not remain insulated from wave of financial reforms on the ground of their rural nature and welfare orientation.

The government’s concern relating to the performance of RRBs increased in June 1994, when out of 196 RRBs, 172 were found unprofitable. In few cases, besides capital, there had been an erosion of public deposits also. Further, it was observed, “150 RRBs out of 196 incurred losses in each of the years from 1989 to 1994 and many of them had completely eroded their equity and resources.” Under these circumstances, in 1994-95, the RBI implemented banking reform measures in RRBs in order to boost up their viability and profitability.

The profitability of RRBs, though improved in the years 1995-96 and 1996-97, profit was overshadowed due to the introduction of income recognition and asset classification (IRAC) norms in 1995-96 and the provisioning norms with effect from 1996-97.

As a measure of rejuvenating them, the government of India released a sum of Rs. 223.57 crore during 1995-96 for the restructuring of 53 RRBs out of
selected 70 RRBs. A provision of Rs. 200 crore was also made in the union budget for 1996-97 for recapitalization of 70 RRBs in 1996-97. The budget for 1997-98 provided for Rs. 270 crore for the same purpose.

In 1999-2000, out of 196 RRBs, 162 showed profits and of them, 55 had wiped out accumulated losses as well. The viability based categorisation of RRBs, as on 31 March 2000, showed that out of 196 RRBs, 81 RRBs have wiped off their accumulated losses and in a way attained a sustainable viability, whereas, 89 other RRBs have achieved a turn around and attained a current viability status leaving only 26 RRBs which continued to incur losses. In 2003-04, 163 RRBs earned profits amounting to Rs.953 crore while 33 RRBs incurred losses to the tune of Rs.184 crore. Ninety RRBs had accumulated losses as on March 31, 2004. The aggregate accumulated loss of RRBs amounted to Rs. 2,725 crore during the year 2003-04.

The above facts, obviously, raise doubt regarding the suitability and effectiveness of banking sector reform measures in solving the problems encountered by the RRBs over the years.

However, the matter of fact was that, while the RRBs of our country were struggling for their existence due to the alleged restrictive policy conditions, poor clientele base, low recovery rate and higher cost of operation, the Grameen Bank of Bangladesh was gaining its popularity in the world for its success in implementing the similar objectives as in case of our RRBs. The experience of Grameen Bank had shown that an access to institutional credit on easy terms and conditions could make a sea change in rural economic scenario. The Grameen Bank has also proved that the poor are credit worthy and an efficient financial institution can improve the life of the rural poor, without putting a threat to the viability of the institution.

Hence, questions about operational policy, managerial efficiency, and the ability of RRBs to serve the society come to the fore front. Further, with the implementation of banking sector reforms in RRBs in 1993-94, there has been a sea change in the objectives and operational policies. The RRBs are now exposed to aggressive competitive market conditions from their protected and regulated

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10 Financial Statements of Regional Rural Banks, 2001, NABARD, Mumbai
11 Financial Statements of Regional Rural Banks, as on March 2004, NABARD, Mumbai.
regime. Thus, unless the RRBs are equipped to face the challenges imposed by the banking sector reforms, their existence would be at stake.

Under this backdrop, the present study entitled *Financial Viability and Profitability Problems of RRBs – An Empirical Study on South Assam* has been undertaken to get answers to these pertinent issues and examine how far the banking sector reform measures has enabled the RRB in the study area in improving its profitability and viability as well as to prescribe policy measures for improving the financial health of the RRB operating in this part of the country, the Barak Valley in Southern Assam

### 1.4. Conceptual Framework:

The viability of a bank like RRB needs to be assessed from both the social as well as commercial or financial considerations. But in today’s era of competition under the wave of liberalization and globalization, the viability of any organisation is being viewed from commercial aspects only. Further, because of the difficulties in measuring social viability due to complexities in its measurement and inadequacy of well accepted methods to quantify the social gains generated from the services rendered by a financial institution like RRBs, the present study concentrates on the aspect of financial viability only.

The term *financial viability* is used to refer the capability of the organisation to render services as a sound and healthy financial institution so that it can fulfill the banking needs and aspirations of the rural clienteles, as per the pre determined goals and objectives for which the organisation was established. The ‘financial viability’ of a project denotes its long run ability to meet its total cost out of its own resources and at the same time generate reserve or surplus for capital build up. It not only means the earning of profit but a sustained profitability with the ability to function and grow as an independent unit. Thus, viability implies profitability with self sufficiency and sustained growth over a period of time. Nevertheless, the financial viability may be viewed from two aspects - current viability and sustainable viability.

Current viability denotes the ability of the institution to meet the cost of management and the risk cost out of the gross financial margin available and the institution be in a position to earn reasonable profit.
Sustainable viability, on the other hand, indicates the ability of the institution to completely wipe out all accumulated losses and to adequately provide for bad debts/assets and start afresh with a clean balance sheet.

However, the problems of financial viability of RRBs are centred around the following three aspects:

**a) Profitability:**
Profitability is the first pre condition for achieving financial viability. The term profit has been considered from economic or commercial points of view, keeping the aspect of social profit aside. The term profitability is used to refer the profit earning capacity of the RRB. It does not refer to the volume of total profit but how efficiently the profit is earned. Profitability is measured by relating profit with the variables on which the volume of profit depends, such as, working fund, volume of business, etc.

**b) Managerial efficiency:**
The managerial efficiency is another important key to achieve both the commercial objectives of earning profit and the social objective of serving the poor. Managerial efficiency ensures commercial efficiency of a bank. It is measured in terms of different efficiency ratios, e.g. Business growth rate, business efficiency ratio, employee efficiency ratio, income efficiency ratio, business cost efficiency ratio, etc.

**c) Customers' satisfaction:**
Banks being service industry, Customers' Satisfaction (C.S.) plays a vital role in determining profitability and viability of a bank. Customer satisfaction (in RRBs) has been considered as the emotional response to the experiences associated with the quality of products, services, timeliness, efficiency, ease of access, environment, other facilities including the behaviour and attitude of the service providers in comparison to the customer’s expectations. It is the transaction specific effective response to the evaluation of discrepancy between the prior expectations and actual experience relating to banking services. In the event of its failure to satisfy the varied requirements of its customers in the competitive market conditions, the RRB, as an agent of supplying banking services, will be out of the domain of choice of its customers and its viability will be jeopardized. Therefore, the issue of customers’ satisfaction has been taken as another important aspect of viability problems.
1.5. Review of Literature:

The RRBs came into existence on 2nd October, 1975 following the recommendations of the Narasimham Group. Since then a wide range of literature is available on RRBs. However, most of them are relating to the performance, achievements and problems of RRBs in general. An extensive review of the literature on the RRBs is as under.

On the issue relating to the general problems faced by the RRBs in their functioning, Rao (1988), Sangawan (1989), Dhabal and Bhattacharya (1989), Singh (1989), Kuchhaditya and Shiyani (1998) and Basu (1998) in their studies expressed concern over the poor recovery rate and mounting over dues of the RRBs along with the subject of multi level control by RBI, NABARD, Sponsor Bank, and the Government of India. The studies recommended effective supervision by the bank officials, organising recovery camps and resorting legal action against selected affluent wilful defaulters to improve the recovery rate.

Chaudhuri and Kumbhare (1993) in their paper entitled ‘Rural Credit Structure and Flow’ observed that considerable improvement in the access of the rural borrowers to the formal credit institutions is mainly due to the directed institutional credit flow for priority sector and wide network of credit institutions. This has obviously, reduced the dependence of rural borrowers on informal sources of credit. But at the same time, in doing so, the rural financial institutions like RRBs had to function with a narrow / negative margin of earnings from their operations. Along with this, the rising over dues had been the major problem for these institutions. Analysing the working results of the 196 RRBs, the study observed that the RRBs as a whole had incurred a net loss of Rs. 71.40 crore during the year ended in March 1991. To resolve the issue of low recovery rate and mounting overdue leading to huge losses, the study emphasised on credit planning and suggested financing through informal sector linkage.

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13 Sangawan, S S “Viability of Rural Credit Structure: A Case Study of Regional Rural Banks”, Mittal Publications, New Delhi, 1999
18 Chaudhuri, B R and Kumbhare, S L “Rural Credit Structure and Flow: Some Issues” The BECON-1993, Pune
Dealing with the problems related to ‘Banking with the Poor’, Rangarajan (1994) identified that along with low recovery rate; the incorrect identification of beneficiaries, inadequate availability of proper infrastructure, lack of marketing facilities, etc. were the principal factors responsible for the failure of RRBs to bring about the desired result in banking activities with the poor rural people. The study also articulated that the failure of formal rural credit institutions like RRBs in the recovery front led to the emergence of NGOs and SHGs to act as the linkages between the credit institutions and the rural as well as the urban poor. Therefore, he stressed on people’s participation through the NGOs or SHGs to solve the problem.

