

A STUDY ON THE VIABILITY OF RRBs AS RURAL FINACIAL INSTITUTIONS IN THE LIBERALISED ENVIRONMENT

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Introduction

The linkage between industrial development and overall economic development of a country is an established fact. As a developing economy the pace of development in India lies with rapid industrialization. And industrialization in turn, depends on development of other sectors like agriculture and allied services. Since India lives in its villages, they are considered as the backbone of the economy. So the overall development of India depends on the empowerment of its rural sectors viz. agriculture, small business, small scale and cottage industries, etc.

After 50 years of independence still nearly 65 per cent of total population live in rural areas. The march towards an economic self-reliant and self-sustaining economy is thus largely depending upon the strength of the rural sector. During the last five decades of Indian planning several policy measures have been introduced. But still rural India is languishing under poverty, inadequate health care facilities, scanty sanitary and drinking water accessibility, poor housing, mass illiteracy and many other similar type of economic and social handicaps. All the attempts made by our planners have belied the expectations of the masses. Thus still today, the upliftment of rural economy and its people assume immense significance.

Long run sustainability of industrial growth depends upon the development of rural areas, which accounts for two-third of the population and hence can constitute the necessary effective demand and market. Rural savings can provide capital resources for the development of industry and other sectors (Yajori, 1997).

Generating rural surplus and its recycling is thus the *sin qua non* of our economic development for which empowerment of rural masses is crucial. For this task of upliftment, over the years an array of economic and social institutions has been established. Among these institutions, the role of banks as the provider of finance to the rural people is well established.

Prof. Joseph Schumpeter (Quoted in Shetty, 1998) first established the explicit linkage between financial institutions like banks and economic development. And over the years their importance has been felt increasingly in all quarters of the economy. More particularly in the contemporary situation, banks are not considered merely as dealers in money, but as the leaders in development have to play a crucial role because the banks today are not just the storehouse of the country's wealth but are the reservoirs of resources necessary for development (Parischa, 1993).

The Emergence of Rural Banking in India

The emergence of modern banking in India can be traced back to early nineteenth century with the establishment of three Presidency Banks (*ibid.*). But prior to the independence there was no system of regular banking industry in the country. These were largely run on the basis of commercial principles, and there was no question of commercial banking coming in to fulfill the social needs of the economy. The banking industry itself was in a state of confusion, dislocation, stagnation and failures (Jha, 1998). Only after the first nationalization of banks in 1969, the focus of commercial banks was shifted to the rural areas with the mechanism of priority sector lending targets. Since early seventies, there was a growing realization that the ethos and attitudes of commercial banks were not conducive to meeting the credit needs of agriculturists and other weaker sections in the rural areas in view of the relatively high cost structure and inadequate local environment (Ammanaya, 1989).

The All India Rural Credit Review Committee observed that, even after the commercial banks had overcome their earlier reluctance of carrying banking facilities to smaller centres and had derived deposits from these centres which grew steadily, they had not, till

recently, made any significant progress in fulfilling the complementary responsibility of meeting the credit needs of the semi-urban and rural areas (RBI, 1969). The Banking Commission, 1972 also recommended that the structure of banks in rural areas should be such that provides a wide range of banking services and is economically viable (GOI, 1972). Although the Banking Commission, 1972 recommended for an alternate rural credit institution, it is the recommendation of the working group of Sh. Narashimham that could give birth to Regional Rural Banks (RRBs) in 1975 (GOI, 1975). The Committee, appointed to study in depth the problem of devising alternative agencies to provide institutional credit to the rural people, identified various weakness of the cooperative credit agencies and commercial banks, and recommended a new type of institution "which combines the local feel and familiarity with problems which cooperatives possess and the degree of business organisation, ability to mobilize deposits, access to central money market and a modernized outlook which the commercial banks have" (Desai, 1987).

