PERFORMANCE EVALUATION OF REGIONAL RURAL BANKS IN INDIA

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ABSTRACT

Regional rural Banks plays a vital role in the agriculture and rural development of India. The RRBS have more reached to the rural area of India, through their huge network. The success of rural credit in India is largely depends on their financial strength. RRBs are key financing institution at the rural level which shoulders responsibility of meeting credit needs of different types of agriculture credit in rural areas. At present, most of the regional rural banks are facing the problems of overdue, recovery, nonperforming assets and other problems. Therefore, it is necessary to study financial performance of RRBs in India. This paper attempts to analyze the financial performance of RRBs in India during the period 2006-07 to 2010-2011. The study is based on secondary data collected form annual reports of NABARD and RBI. An analytical research design of Key Performance Indicators Analysis such as number of banks and branches, deposits, loans, loans, investments and growth rate index is followed in the present study. The study is diagnostic and exploratory in nature and makes use of secondary data. The study finds and concludes that performance of RRBs has significantly improved.

Keywords: Regional Rural Banks, Key Performance Indicators, Growth Rate, Rural Economy, NABARD**.**

INTRODUCTION

Regional Rural Banks have been in existence for around 36 years in the Indian financial scene. The institution of Regional Rural Banks (RRBs) was created to meet the excess demand for institutional credit in the rural areas, particularly among the economically and socially marginalized sections. The Banking Commission (1972) recommended establish an alternative institution for rural credit and ultimately Government of India established Regional Rural Banks as a separate institution basically for rural credit on the basis of the recommendations of the Working Group under the Chairmanship of M. Narashimham. In order to provide access to low-cost banking facilities to the poor, the Narashimham Working Group (1975) proposed the establishment of a new set of banks, as institutions which "combine the local feel and the familiarity with rural problems which the cooperatives possess and the degree of business organization, ability to mobilize deposits, access to central money markets and modernized outlook which the commercial banks have".

Subsequently, the Regional Rural Banks were setup through the promulgation of RRB Act of 1976. The RRBs Act, 1976 succinctly sums up this overall vision to sub-serve both the developmental and the redistributive objectives. The RRBs were established "with a view to developing 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 small and marginal farmers, agricultural labourers, artisans and small entrepreneurs, and for matters connected therewith and incidental thereto". Their equity is held by the Central Government, Concerned State Government and the Sponsor Bank in the proportion of 50:15:35 respectively. The mandates of these rural financial institutions were:

1. To take banking to the doorsteps of the rural masses, particularly in areas without banking facilities;
2. To make available cheaper institutional credit to the weaker sections of society, who were to be the only clients of these banks?
3. To mobilize rural savings and canalize them for supporting productive activities in the rural areas;
4. To generate employment opportunities in the rural areas
5. To bring down the cost of providing credit in rural areas

REVIEW OF LITERATURE

A number of studies have been conducted to see the functioning and performance of regional rural bank in the country. The literature available in the working and performance of RRBs in India is a little limited. The literature obtained by investigators in the form of reports of various committees, commissions and working groups established by the Union Government, NABARD and Reserve Bank of India, the research studies, articles of researchers, bank officials, economists and the comments of economic analysts and news is briefly reviewed in this part. Some of the related literatures of reviews are as follows.

The Kelkar Committee (1986) made comprehensive recommendations covering both the organizational and operational aspects. Several of these were incorporated as amendments to the RRB Act, 1976 such as:

1. Enhancement of authorized capital of RRBs from Rs 1 crore to Rs 5 crore and paid-up share capital from Rs 25 lakhs to Rs 1 crore;
2. Appointment of Chairman of RRBs by the concerned sponsor bank in consultation with NABARD;
3. provision of assistance to RRBs in greater measure by sponsor banks in training RRB staff and giving financial assistance to RRBs in their first five years of their existence;
4. Provision for amalgamation of RRBs in consultation with all the concerned parties.

5. Empowering the sponsor banks to monitor the progress of RRBs and also to arrange for their inspection, internal audit etc.

Though the progress of implementation was tardy (the amended act came into force only by end-September, 1988), there was enough scope for improvement thereon.

NABARD (1986) published "A study on RRBs viability", which was conducted by Agriculture Finance Corporation in 1986 on behalf of NABARD. The study revealed that viability of RRBs was essentially dependent upon the fund management strategy, margin between resources mobility and their deployment and on the control exercised on current and future costs with advances. The proportion of the establishment costs to total cost and expansion of branches were the critical factors, which affected their viability. The study further concluded that RRBs incurred losses due to defects in their systems as such, there was need to rectify these and make them viable. The main suggestions of the study included improvement in the infrastructure facilities and opening of branches by commercial banks in such areas where RRBs were already in function.