Sinha Roy (1994) and Velayudhan (1994) in their comprehensive study of RRBs in West Bengal also expressed a similar view with Rangarajan and alleged the dismal performance of RRBs in recovery front as the prime factor that pushed them towards their non-viability. Yaron (1994), in his comprehensive study on the rural financial institutes of Thailand, Indonesia and Bangladesh laid major thrust on their financial self sufficiency and substantial outreach. His study observed that traditionally, the rural financial institutions (RFIs) have been sustained by various types of subsidies to ensure continued operation because of the high initial start-up cost. Yaron observed that that the RFIs, established to implement targeted and often subsidised loans, have suffered from inadequate planning, inefficient operations and also by inimical economic, political, social and infrastructural environment. The inadequate and depressed interest rates combined with concessional funds from State or Government agencies discouraged their deposits mobilisation. The RFIs have been looked as disbursement windows rather than balanced and full-fledged financial institutions. Unmotivated by commercial imperatives, these institutions have suffered from inadequate credit evaluation, management and monitoring with inevitably poor loan collection. The other causes of failure of the RFIs are:

- Specialised RFIs were established with an objective to serve the targeted groups only.

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• Legally imposed ceilings on lending interest rates have not allowed them to compensate against the high risks present in agricultural credit due to vagaries of nature.

• Preference towards large scale borrowers / entrepreneurs instead of small scale entrepreneurs to minimise the transaction cost of lending and strict collateral requirements have discouraged small borrowers.

To make the RFIs financially viable, he recommended the following:

• The rate of interest should be high enough to cover the non-subsidised financial cost and administrative cost.

• Reduction of administrative cost.

• Higher rate of interest to attract deposits.

• Increase in recovery rate.

Relating to the problems associated with the rural banking, Kotaiah (1995) observed that one of the major difficulties of rural financial institutions to fulfill the credit requirements of the rural community is the high transaction costs owing to their small and frequent credit needs. Further, the natural calamities, under financing, inadequate income generation from loan investment due to lack of proper infrastructure, etc, affects the recovery performance of the rural financial institutions adversely. To reduce the cost of operation and improve the recovery performance, the study suggested bank-SHGs and NGOs linkage programme.

Mukherjee (1996), in reviewing the performances of RRBs, identified a number of factors which have adversely affected the performance of the RRBs. Important among them are:

• significantly low credit worthiness of the borrowers,

• unavailability of collateral securities against borrowings,

• infrastructural and marketing bottlenecks thwarted the borrowed funds to be tied in quick income generating activities,

• absence of proper selection of activities,

• political manoeuvring of institutional borrowings, and

• inherent attitudes of banking staffs to care more for interests of the rich and powerful class neglecting the poor and deprived.

24 Mukherjee, N. "Credit Needs of Rural Poor and the Regional Rural Banks", Kurukshetra, Vol 45, No 10, July, 1996
Some of the important suggestions forwarded by him to improve the performance and financial viability of RRBs were,

- disbursement of loans to both target and non-target groups,
- a proper mix of various types of deposits,
- attractive and convenient savings/deposit schemes,
- encouragement of tiny savings deposits,
- change in attitude of the banking staffs towards the poor and illiterate rural people, and
- greater interaction with the local groups in loan disbursements and loan recovery.

Highlighting the unique nature of RRBs in India’s rural banking structure, of the country and their importance in delivering rural credit for upbringing of the rural economy, Panchamukhi (2001)\textsuperscript{25} pointed out the following inherent deficiencies in the system:

- The obligations of priority sector lending and other investment norms contributed to an increase in loan losses and NPAs.
- Decline in profitability and increase in NPAs have led to the gradual erosion of their capital base.
- Delay in processing the loans due to lack of commercial decision making, professional management and automation.

Singh (1989)\textsuperscript{26} delved the viability problems of the RRBs and observed that the very nature of environment in which they operate, the objectives set before them in providing credit at concession rates, inadequate interest surplus to cover their operational costs, poor recovery and consequent slow re-cycling of funds are the some of the important factors that have contributed to the poor performance of RRBs. For the better future prospects of the RRBs, he proposed linking further programme of branch expansion with the infrastructural development in rural areas, provision of rural consultancy services etc.

\textsuperscript{25} Panchamukhi, V R 'Lessons from the National Experience of India in Mobilising Domestic and external resources for Economic Development'. Asia-Pacific Development Journal. Vol 8, No 1, June 2001

Sathye (1996)\textsuperscript{27} has uncovered the fact that the RRBs have become more and more conservative in rural lending in order to avoid credit risks, reduce their NPA and achieve viability. As a consequence there is a sharp decline in credit-deposit ratio. He observed that in the changed banking scenario, the RRBs prefer to invest their funds in more safe avenues than to lend in their areas of operation. Ghosh (2005)\textsuperscript{28} has also highlighted that the decline in Credit-Deposit ratio for rural areas showing the fact that the ratio has declined from about 65 per cent in the 1980s to around 60 per cent in the early 1990s and further to below 40 per cent in 2001. Ghosh opined that this falling trend in Credit-Deposit ratio has improved the viability position of RRBs at the cost of diversion of funds from the rural areas to the urban areas and reduced the flow of credit for agricultural and rural development. This is just the opposite of the philosophy for what the RRBs were established as a separate financial institute of rural masses.

Patel (1996)\textsuperscript{29} criticised the role played by the sponsor banks, the government policies, as well as the indifferent attitude of the RRB officials. Deshpande, Mudgal and Gupta (1998)\textsuperscript{30} observed that though RRBs have been successful to create awareness for banking among rural masses, yet they have lost their initial image of low cost bank or the image of Poor Man's Bank. To them, RRBs, as an institution, have been facing a massive challenge for its survival owing to huge accumulated losses and operational deficiencies in their functioning. They opined that the RRBs can act as a catalyst for the growth process, provided, their functions are adequately supported by techno-economic teams, instead of just sanctioning loans for unviable projects in the name of helping the weaker sections of society.

Mehta and Kaveri (1999)\textsuperscript{31}, on the other hand, pointed out that the problems like, low capital base, high cost of intermediation, poor recovery of dues, thin interest spreads, limited investment opportunities of surplus funds, compulsion to lend even unviable government sponsored schemes, pay parity of RRB staffs with their sponsor bank counterparts and low employee motivation

\textsuperscript{28} Jayati Ghosh: Bank Nationalisation: The Record, MACROSCAN, 2005.
level are the prime factors responsible for low profitability and non-viability of RRBs. Acknowledging the initiatives taken by the RBI, NABARD and the Government of India to make these institutions economically viable, the study discerned that the RRBs would also have to change their operational activities in order to adapt with the changed scenario. Mishra (2000)\(^{32}\) had also expressed the similar view with Mehta and Kaveri (1999) and pointed out that in spite of achieving a commendable success in respect of geographical coverage, branch expansion, deposits mobilizations as well as credit deployment; the RRBs have failed to achieve success in terms of commercial profitability and viability because of a set of problems such as:

a) Competition from other agencies,
b) Wrong identification of beneficiaries,
c) Non availability of good premises for the location of their branches in rural areas,
d) Misuse of credit by the borrowers and mounting over dues,
e) Inadequate volume of credit for non-agricultural activities, and,
f) Inadequacy of trained staffs.

Mishra, therefore, suggested the following steps to improve the functioning of the RRBs:

a) Constitution of village committees for the identification of borrowers, and production of ‘No Dues’ certificates by the borrowers before disbursement of loan,
b) A coordination between the credit and non-credit institutions,
c) Utilization of refinancing and borrowing facilities for raising their earning assets to the maximum possible limits and mobilization of low cost deposits.
d) Timely supply of credit by speeding up the loan sanctioning procedures, and
e) Development of closeness and good rapport with their clientele.

Kaveri and Srivastav (2001)\(^{33}\) in their study on informal lending in the North East observed that the inadequate infrastructure, low level of industrialisation, deterioration in the law and order situation, adoption of the primitive agricultural technique, restrictive ownership rights, etc. have vitiated recovery climate and resulted in high level of NPAs. This led the banks to deploy

negligible credit in rural areas and resulted a fall in credit deposit ratio. Consequently, the rural households have no option but to borrow from informal sources. On the other side, the lengthy and complex procedures along with delay in sanction of credit by rural financial institutions including RRBs is also one of the responsible factors that forced the rural people to approach to the informal sources for their credit requirements at a much higher rate of interest. Therefore, he suggested involvement of Gaon Panchayets and SHGs by the RRBs for selecting the potential borrowers and viable projects.

The financial reforms measures initiated in 1991 onwards, following the Report of the Committee on Financial System (Narashimham Committee); were aimed at transforming the credit institutions, including rural ones, into organisationally strong, financially viable and operationally efficient through:

a) Additional capital contribution to NABARD by RBI and the GOI  
b) Recapitalisation and restructuring of RRBs  
c) Simplification of lending procedures  
d) Preparation of special credit plans by Public Sector Banks (PSBs) - the service area approach  
e) Launching of Kisan Credit Cards (KCCs)  
f) Linking of rural financial institutions (RFIs) with SHGs and NGOs.  
g) Deregulation of interest rate, etc.

The rural economic environments under which the rural financial institutions operate, have also undergone a remarkable change with the

a) changes in cropping pattern,  
b) increase in the activities of the non banking financial corporations (NBFCs) in rural areas,  
c) expansion in literacy and education and the resultant change in the pattern of demand for financial services  
d) integration between rural and urban areas and the resultant increase in the mobility of labour, capital and even credit between the two areas,  
e) supply of fertilisers and pesticides to the farmers by the suppliers on deferred payment basis,  
f) forward-trading by the commission agents in the form of advancing money to the farmers towards the purchase of output from them, etc.
Therefore, the reform measures have opened up new avenues before the RFls; but at the same time, have introduced new challenges to them also. Thus, these institutions have to adapt themselves suitably with the new environment for their sustainability and viability.

