CHAPTER VIII

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The UCBs have been occupying a unique place in the cooperative credit structure in India and are expected to assume the leadership in undertaking promotional and developmental programmes for the growth and success of the cooperative movement in urban and semi-urban centres of India.

With the growing urbanisation, the consequent problems of urban poor and their sufferings merit immediate attention and action. The UCBs have a pioneering role to play in mitigating the intensity of such problems. But, mere quantitative growth and wide geographical network of the UCBs cannot provide a straight jacket solution for the problems of urban masses. In order to promote the habit of thrift among the small men with small means and to bridge the credit gap in financing the urban and semi-urban poor, the UCBs are expected to be operationally efficient and financially sound. For this purpose, periodical monitoring and evaluation of their performance is quite necessary. Such an analysis provides the necessary feedback and triggers the process of corrective actions. This is essential not only to improve the operational efficiency but also to examine the financial strength of the UCBs. The present study is a modest and humble attempt towards
this end. It aims at analysing the performance of UCBs in Karnataka in the major functional areas, viz., deposit mobilisation, credit deployment pattern, recovery performance, management of operating cost, etc.

Summary of Findings:

The main findings of the study are as under:

A) Analysis of Deposit-Mix:

i) Deposit-mix by nature reveals that the percentage of fixed deposits to total deposits is the highest followed by that of the other deposits which are of fixed nature. The higher proportion of these deposits signifies that urban and semi-urban savings are interest-elastic or growth-with-stability oriented. The preponderance of fixed deposits and other deposits of fixed nature implies high cost of deposit-mix, greater degree of financial risk and lesser scope for profitability.

ii) The relatively lower proportion of savings deposits and regular declining trend in the same indicates that the UCBs efforts are not effective in cultivating the habit of thrift and savings among the people with moderate means in urban and semi-urban centres of Karnataka State. This kind of situation also indicates that the UCBs in Karnataka have failed to mobilise the low-cost deposits.
iii) The regular rising trend in current deposits shows the ability of the UCBs to attract traders, petty business persons, artisans, etc. However, the relative share of current deposits in total deposits is quite insignificant (approximately 6 percent).

iv) Analysis of deposit-mix by source reveals that the percentage of deposits from members to total deposits has shown a general declining trend over the period. The average proportion of such deposits forms approximately 50 percent of total deposits. This shows the lack of interest, preference and participation of the members in the deposit business of their own banks. It also shows that the UCBs in Karnataka have acted as mere credit purveyors but not as catalysts in promoting the habit of savings among the members.

v) The regular rising trend in the percentage of deposits from societies and other institutions reflects better efforts of the UCBs in garnering the institutional deposits. However, average share of such deposits is quite insignificant, approximately 3 percent. This gives a signal to the UCBs to mobilise more and more deposits from the institutional customers.

B) Deposit Mobilisation - Performance Appraisal:

i) In absolute terms, the deposits recorded a regular upward trend. However, the yearly percentage growth rate has
not been uniform and has shown a general declining trend. The uneven growth rate and a general downward movement in the yearly percentage growth rate are the symptoms of declining ability and inconsistency of the UCBs in mopping-up urban and semi-urban financial surplus and savings.

ii) The deposits of the UCBs in Karnataka are heavily concentrated in four districts, viz., Bangalore, Belgaum, Bijapur and Dharwad. The concentration in these four districts is to the extent of 70 percent of total deposits of the UCBs in Karnataka. Again, the other four districts, viz., Chitradurga, Daxin Kannada, Uttar Kannada and Mysore jointly share about 25 percent of total deposits in the State. This signifies either poor performance in the majority of the districts, or the absence of the UCBs or their branches, and/or lack of deposit potentiality in the remaining districts.

iii) Average deposits per UCBs, in absolute terms, have recorded a regular rising trend. However, the percentage variation in average deposits per UCB have shown a general downward movement. It may be inferred that average deposits per UCB showed an upward movement mainly due to stagnancy in the growth of the UCBs in number coupled with the absolute growth in deposits.

iv) There is a rising trend in the average deposits per branch of UCB from year to year. However, the percentage
variation in deposit per branch has shown a declining trend. This reflects the declining ability of the UCB's branches in mobilising the deposits.

v) Cost of Management Per Rupee of Deposit:

The steady rising trend in the cost of management per rupee of deposit mobilised by the UCBs in Karnataka reveals that the deposit mobilisation by the UCBs is not cost-effective. In addition to the cost of management, the deposits of the UCBs have higher interest cost liability due to the predominance of high interest-cost-oriented fixed and other deposits in the deposit-mix.

