Introduction
I. INTRODUCTION

Agriculture sector plays a strategic role in the process of economic development of a country; especially its role in the economic development of the low income countries is of vital importance. In other words, where per capita real income is low, emphasis is being laid on agriculture. As defined in World Development Report 2005, low income economies are those economies where Gross National Product (GNP) per capita is either $765 or lower to it in 2003. Middle income economies possess GNP per capita between $766 to $9385, lastly, high income economies with GNP per capita $9386 and above.

The per capita income level is much low in India as compared with other developed countries. According to World Development Report (2005), India is termed as low income economy. The per capita income in India is about 1/77 of US level of per capita income. Thus, India being a low income economy, the importance of agriculture in the Indian economy is clearly emphasized by the following points:

(i) Share of agriculture in National Income: Agriculture has got a prime role in Indian economy, though the share in national income has come down. The contributory share of agriculture in Gross Domestic Product (GDP) was 55.4% in 1950-51, 52% in 1960-61 and is at present reduced to nearly 22%, but still significant.

(ii) Important contribution to employment: Agriculture sector, at present, provides livelihood to about 65% to 70% of the labour force.

(iii) Important source of industrial development: various important industries in India find their raw material from agriculture sector, cotton and jute, textile industries, etc., are directly depended on agriculture. Handloom, spinning, oil milling, rice thrashing, etc., are
various small scale and cottage industries which are dependent on agriculture sector for their raw material. This highlights the importance of agriculture in industrial development of the nation.

(iv) Importance in international trade: India’s foreign trade is deeply associated with agriculture sector. Value of agriculture exports to total exports of the country has been ranging between 15% to 20%. Besides, goods made with the raw material of agriculture sector also contribute about 20% in Indian exports. In other words, agriculture and its related goods contribute about 38% in total exports of the country.

Thus, agriculture is the backbone of the Indian economy. We have attained self-sufficiency in the production of food grains, which is an achievement when viewed in the context of steady upward trend in the growth of country’s population. However, in the last decade, signs of stagnation and even some degree of deceleration in agricultural growth have been noticed and this trend calls for immediate attention. The average annual growth rate of value added in agriculture, including allied sectors, declined from 4.7% during eighth plan to 2.1% during ninth plan. Advance estimates for the year 2004-05 indicates the further decline in the growth rate to 1.1%.

Apart from this, labor productivity in agriculture is low compared to non-agriculture sector. In other words, 36% of working population engaged in non-agricultural activities contributes 73% of GDP. This contradiction clearly states that per labor productivity in agriculture sector is approximately half than that in non-agriculture sector. It is the indication of backwardness that still persists in Indian agriculture. As a result of this farmers’ income from their farm operations is just sufficient to provide
minimum necessaries of life. Hence, farmers in India cannot expect their credit needs to come from their savings. Therefore, farmers have to rely upon outside finance. Modern agriculture is a costly affair. Credit is needed to adopt new farm technology, which helps to augment the productivity of agriculture. Increased agricultural productivity is essential for the following reasons: to supply an economic surplus that can be consumed or used for further production in agriculture; to make possible the release of labor and other resources for use in non-agricultural sectors; and to increase the purchasing power of rural people. In short, effective arrangements are needed to provide credit facilities so that agriculturists may adopt better techniques of production which is essential for agricultural growth.

The different studies conducted show a strong relationship between agricultural growth and availability of credit. Broadly, credit in agricultural sector may be divided into short-term loans to meet the input expenses and medium and long-term loans to facilitate the development of fixed farm assets such as land. This gap arises in relation to static or dynamic production function. Under a static functioning, the level of input use per hectare of cropped area being constant, the year to year variation in the amount of credit reflects the changes in input prices. Under a situation of diminishing returns, however, increasing input use is required to maintain the same level of output. The supply of credit related to static production conditions will not contribute to increase in output, although the withdrawals of it might lead to a decline in output. Under dynamic functions, credit requirements would rise from year to year even if input prices remain constant. The growth in credit under such dynamic conditions would lead to increased
output. In the same way the investment credit too would lead to an improvement in the production potential of the farms through the process of net capital formation.

Agricultural credit, thus, in a practical sense, is a nucleus of the system of farm operation. It provides flow to the system averting ruins which would have occurred due to the lack of monetary capacity of farmers. Thus, adequate and timely credit to the farmer is, vital and indispensable for the rehabilitation and progress of agriculturists. In low income countries like India agriculture assumes even more importance. Farmers' inability or least limited ability to save does not allow him to finance his pursuits and raise better production from his farms. Agricultural credit through institutional channels is the only way to break agricultural stagnation. Private functioning agencies play a limited role keeping in view the larger public interest.