In the year 1989 for the first time, the conceptualization of the entire structure of Regional Rural Banks was challenged by the Agricultural Credit Review Committee (Khusro Committee), which argued that these banks have no justifiable cause for continuance and recommended their mergers with sponsor banks. The Committee was of the view that "the weaknesses of RRBs are endemic to the system and non-viability is built into it, and the only option was to merge the RRBs with the sponsor banks. The objective of serving the weaker sections effectively could be achieved only by self-sustaining credit institutions."

The Committee on Financial Systems, 1991 (Narasimham Committee) stressed the poor financial health of the RRBs to the exclusion of every other performance indicator. 172 of the 196 RRBs were recorded unprofitable with an aggregate loan recovery performance of 40.8 percent. (June 1993). The low equity base of these banks (paid up capital of Rs. 25 lakhs) didn't cover for the loan losses of most RRBs. In the case of a few RRBs, there had also been an erosion of public deposits, besides capital. In order to impart viability to the operations of RRBs, the Narasimham Committee suggested that the RRBs should be permitted to engage in all types of banking business and should not be forced to restrict their operations to the target groups, a proposal which was readily accepted. This recommendation marked a major turning point in the functioning of RRBs.

The contemporary literature on banking efficiency spells out two distinct approaches to measure efficiency (1) accounting measure (2) economic measure.

Accounting measure refers to the use of various financial ratios that focus on one or more outputs and their relevant inputs to measure the performance of a banking unit. The financial ratio approach has been widely used by the researchers and working groups/committees to analyze the performance of RRBs. Most of the studies on the performance evaluation of RRBs concentrated on the banks in particular state/region. Some of the studies are: Singh (1992) analyzed the performance of RRBs banks in Punjab. Prasad (2003) evaluated the performance of RRBs in India. Moreover, Pati (2005) developed the performance of RRBs in the north-east region. The study of Bagchi and Hadi (2006) concentrated on the performance of regional rural banks in West Bengal. Few studies also exist in the literature which concentrated on the efficiency of a single regional rural bank. Some of the studies conducted so far are: Sudhaker et al., (1984) evaluated the performance of Cauvery Grameen Bank in Mysore district; Parmar (1986) assessed the performance of Banaskantha Mehsane Grameen Bank in Gujarat; Sangwan (1988) analyzed the performance of Chattanja Grameen Bank in Andhra Pradesh; Jagadeesha et al., (1990) evaluated the performance of Tungabhadra Garmeen Bank in Karnataka. Further, Hosamani (2002) explored the performance of Malaprabha Garmeen Bank in Karnataka and Yadappanvar and Nath (2003) assessed the performance of Aurangabad and Jalna Grameen Bank in Maharashtra. Though financial accounting ratios are simple to use and relatively easy to understand, but their use to measure bank performance is plagued by various problems. As a precautionary measure, regulatory frame works (such as CAMEL rating) based on these ratios has been put in place in most of the supervisory systems across the globe. Further, Sherman and Gold (1985) noted that financial ratios do not capture the long-term performance. This measure also helps in the analysis of bank's performance in terms of individual parameters determining the overall efficiency level as it is difficult to precisely measure the efficiency of banks.

Therefore, in recent years, there is a trend towards measuring bank performance using economic measure. This measure provides accurate, composite and precise estimate of efficiency of banks comparing each bank against the top performers in the banking industry. A scan of the existing literature on the efficiency of Indian banks provides that there exists various studies that analyzed the efficiency of Indian commercial banks using most popularly used parametric technique of Stochastic Frontier Analysis (SFA) and non-parametric technique of Data Envelopment Analysis. The notable studies belonging to this group are: Noulas and Ketkar (1996), Bhattacharyya et al., (1997), Das (1997), Saha and Ravisankar (2000), Mukherjee et al., (2002), Kumar and Verma (2003), De Kumar (2004), Chakrabarti and Chawla (2005), Kaur and Sharma (2005-06), Kumar and Gulati (2008), etc. To the author's knowledge, there is virtually no study except Reddy (2005), Khankhoje (2008), Sathye (2008) and Mohindra (2011) which analyzed the performance of RRBs by using Frontier and Data Envelopment Analysis approach respectively.

OBJECTIVES OF THE STUDY

1. To measure financial performance of Regional Rural banks in India.
2. To analyze the key performance indicators of RRBs in India
3. To evaluate progress of the RRBs during 2006-07 to 2010-11.
4. To study the growth-pattern of Regional Rural Banks in India.
5. To make important suggestions to improve the working of RRBs.