C) Analysis of Credit-Mix:

Analysis of the Credit-Mix of the UCBs reveals the following:

i) There is an uneven and downward trend in the growth rate of total credit deployed by the UCBs. It reflects the diminishing ability of the UCBs in the deployment of costly deposit resources. It may be due to restriction regarding priority sector lending, ineffective credit planning and management, credit control measures of the R.B.I., etc.

ii) The nature-wise analysis of credit-mix reveals that the loans as a percentage of total credit have shown a declining trend, while the cash credit and overdraft as a percentage of
total credit have shown a regular upward trend. This implies increasing credit by the UCBs in Karnataka to business class borrowers.

iii) The purposewise analysis of credit reveals that the credit for activities allied to agriculture forms a very insignificant proportion of total credit. The average proportion of such credit is about 3 percent of total credit.

iv) Despite the refinance facility and the benefits of credit guarantee schemes extended to credit for small-scale and cottage industries, the UCBs in Karnataka are quite hesitant to venture into the field of industrial financing. It is evinced from the declining proportion of such credit and relatively smaller share of such credit in total credit, i.e., 10 percent of total credit.

v) The percentage of credit to small road transport operators in relation to total credit indicates an upward trend. Thus macro analysis shows better performance of the UCBs in this sphere. However, the average proportion of such credit constitutes only 7 percent to total credit which is not significant. Further, only five districts, viz., Belgaum, Chitradurga, Tumkur, Mandya and Uttar Kannada have performed better in respect of credit to transport operators. The performance of majority of the districts is far from satisfactory.
vi) The UCBs in Karnataka have concentrated much on traditional credit to trade and commerce as reflected by an average proportion of about 21 percent of total credit for this purpose. The districtwise position is also in line with this inference. This warrants far re-orientation and diversification of credit policy of the UCBs.

vii) Although, the credit by the UCBs to self-employed persons and professionals shows an upward trend, the average proportion of such credit is quite low, i.e., approximately 6 percent of total credit. This is a suitable and productive avenue for the UCBs to deploy more credit than what they have done already.

viii) The credit for educational purpose forms a negligible proportion of the total credit granted by the UCBs. It is not even two percent of the total credit deployed by the UCBs in Karnataka. This is yet another avenue for the UCBs to enhance their credit deployment.

ix) The percentage of credit for housing schemes shows ups and downs. It works out approximately 16 percent of total credit deployed by the UCBs in Karnataka.

x) There is a declining trend in the proportion of credit for consumption purpose. It implies right step in the right direction in the sense that the unproductive credit for
consumption purpose is being gradually discouraged. However, the average proportion of such credit to total credit is on the higher side i.e., approximately 20 percent of total credit. This calls for still more reduction in such credit.

D) Credit Deployment - Appraisal of Performance:

Appraisal of UCBs Performance in the sphere of credit management reveals the following.

i) The UCBs in Karnataka have provided short-term credit (loans) much in excess of the available short-term resources. The higher percentage of short-term credit in relation to short-term funds indicates lack of perfect linkage between short-term resource and short-term credit. This reflects the defective planning and deployment of short-term credit by the UCBs.

ii) The average percentage of long-term credit to long-term resources has been very low (approximately 40 percent). Thus there is a wide gap between long-term credit and long-term resources. This highlights poor planning even in respect of long-term credit provided by the UCBs.