Three types of loans are provided to Indian farmers to meet their financial requirements – short term loans, medium term loans and long term loans. Short term loans are provided for a period of less than 15 months to meet out expenses of routine farming and domestic consumptions. This type of loans is demanded by farmers for purchasing seeds, fertilizers and for meeting out family requirements. Medium term loans are provided for a period of 15 months to 5 years. This type of loan is taken by the farmers to purchase agricultural equipments, animals and for land improvements. Long term loans are provided for a period of more than 5 years. This type of loan is taken by the farmers to purchase land and expensive agricultural equipments and for payment of old loans. Indian farmers acquire above types of loans from two sources: Non-
institutional sources like money lenders, landlords, big business men, etc.; institutional sources like commercial banks, cooperative banks and government sources.

The efforts to build up the institutional credit system for agriculture in India was initiated in 1904 through cooperative movement since the system of loans advanced by the government under taccavi was a failure for various reasons. Gradually, cooperatives assumed more positive role and there was not only a steady quantitative expansion in their numbers but also a growing diversity in their functions. Passing through many stages of reorganization, the cooperative sector has grown as major source of rural credit in India. But the viability of the cooperative system has remained an elusive issue. Out of the 70,783 primary agricultural credit societies, only 60% are considered viable. About 170 District Central Cooperative Banks out of 369 were able to generate profits. Thus the performance of cooperatives, however, was far from satisfactory as was evident from the All India Rural Credit Survey, 1951-52. The All-India Rural Credit Survey (1951-52) brought out the fact that in spite of various procedural and administrative reforms as well as statutory credit facilities from the Reserve Bank of India, the cooperative system could account for only 3.1% of the total borrowings of cultivators. The cultivators continued to depend on the money lenders and the traders for more than 79% of the estimated requirements. But the cooperative movement has undergone far reaching changes based on the recommendations made by successive bodies and expert committees like the All India Rural Credit Survey Committee 1952, the National Development Council 1958, Shri Mehta Committee 1960, Shri Patel Committee 1961, the Conference of State
Till 1968, the official policy was in favor of developing co-operative system. In 1969, All India Rural Credit Review Committee found that over large parts of the country, small farmers have been lacking in their access to cooperative credit. Apart from this, the government has also realized that cooperatives are not adequately meeting the credit requirements of agriculture. Therefore, keeping this fact in mind, the government through social control (1968) brought commercial banks in the realm of agricultural credit and, further, in 1969 nationalized the 14 major banks of the country. Moreover, single agency approach has changed into multi-agency approach. But, instead of all this, commercial banks could not come to expectation. They faced numerous problems. Some of the major problems were: commercial banks did not supplement the cooperative societies in a cordial manner, secondly, they confined themselves to mobilize saving from rural areas and started to canalize this saving in urban areas. Thirdly, the nature of operations and profitability of commercial banks as well as their high cost structure of the commercial banks proved to be a great handicap. Fourthly, commercial banks were lacking trained personnel which may suit to the prevailing local environment. Lastly, distribution of the benefits of the commercial banks was not based on the criteria of equality. It was noticed that small and marginal farmers left without credit though massive amounts flowing into the agricultural sectors.

Thus, keeping all these shortcomings in view, Banking Commission 1972 recommended that a chain of rural banks to be set up in addition to the regular branches
of commercial banks. This gave birth to Regional Rural Banks (RRBs) in 1975 mainly to
overcome the gap left unfulfilled due to the failure of cooperative banks on the one hand
and commercial banks on the other. Moreover, after the declaration of emergency in
1975, the government announced the 20 point economic programme. The sole objective
of this programme was to devise alternative agencies to provide institutional credit to
landless laborers, rural artisans, small and marginal farmers. Steps were also initiated to
liquidate rural indebtedness of all sorts of rural folks. Apart from all this government of
India appointed a working group under the chairmanship of N. Narsimham. The group
observed that in a country of the size and regional diversity as ours, no single pattern, be
it commercial banks, cooperative credit can be expected to meet all the emerging
requirements in all areas. Thus, the Regional Rural Banks (RRBs) ordinance was
promulgated by the President on 26 September 1975, which came into force with
immediate effect. It is out of the recommendations of this working group and the
ordinance that the scheme of regional rural banks emerged.