The promulgation of Regional Rural Banks Ordinance on 26th September 1975 (later on replaced by RRB Act, 1976) paved the way for establishment of rural banks for the development of rural sectors. In the preamble, the Act says that the objective of setting up of RRB is to "develop the rural economy by providing, for the purpose of development of agriculture, trade, commerce, industry and other productive activities in the rural areas, credit and other facilities, particularly to the small and marginal farmers, agricultural laborers, artisans and small entrepreneurs, and for matters connected therewith and incidental thereto" (RRB Act, 1976). The first five RRBs were established on October 2, 1975 and by the end of March 2001, 196 RRBs are operating in India with 14311 branches.

The establishment of RRB heralded a new era of Indian banking. The initial expectation was that these banks would be able to bridge the gap between rural poor and urban rich. But over the years it is found that rural credit has been associated with poor recovery and high cost of servicing. A large amount of money of different lending institutions is choked in the rural financing. During the last 20 years several outstanding economists have analyzed this problem of rural credit. But it is surprised and rather sad that despite the best analysis of the problem and the said advice tendered over the years the problems instead of being resolved, appear to be compounded (Tarrapore, 1994). The RRBs because of the predominance of rural

sector in their operational domain, are severely affected by this default syndrome. The large volume of NPA coupled with high operational expenses has generated heavy accumulated losses for these RRBs. Particularly during the era of liberalization criticism has been raised over their viability. Being the custodian of public money they have to augment the existing resources through generation of more money, side-by-side meeting the avowed objectives enshrined in the Act. But the failure of these banks has put question mark on their functioning. Even to an extent RRBs restructuring has also been debated at length without a resolution of the problems of this sector. All the alternatives, viz., merger with the sponsor bank (Khusro Committee), merger into rural subsidies of commercial banks (Narashimham Committee) and the merger of all RRBs into a nation-wide National Rural Bank could not be implemented due to their serious drawbacks (*ibid.*). The latest initiative in this regard to provide financial assistance and managerial strengthening was made with budgetary provision of huge sum of money for restructuring of many unviable RRBs. Despite this and many other initiatives by NABARD and RBI any substantial qualitative improvement has not been noticed. Particularly during the ongoing liberalization phase, where accountability of public financial institutions is gaining more importance in the society, these RRBs have not shown the desired results. Their viability and effectiveness in managing rural credit are still under scrutiny. There is thus an urgent need to evaluate their performance and to provide some strategic measures to improve their position. Keeping the above need in the background an attempt has been made to study the overall situation of RRBs in India with a special reference to one RRB in North-east region. Further, on the basis of the findings the problem areas are identified and their solutions have been presented.

Banking Sector Reform and Regional Rural Banks

With the basic objective of catering to the credit needs of the small-scale sector, agricultural sector and other allied sectors the nationalization of banks was undertaken. "The nationalization was in recognition of the potential of the banking system to promote broader economic objectives, such as growth, better regional balance of economic activity and the diffusion of economic power. It was designed to make the system reach out to the small man and the rural and semi-urban areas and to extend credit coverage to sectors hitherto neglected by the banking system and through positive

affirmative action provide for such expansion of credit to agriculture and small industry in place of what was regarded as a somewhat oligopolistic situation where the system served mainly the urban and industrial sectors and where the grant of credit was seen to be an act of patronage and receiving it an aspect of privilege" (RBI, 1991).

The consequence of nationalization however, has not been very encouraging. The quality of credit assets fell as loan sanctioning became more a mechanical process rather than credit assessment decision. Political interference has been an additional malady. Credit disbursals with no proper post-sanction supervision led to the deterioration of the quality of the loan assets of the banks. Further, the subsidized lending rates coupled with the high level of low yielding SLR investments (investments in designated securities for the purpose of meeting the statutory liquidity ratio requirements of Reserve Bank of India) adversely affected the profitability of the banks. The haphazard branch expansion to meet the objective of nationalization has landed many public sector banks in trouble. The presence of high operating cost and strain on managerial resources resulted in low profitability. The quantitative expansion of banking business has also not matched with qualitative banking services. Thus there was a need to review the entire banking system. This need was felt greater with the initiation of real sector reform process in 1991. The real sector reform unleashes many new opportunities of business with a global reach. Thus to meet the challenges of liberalization and globalisation the banking sector reform has been initiated. The reform in banking sector was also thought of due to its inherent weakness and dismal performance. Some of the factors that led to the lackluster performance were:

- Greater emphasis on directed credit;
- Regulated interest rate structure;
- Lack of focus on profitability;
- Lack of transparency in the bank's balance sheet;
- Lack of competition;
- Excessive regulation on organisation structure and managerial resource;
- Excessive support from Government;
- Poor customer service, outdated technology and high transaction cost; and
- Political interference.

