REGIONAL RURAL BANKS

The need for evolving a hybrid type of credit agency which combines the resource orientation of the commercial banks and the rural orientation of the co-operatives has been expressed in the reports of a few of the committees which have looked into rural credit problems.

To review the flow of institutional credit especially to the weaker sections of the rural community, the Government of India appointed a Working Group in 1975 under the chairmanship of Narasimhan. The Group identified certain deficiencies in the functioning of co-operatives and commercial banks and recommended the setting up of state-sponsored, regionally based and rural oriented banks called Regional Rural Banks (RRBs) which would encompass local feel and familiarity with several problems which the co-operatives possess and the degree of business organization, ability to mobilize the deposits, access to central money markets and a modernized outlook which the commercial banks have. The Government of India accepted this recommendation and RRBs were established in 1976.

The main objective of RRB is to provide finance to small and marginal farmers, agricultural labourers, artisans and small entrepreneurs whose annual income is less than Rs.10,000.

Features

The idea behind the establishment of RRBs is to develop a comparatively backward area where the commercial bank and co-operative is relatively poor. The main difference from the commercial bank is that the area of operation of RRB is confined to a region comprising one or two contiguous districts. One of the tasks envisaged for the RRBs is to maintain their cost of operations at a lower level than that of the commercial banks. So the salary structures of the staff were comparable to that of the State government employees.

RRBs are sponsored by schedule commercial banks. A few non-public sector commercial banks and state co-operative Banks are also allowed to sponsor RRBs. The sponsoring bank provides managerial assistance to RRBs for the first five years. The management of RRB is through a nine member Board of Directors headed by a chairman who is an officer of the sponsor bank. The Board consists of three nominees of Government of India, two nominees of the concerned State government, four including the chairman by the sponsor commercial bank.

The authorized share capital of a RRB has been fixed at Rs.5 crore and issued capital is Rs. one crore. Of this, 50 per cent is subscribed by the central government, 15 per cent by the concerned state government and 35 per cent by the sponsor bank.

Progress of RRBs in India

S. No.	Particulars	1976	1980	1990	2000	2009
1.	Number of RRBs	40	85	196	196	86
2.	Number of branches	489	3,279	14,444	14,301	15,199
3.	Deposits (Rs.in crores)	7.72	199.83	4,150.52	32,204	1,17,984
4.	Advances (Rs.in crores)	7.02	243.38	3,554.04	13,184	69,030
5.	Number of loss making banks	23	60	NA.	34	6

Purpose-wise Break up of RRB advances

(Amount Rs. in crores)

Sl.No.	Purpose	1990		2009	
		Amount	Per cent	Amount	Per cent
1.	Short term (crop loan)	615	17.3	24,986	36.2
2.	Term loans for agriculture	669	18.8	11,480	16.6
3.	Advances to activities allied to agriculture	555	15.6		0.0
4.	Indirect Advances	43	1.2	-	0.0
4.	Rural artisans, village and cottage industries	277	7.8	2220	3.2
5.	Retail trade and self employment	1052	29.6	5,015	7.3
6.	Consumption loans/other purposes	344	9.7	25,329	36.7
	Total	3555	100.0	69,030	100.0

Source: Report on Trend and progress of Banking in India, 1990-91 and 2008-09.

Performance

As scheduled banks, they mobilize deposits and they have been allowed to offer slightly higher rate of interest, i.e., 0.5 per cent per annum, on their deposits upto five years. RRBs have been advised to render other banking services like collection of cheques and bills, issue of drafts, collection of'-insurance premia, safe custody etc. About 60 per cent of the total advances made by RRBs were claimed by agriculture and allied activities.

The Committee set up by the RBI in 1977 under the chairmanship of M.L.Dantwala to review the working of the RRBs recommended that RRBs should be extended to such areas where DCCBs are not able to adequately serve the PACS under their jurisdiction. The CRAFICARD (1981) recommended that the RBI may transfer the business of commercial banks rural branches to RRBS when such proposals are presented.

The Kalyanasundaram committee (1986) was appointed to study the wage structure and service conditions of the RRB staff.

The Agricultural credit Review committee (ACRC) headed by Prof. Khusro in 1989 recommended that the RRBs and their branches can be merged with their sponsor banks due to the following reasons:

a) The performance of commercial banks in rural lending in terms of branch expansion and recruiting technically qualified staff for rural branches is better than RRBs.

b) The accumulated loss and over dues of RRB were very heavy.

However, the Government of India has decided not to merge the RRBs with sponsor banks.Instead, the government has decided to implement the recommendations of the Kelkar committee (1986) in- a bid to revive these banks.

The steps proposed for strengthening the RRBs include:

i) Enhancing their authorized capital from Rs.1 crore to Rs.5 crores and the issue (paid-up share capital from Rs.25 lakhs to 1 crore)
ii) Reducing the interest rates from 8.5 per cent to 7 per cent on the refinance loans provided by the sponsor banks, and
iii) Channelising their surplus funds into more profitable investments, such as the government securities.