Regional Rural Banks

The establishment of the Regional Rural Banks has been the land mark in
the history of rural banking. These banks were introduced in 1975 to strengthen the
institutional rural credit structure. Hence, on October 2, 1975, five RRBs were set up at
Moradabad and Gorakhpur in Uttar Pradesh, Bhiwani in Haryana, Jaipur in Rajasthan, and
Malada in West Bengal. These banks were sponsored by the Syndicate Bank, State Bank
of India, Punjab National Bank, United Commercial Bank and United Bank of India.
(i) Objectives: The RRBs have certain important objectives like, to identify a specific and functional gap in the present institutional structure; to supplement the other institutional agencies; to fill the gap within a reasonable period of time etc.

(ii) Capital Resources: each RRB is sponsored by a nationalized bank known as sponsoring bank which provides all sorts of help to these RRBs. Each RRBs must have an authorized capital of rupees one crores divided into one lakh shares of rupees hundred each. The paid up capital of the bank would be Rs. 25 lakhs which would be raised by the government of India, the concerned state government and the sponsoring nationalized bank in the ratio of 50:15:35. On the recommendations of the working group in 1986, the government has increased the authorized capital to Rs. 5 crores and issued capital of Rs. 1 crore respectively to improve their viability.

(iii) Management: the management of each RRB is vested in nine member board of directors, headed by a chairman. The strength of the board could be raised to 15 with the approval of the government of India.

(iv) Area of operation: RRBs are financial institutions. The area of operation of these banks is specified. The jurisdiction of each RRB was to be within specified districts in a state. In a sense, the region served by a RRB is normally a cluster of districts which varies between one to five. Its branch offices will generally cover one to three blocks and be in a position to finance five to ten farmers’ service societies. As regard the area of operation of these banks, it is selected very carefully. One criterion adopted is the absence of banking facilities either cooperative or commercial in the area. Besides,
continuity of the area, areas having certain homogeneity in agro-climatic conditions and rural clientele is also taken into consideration while specifying the area of RRBs.

(v) Sponsorship: each RRB will be sponsored by a scheduled commercial bank. It will be set up at the initiative taken by the sponsoring bank in consultation with the concerned state government and central government and under license from the Reserve Bank of India. The sponsors will provide assistance to these banks in several ways. The sponsor bank will subscribe to the share capital of RRB. It will assist RRB in its establishment, recruitment and training of the personnel. They may also provide managerial and financial assistance with the mutual agreement of sponsor bank and the RRB.

(vi) Expansion of operations of RRBs: initially, five RRBs were established on 2nd Oct 1975. Its number has increased to 196 at the end of June 2004 with 14507 branches, 82.6% of total branches are in rural areas. The deposits as on 31 march 2003 registering a growth rate of around 16% out of the total deposits, term deposits constitute 56%, saving deposits 4%. As at the end of March 2003, RRBs advances and investments stood at Rs. 20700crores and 28400 crores respectively. The gross Non Performing Assets of RRBs stood at Rs. 3200 crores, 14.4 % of their total loans. The banks have granted advances to small and marginal farmers, landless laborers and rural artisans which constituted about 90 percent of the total.

The RRBs have come a long way since their inception in 1975 and have now become an integral part of the rural financial system. As a part of the Financial Sectoral Reforms, Government of India, Reserve Bank of India and NABARD have initiated various measures during 1991-92 for improving the functioning of RRBs. These
measures were aimed at improving viability, competitiveness, profitability and efficiency of financial institutions. There is a perceptible change in the role and operations, of RRBs compared to the pre-reform period. Even so, high cost of operations, built up of non-performing assets, accumulated losses, etc. still haunt the viability of RRBs.

Traditionally, the restricted clientele, low capital base and high cost of intermediation, poor recovery of dues and slender interest spread affected the viability of RRBs. In addition, the limitations imposed by the economic potential of the area of operations of some of the RRBs, multiple functional controls, and restricted investment opportunities also have a bearing on the profitability of RRBs. The solvency problems were aggravated by the political compulsions to lend under credit linked subsidized programmes of the Government, the award of the National Industrial Tribunal giving pay parity for RRB staff with their sponsor banks, pronouncements of loan waiver schemes by governments, inadequate motivational efforts and incentive mechanism for the staff. Some of these aspects have been addressed through the revamping measures under implementation. The extensive bank/branch network taking the banking services to the door steps of the poor in far flung rural areas, mobilization of rural deposits and meeting the credit needs of the rural clientele are the major strengths of RRBs.