To address the causal factors of the dismal performance and to

cope up with the liberalization pressure a high level committee under the chairmanship of M. Narashimham was set up in 1991. The report of this committee heralded the banking sector reform in India. In 1998 the second report on banking sector reform also came from the same committee. Thus within the last decade of reform the banking industry in India has undergone seminal metamorphosis. The consequences of those changes have been far-reaching and revolutionary.

These reforms tried to enhance the viability and efficiency of the banking sector. To tackle the internal deficiencies of the sector, new norms relating to accounting practices, prudential standards and capital adequacy requirements were suggested. On the other hand, for improving the external environment, the reform aimed to transform the highly regulated environment into a market-oriented one.

The implications of such reform have been multifarious. Some of the important implications are:

To enhance the competitiveness in this sector, the industry was open for the private sector and foreign banks. This lowered entry barrier thus encouraged many to establish private banks and opening foreign bank branches and subsidiaries.

The phased deregulation of interest rate initiated in 1994 has liberated the banks from the clutches of Government. They are now free to set up their borrowing and lending rates as per the market condition.

Abolition of branch licensing and relaxation of branch expansion norm have enabled them to revamp their branch networking to suit their business need.

The introduction of prudential norms, which relate to income recognition, asset classification, provisioning for bad and doubtful debts and capital adequacy has brought more transparency in their operations.

Reduction of pre-emptive reserves like SLR and CRR has released more money for business at the hands of the banks.

Permission to invest in stock market has also given opportunity to augment their bottom-line.

The concerted approach to handle the NPA has also helped the banks to improve their recovery and augment their profitability.

Besides these above important measures, several others have also been implemented from time to time to improve the performance of this sector.

Thus the reform has brought many new things to this sector and also discarded many old concepts. The conceptual changes witnessed during this reform process are portrayed in the following chart.

<i>Items</i>	<i>What is in</i>	<i>What is out</i>
Objectives	Profitability	Developmental & social
Interest of	Shareholders	Priority sector
Strategies	Pro-active	Passive
Segment	Target Banking	Mass banking
Business	Fee based	Fund based
NPA management	Recovery management cell	Credit monitoring cell
Concentration	Investment	Advances
Human resource policy	Hire & Fire	Job security
Credit rating	Individual	Corporate

Source: Project.subcom.

Since RRBs are a part of overall banking system most of the reform measures have also affected their operation. The expansion of operations to non-traditional areas like consumer loans, housing loans etc. have boosted their income generation ability. The permission to relocate and closer of bank branches has also helped them to augment their business. But the enhancement of pay structure has increased their operational expenses, which in turn has affected their profitability. Further, they have also been lagging behind the technological revolution and growingly losing their business to other commercial banks.

RRBs- The Present All-India Scenario vis-a vis of NE Region

Over the last 26 years RRBs have made commendable contribution to the rural development. A total number of 196 RRBs with more than 14000 branches have reached nook and corner of 23 Indian states. Only two states namely Goa and Sikkim have no RRB. From the key indicators presented in Table 15.1, it is found that credit-deposit ratios of RRBs in most of the states are not encouraging. The all-India ratio stands at 41 per cent, with highest in Kerala (121 per cent) and lowest in Jammu & Kashmir (17 per cent). The non-performing assets is still large i.e. 18 per cent at all-India level, with as high as 64 per cent in Tripura and at the lower end, 5 per

cent in Kerala. Credit recovery seems to be the main problem area for the RRBs. By the end of June 2000 the all-India figure of recovery for RRBs is 69 per cent, with highest in Kerala (90 per cent) and lowest in Tripura (18 per cent). The employees' productivity is highest in Punjab i.e. Rs.110 lakhs per employee and lowest in Manipur i.e. Rs. 30 lakhs. Similarly, the highest productivity per branch is found to be Rs. 602 lakhs for the state Tripura, and lowest of Rs. 85 lakhs in Nagaland. The all-India average of per employee productivity and per branch productivity is Rs. 77 lakhs and Rs. 378 lakhs respectively.