Problems

i) There is a lack of managerial efficiency due to larger area of operation. Some RRB cover 10-15 lakh population

ii) Lack of uniform guidelines for recruitment and promotion.

iii) The number of loss making banks in 1976 was 23 and it rose to 149 in 1988 but declined to 6 in 2009. The accumulated loss of RRB was Rs.550 crores (1991) which was more than their entire paid up capital and reserves. However, the loss declined to Rs.36 crorein 2008-09.

iv) Lack of both the .expertise of commercial banks and local feel of the co-operatives.

v) RRBs could not meet the credit needs of non-farm sector effectively.

Factors influencing the performance of RRBs

Since their inception, the financial health of RRBs has been indifferent. A host of factors, both internal and external, has had a bearing on the performance of RRBs. Some of the major factors that had a bearing on the performance of RRBs are as follows:

i) Area of operation: The RRBs are constrained in their operations by their limited area of operation. This coupled with their narrow base of business activities and the low clientele base, has resulted in high risk exposure of RRBs.

ii) Clientele base: The customers of RRBs comprise small and marginal farmers, small scale sector, small transport operators, SHGs, etc., whose credit requirements are mostly small. RRBs are unable to cross-subsidize their lending business as they do not generally provide credit to wealthy borrowers with large needs, thereby affecting their capacity to earn higher incomes.

iii) Capital base: RRBs as a group have a low capital base, and their authorized capital of Rs.1 crore places serious limitations on their business size. Furthermore, in the case of some of the RRBs their deposit liabilities are very large compared to their capital base. For instance, as as on March 31, 2004 while 2 RRBs had deposit liabilities of over Rs 1,000 crore, 24 RRBs had a deposit base ranging between Rs.500 to Rs.1,000 crore, and 146 RRBs had deposit liabilities between Rs.100 to Rs.500 crore. In view of their low capital base, in the event of inefficient use/misuse of funds resulting in a financial problem, the stakeholders would have to bail out the bank.

iv) Organizational structure: The size of financial assets, as well as linkages which are necessary for effective banking services has been limited by the small organizational structure of RRBs. This has also come in the way of growth in business volumes and garnering a larger share of the rural financial market.

v) Loan delinquencies: RRBs loan recovery rates have declined over the years, resulting in a large over hang of NPAs (around Rs.3,200 crore) which has come in their way of recycling funds and increasing the flow of credit to the rural sector. The directed lending policy for RRBs has resulted in low quality of assets. This coupled with high cost of funds and below cost interest rates on loans has led to high accumulated losses and piling up of bad assets in the case of many RRBs.

vi) Cost structure: RRBs are characterized by high cost of servicing numerous small accounts and high wage cost. Furthermore, RRBs get credit from sponsor banks and refinance from NABARD at rates of interest higher than the market rates. This places limitations on their ability to reduce the rates they charge to their ultimate borrowers, although they are compelled to do so on account of competition from banks.

vii) Perceived as specialized bank: There has been an uneven growth of RRBs due to the diffusion in the perceived objectives of RRBs over time. Despite the pressures of credit expansion, improvement in recovery performance, profit orientation and strict compliances to banking norms, the general perception has been that RRBs have got only social objectives, without any viability consideration, which has to be changed.

viii) Financial management skills: Poor financial management skills, coupled with pressures from various quarters (like sponsor banks) appears to have resulted in inefficient allocation of resources by RRBs which in turn is reflected in the high incidence of NPAs and parking of large funds with sponsor banks (policy changed in 2002-03) .

ix) Staff structure: Limited exposure and lack of appropriate training, has resulted in RRBs staff lacking the necessary skills and capacity to cater to the changing requirements of the rural sector. Furthermore, the ban on recruitment has also resulted in ageing staff structure constraining efficiency in operations. Uniform norms and personnel policies have been applied to RRBs through out the country ignoring local touch thereby causing staff unrest, poor industrial relations, innumerable litigations and lowering of staff morale as also their involvement with the development tasks (Rao Committee, 2002).

x) Dependence on sponsor banks: Another weakness observed in the case of RRBs is their failure to adequately integrate with the financial markets of the country due to their heavy dependence on sponsor banks for financial/ business initiatives. RRBs are also some times perceived as potential competitors, due to the presence of the sponsor banks in the same area of operation. Despite the best intentions at the policy levels in sponsor banks, the RRBs have suffered at the ground level wherever there has been any conflict of business interests of RRBs and their sponsor banks. RRBs have therefore, not been able to establish systems and procedures required for providing efficient services to their clients, as also for efficient management of their financial resources.

xi) Professionalism in management: The Chairmen of most of the RRBs are from sponsor banks, which limits the freedom and decision making capacity of the RRBs. Even for small matters RRBs have to refer to their sponsor banks, which lead to delay in decision-making and reduce efficiency. Furthermore, the Board of Directors of RRBs may not always function effectively as some of the members do not have necessary skills and expertise to take important financial decisions.

xii) Erosion of deposits: In the case of few RRBs, there has also been an erosion of public deposits, besides capital.