On the issue of the impact of financial sector reform measures a wide range of literature are available with strong arguments both in favour as well as against the implementation of reform measures in RRBs.

Singh, Arora and Mankad (1995) in their study expressed the view that the winds of globalisation and liberalisation of the economy and the resultant increase in competitiveness along with hard commercial logic has swept away the will of the bankers as well as of the government for using the credit for rural development as evidenced by the move to close down the so-called loss making branches, most of which are in rural areas. People of these areas need credit at a reasonable cost for their survival as well as for growth. Their opinion regarding such type of move by the Government and bankers is ‘to seek the remedy for the disease by killing the patient’. They opined that the poor are fully bankable and the main problem associated with the credit to the poor is not the cost of credit but the easy and better access to credit facilities. The suggestions forwarded by the study for better performance of the RRBs were the use of SHGs and the NGOs as the financial intermediaries between the banks and the poor for the motivation and guidance of the later.

Agarwal (1996) in his study on the impact of financial liberalisation on banking and stock markets has expressed the view that the reforms in industry and trade policies in mid-1980s along with the influence of international liberalisation and deregulation have led to the reform of the financial sector of Indian economy with a view to

- Increase the spread
- Improve the capital base and
- Reduce the non-interest operating expenses.

The above study, however, expressed doubt over the benefits of the implementation of the recommendations of Narashimham Committee, with the apprehension that it was very likely to disturb the existing structure and

34 Singh Arora, S and Mankad, D: "Banking on The Poor", National Bank News Review, Apr-June-1995
functioning of the banking system in India in general and more particularly, affect the rural banking scenario of the country adversely, under the pressure of commercial profit.

Rajagopal (1997)\textsuperscript{36} in his study on the impact of reforms on Indian banking asserted that there is a need of re-engineering the banking sector of the economy through introspection, innovation, invention and implementation of new solutions. But Bandhyopadhyay (1997)\textsuperscript{37}, on the other hand, stressed on the human resource development to combat the challenges before the entire banking sector. Welcoming autonomy in the banking sector with the implementation of reform measures in banking, Kulkarni (1997)\textsuperscript{38} expressed his doubt that in the absence of the required changes in the mindset of the employees, the banking sector reform measures are hardly going to yield any optimism in RRBs in near future. Prasad (1998),\textsuperscript{39} however, stressed on the organisational development of RRBs to meet the challenges placed before them by the financial sector reforms and also for their survival and growth. Arunajateson and Balaji (1999),\textsuperscript{40} in analysing the deficiencies in rural credit delivery system expressed their views that there was a total lack of efforts to carry out any supervision and recovery process and suggested setting up of credit management departments to evaluate the rural credit worthiness of the borrowers before advancing any type of loans.

However, Deshpande and Shrivastava (1999),\textsuperscript{41} in their analysis on the performance of RRBs after financial sector reforms observed that there was a turn around in the performance of RRBs after the implementation of financial sector reforms measures as exhibited by the increase in volume of business, high employee productivity, improved loan recovery system, control of transaction cost, improved investment level, lending to higher income groups, etc. However, Majumder (1999)\textsuperscript{42}, on the other hand, in his review of rural credit system, contradicts this view and opined that there has been a total neglect of rural credit

\textsuperscript{40} Arunajateson, S. and Balaji, S. - "Rural Credit - Deficiencies in Delivery" - The Hindu Survey of Industries, 1999.
\textsuperscript{42} Majumder, N. A.: "Reviewing Rural Credit" - Economic and Political Weekly, Vol 34, No 23, June, 19-25, 1999.
by the policy makers during the period 1991-96 and this is largely due to the adverse environment created by the financial sector reforms.

Satish (2004)\textsuperscript{43} held an overall positive impression about the deregulation of rate of interest for the rural financial institutions (RFIs) in the context of financial sector reforms. His study expressed the view that the state government, the central government, central bank and NABARD should confine themselves to the role of institution-building rather than to subsidize the interest rates of RFIs. A similar viewpoint, based on both conceptual and empirical analyses, was also provided by Desai and Mellor (1993)\textsuperscript{44} and Desai and Namboodiri (2001)\textsuperscript{45}. However, the study by Satish seems to have missed the most fundamental reason that necessitated the formation of state-owned RFIs was inherently imperfect rural financial market that gets compounded and become more complex due to the vagaries of the weather to which agriculture is exposed.

Reddy (2000)\textsuperscript{46}, held the view that in spite of several measures taken to improve the flow of institutional credit to agriculture and rural areas, there has been mismatches in the demand and supply of credit. In his study on the futures of rural banking, he expressed his concern over the issues like high NPAs, high cost of financial intermediation, bias towards lending to the well to do groups among the rural community, non availability of timely credit and procedural complexities for obtaining loans, etc. Ghose Dastidar (2000)\textsuperscript{47}, however, revealed that the reform measures in the banking sector implemented so far has necessitated a paradigm shift of the RRBs as the liberalisation in the economy has opened up the market for all. As against living under the umbrella of protection the RRBs are now exposed to an environment of competition. In such a situation, unless they perform well, they will perish. They are to gear themselves from the regime of “Profit not a must” to “Profit must for survival”. However a satisfactory performance of the RRBs depends on a number of factors, such as mobilisation of required resources, looking for prospective borrowers and prospective avenues of business, acquiring the necessary skill, quality lending, acquiring expertise to

\textsuperscript{43} P Satish: 'Rural Finance: Role of State and State-owned Institutions' (EPW, March 20, 2004).
\textsuperscript{46} Reddy, Y V: "Future of Rural Banking". RBI Bulletin, January, 2000
reduce NPAs, etc. Ghose Dastidar (2000) opined that all these factors are interlinked and have to be dealt with in totality with a pragmatic approach. **Bhatt and Throat (2001)** in their study on India’s RRBs observed that despite the increase in geographical coverage and intermediation activities, the RRBs are suffering from poor financial health due to the lower recovery rate and loan losses which had wiped out the equity and reserves of some of RRBs in early part of 1990s. This had necessitated an urgent move to reform the RRBs and make them viable. But despite the implementation of the financial reform measures to make them viable, the study observed less satisfactory performance of the RRBs in the post reform period.

**Majumdar (2001)** in his monograph has expressed the view that though India is the pioneer of evolving its own institutional framework for rural credit, today the entire rural credit delivery system is in a moribund state and the 1990s was the lost decade for agriculture and rural credit. He claimed that with the euphoria of liberalisation and globalisation of the economy in 1990s and in the context of financial sector reforms inspired by the borrowed wisdom of market-led growth, rural credit became the Cinderella of Indian policy makers both at the government of India level and at the RBI level. He also remarked that the first Narashimham Committee recommendations and the World Bank prescriptions demonstrate nearly the same thing and with the run towards the globalisation and liberalisation our policy makers are distancing themselves from the goal of poverty alleviation perhaps on the mistaken belief that in a market led economy; the poor must fend for themselves. The dilution of the priority sector definition, has encouraged the bankers even the RRBs to reduce the credit flow to agriculture and allowing RRBs to lend to non target groups has created a reverse flow of funds from the rural to the urban sector. He opined this as the ‘**direct result of a fantastic Delphic version implanted on the Indian policy makers by the market messiahs.....It was not merely a case of benign neglect : it was a case of creating, as a by-product of misconceived financial sector reforms, an adversarial environment for rural credit**’. According to him, in the context of the new development perspectives the rural credit should not be viewed as a merely a marginalised section of the credit market but in terms of the wider idiom of

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accelerating overall GDP growth, and other growth imperatives like poverty alleviation etc.

To rejuvenate the rural credit system he also suggested solving the problems of high transaction cost and low recovery performances with the help of a linkage of the formal credit institutions and the SHGs and NGOs.

Malhotra (2002),\(^50\) is of the view that the ‘era of economic liberalization’ has broadly circumvented the RRBs to a large extent. Though, some initiatives were taken for RRBs in terms of - freedom in interest rate structure, relaxation in target group concept, parity of emoluments to staff with sponsor bank, amalgamation and merger etc., these interventions have been delayed and hesitant. As cardinal changes are contemplated in the rural credit delivery system in near future, it is imperative to synchronize the operations of RRB with the challenges ahead. The opportunities, threats, etc. are to be perceived in context of rapid refinements taking place on financial horizons and there is eminent necessity for carrying out reforms in RRBs to overcome their limitations.

Kamesam (2002),\(^51\) expressed his opinion that the deregulation in interest rates, grant of functional autonomy to banks in the area of credit, entry of foreign banks and emergence of new private banks has made the banking environment more competitive. He held the view that the second phase of financial sector reforms has provided the necessary architecture for strengthening the Indian banking system. He stressed on the need for further strengthening of the regulatory and supervisory regime to ensure stability of the financial system in the present era of globalization, financial sector conglomeration and ‘bundling’ in the provision of financial services. The other important observations of his study were:

a) In spite of conscious and persistent efforts through the prescription of strict objective norms for the identification and classification of NPAs and their management, these problems continued to be the foremost challenge of the Indian banking system.

b) The delay in recovery of dues through the legal process is mainly, due to the very nature of Indian legal system.