iii) The financial stake in terms of involvement of members' funds for the credit business of the UCBs has shown a regular decreasing trend. The average proportion of the members' funds constitutes 15 percent of total working funds. The low and
declining degree of financial stake implies the decreasing involvement of the UCBs and their members in credit business. This may have adverse impact on the loanable funds position of the UCBs. It also indicates that the management of the UCBs may take little interest in credit business and recovery of outstanding credit.

iv) The proportion of credit deployed to working capital has shown a declining trend over the years. The average proportion of credit deployed to working capital has been 65 percent. This signifies that the efficiency and effectiveness of the UCBs has been diminishing. The widening gap between credit deployed and working capital implies the presence of idle funds with the UCBs.

v) The declining CDR of the UCBs during the study period supports the inference that the UCBs have not been able to deploy their resources in an optimum manner.

vi) Analysis of credit disbursement pattern reveals that the percentage of small loans to total credit has been very low and has shown a declining trend over the years. This signifies that the UCBs in Karnataka have failed to cater to the credit needs of small borrowers i.e., people of smaller means whose credit worthiness is low. There has been a high degree of concentration in big loans with too few borrowers at the cost
of small borrowers, which defeats the basic objective of the UCBs.

vii) Sizewise analysis of the number of borrowers reveals that the UCBs in Karnataka have inclined more towards catering to the needs of large-scale borrowers borrowing big loans. In other words, a small number of borrowers have got larger credit assistance from the UCBs. Only 11 percent of borrowers have procured the credit assistance to the tune of 54 percent of total credit. Thus, there is a high degree of concentration of credit in the hands of only few borrowers, signifying thereby the ineffectiveness of the UCBs in catering to the credit needs of a large number of small borrowers.

viii) The credit for small-scale and cottage industries forms relatively an insignificant portion of the total credit. This calls for diversification and re-orientation of credit policy.

ix) Incidence of credit per account has shown general upward trend. It is due to the higher percentage variation in credit business than that in the number of accounts. This implies that the UCBs have failed to cover a large number of borrowers in the process of providing credit.

x) Short-term loans for SCs/STs did not show much increase over the years. The average total credit for these sections accounted for about 2.38 percent of total short-term credit.
(STC) which is quite insignificant. The average long-term credit (LTC) for SCs and STs was about 3 percent of total L.T.C., which is quite insignificant. This signifies the ineffectiveness of the UCBs in providing adequate credit to these socially oppressed and economically exploited sections of the society. The target set by the RBI in the sphere such credit is 15 percent of total loans/credit provided by the UCBs.

xi) Analysis of Recovery performance in terms of outstanding and overdues reveals that the percentage of overdues to total loans outstanding has been marked by ups and downs. The average proportion of overdues in relation to total loans outstanding was 13 percent.

xii) Although the percentage of chronic overdues to total overdues showed a marginal decline over the period, the same constitutes sizeable portion of total overdues i.e., 30 percent. Since any amount of chronic overdues is not desirable, the present percentage of chronic overdues reflects the greater risk associated with credit collections.

xiii) Age wise analysis of the overdues reveals that more overdues have been of the age of one year or less than three years. The proportion of such overdues in the total overdues has increased marginally, while the overdues of more than 3 years old, as a percentage of total overdues, have shown a
marginal decrease. This indicates that the UCBs have concentrated much on the recovery of overdues of three years old. It should be observed that if the overdues of less than 3 years old are not properly controlled and collected at the initial stage, the UCBs have to follow an ongoing process of controlling the overdues of three years and more than five years old by way of legal action.

F. Analysis of Profitability:

i) The overall profitability of working funds (ROWF) is quite low. The average net profit accounts for about 2 percent of total working funds.

ii) Analysis of the causative factors responsible for poor return on working funds reveals that the poor profitability of working funds has been mainly due to:

a) higher level of financial risk resulted from preponderance of high cost deposits in total deposits;

b) lower level of average return on account of preponderance of low-return credit in total credit; and

c) poor operating cost effectiveness which is evinced by an increasing trend in the management cost per rupee of banking business.
iii) The management cost per rupee of banking business has witnessed an increasing trend over the years. In fact, this should go on decreasing as the volume of credit increases over the period. This shows that man power and other physical facilities have not been efficiently utilised.

iv) The cost of management as a percentage of working funds is much higher than the prescribed limit of 2 percent during all the years under study. This signifies that the UCBs in Karnataka have not been operationally efficient and have failed to exercise cost control measures. High and rising management cost in relation to working funds is another factor which has affected overall return on working funds of the UCBs adversely.