The interesting observation made from this table is that although Tripura is placed on the higher side of parameters of employee's productivity and branch productivity, the overall positions of RRBs in this state are very grim. They are incurring losses, carrying proportionately large amount of accumulated loss, their CD ratio is only 30 per cent, the NPA is highest at 64 per cent and they have a very dismal credit recovery rate i.e. only 18 per cent. Doing business does not mean only extending credit and accepting deposits. The most important part of total business is to make good credit recovery and maintaining lower NPA. Similar type of situation is also found in many states. Thus the overall performance of RRBs in India is reflected in quantitative figures only, quality has been the casualty in almost all the states. In the year 2001, net loss figures are found in the states like Manipur, Orissa and Tripura. Out of 196 RRBs, 172 RRBs have earned profit during the year 2000-01 as against 162 banks in 1999-00 (NABARD,2000-01). RRBs with no accumulated losses were high in the case of Punjab (4 out of 6), Andhra Pradesh (12 out of 16) and Karnatak (8 out of 13). Simultaneously, the loss-incurring RRBs vis-à-vis the total number of RRBs was particularly high in the case of Orissa (4 out of 6), Madhya Pradesh (6 out of 24) and Bihar (5 out of 22) (*ibid.*). Out of 23 states the RRBs of only three states have no accumulated losses behind them.

In total by the end of March 2001, 11 RRBs are operating in north-east region with 651 branches and 3252 employees. Out of 11 RRBs, Assam has 5 RRBs and all others have one each. Among all the states of this region obviously Assam has largest deposits and loans outstanding, followed by Tripura and Meghalaya. Out of seven states, RRBs in 5 states are earning profit except in Tripura and Manipur where they are earning losses. These states are carrying around 10 per cent of the total accumulated losses of all the states

in India. Out of Rs. 268.74 lakhs accumulated losses, Tripura alone carries more than 50 per cent. Among the NE states besides Arunachal Pradesh, the CD ratio of all other states is very poor. The overall CD ratio is only 30 per cent in comparison to all India figures of 41 per cent. The NPA level continues to be very grim, i.e. at 46.6 per cent for all the states in this region.

Tripura is having highest NPA of 64 per cent and Arunachal Pradesh has the lowest at 19 per cent. The credit recovery is also very poor in all the states. Among all the states the RRBs of NE region show a dismal performance. Thus the indicators portray that