\(^{50}\) Malhotra, R.: India’s Regional Rural Banks (RRBs) – The Forgotten Case in Financial Sector Reforms. (NABARD) April 2002.

\(^{51}\) Kamesam, Vepa, (Deputy Governor, Reserve Bank of India): "Challenges before the Indian Banking Industry" Address at the Annual General Meeting of the Indian Banks’ Association at Mumbai on August 31, 2002.
Sinha et al (2003)\textsuperscript{52} critically remark that the series of reform measures such as, infusion of fresh capital, encouraging them to achieve better repayment levels, and allowing them to close down non-viable branches, etc., in the late 1990s have improved the functioning and performances of RRBs. Their study observed that, whilst, in 1996–97, the majority of RRBs had been incurring losses; by 2001, over 85% were earning current profits. But these improvements were, in a large measure, attributable to a shift towards a wealthier clientele.

The policies introduced during the reform period – starting in the early 1990s – have been instrumental in reorienting RRBs towards financial viability, an objective that was lost midway through their evolution – particularly in the 1980s. These policy changes have enabled RRBs to explore new markets and operating procedures with the aim of achieving viability. While policies allowing relocation of branches, improved remuneration and incentives for RRB staff and liberalised lending arrangements (lending to the 'non-priority' sectors, deregulation of interest rates) have all have a positive effect on RRBs’ operations, these are not a complete solution to make RRBs viable. The introduction of income recognition and asset classification norms had a negative short-term impact on viability. Further, such measures have not been backed by a supporting regulatory framework that enables participation in cheque clearing and issuing of drafts and operational measures like the computerisation of branches.

Thus, while the RBI and NABARD deserve credit for introducing changes aimed at professionalizing RRB operations, the basic character of the RRBs’ business – which has traditionally been with small rural clients – remains largely unchanged. The analyses of sample RRBs covered by their study (Sinha et al, 2003) demonstrate that there is no inherent contradiction between the viability and outreach objectives. The combination of product design and efficiency of operations can override this tension. The important observation of the study is that the RRBs focused on operational efficiency have achieved good operating results even while continuing to serve significant numbers of low-income clients. To them, an analysis of product design, client demand patterns and establishment of

\textsuperscript{52} Sanjay Sinha, Tanmay Chetan, Orlanda Ruthven and Nilotpal Pathak: "The Outreach/Viability Conundrum: Can India’s Regional Rural Banks Really Serve Low-Income Clients?" Working Paper 229, Overseas Development Institute, 111 Westminster Bridge Road, London, SE1 7JD, UK, October, 2003.
appropriate delivery mechanisms are the key factor that would lead the RRBs to achieve both outreach and viability objectives.

Further, the study highlighted the quality of branch management as the crucial ingredient for achieving both viability and outreach objectives. The study observed profitability as a variable which is strongly correlated with proactive and well-judged management. Programmes of capacity building and motivation among managers are likely to generate high returns. However, relating to the problems of higher transaction costs in lending operations to the rural poor the study opposed linking with SHGs or NGOs as a remedy to the problem as the loans to self-help groups (SHGs) are costly to administer in staff time. Another notable finding of the study is that the decline in rate of interest on deposits during the post reform era has arrested the RRBs to follow the route of investments as a safe income option.

Bhattacharyya (2003)\(^{53}\), in his study entitled “Rural Credit and Class Differentiation - West Bengal under Left Interventionist Regime” observed that after the recommendations of the Narasimham Committee, the main aim of the banking system has been to maintain sound health of the banks. Therefore, there is a dichotomy between the objectives of maintaining growth with stability, in one hand, and sound health of the banking system by providing credit in a restrictive manner, on the other. However, the study has shown a large proportion of borrowers waived under Agricultural and Rural Debt Relief Scheme, 1990 (ARDRS, 1990) was motivated mainly by the vested political interest. In case of the poor farmers, it was poverty but for the large farmers, it was the willful default or unproductive use of loans. The study cautioned that such loan waivers affect the recovery performance of the banks adversely by discouraging the borrowers in their loan repayment and should not be adopted for political benefits.

IBA Committee on “Banking Industry Vision 2010,”\(^{54}\) in its report (2003), urged an urgent need to enlarge their role, functions and range of services offered by the rural financial system so as to emerge as "one stop destination for all types of credit requirements of people in rural/semi-urban centers. Barring commercial banks, the other rural financial institutions viz. the cooperatives and

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Regional Rural Banks (RRBs) have a weak structural base and the issue of their strengthening requires to be taken up on priority basis. Regional Rural banks (RRBs) as a group needs to be made structurally stronger and suggested NABARD to take the initiative to consolidate all the RRBs into a strong rural development bank. Sahu and Rajsekhar (2005), has however, shown that with the impact of economic reforms there has been a decline in the flow of credit to the agricultural sector in the country. The decline is mainly because of the fact that both the commercial banks and RRBs have now become more conscious towards profitability and therefore, after being allowed to lend to the non-target group of borrowers, these institutions are least interested to lend to this sector. This is however, something contrary to the policy taken by the union government, which desires to increase agricultural credit.

However, it is noteworthy that our neighbouring country Bangladesh has now been able to draw attention of the whole world with the introduction and implementation of the similar rural banking concept in a different way. Bangladesh has become successful to bring down the rural poverty level to a considerable extent by pioneering and popularising the unique micro credit concept through the establishment of the Grameen Bank, the brain child of Dr. Muhammad Yunus*, in 1976.

Das (1999), after examining the performances and progress of the Grameen Bank Bangladesh, observed that the earlier myth that Bangladesh is synonymous with poverty has been exploded and the major credit goes to policies adopted / invented by the Grameen Bank of Bangladesh towards micro credit. Hussain (1984, 1988), and Rahaman (1987), in their studies on performance and impact of Grameen Bank in rural life of Bangladesh broadly observed that the Grameen Bank has become successful in improving the economic conditions of the borrowers as well as in alleviating poverty in the area of the Bank’s operation. The operational design of the Bank such as targeting the rural poor

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55 Sahu, G.B and Rajsekhar D. 'Banking Sector Reform and Credit Flow to Indian Agriculture'. Economic and Political Weekly, Dec. 31, 2005

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* Dr. Muhammad Yunus has been awarded Nobel Peace Prize in 2006 for his contribution in poverty removal programme in Bangladesh through the innovative concept of micro credit programme implemented by Bangladesh Grameen Bank.
women as the clients, programme implementation system, decentralised and participative management style and similar other innovative policies are the contributing factors behind the success of the Grameen Bank. Gibbons (1993), in his study on the performance of the Grameen Bank of Bangladesh, has pointed out that the close relationship of the Bank with the borrowers, peer pressure and peer support on loan recovery, effort to reach the poorest, process of group formation, time taken by the Grameen Bank to establish new branches, creation of an atmosphere of respect towards institution by the Branch managers, etc. are the factors acted behind its success. Thus the operational method and the style of management play significant role for the success of rural banking.

During the last three decades of existence of RRBs, several working Groups and Committees* were set up by RBI, NABARD and the Government of India at various points of time to deliberate on the issues relating to the problems of RRBs and suggest measures to address the same. The focus has varied over time depending on the immediate concerns and the prevailing policy regime. While some of the issues relating to RRBs have lost their significance over time, others have become more relevant. However, while most of the committees have highlighted the significance of the RRBs as one of the important institution to fulfill the credit needs in rural areas, at the same time, these committees have expressed concerns over the problem of lower recovery rates, mounting over dues, continuous losses and the problem of non viability.

The Committee to Review Arrangements for Institutional Credit for Agriculture and Rural Development, (CRAFICARD, 1981), was the first committee to raise the question of viability of RRBs. After the financial reforms in 1991, the non viable situation of RRBs once again, had drawn attention to the policy makers, the government and bankers. The option of restructuring through merger/amalgamation as a means to revive the RRBs from their non-viable stage to sound financial health started gaining momentum with the recommendation of The Expert Group on RRBs (Thingalaya Committee) in 1997. Later on, The Expert Committee on Rural Credit (Vyas Committee, 2001) and The

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60 Gibbons, David S 'The Grameen Reader', Grameen bank of Bangladesh Publication, Dhaka, Bangladesh 1993
Committee on Restructuring of Regional Rural Banks, (Chalapathy Rao Committee, 2003) also supplemented this view.

More recently, the Internal Working Group (Sardesai Committee, 2005), set up by RBI, re-examined the issue of restructuring the RRBs and in its well thought-out opinion, favoured the path of merger and amalgamation as the best option to improve the operational viability of RRBs and take advantage of the economies of scale. Accordingly, in January, 2006, four RRBs of Assam under the sponsorship of United Bank of India have been merged and gave birth to Assam Gramin Vikash Bank. As a result of this merger / amalgamation, the erstwhile Cachar Gramin bank has now become Cachar Division of Assam Gramin Vikash Bank (AGVB) and its branches are operating under the parental guidance of AGVB.