Suggestions:

In the light of above findings, the following suggestions have been made for improving financial and operational health of the UCBs in Karnataka:

1. Increasing the Equity-base:

The equity base of the UCBs is very poor. The UCBs' owned funds (share capital & reserves) constitute approximately 15% of the total working funds. In view of relatively the smaller share of owned funds and the bigger share of high cost external funds, the financial risk of the UCBs is high. Hence,
the UCBs have to enhance their equity base. This ensures the availability of funds without attracting any financial commitment on the part of the UCBs, strengthens the financial base and creates public confidence in their working. Such an image will go a long way in mobilising the low-cost funds in the form of deposits. The equity base may be increased by way of open membership in the place of restricted and limited membership to certain known people or relatives.

2. **Inculcating Thrift and Savings Habits:**

As the low-cost deposits in the form of savings and current deposits constitute relatively smaller portion of total deposits, the UCBs have to inculcate thrift and savings habits among the urban mass, who are generally doing jobs or business, by way of transforming their investment behaviour. The UCBs have to effect a transformation in their savings behaviour in such a way that the attitude of the people towards the UCBs is positive. The UCBs may follow door-to-door campaign in order to explain the benevolent effects of the urban co-operative banks and thereby to make a positive change in their behaviour.

3. **Environmental Scanning for introducing Need-based Deposit Mobilisation Policy:**

Urban people save for different motives. They may be interested in regular interest income, or growth of their
investment, or regular annuity after their retirement or owning a property or house after some time. Hence, the deposit policy introduced by the UCBs should be based on the nature of motives of the savers. If there is no matching between the nature of the savers' motives and the nature of UCBs' deposit policy, the UCBs may not attract different savings from different savers.

4. Attracting Institutional Savings & Deposits:

As the share of institutional savings and deposits in total deposits is very meagre, the UCBs have to attract savings from the institutions like schools, colleges, associations, etc. Such deposits will remain with the UCBs relatively for longer period without attracting high level of financial risk associated with other type of deposits like fixed deposits.

5. Improved Customer Services:

The volume of deposits mobilised by the UCBs depends upon the number of existing satisfied customers and the quality of the services rendered. The UCBs should not forget the fact that the modern banks are the banks for the customers, of the customers and with the customers in view of keen competition posed by the banking and non-banking financial institutions while attracting savings from the public. It is the quality of the right services provided to the customers at right time.
that affects the savings and investment behaviour of the customers.

6. Linking of Housing Credit with Deposit:

The complexity of housing problem is increasing at urban places in India over the period. The demand for the house credit for purchasing or construction of houses at urban places has been increasing. But the supply of such credit by the banks is not increasing at the same rate. In view of this, the UCBs have to introduce certain deposit schemes in such a way that the housing credit is provided only to those customers/borrowers who deposit certain amount their savings during the pre-sanction period. Such a scheme will increase not only the deposit base and also will enable the UCBs to provide the credit to the right borrower for the right purposes, which in turn improves the recovery performance.

7. Linking of Credit for Transport Operators with Deposit:

Analysis of credit for transport operators like pliers of auto-rikshaws, motor cycles, etc., and the credit for petty-business is increasing at urban places. In this context, the UCBs have to devise a credit scheme in such a way that such credit is provided only to those borrowers who have kept certain amount of deposits during pre-sanction period. This scheme also improves the recovery performance and the deposit-base of the UCBs.
8. Trade-off between risk & return:

The analysis of deposit-mix of the UCBs reveals that there is a high degree of preponderance of fixed deposits (about 42% of total deposits) and other deposits of fixed nature (about 28% percent of total deposits). This signifies interest-elasticity of urban and semi-urban savings and deposits. A high proportion of these term-deposits implies high cost of deposit funds, greater degree of financial risk and restricted scope for profitability. Therefore, it is necessary that the UCBs deploy their scarce and costly resources most judiciously to bring in maximum return. This calls for an immediate action on the part of the UCBs to trade-off between the risk and return in respect of these term-deposits.