Table 15.1 : Selected Indicators of RRBs in India as on 31st March 2000-01

Sl. No.	States	No. of RRBs	No. of Branches	CD Ratio	Recovery as on 31.3.00 (%)	NPA (%)	Accumulated Losses Rs. Lakh	Profit/Loss Rs. Lakh	Per Employee Productivity Rs. lakh	Per Branch Productivity Rs. lakh
1	Arunachal Pradesh	1	19	107	38	19	68	33	99	338
2	Assam	5	401	27	38	33	11029	347	58	386
3	Manipur	1	29	38	35	46	1093	-32	30	109
4	Meghalaya	1	51	25	43	45	0	319	84	300
5	Mizoram	1	58	34	54	35	600	42	51	169
6	Nagaland	1	85	28	28	42	144	9	24	85
7	Tripura	1	85	30	18	64	13940	-819	72	602
8	North-East Region	11	651	30	-	46.6	26874	-101	62	308
9	Andhra Pradesh	16	1101	66	73	11	5492	7096	89	465
10	Bihar	22	1869	23	50	32	57862	3888	72	307
11	Gujurat	9	388	49	77	15	3110	2114	92	388
12	Haryana	4	192	50	79	11	2866	3104	97	530
13	Himachal Pradesh	2	130	25	76	6	0	664	107	485
14	Jammu & Kashmir	3	262	17	42	21	7937	172	61	282
15	Karnatak	13	1093	81	77	11	2485	7479	76	404
16	Kerala	2	325	121	90	5	0	3260	68	545
17	Madhya Pradesh	24	1496	32	62	21	42889	2048	72	304
18	Maharashtra	10	581	49	66	21	11421	1310	68	291
19	Orissa	9	823	51	66	19	39542	-1108	65	336
20	Punjab	5	202	38	85	9	405	2327	110	414
21	Rajasthan	14	1025	41	72	13	23671	1533	75	323
22	Tamil Nadu	3	212	84	84	6	1776	918	77	393
23	Uttar Pradesh	40	2995	31	60	27	24313	24640	85	429
24	West Bengal	9	871	32	47	28	29661	1565	72	433
25	All India	196	14311	41	69	18	280303	60906	77	378

Source: Compiled from Key Statistics for RRBs, NABARD, 2000-01.

there has been tremendous progress in quantitative terms but quality has suffered, progress has been halting and significant regional disparities persist (Shivamaggi, 2000).

A Case Study on Subansiri Gaonlia Bank (SGB)

Performance indicators of Subansiri Gaonlia Bank (SGB), have been presented for a period of ten years, i.e. from 1991-92 to 2000-01, for the purpose of a microanalysis of the problem of RRBs. SGB is one of the five RRBs of Assam. It was established on 30th March 1982 under the Section 3(i) of the RRB Act, 1976. This bank covers four districts of Assam, namely, North Lakhimpur, Dhemaji, Dibrugarh and Tinsukia. The Headquarters of the bank is located at North-Lakhimpur. The bank covers 4620 Revenue villages falling in 23 Development Blocks of the 8 Sub-divisions. The districts North Lakhimpur and Dhemaji lie towards the North while the other two lie towards the South bank of river Brahmaputra. Out of the total 45 branches spread across the four districts, North Lakhimpur has 16 branches followed by Dibrugarh 12 branches, Dhemaji 9 branches and Tinsukia 8 branches. All branches of Dhemaji district and 7 branches of North Lakhimpur district are in flood prone areas. The economy of these four districts is based on agriculture and allied activities. Dibrugarh and Tinsukia are comparatively better off districts than the other two because of their extensive tea cultivation. Over the years other activities like business, industry and services have

Table 15.2 : Selected Indicators of SGB (1991-92- 2000-01)

Year	Deposits Rs. Lakh	Loan Rs. Lakh	C/D Ratio %	NPA %	Recovery %	Profit Rs. Lakh	Accumulated loss Rs. lakh	Profit as % of working Fund
1991-92	1128.38	714.68	63.63	-	-	-69.99	231	-4.63
1992-93	1226.72	841.03	68.56	-	22.92	-85.11	337	-5.39
1993-94	1763.30	928.83	52.68	-	18.44	-106.46	512	-5.00
1994-95	2486.58	1019.72	41.00	-	12.33	-119.06	674	-4.31
1995-96	2936.00	1075.23	36.62	-	6.59	-161.26	928	-5.16
1996-97	3245.63	1140.43	35.13	71.04	17.98	-13.81	1430	-0.41
1997-98	4467.50	1105.93	24.76	64.43	18.45	65.09	1365	1.42
1998-99	6006.12	1244.30	20.72	52.88	16.31	176.98	1188	2.88
1999-00	7374.20	1360.00	18.44	39.383	36.30	74.08	1114	0.99
2000-01	7804.14	1623.95	20.81	31.91	-	119.64	1026	1.47
Average	3843.85	1105.41	28.69	52.02	18.66	-11.99	880.50	-0.29
Growth Rate	25.66	7.88	-14.30	-18.80	19.44	10.02	18.89	-

Source : Compiled from Annual Reports of SGB.

been picking up in these four districts (Pati, 2002).