1.5.1. Major findings of the literature survey:

The foregoing review of available literature regarding the genesis, operation and performance of RRBs at the international, national as well as regional levels, we can categorize the major observations as under:

- The RRBs emerged as an institution of rural credit delivery system to abridge the credit gap that existed in the rural areas. These RRBs were established as a purveyor of credit requirements of the economic units of the countryside. A number of studies acknowledged RRBs as the much required financial institution to serve the credit needs of the rural poor as well as for the rural economic development.

- Sustainability of credit market has to be viewed from various perspectives like policy makers' agenda, bankers' mission to serve the rural areas and clientele's perception regarding the efficacy of the banking system to serve their needs. Further, risk and uncertainty associated with agriculture adds yet another dimension to the problems in rural finance and viability of credit institutions.

- A number of studies addressed to the assessment of the performance of the RRBs and their major observations are:
  
a) During the initial years, the commercial aspect like profitability was not given any importance. These banks served as the credit disbursing agencies to
finance various government sponsored social welfare schemes, designed especially for uplifting the rural people from their poor economic status.

b) In respect of geographical coverage the RRBs have penetrated into every nook and corner of the country through its vast branch network. It has achieved a commendable height in respect of providing banking services to the rural clienteles. On 31st March, 2005, the total no. of branches was 14433, spread over 522 districts of the country with volume of deposits and outstanding loans and advances worth Rs.61425 crore and Rs.32559 crore respectively.61

c) During the pre reform era the C-D ratio of RRBs was higher than that of the post reform era. The principal factor responsible behind the drastic fall in C-D ratio, as assigned by the studies is that the RRBs have become more cautious and selective in their lending activities in order to avoid the risks associated with rural lending as well as to keep their recovery rate high.

d) In respect of recovery performance these banks performed very poorly and this has resulted in the accumulation of mounting over dues and unmanageable NPAs.

e) Lack of supervision and follow up and indifferent attitude among the staffs, were the important factors responsible for the poor recovery performance. Further, the populist policy of loan waivers and weak legal framework contributed much towards lowering the recovery rate.

f) The improper identification of beneficiaries and misutilisation of borrowed fund were considered as important factors responsible for large scale default in loan repayment.

g) Till 1990's, these RRBs were incurring losses and the accumulated losses increased to such a high level in 1994 that it started eating the equity capital and even deposits.

The host of problems that pushed the RRBs towards the non profitable and non-viable zone were

a) Limited commercial prosperity due to the compulsions in lending to the priority sector and targeted group of clienteles.

b) Limited area of operation.

c) Administered interest rates.

d) Progressive hike in salaries and allowances of the employees.

61 Statistics on Regional Rural Banks as on 31st March 2005, NABARD, Mumbai
e) Low capital base.

f) High operation cost involved in handling small loans.

g) Thin interest spreads.

h) Improper selection of beneficiaries.

i) Lack of potential projects to be financed by these banks in their operational area.

j) Lack of proper infrastructural facilities in the rural areas for efficient and productive use of credit.

k) Low recovery rate associated with the factors like poverty of the rural people, crop failure, natural calamities, inadequate follow-up of loans, wrong identification of borrowers, misuse of loans, willful defaults backed by political powers, inadequate legal framework for recovery of loans, and so on.

l) Operational problems in smooth and efficient functioning of the RRBs due to the multilevel controls exercised by the sponsor bank, the RBI, and NABARD.

The major findings of the studies committed to analyze the impact of financial sector reforms on RRBs are summarised as under:

a) The reform measures have made a paradigm shift in the operational aspect of RRBs and they are now guided by commercial motives, similar to those of the other commercial banks

b) As a result of the implementation of the reform measures these RRBs have been pushed into the competitive market economy, purely driven by the motive of earning profit amidst competition, from the subsidised, controlled and protected regime.

c) The implementation of reform measures though transforming the RRBs towards attaining their good financial health but the social aspect of rendering banking services to the rural poor has been given up.

d) The RRBs are now facing hurdles to fulfill the requirement of asset classification and provisioning as per the prudential norms.

e) Even after the implementation of reform measures the RRBs are subjected to various impediments which act on the way of achieving their financial viability and profitability. Some of these impediments are – lower recovery rate and high over dues, higher rate of NPAs, lower interest spread, and so on.
A number of committees [mainly, the Vyas Committee (2000), the Chalapati Rao Committee (2002) and the Sardesai Committee (2005)] constituted to identify specific organisational issues and structural changes in order to help these banks to adapt themselves into the new environment. They favoured reorganization in the structure of RRBs in the following lines:

a) Formation of only a few RRBs, making 4 or 5 zones.

b) Converting the RRBs as subsidiary of the sponsored bank.

c) Merger of loss making branches into one unit in an area.

d) State wise Merger of RRBs sponsored by the same commercial bank.

e) Merger of RRBs sponsored by different banks in the same state.

f) Entry into non target group for expansion of business and operation beyond the service area.

g) Relocation and/or closure of the loss incurring branches

1.6. The Research Gap:

From the review of available literature we find research gaps in the following areas:

- No significant study on the problems related to the viability and profitability of the RRBs in the present liberalized regime has yet been under taken.

- The problems related to the RRBs are region specific depending on the socio-economic and geographical conditions of their operational area. But, no study of high magnitude has so far been made on the problems and prospects of RRBs in Assam and more particularly in the Barak Valley of the southern part of Assam.

In view of the above research gaps, the present study is an endeavour to make an in-depth investigation into the problems related to the viability and profitability of the RRBs in the context of present liberalized regime and more particularly in the present era of amalgamation and merger of RRBs.

1.7. Rationale of the Study:

Review of the above literature clearly indicates that the role of RRBs in uplifting the rural poor can hardly be denied. Yet, the matter of concern is that the rural credit delivery system is facing a variety of problems such as poor recovery rate, over dues, high NPAs, inefficient management, lower scope of profitable
investment due to their rural location, thin interest spreads etc. These problems are not only affecting the profitability but also posing a threat to the viability of RRBs as a credit delivery system in rural sector of the country. The problems can broadly be divided into three categories:

- Problems related to Operational efficiency
- Problems related to Structural or organisational efficiency
- Problems related to Managerial efficiency.

In order to study the aforesaid problems at grass root level a study on the viability and profitability problems of RRBs is highly necessary.

Further, as the problems encountered by the RRBs are not uniform for the country as a whole because of its regional diversity and regional specificities. The significance of the study lies in identifying the factors influencing or likely to influence the operation and performance of the RRB in this region, especially in the context of various restrictions and norms implemented with the financial sector reforms. The significance of the study also lies with the quest to know whether the RRBs are performing as per the guide lines set by the banking sector reform policy, how far these are ensuring the RRBs in solving their relevant problems, and what are the difficulties encountered by them while following these guidelines.

To achieve the overall efficiency of the RRBs in the state as a whole, recently, four RRBs viz., Pragjyotish Gaonlia Bank, Lakhimi Gaonlia Bank, Cachar Gramin Bank and Subansiri Gaonlia Bank were amalgamated into one unit and a new RRB has been formed under the nomenclature ‘Assam Gramin Vikas Bank’ (AGVB)*. However, the AGVB is simply formed by merging the aforesaid four RRBs (Equity Merger) with a view to manage them more efficiently under

- a unified control,
- enhanced capital base and
- expansion in their area of operation.

But the operation of the AGVB will continue with the same set of staffs and branches that existed with the earlier four RRBs operating in the 25 out of 27 districts of the state. Hence the operational area of the newly formed AGVB is

simply the summation of the operational areas of the earlier four RRBs of the state. Thus, the operational efficiency of the AGVB will largely depend on the efficiency of the branches of the erstwhile RRBs of the state. The financial information and experience of the RRBs prior to the merger would be useful guidelines for the newly formed one.

The erstwhile Cachar Gramin Bank, the only RRB in the southern Assam is now an important component of the AGVB. Therefore the experience of its banking operation in the region would definitely act as guide line for the formulation of policy as well as for operational efficiency of the present AGVB.

This study contributes to the literature on RRBs primarily in two ways.

➢ First, the issues concerning RRBs are an area that is less visited empirically (econometrically) compared to the vast literature on commercial banks. Whatever studies have emerged on the topic, they have primarily relied on exploratory analysis done for a particular year or on a group of RRBs to draw inferences. As the present study considers the entire period of 24 years since the inception of the RRB under study (from 1981 to 2004-05) rather than a few years for empirical analysis its results are broad based.

➢ Second, given the attention at the policy level to restructure the RRBs, it is necessary that the behaviour of RRBs be analysed separately taking into consideration the regional specificity of the operational area, than all RRBs bunched together so that it helps in region-specific policy formulation. Such an approach has been followed in this study.

The proposed study thus, will not only serve its academic relevance but it would also facilitate the policy formulators, the government and the management of the RRBs for formulating their future course of actions. Further, the study will also add to the existing stock of knowledge in the relevant field and serve as the guidance to the future researchers as well.

1.8. **Objectives of the Study:**

The broad objective of the proposed study is to examine the financial viability and profitability aspects of the RRB in Barak valley of south Assam. However, the specific objectives of the study are:
• To evaluate the financial performance of the RRB under study in the context of changes in operational environment introduced by the banking sector reform measures.