9. Diversification of Credit Policy:

It is found that credit expansion of the UCBs is not in par with the growth in deposit. The average proportion of credit for certain purposes such as, credit for Agriculture, Road Transport Operators, self-employed persons and professionals form a very insignificant share in total credit provided by the UCBs. Especially the percentage of credit for small-scale and cottage industries is not only low but also is showing a declining trend. In view of this condition prevailing in the sphere of credit dispersion, it is advisable for the
UCBs to adopt a sufficiently wide and diversified credit policy suited to the needs of time and of different categories of members. The credit policy pursued by the UCBs should be more imaginative and should be in tune with the programmes of economic development.

In this connection, the UCBs may diversify their credit towards small road transport operators, self-employed persons and professionals and small-scale and cottage industries with special attention. This kind of diversification of credit would contribute not only to the growth rate in credit and profitability of the UCBs but also to the overall development of urban and semi-urban areas and the people served by these co-operative units.

10. Shift in Emphasis from Security to Purpose:

The study reveals that secured credit predominates in the total credit-mix of the UCBs. Even among the purposes, there is a high concentration of credit for consumption purpose and for repayment of prior debts. This state of affairs is not conducive for the healthy growth of the UCBs. Therefore, there should be a visible shift in credit policy from security to purpose or credit-worthiness of the borrowers. The UCBs should be guided by the need and viability of the project while extending credit.
11. Professionalisation of Credit Operations:

Credit Management implies a process of activities such as credit investigation, documentation, appraisal, review, follow-up, recovery and write-offs. Formulation and appraisal of credit schemes of small scale and cottage industries, transport operators, self-employed persons, professionals, housing, etc., require the examination of technical, financial, economic, organisational, managerial, commercial and legal aspects. All these need decision-making skills. The appraisal of all these factors merely on the judgement based on the past experience and existing accounting data may prove to be inadequate. The individual judgement should be supplemented by specific information and data pertaining to external environment in general and the borrowers' financial position in particular. Such information can be obtained by the modern methods of financial analysis for credit appraisal, review and follow-up. This calls for professionalisation of lending operations of the UCBs.

12. Gradual Reduction of Unproductive Loans:

It is seen that the credit for consumption purpose and for repayment of prior debts predominates in the credit-mix of the UCBs. If such unproductive loans are given without observing any checks and controls, this would encourage wasteful expenditure causing inflationary pressures. Such
credit, coupled with absence of supervision and control over end-use, and poor or rather absence of effective machinery for recovery of credit would result in overdues. Therefore the UCBs have to observe self-discipline in regard to granting of credit for consumption purpose, repayment of prior debts and for meeting ceremonial expenditure. The proportion of such credit should be reduced in a phased manner.

13. Exploration and Exploitation of Profitable Avenues for Credit Deployment:

It is found that the UCBs have not been as aggressive in increasing their loans and advances as they have been in augmenting the deposit resources. The UCBs should actively explore their credit deployment opportunities by conducting surveys within their respective area of operation to identify the scope for and purposes of credit deployment. Such surveys will ensure the optimum use of all available funds.

14. Major thrust for Credit to Small Borrowers:

The study reveals that the UCBs have advanced a large proportion of total credit to big borrowers. As the UCBs are meant to cater for the needs mainly of persons of moderate and small means, they should aim at providing credit to a large number of small borrowers. This act of diversification minimises the default-risk associated with the present credit
policy of putting all the eggs in the same basket i.e. providing too much credit to too few borrowers.