A cursory look at the indicators of SGB presented in Table 15.2 suggests that the bank has not been able to provide more credit to the rural people. During the last decade the deposits has grown at a rate of more than 25 per cent against which the loan amount has shown only 8 per cent growth rate. The deposit outstanding is proportionately very high in comparison to loan outstanding. As a result the C/D ratio has fallen sharply from 63.6 per cent in 1991-92 to merely 20.8 per cent in 2000-01. The NPA although has decreased over the years is still at alarming proportion. Recovery for SGB is miserably poor. While at all India level it is at 69 per cent for the year 1999-00, for SGB it is only at 36 per cent. Thus, obviously the profit is affected. Only for the last 4 years the bank has been able to earn some profit. In the books of accounts there is still a huge accumulated loss which needs to be recovered.

SGB as a rural bank operates mostly in rural areas and rural sectors mainly fall under priority sector. Thus the loan portfolio of the bank is obviously dominated by priority sector loans. From the Table 15.3 it is evident that over the years the share of priority sector has come down from more than 90 per cent to the RBI prescribed

Table 15.3 : Trend of loan to Priority sector and other sector

Year	Loan to Priority Sector Rs. lakhs	Loan to other Sector Rs. lakhs	Total Loan Rs. lakhs	% of Priority Sector Loan To Total Loan	% of Other Sector Loan to Total Loan
1991-92	651.94	62.74	714.68	91.22	8.78
1992-93	763.46	77.57	841.03	90.78	9.22
1993-94	839.96	88.87	928.83	90.43	9.57
1994-95	902.22	117.50	1019.72	88.48	11.52
1995-96	916.24	158.99	1075.23	85.21	14.79
1996-97	889.03	251.40	1140.43	77.96	22.04
1997-98	813.47	292.46	1105.93	73.56	26.44
1998-99	787.49	456.81	1244.30	63.29	36.71
1999-00	708.63	651.37	1360.00	52.11	47.89
2000-01	723.07	900.88	1623.95	44.53	55.47
Average	799.55	305.86	1105.41	72.33	27.67
CV	11.14	92.13	23.67		
Growth Rate	-0.15	35.60	7.88		

Source : SGB Annual Reports from 1991-92 to 2000-01.

limit of 40 per cent i.e. in 2000-01 the share is only 44 per cent. The declining share of such loan indicates that the bank is now channelising its resources to other profitable sectors where return is assured or comparatively more.

In the priority sector, agriculture or farm sector commands the largest share. It is experienced in Indian context that the recovery from farm sector has always been poor. From the sector-wise recovery figures presented in Table 15.4 it is revealed that the

Table 15.4 : Recovery position in Farm and Non- Farm sector

Year	Farm sector				Non-Farm sector			
	Demand Rs. Lakhs	Reco- very Rs. Lakhs	Over- due Rs. Lakhs	Reco- very %	Demand Rs. Lakhs	Reco- very Rs. Lakhs	Over- due Rs. Lakhs	Reco- very %
1995-96	420.63	62.54	358.04	15	336.40	74.22	262.18	22
1996-97	415.62	53.76	361.86	13	406.64	97.92	308.77	24
1997-98	NA	NA	NA	NA	NA	NA	NA	NA
1998-99	416.48	39.95	376.53	9.6	335.58	82.70	252.88	24.6
1999-00	414.22	108.92	305.3	26.3	383.84	180.79	203.05	47.1

Source : SGB Annual Reports.

recovery rate in non-farm sector is more than the recovery rate of farm sector. It is because of the fact that most of the borrowers in farm sector are small and marginal rural farmers and recovery from them has been a constant problem due to various reasons. Further, the operational area of SGB is flood prone, which also explains the situation to some extent. But the overall recovery performance is far from satisfactory.