• To assess the extent of reorientation of the RRB in study area in response to the changes generated by the banking sector reform measures.

• To make a critical analysis about the prospect of the bank as a viable and profitable financial institution, so that it can fulfill the needs and aspirations of the rural clientele.

• To gauge the customers’ perception about the bank, relating to the quality of services rendered by it.

• To prescribe policy measures for further improvement in the financial performance of the RRBs of the country in general and of the study area in particular.

1.9. Hypotheses of the study:

The entire study is based on the following hypothetical interactive model, developed especially as the conceptual framework for achieving profitability and viability of a financial institution like regional rural banks (Diagram-1.2).

We proceeded with the basic premise that the profitability and viability of a financial institution are inter related and one reinforces the other. Secondly, the ways and means to accelerate profitability and viability of RRBs are to be generated from within their operational activities. Further, for viability and profitability of RRBs, the macro-economic policies of the government and other external factors like infrastructural facilities and business potentiality under the operational area are of crucial importance along with their proper business strategy and managerial efficiency.

The model is self-explanatory and based on the following chain of reasoning:

➢ Profit earning is the basic pre condition for viability.

Therefore, our Hypothesis No.1 (H1): Profitability of a bank ensures its viability.
Further, profit of a RRB arises from its banking business which includes: a) Mobilisation of deposits, b) Disbursement of loans and advances, and c) non-fund (fee based) business such as consultancy, commissions, fees, etc., on various services provided to its customers. Thus, to improve the viability and profitability aspects of RRB, the first pre condition is its growth of business.

Therefore, we have taken:

**Hypothesis No. 2 (H2):** The growth of deposits mobilization leads to profitability and profitability in turn leads to viability.

**Hypothesis No. 3 (H3):** The growth of loans and advances leads to profitability and makes the bank viable, and,
Hypothesis No. 4 (H4): The growth of fee-based business makes the RRB profitable and viable.

However, a mere increase or growth of deposits, loans and advances and fee-based business in quantitative terms are not sufficient for the profitability of a bank. The growth of business should be talented with efficient business management.

For example, unless, the funds are managed with proper portfolio, the increase in deposits may lead to losses because deposits have their own interest cost. Similarly, an increase in loans and advances with slackness in the pre-sanction scrutiny of borrowers, selection of projects and loan follow-ups would lead to loan defaults, low recovery performances, mounting over dues, higher NPAs, and huge losses to the bank. Equally, if the fee-based businesses are not cost effective, the growth in such business will yield negative returns.

For that reason, the hypothesis relating to efficient business management in the model is:

Hypothesis No. 5 (H5): An efficient business management leads to profitability and viability of the bank.

Nevertheless, failure of the bank to fulfill the needs and aspirations of the people of the society may prove to be fatal for the bank. This is because, in the competitive banking regime, if the bank fails to satisfy its customers, then the customers would reject it by accepting the others. Thus, the bank would loose its customers, existing as well as prospective, and under that situation, it cannot sustain its business. Hence, the model takes

Hypothesis No. 6 (H6): A higher degree of customers’ satisfaction has a positive impact on the viability and profitability, the RRB.

The policy environment, under which the bank is to operate, largely influences its profitability. However, these policies are subject to change with the dynamic changes in the society and needs of the time. Therefore, the RRB should have the adaptability to switch over itself from one policy set up to another to sustain its profitability, and viability.

Therefore, the next hypothesis taken in the model is:
Hypothesis No.7 (H7): In order to remain profitable and viable, the RRB should have the capacity to adapt itself with the changing policy environment under which it has to operate.

However, the operational hypotheses have been set on the basis of aforesaid general hypotheses and tested by the facts and application of statistical tools in the respective chapters, discussed hereafter, 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’. [This operational hypothesis is taken as per our model hypothesis no. 7]

➢ $H_0^2$: “The financial performance of the bank under study has not improved, in spite of the implementations of banking sector reform measures in RRBs.” [This operational hypothesis is related to $H_2$, $H_3$ and $H_4$ of our model]

➢ $H_0^3$: “The profitability of the bank under study is independent of the measures implemented by the banking sector reform.” [This is related to hypothesis no.1 in our model]

➢ $H_0^4$: “The operational efficiency and viability of the RRB under consideration has not improved even after the implementation of reform measures.” [This hypothesis is compatible with our general hypothesis $H_5$ in the model]

➢ $H_0^5$: “The RRB has failed to satisfy its customers’ aspirations.” [It is in line with our hypothesis $H_6$ in the model]

1.10. A brief introduction to the Study Area:

Some researchers believe that the name ‘Assam’ may have been derived from the Sanskrit term "Asom" that means unparalleled, or one with no equal. The term ‘Asom’ in Sanskrit also means undulated or uneven. The rugged nature of the land of Assam may also be a reason for her name. In addition, the Ahoms ruled Assam for six hundred years till the early part of the 19th century. The words ‘Ahom’ and ‘Asom’ are pronounced similarly, and hence the Ahoms may also have given ‘Assam’ its name.\(^{62}\)
Assam, located in the northeastern part of India, is bounded to the north by Bhutan and the state of Arunachal Pradesh; east by the states of Nagaland and Manipur; south by the states of Mizoram and Tripura; and west by Bangladesh, and the states of Meghalaya and West Bengal. The state and has an area of 30,285 square miles (78,438 square kilometers) which accounts for about 2.4 per cent of the country’s total geographical area.

The State of Assam can be divided into three broad physiographic units, viz.

1. The Brahmaputra Valley in the north, commonly known as North Assam or Upper Assam,
2. The Barak Valley in the south, commonly known as South Assam and
3. The Hills Region that lies in between the two valleys.

South Assam or Barak Valley is on the bank of the river Barak and surrounded by hills on the three sides. Kushiara, Longai, Singla, Ghagra, and Katakhal are the major rivers and tributaries of Barak flowing over the region. It is located between 24°8' and 25°8' North and longitude 92°15' and 93°15' East. The geographical location of the study area within the state is depicted in the map of Assam as shown below (Diagram-1.3).

**Diagram-1.3**

Geographical Location of the Study Area

![Geographical Location of the Study Area](http://www.assamnic.in)
The region comprises three plain districts, viz. Cachar, Karimganj and Hailakandi with a total area of 6,922 sq. km. comprising 2313 villages and 8 towns

<table>
<thead>
<tr>
<th>Table-1.1</th>
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<tbody>
<tr>
<td><strong>Socio-economic Profile of South Assam</strong></td>
</tr>
<tr>
<td><strong>Items</strong></td>
</tr>
<tr>
<td>Geographical area (in Sq Km)</td>
</tr>
<tr>
<td>Rural area (in Sq Km)</td>
</tr>
<tr>
<td>Urban area (in Sq Km)</td>
</tr>
<tr>
<td>Population as per 2001 census (in lakh)</td>
</tr>
<tr>
<td>Density of population (per Sq Km)</td>
</tr>
<tr>
<td>Literacy rate %</td>
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<tr>
<td>% of Rural Population</td>
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<tr>
<td>Sex Ratio (no of females per 1000 males)</td>
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<tr>
<td>% of working population</td>
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<tr>
<td>% of area under cultivation</td>
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<tr>
<td>% of area under forest</td>
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<tr>
<td>No. of registered factories (as on 2002)</td>
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<tr>
<td>Annual rainfall (mm) (as per records for 2003)</td>
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<tr>
<td>No of inhabited villages (2001 census)</td>
</tr>
<tr>
<td>No of towns</td>
</tr>
<tr>
<td>No of municipalities/ Town Committees</td>
</tr>
<tr>
<td>Number of Development Blocks</td>
</tr>
<tr>
<td>Gaon Panchayets</td>
</tr>
<tr>
<td>No. of banks Branches</td>
</tr>
<tr>
<td>Pub. Sec Banks</td>
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<tr>
<td>Pvt. Sec Banks</td>
</tr>
<tr>
<td>RRB</td>
</tr>
<tr>
<td>Assam Cooperative Apex Bank Ltd</td>
</tr>
<tr>
<td>Total</td>
</tr>
<tr>
<td>No of people per bank office</td>
</tr>
</tbody>
</table>

| **Major economic sectors** | Agricultural and allied activities, handicrafts, trade and business |
| **Existing Industries** | Tea, Paper, cement, food products, bricks, timber and sawing handicrafts, Cane and bamboo products, SSI |
| **Prospective industries** | Handloom, cane and bamboo products, bricks, small engineering, SSI, agro based industries, food processing and packaging, food products, etc |

The profile of the study area is summarized in the Table-1.1. About 99.47% of the total geographical area of the region is rural and only 0.53% is under urban area. As per the Population Census (2001), out of total population of 266.38 lakh in the State (2.59% of the total population of the country), 29.89 lakh are in South Assam (11.22% of the state population and 0.29% of the total population of the country) with sex ratio 942 (as against 932 for Assam as a

whole and 933 for the nation as a whole). The density of population in the region is 432 persons per square kilometer which is higher than the density of population in the state as well as of the country (340 and 324 for the state and the country as a whole, respectively). Within the region, Karimganj district has the highest density (557 persons per square kilometer) followed by Hailakandi (409) and Cachar districts (380) respectively. The literacy rate is 65.80%. The rural population comprises of 89.27% of the total population. Total working population in the region is 31.79% of the total population and out of them 63% are engaged in agriculture (i.e. cultivators and agricultural labourers).