At present RRBs are working in all the states except in Sikkim and Goa. Presently 196 RRBs are working in the country. Since April 1987, no new RRB has been opened keeping in view the recommendations of Kelkar Committee. In this background various committees were appointed to look into the aspect of viability of RRBs. The Dantawala Committee (1977) recommended for continuation as also expansion of Regional Rural
Banks, as an integral element of the rural credit system. The RBI study on viability headed by Sivaraman (1981) opined that each Regional Rural Bank would require about six years and a network of 70 branches having outstanding loan business of rupees eight crores to attain viability. The amendment of Regional Rural Banks Act (1987) enhanced authorized share capital to rupees five crores and paid up capital to rupees one crore.

The Agricultural Finance Corporation study at the instance of NABARD, recommended for establishment of urban branches with all banking facilities on the lines of commercial banks. Narasimhan and Khusro Committees on Financial Sector Reforms observed that the non-viability of Regional Rural Banks was an inherent phenomenon, as evident from the small number of Regional Rural Banks making profits. Narasimhan had suggested many options, the implementation of which was subject to the decision of Regional Rural Banks. But Khusro on the other hand opined that Regional Rural Banks did not find a place in the financial sector and hence, they should be either merged with sponsor banks or eliminated by creating rural subsidiaries of commercial banks. The Government of India looked into the recommendations of these committees and decided to revamp the Regional Rural Banks by strengthening their capital base. Hence, accordingly it was decided by the Government to restructure 49 Regional Rural Banks. The Committee was formed for this purpose consisting of chairmen of four public sector banks such as Bank of Baroda, Punjab Bank and Sindh Bank, officials of RBI, NABARD and the Chairmen of concerned Regional Rural Banks. Various modalities for restructuring RRBs were drawn up by this committee. As per the recommendation of this
committee each Regional Rural Bank in consultation with sponsoring bank has to prepare a five-year plan to attain viability which was known as Development Action Plan (DAP). With these measures it is believed that the Regional Rural Banks would attain viability and continue to contribute significantly towards agricultural credit in the country.

Thus various policy measures to make RRBs viable were implemented in the light of financial sector reforms during WTO era. However, there are concerns which are specific to the Indian situation. The ultimate objective of financial sector reform in India should be to improve the operational and allocational efficiency of the system. Even from the point of view of meeting some of the socioeconomic concerns, it is necessary that the viability of the system is maintained. It is in this context that a fresh look at the performance of Regional Rural Banks is called for. An objective and rigorous evaluation of the performance of Regional Rural Banks was felt. The Malaprabha Grameena Bank was one of the Regional Rural Banks considered for restructuring in Karnataka. Hence, the Regional Rural Banks in Karnataka in general and Malaprabha Grameena Bank in particular was selected in the present study with an overall objective of evaluating their performance during pre and post WTO period.

1.1 Specific objectives

1. To classify the Regional Rural Banks in Karnataka into different categories based on the composite growth index.

2. To study the growth of Malaprabha Grameena Bank in terms of physical and financial indicators during pre and post WTO periods.
3. To work out different financial ratios of the bank for assessing the performance in the selected periods.

4. To estimate spread and burden ratios of the bank during the two periods for analyzing functioning efficiency.

5. To workout the Break-even volume business of the bank.

6. To identify the important physical and financial indicators influencing the performance of the bank in the two periods.

7. To estimate the sources contributing to profitability growth during post-WTO period.

8. To examine different dimensions of the overdues and non-performing assets and to suggest appropriate policy measures.

1.2 Hypotheses

Keeping in view the objectives of the study the following hypotheses have been framed.

1. There is a positive growth in the physical and financial indicators of the bank

2. The performance of the bank differs between the Pre-WTO period and Post-WTO period

3. The bank is performing above the break-even level of business

4. The overdues and non-performing assets are declining over the years

1.3 Scope of the study

The present study is an attempt to evaluate the performance of Malaprabha Grameena Bank by using various statistical and econometric techniques. Both
quantitative as well as qualitative variables were considered for the study. The main emphasis of the investigation was placed on the working of the bank. The performance of the institution was not subjected to holistic approach in the context of WTO, in the earlier studies. The conclusions drawn in the present study are broadly applicable to those institutions operating under similar situations. The present study would help the planners, policy makers and administrators in policy formulations.

1.4 Presentation of the study

The investigation has been presented in five chapters. Chapter one deals with the significance and relevance of the problem, the issues involved and the specific objectives of the study. The review of literature connected with the present investigation is presented in chapter two. In third chapter methodology adopted for evaluating the objectives is discussed. The fourth chapter summarizes the results. The last chapter brings out the overall findings and suggests the major policies for improving the performance of Regional Rural Banks.