Recently the quality of assets in Indian banking system has been considered as the main roadblock in the process of financial sector reform. This has become one of the principal reasons of the poor international credit rating of our economic system. This has in turn has been affecting the international capital flow to our country. The large volume of NPA in various scheduled commercial banks in the country indicates that RRBs being a part of the system is not solely responsible for this menace. So far as the SGB is concerned the quality of assets has shown a marked improvement. But the growth of doubtful assets, which is around 37 per cent, is sending a wrong signal to the bank managers. This is a clear indication of the fact that the quality of assets of the bank is very poor and which has been affecting the profitability of the SGB. The poor state of loan assets is a product of bad recovery management.

The Problem Areas and Strategies to Tackle Them

Branch Networking

Despite of 26 years of presence, RRBs have been able to establish just over 12000 branches in rural areas. But other public sector commercial banks although are not specifically meant for rural areas have more than 19000 branches in rural areas. Further in many areas branches of both RRBs and of public sector bank are operating. Since the later enjoys a greater public confidence, the business of the former gets a setback. It is evident from the share of the outstanding rural credit. Public sector banks have extended nearly 50 per cent of total rural credit, where as RRBs only have just over 8 per cent. It is also found that the branches of the sponsor bank of the same RRB are also functioning in one area. Thus the clash in operational areas of both the branches has proved detrimental to the business of the RRBs.

To tackle the above mis-match in branch location consolidation of two or more weak branches of a RRB can be tried. In other cases re-location of branches to a better place can also be resorted to.

Branch Autonomy

Operational autonomy in credit decision-making and in matters of internal organisation and management is one of the critical elements of the reform. Thus devolution of power to branch managers is a must. They should get enough power to decide about the loan application and about the re-schedulement of the installments as and when necessary. This will help in reduction of NPA through improved recovery. Devolution of power will also facilitate realistic target setting for busy season and lean season.

Table 15.5 : Asset Quality of SGB

(Rs. in Lakhs.)

Sl. No.	Category	1996-97	1997-98	1998-99	1999-00	2000-01	Average	Growth (%)
1.	Standard	329.86	393.43	586.34	818.33	1105.67	646.73	37.05
2.	Sub-standard	44.53	45.92	47.59	59.20	58.40	51.13	8.29
3.	Doubtful	84.84	69.84	133.20	182.17	253.21	144.65	36.97
4.	Loss	681.20	596.75	477.17	300.31	206.67	452.42	-26.45
5.	Total	1140.43	1105.94	1244.30	1360.01	1623.95	1294.93	9.57
	1 as % to 5	28.92	35.57	47.12	60.17	68.09	47.98	25.08
	(2+3+4) as % to 5	71.08	64.43	52.88	39.83	31.91	52.02	-18.80

Source : SGB Annual Reports from 1996-97 to 2000-01.

Operating Cost

It is observed that the high ratio of operating expenditure to other expenditure has affected the profitability of RRBs. This has been more than 40 per cent for most of the RRBs. Salary and other allowances to staff members and maintenance of office constitute the largest chunk of this expenditure.

In this regard operational target could be fixed with the help of zero-based budgeting. Further, automation of operation at branch level could also help in containing the office expenditure to a large extent.

Loan Recovery and NPA Management

No need to mention here that recovery of loan in Indian banking sector has been a constant problem. Despite of several policy measures and prescriptions initiated by GOI and RBI, the recovery remains grim as it was during pre-liberalized era. It was a general feeling that after liberalization things will improve. Perhaps during this reform era borrowers have learned many innovative ways of playing safe with bank borrowings. Several financial institutions are today trying hard to recover their dues. The blockage of more than Rs. 50000 crore of commercial bank's credit in the banking system is a testimony of the inefficient credit management. In addition to the weakness of the banking system, the apathetic and non-supportive judiciary system has also aggravating the problem.

Many new businesses are being floated during this liberalization phase. Simultaneously big uncertainties of market have also marred their future. Thus despite of improved performance in many sectors of the economy the poor recovery syndrome still persists. The problem has become more acute with the rural credit and more particularly for RRBs, since most of their business flows from rural sectors. The overall recovery position in all the states is only 69 per cent and less than 40 per cent in NE states and further goes down to 19 per cent for SGB.