The topography of the Barak valley is heterogeneous composed of high hills, low lands called 'Beels' and 'Haors', and level plains dotted with low ranges isolated hillocks called 'Tillas'. The river Barak flows through the plain regions of the valley. The Valley experiences hot and humid climate as high as 85.90 per cent or more in the majority of the districts. Variation of temperature with a maximum of $38^0$C and minimum of $14^0$C to $16^0$C is also noticed in different parts of the valley. The Valley is characterized by heavy rainfall during the rainy season. The highest rainfall recorded in the valley was 4587 mm in 1998 and the lowest rainfall was 1552mm recorded in 1979. As a result of heavy rainfall, the region suffers from recurrent floods which affects the cultivation works and cause enormous damages to the crops, livestock, land, property and bring untold miseries to the people at large.

Agriculture is the main occupation of the people. It accounts for 63% of the total work force, according to 2001 Census. The soil, topography, rainfall and climatic condition of the valley are congenial for cultivation of paddy, which covers nearly 73 per cent of the gross cropped area and more than 90 per cent of the total area under food-grains. However, different pulses, tea, sugarcane, potatoes, oil seeds, coconut and betel-nut cultivation are also practiced on a substantial scale. There is little practice of Jhum cultivation or shifting cultivation in the valley.

Forests are an important part of the valley’s economy. Timber, cane and bamboo are the major forest product, available in the region. Tea is another product of the valley. There are 127 tea gardens in the valley which comprises about 27% of the total tea gardens of the state.
The region is well connected to different parts of India through roads, railways and air. It is also gateway to other states in North East Region viz. Manipur, Mizoram, and Tripura. It is connected by National Highway 44, 53 and 54 and meter-gauge railway route under Badarpur Division of North East Frontier Railway. The railway route connects Guwahati, via Lumding; Tripura up to Kumar Ghat and the State of Manipur up to Ziribum. The valley is blessed with an airport with Runway Length 5857 feet at Kumbhirgram, 28 K.M. away from Silchar town. It has the capacity to handle the B-737, DO-228, AN-32, AN-74, IL-74 category of aeroplanes and Mig and Cheetah Helicopters. Beside rail road and air transport system the water transport occupies an important role in the area. A large volume of goods and traffic are transported through country boats and it assumes a pivotal role in transport system of the valley during flood situations.

But in spite of a good road, rail and air connectivity, the region’s transport system is backward and uncertain due to land slides, water logging and flood situation, particularly during the rainy season.

The area has a good infrastructure for education. There are a Central University, a medical college, engineering college, polytechnic, Industrial Training Institute (one of each); teachers’ training colleges, general degree colleges, and a number of higher secondary, secondary and primary schools to impart different types of education and training to the youth of the Valley.

Good postal facilities with 109 post offices supported by speed post service at 36 centers are also available in the Valley. Besides these, a large number of private courier service providers are also functioning in the region. The telecommunication services of the region have also developed with the introduction of cellular services by both the public and private operators.

In spite of all these, South Assam is industrially backward compared to the upper Assam or Brahmaputra valley because of disadvantageous geographical location, lack of basic and heavy industries, backward transport and communication system, higher transport cost and Shortage of power. One paper mill, two flour mills, one cement production unit and other few small scale industries along with some tea gardens and few saw mills are the only industrial units operating in the region. The region has only 233 registered factories as on
2002\(^{54}\) (145 in Cachar, 63 in Karimganj and 25 in Hailakandi). Besides these, handlooms and different traditional handicrafts mainly based on forest products are also operating either at tiny level or cottage level in the valley. The ONGC is also operating their exploration works in the region.

However, there is ample scope of developing small engineering units, handlooms and handicrafts, agro and forest based industries, food processing and packaging industries in the region. The District Industries Centers (DICs), Small Industries Service Institute (SISI), Industrial Training Institute (ITI) and different NGOs are imparting training to the youths in establishing small scale and cottage industries and encouraging them to develop entrepreneurship and for self employment. However in the event of scarcity of finance the youths are unable to realize their acquired entrepreneurial skills.

The Agricultural credit is disbursed through a multi-agency system consisting of Commercial Banks, Co-operative Banks and the Regional Rural Bank. The Cachar Gramin Bank, the Regional Rural Bank of the study area, was established in 1981 under Regional Rural Banks Act 1976. Till 11th January 2006, Cachar Gramin Bank acted as the only RRB in South Assam. However, on 12th January 2006, Assam Gramin Vikash Bank was formed through a merger of the four RRBs of the state sponsored by the United Bank of India, viz., Cachar Gramin Bank, Pragjyotish Gaonlia Bank, Subansiri Gaonlia Bank and Lakhimi Gaonlia Bank. As a result, the 44 branches of erstwhile Cachar Gramin Bank have now come under Assam Gramin Vikash Bank and at present they are performing the functions of RRBs within the region with almost the same set of staffs and similar operational policies.

### 1.11. Research methodology:

**1.11.1. Research population and sample:** All the 44 branches of erstwhile Cachar Gramin Bank\(^{6}\), the only RRB of the study area, spread over the three districts of Barak Valley in Southern Assam (viz., Cachar, Karimganj and Hailakandi) constitute the research population and the financial information of all these

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\(^{54}\) In this connection, it is worth mentioning that the Cachar Gramin Bank (CGB) acted as the only RRB in the study area - the three districts of Barak Valley (viz. Cachar, Karimganj and Hailakandi) in Southern Assam, until 11th January 2006. Presently it has been merged with the other three RRBs of the state, viz., Pragjyotish Gaonlia Bank, Subansiri Gaonlia Bank and Lakhimi Gaonlia Bank, to form Assam Gramin Vikash Bank (AGVB) on 12th January, 2006. As a result, all the branches of erstwhile CGB, spread over the three districts of Barak Valley are now functioning as the branches of AGVB under Cachar Zone with the same set of staffs and set-ups.
branches have been taken under the study for the purpose of viability and profitability analysis.

However, for the analysis of customers’ satisfaction, a sample of 154 customers* drawn at random from 22 purposively selected banks branches. (The distribution of selected bank branches between rural semi-urban and urban areas and the profile of the customers are presented in Chapter-VI, Table 6.2 and Table-6.3 respectively). After editing the collected data, fourteen (14) respondents were excluded from the analysis because of their erratic responses. Thus, ultimately, the analysis is based on the sample size of 140 customers from 22 branches of the bank under study and from different fields of occupation, sex and educational level.

1.11.2. Variables Selected: The entire analysis has been divided into four parts, namely, a) Overall Financial performance appraisal, b) Analysis on profitability problems, c) Analysis on viability problems, and d) Perception of customers about the service quality of the bank under study. Therefore, four different sets of variables were taken into account considering their suitability and appropriateness to explain / analyze the phenomenon.

a) For analyzing the financial performance of the RRB under study, the we have taken into consideration, the aspects like:

i) Expansion of operational area and branch expansion.

ii) Number of population served by the RRB.

iii) Deposits mobilization; particularly, in terms of

iv) Credit disbursement; in terms of

v) NPA position.

vi) Income, and

vii) Volume of profit and loss.

b) For profitability analysis of the bank under study, we have considered 13 variables relating to the volume of business, income, expenditure and productivity. The definitions of the selected variables and their relative significance in influencing the profitability of the bank are explained in the relevant chapter (Chapter-IV, Table-4.1).

* ‘Customers’ of the bank considered in the study are either (i) depositors or (ii) borrowers or (iii) the persons using fee based services rendered by the bank. However, in the random sample, the third category of customers did not appear.
c) The viability analysis is based on the 11 widely accepted financial efficiency ratios, explaining the aspects of i) Business efficiency, ii) Employee efficiency, iii) Branch level efficiency, iv) Income efficiency, and v) Cost efficiency. The definitions of these variables / efficiency ratios are detailed in the concerned chapter dealing with Viability analysis (Chapter-V, Table-5.1).

d) To examine the customers' perception about the service quality we considered 21 attributes reflecting various aspects of customers' satisfaction. The list of the considered attributes is presented in relevant chapter (Chapter-VI, Table-6.1).

1.11.3. Period of study: The study covered the period from 1981 to 2004-05, i.e. a period of 24 years of operation of the erstwhile Cachar Gramin Bank (the only RRB of the region) since its inception. However, in order to examine the impact of financial sector reform, the time series data has been divided in to two distinct periods consisting 11 years of ex-ante reform (1983 to 1993-94)* and 11 years of ex-post reform (1994-95 to 2004-05). In the study, the term 'two periods under study' or 'two consecutive periods' or 'two successive periods' has been used to imply the pre reform period (i.e., from 1983 to 1993-94) and the post reform period (i.e., from 1994-95 to 2004-05) respectively, unless stated otherwise.