HYPOTHSIS OF THE STUDY

1. The RRBs in India have made a substantial quantitative progress.
2. The qualitative progresses of RRBs have been found to be highly impressive.
3. The macro performance is highly substantial.

PROBLEMS OF THE STUDY

1. First and important problem of the research work is analysis of financial data.
2. Information from NABARD and RBI was difficult to be obtained.

SIGNIFICANCE/ IMPORTANCE OF THE STUDY

The research study is significant to evaluate financial performance of RRBs in India. The results/ findings of the present study are useful to the policy planners in their efforts to improve the working of the RRBs in India.

SCOPE AND COVERAGE OF THE STUDY

1. It covers all RRBs working in India.
2. The study covers a specific period from 2006-07 to 2010-11 i.e. after globalization and amalgamation.
3. There is macro evaluation of performance of all the RRBs in India.

Area of the Study

The study is based on the performance of RRBs in India. Therefore, study covers all RRBs in India to the fulfillment of objectives of the study.

Period of the Study

For collection of the secondary data on financial performance of the RRBs in India, five years i.e. from 2006-2007 to 2010-2011 were taken as the reference period. The accounting year of the bank commences on 1st April of every year and ends on 31st March of next year.

RESEARCH METHODOLOGY

The financial performance of the RRBs in India has been analyzed with the help of key performance indicators. The year 2010-2011 was taken as the current year and year 2009-2010 was base year for the calculation of growth rate. Analytical Techniques Employed-Growth rate analysis was undertaken with a view to studying financial performance related to the RRBs. Growth rate is measured with the help of following formula-

Growth Rate = Yt -Yt-1 / Yt-1

Yt= Current Year, yt-1=Base Year.

RESEARCH DESIGN

The present study is diagnostic and exploratory in nature and makes use of secondary data. The study is confined only to the specific areas like number of branches, district coverage, deposits mobilized, credits and investments made by the Indian Regional Rural Banks (RRBs) for the 5 years period starting from 2006-07 to the year 2010-11.

METHOD OF DATA COLLECTION

The present study is empirical in character based on the analytical method. The study is mainly based on secondary data which is collected, compiled and calculated mainly from annual reports of the NABARD and RBI. Other related information collected from journals, conference proceedings and websites.

Key Performance Indicators and Growth of RRBs

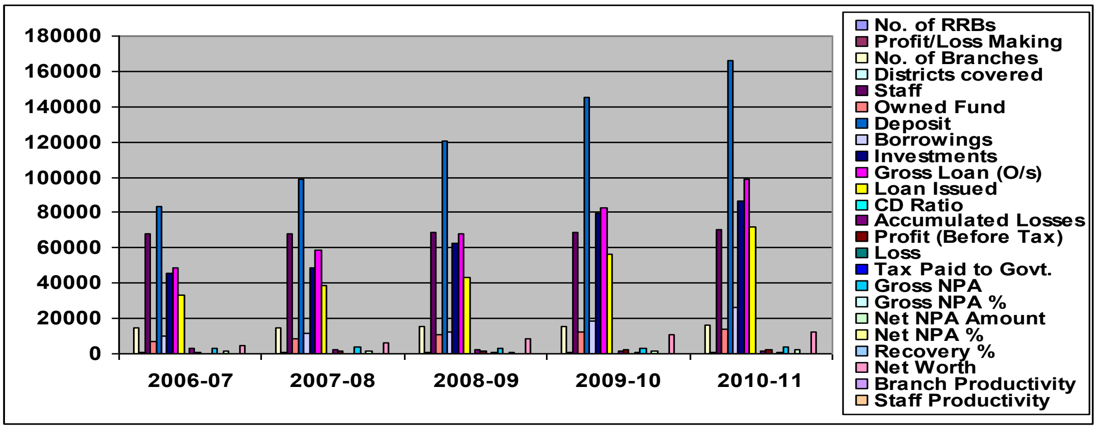
Table 1 presents the key performance indicators and growth of RRBs from year 2006-07 to 2010-2011, **Graph 1** presents key performance indicators and **Graph 2** presents growth rate of RRBs.