Any strategy for good recovery should be considered taking into account the efficiency of loan appraisal and credit delivery system. To begin with the loan appraisal system, proper training to at least one staff per branch is highly essential and the branch manager should have enough power to decide about the loan application.

For credit delivery, voluntary agencies like NGOs, SHOs etc. could provide a yeoman service. The experience of India and in other countries, where voluntary agencies have provided such service,

shows that where these agencies have been able to provide assistance to borrowers, disbursements are much faster and by timely disbursements it is possible to also ensure effective loan recoveries (Tarrapore, *op.cit.*). Among other techniques, profit sharing by the employees of the rural financing institutions and social cohesiveness in rural lending with peer group pressure to bring about a total aversion to loan defaults could also be tried in different situations. Organizing loan recovery camps with the associations of Gram Panchayat of village development councils/committees could also bring some positive result in this direction.

As an offshoot of bad recovery, the presence of huge NPA and their management has been the biggest headache of Indian banking system. So far as the RRBs are concerned the occurrence of NPA is more likely because of their large exposure to priority sector lending, which is dominated by small and marginal borrowers in agriculture and allied sectors. To arrest further contamination of loan portfolio, the SGB has reduced its exposure to priority sector to a great extent. It is also observed from the last ten years figures that the bank has invested more amount in various securities and extended less and less loan to borrowers. Thus the basic purpose of the bank as a catalyst of the rural development has been defeated.

Over more than a decade the problem of NPA and the means to tackle it has been discussed at length. But the menace of NPA has been spreading like wild fire and the entire financial sector is sick of it. As per the estimate of the consultancy firm Ernest & Young, the NPAs of Indian banks and financial institutions stand at \$25 billion (about Rs. 1.23 lakh crores) against the RBI estimate of \$16.7 billion in its last annual report. Out of this huge amount Indian public sector banks alone accounts for Rs. 54773 crore as on 31st March 2001. As a constituent of the overall system the RRBs in India accounts for Rs. 2800 crore, which is 18 per cent of their total loan outstanding. When it comes to the RRBs in North-east region the NPA figure stands at 46.6 per cent of total outstanding loan portfolio and for Subansiri Gaonlia Bank (SGB) it is at 32 per cent.

To tackle the growing menace of NPA in Indian financial sector, in recent years serious attempts have been made. Among them the establishment of Debt Recovery Tribunals (DRTs), tightening of provisioning norms for various categories of assets etc. are prominent. But the recent Securitisation and Reconstruction of Financial Assets and Enforcement of Security Interest Ordinance, 2002 promulgated on June 21, 2002 has given wide authority to

banks to deal with NPA. Now they can change or take over the management, they can sell or lease out the business of the borrower; they can take possession of all the secured assets; and they can also reschedule the payment of debt by the borrowers. Besides, the ordinance has the provision of establishing Assets Reconstruction Company (ARC) to take over the contaminated portfolio of banks at a discount and thus help in cleaning-up their balance sheets. The ARC option is however, will not into the rescue of RRBs because of the prevalence of small amount loan in their portfolio. The local initiatives are like collaboration with village bodies and micro financing through Self Help Groups (SHOs) could yield better results for these rural financing institutions.

Conclusion

The wind of liberalization has transformed the Indian banking sector into a new high. It has unleashed many opportunities for the banks and also simultaneously posed serious challenges to their survival. The viability of banks are growingly depending upon the ability to cope-up with the challenges by providing optimum customer satisfaction through just-in time solutions, by containing operating expenses and improving the quality of portfolios. As rural financing institutions, RRBs's viability has also been under constant pressure. The responsibility of catering to the need of rural masses and at the same time competing with other commercial banks, have put them in a piquant situation. The poor recovery of rural loans and growing operating expenditure are the main stumbling blocks for their growth in profitability. Every effort has to be made by RRBs to improve their portfolio quality and to arrest further slippage of assets to NPAs. The ability of RRBs to manage the transition to a technology-oriented and customer-driven entity will shape their future performance.

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