15. Simplifying the Lending Procedure:

Considering the clientele of the UCBs, the loan application forms should be as simple as possible so that the procedure is easily understood by the borrowing-members. Adherence to a highly complex and lengthy procedure and compliance with several unnecessary technicalities would prevent the borrowers from approaching the UCBs for credit assistance.

16. Effective Supervision over End-use of Credit:

Majority of the UCBs do not have adequate machinery for supervision over the end-use of credit and recovery. A heavy reliance is placed on the local directors for the recovery of loans. It is essential that the UCBs have supervisory staff for follow-up of loans granted and for timely recovery of credit.

17. A Separate Recovery Cell:

The study reveals that the average percentage of overdues is about 13 percent of total credit outstanding. The chronic overdues formed an average proportion of about 30 percent of total overdues and 4 percent of total credit outstanding. Since any amount of chronic overdues is not desirable, the present position of chronic overdues reflects
the greater degree of risk associated with credit collection. In this context, the UCBs in Karnataka, instead of placing a complete reliance on the local directors for the recovery of "credit, should set up a separate recovery cell. This would ensure a continuous machinery for the collection of credit outstanding in general and overdues in particular.

The separate recovery cells so established should undertake the recovery of overdues, as far as possible, by persuasive measures. The coercive measures such as legal action, auction of the pledged or mortgaged property, etc., should be resorted to only in exceptional cases. Because such measures involve additional cost and delay in the form of lengthy legal litigation. The coercive measures have also an adverse impact on the image of the UCBs.

18. Resource-Based Credit Policy:

The study reveals that there is mis-matching between short-term credit and short-term resources and long-term credit and long-term resources, which has affected the overall profitability of the working funds. Therefore, it is desirable that the UCBs have to follow resource-based credit policy so that there will not be any scope for diversion of high-cost funds to low-return credit outlets. Such a resource-based credit policy will also eliminate the situation of idle funds with the UCBs.
19. **Commercial Motive-Oriented Social Banking Practices:**

Promoting social-welfare by the UCBs by providing huge amount of low-return credit to priority sectors need not be at the cost of the UCBs. Such a social-banking credit policy should not affect the very survival of the UCBs. Because the UCBs are not the charitable institutions to provide credit at cheaper rate by neglecting the cost of funds used for such credit. They have to carry on such lending practices by charging the reasonable rate of return on the funds deployed.

20. **Cost Audit and Management Audit for controlling Cost of Management:**

The study has revealed that there is lack of operating cost effectiveness at the UCBs' level. This has affected the overall profitability of the working funds. Hence, it is imperative on the part of the UCBs to arrest the increase in cost of management by introducing cost control measures like cost audit, management audit, evaluation of experience curve of bank employees, etc. If the ineffectiveness of the management cost is due to mis-matching between the job traits and the man traits, the banks' recruitment and promotion policies and practices may be streamlined so as to avoid the evil consequences of putting the wrong pegs into the wrong holes. In order to tone-up the operational efficiency of the existing
personnel, they may be properly trained and developed to become fit for doing banking business on commercial principles.

21. Introduction of Merchant Banking Services:

In view of high financial risk, high proportion of low-return credit and ineffectiveness of operating cost, the UCBs' overall return on working funds has been adversely affected. Therefore, the UCBs have to search for the ways and means of augmenting their income-base by way of providing merchant banking services like guiding on feasibility of the projects, counselling, etc.

22. Monitoring Operational and Financial Health at Regular Intervals:

The UCBs in Karnataka have become the victims of several operating maladies like poor recovery, mounting overdues, concentration of big size loans in the hands of too few borrowers, etc., and financial problems like poor investment profitability, lack of linkage between credit-mix and deposit-mix, etc. Hence, to improve the operating and financial health, the UCBs have to undertake performance evaluation studies at regular intervals. Such periodical evaluation enables the UCBs to be operationally viable and financially profitable.
To sum up, the above measures, if properly adhered to or implemented, will definitely improve the efficiency and effectiveness in the spheres of deposit mobilisation and credit management by the UCBs in Karnataka in particular and other UCBs in India in general.