1.11.4. Data sources: Both primary and secondary data have been used for the purpose of statistical analysis. Primary data has been used, mainly, for assessment of customers' perception about the service quality of the bank under study. The necessary statistical information for the specified purpose has been collected from the field survey conducted with the help of a specially structured questionnaire (Appendix-1), during the months of August, 2005 to October 2005. The survey was conducted by personally visiting the selected branches; spread over rural, semi-urban and urban areas. We remained present during the banking hours of full working days (10 a.m. to 2 p.m.) in the respective branches and identified those customers (either a depositor or a borrower) having their banking experience with that particular branch at least for last one year simply by asking the persons who were entering the particular bank branch during that time. After this identification,

* Since the erstwhile Cachar Gramin Bank was established at the fig end of 1981, therefore, the years 1981 and 1982 are excluded to avoid the effects of the extreme low values of the parameters on the estimates, due to its infancy stage. Further, the banking reforms measures were introduced in case of RRBs, in 1993-94. Therefore, we have considered 1993-94 as the end of an era for RRBs, and 1994-95 as the beginning of another era with implementation of reform measures on RRBs.
seven (7) regular customers (who were willing to participate in the survey) have been selected at random from each branch for the purpose of collecting information for the purpose. Thus, the sample includes altogether 154 customers for the field survey. In most of the cases, the questionnaire was handed over to the respondents with a request to fill that up as per the given instructions. However, in case of illiterate or academically backward customers, the questionnaire was filled in on the spot, depending on the replies from the respondents. Thus, we have collected 154 filled in questionnaires (*The profile of the respondents is presented in Table-6.3*).

The interviews with officials of the Cachar Gramin Bank (Chairman, Field Officers, RRB employees’ union leaders, lead bank officer, District Manager of NABARD, Regional manager of SBI and UBI provided a significant contribution by providing valuable information relating to the ground level problems to improve customers’ satisfaction, viability and profitability of RRBs.

The sources of secondary data are:

- The annual reports of all the 5 RRBs of Assam,
- The audited financial statements of different branches of erstwhile Cachar Gramin Bank,
- Lead Bank statements,
- State Level Bankers’ Committee (SLBC) Reports,
- RBI bulletins,
- Publications of Rural Planning and Credit Department, RBI.
- RBI data base (URL: http://www.rbi.org.in/scripts/statistics.aspx)
- Various Parliamentary Committee Reports,
- Reports of the various committees constituted by RBI, The Govt. of India and NABARD from time to time,
- Statistics on Regional Rural Banks, published annually by the NABARD, and
- ‘Key Statistics on RRBs’ published annually by the NABARD.
1.11.5. Research tools and techniques:

i) The standard statistical tools such as measures of central tendencies, measures of dispersion, correlation, and regression analysis have been used for analyzing the data on the selected variables for the purpose of the study.

ii) Further to examine whether the reform measures have resulted any significant impact on the performance of the RRB under study, comparisons of means of the parameters for the pre and post reform period have been made applying ‘Paired Sample T-test’ with the level of significance (α) at 0.05.

iii) Two trend lines of the form: \( Y_t = a + bt \) (where, \( y_t \) is the value the variable, \( a = \) the intercept, \( b = \) slope of the trend line representing the growth) has been fitted for the time series data for the two specified periods to compare the growth of the variables.

iv) In order to derive the profit function of the RRB under study for the pre reform and post reform period we have used the following multiple regression model:-

\[
\pi = \alpha + \sum \beta_i x_i + \epsilon_i, \quad \text{and} \quad \pi' = \alpha' + \sum \beta'_i x'_i + \epsilon'_i,
\]

where,

\( \pi \) and \( \pi' \) = net profit or loss of the RRB for the pre and post reform periods respectively,

\( \alpha \) and \( \alpha' \) = the intercepts of the profit functions for the two respective periods,

\( x_i \) and \( x'_i \) = the values of the variable \( x \), affecting the profit or loss of RRB, for the two respective periods

\( \beta_i \) and \( \beta'_i \) = the coefficients of the variable \( x \) and \( x' \),

\( \epsilon_i \) and \( \epsilon'_i \) = the random factors affecting \( \pi \) and \( \pi' \) respectively.

v) To examine the goodness of fit of the regression model, \( R^2 \) and F-test have been used.

vi) In order to determine the components affecting the viability of the RRB under study and examine their relative significance, ‘Factor Analysis’ has been performed following Principal Component Analysis with Oblique Rotation.

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# Y = a + bt, differentiating both sides w.r.t. t we get dy/dt = d(a+bt)/dt = b

As the variables under analysis are mutually interrelated therefore Oblique rotation method has been applied instead of Varimax Rotation, which is the appropriate technique for mutually independent variables.
vii) For the analysis of customers’ perception about the service quality of the bank and the level of customers’ satisfaction, following techniques have been adopted:

a) To express the level of satisfaction (ranging from highly dissatisfied level to highly satisfied level) in cardinal terms, the widely used Likert 5 point scale has been adopted.

b) For meaningful representation of customer satisfaction, three consumer satisfaction indices \((\text{Consumer satisfaction index for } i^{th} \text{ customer } (CSI_{ci}), \text{ Customer satisfaction Index for the } j^{th} \text{ attribute } (CSI_{aj}), \text{ and Overall satisfaction index for the RRB as a whole } (CSI_{o})\) have been derived. The detail explanations of these indices are given in the appropriate chapter (Chapter-VI, § 6.5.2)

viii) In order to determine the number of factors influencing Customers’ Satisfaction in RRB under study and evaluate the relative strength of each the factors in influencing the Customers’ Satisfaction level, the Factor Analysis (FA) has been done.

ix) Statistical softwares, specifically, SPSS-13 for Windows, Minitab-14.4 (windows version) and Microsoft-Excel have been used to analyse the data according to purpose of the analysis, suitability and convenience and applicability of the software.

1.12. Scheme of study:

The study has been organised in seven chapters.

The first chapter, Introductory; is devoted to the statement of the problem, a brief introduction to the study area, extensive review of available literature, finding out the research gap, rationale of the study, objectives, conceptual framework, hypothesis, research methodology and limitations of the study.

The Second Chapter entitled ‘Evolution of Rural Banking system in India (with special reference to RRBs) - a paradigm shift’ is devoted to detailed analysis of the process of evolution of rural banking system in the country since pre-independence period, with special emphasis on the genesis and evolution of regional rural banks. Going through the relevant committee reports,
recommendations and their implementations by the government, the chapter aimed at identify the areas of divergence in objectives and operational approaches of the RRBs in the post reform regime in comparison to that of the earlier period.

Keeping in view of the paradigm shift as in the earlier chapter, an endeavour has been made in Chapter III, entitled, *Financial Performance of RRB in South Assam (Cachar Gramin Bank): A Critical Assessment* to assess critically the financial performance of the RRB in the area under study. It makes a comparative analysis of the bank’s performance in the pre and post reform periods in terms of widely used parameters such as branch expansion, volume of deposits mobilized, volume of loans and advances, priority sector lending, and so on, as mentioned earlier.

After a critical assessment of the performance of the bank under study, Chapter- IV, entitled, ‘Profitability of RRB in the study area: Trend and Determinants’ investigates the aspects of commercial efficiency of the RRB. Profit being an index of commercial efficiency, as well as viability of the bank, the chapter makes a critical assessment of its profitability performance, with a comparison of the same between the pre and post reform periods with the help of standard profitability indicators, viz., spread to working fund ratio, total expenditure to the volume of business ratio, Burden ratio, Manpower expenses to the total expenses ratio and others (as already mentioned). A functional relationship between the volume of profit and some widely used intervening variables has also been derived in this chapter.

The Chapter- V entitled ‘Derivatives of Financial Viability of RRB: an application of Principal Component Analysis’ is devoted to analyse the determinants of viability from point of operational efficiency, based on the widely used efficiency parameters. Besides these, the chapter identified the factors determining the viability of the RRB under study along with their relative significance, with the application of Principle component analysis.

Customers' perception about the service quality has been assessed in Chapter- VI, entitled ‘Service quality vis-à-vis Customers’ Satisfaction in RRB: an Empirical study’. The empirical analysis was made in respect of perception of customers about the quality of services rendered by Cachar Gramin Bank based on the responses from the customers on the basis of 21 widely used attributes. Satisfaction levels of customers, for the attributes and for the bank as a
whole have been derived with the help of specially designed satisfaction indices. Further, in order to identify the factors influencing the customers’ satisfaction and their relative significance we applied principal component analysis.

Finally, the Chapter – VII, Epilogue, deals with the concluding part of the study, wherein, the summary of findings, and conclusion with suggestions for further improvement in the viability and profitability of the RRB in the study area, have been discussed. It also highlights the scopes for further research in the related field of study.

1.13. Limitation of the Study:

The study is mainly based on the financial information relating to the functioning of the Cachar Gramin Bank (CGB) which acted as the only RRB in the three districts of Barak Valley in South Assam, viz. Cachar, Karimganj and Hailakandi for the period 1981 to 2004-05. However, on 12th January 2006, it has been merged with other three RRBs of the state sponsored by the United Bank of India. As a result, all the branches of erstwhile CGB are now functioning as the branches of newly formed Assam Gramin Vikas Bank (AGVB). Since our period of study does not cover the event of merger and formation of AGVB, the analyses and findings are exclusively based on the financial information of CGB.

The functioning of RRBs is highly affected by regional, geographical, infrastructural, institutional, political and other economic factors. Therefore, the findings of the present study may not be fully applicable for the RRBs in other regions of different socio-eco-politico milieu.