Table 1. Key Performance Indicators of RRBs in India

(Figures: - Rs. in Crore)

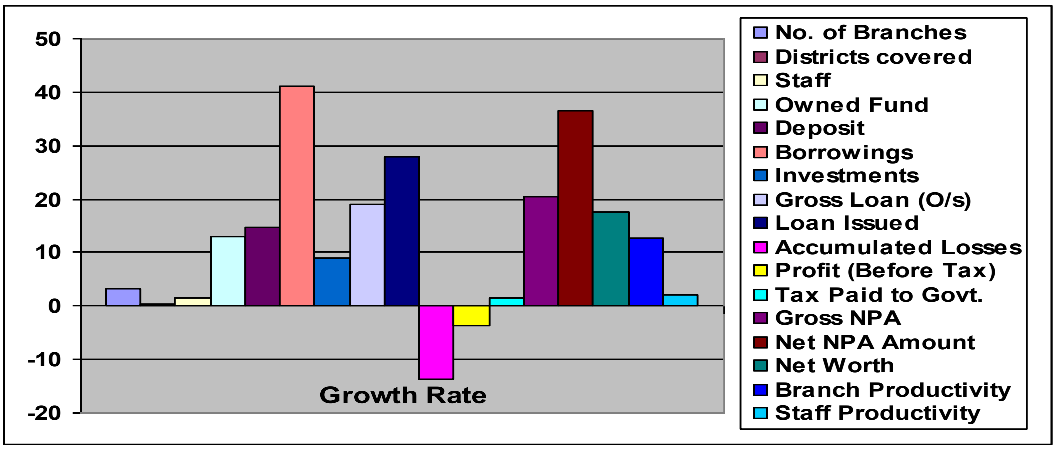
Parameters	**2006-07**	**2007-08**	**2008-09**	**2009-10**	**2010-11**	**Growth**
No. of RRBs	96	91	86	82	82	---
Profit/Loss Making	81/15	83/8	80/6	79/3	75/7	---
No. of Branches	14526	14761	15158	15480	16001	3.36
Districts covered	534	594	617	618	620	0.32
Staff	68289	68005	68509	69042	70153	1.61
Owned Fund	7285.98	8732.59	10895.73	12247.16	13838.92	13.00
Deposit	83143.55	99093.46	120184.46	145035.00	166232.34	14.60
Borrowings	9775.80	11494.00	12733.80	18770.00	26490.81	41.10
Investments	45666.14	48559.54	62629.45	79379.16	86510.44	8.98
Gross Loan (O/s)	48492.59	58984.27	67858.48	82819.10	98917.43	19.14
Loan Issued	33043.49	38581.97	43445.59	56079.24	71724.19	27.90
CD Ratio	58.32	59.52	56.46	57.10	59.51	---
Accumulated Losses	2759.49	2624.22	2325.59	1775.06	1532.39	- 13.67
Profit (Before Tax)	926.40	1383.68	1859.36	2514.83	2420.75	- 3.74
Loss	301.25	55.58	35.91	5.65	71.32	1162.30
Tax Paid to Govt.	139.66	301.12	461.14	625.25	634.22	1.44
Gross NPA	3178.01	3566.34	2804.02	3084.82	3712.00	20.32
Gross NPA %	6.55	6.05	4.13	3.72	3.75	---
Net NPA Amount	1625.41	1929.71	1114.54	1423.31	1941.32	36.39
Net NPA %	3.46	3.19	1.68	1.80	2.05	---
Recovery %	79.80	80.84	77.76	80.09	81.18	---
Net Worth	4526.48	6107.37	8570.04	10472.10	12306.53	17.52
Branch Productivity	9.06	10.75	12.41	14.72	16.57	12.57
Staff Productivity	1.93	2.33	2.74	3.70	3.78	2.16

Source: Reports of NABARD and RBI



Source: Reports of NABARD and RBI.

Graph 1. Key Performance Indicators of RRBs in India



Source: Compiled from Reports of NABARD and RBI.

Graph 2. Growth Rate of RRBs in India

SUMMERY/ OBSERVATION OF THE STUDY (FINDINGS)

Sources of Funds

The sources of funds of RRBs comprise of owned fund, deposits, borrowings from NABARD, Sponsor Banks and other sources including SIDBI and National Housing Bank.

1. Owned Funds

The owned funds of RRBs comprising of share capital, share capital deposits received from the shareholders and the reserves stood at ₹ 13838.92 crore as on 31 March 2011 as against ₹ 12247.16 crore as on 31 March 2010; registering a growth of 13.0%. The increase in owned funds to the tune of ₹ 1591.76 crore was mainly on account of accretion to reserves by the profit making RRBs. The share capital and share capital deposits together amounted to ₹ 4273 crore of total owned fund while the balance amount of ₹ 9566 crore represented reserves.

2. Deposits

Deposits of RRBs increased from ₹ 145035 crore to ₹ 166232.34 crore during the year registering growth rate of 14.60%. Gurgaon GB reported the highest deposit growth rate of 37%. There are Sixteen (16) RRBs having deposits of more than ₹ 3000 crore each.

3. Borrowings

Borrowings of RRBs increased from ₹ 18770 crore as on 31 March 2010 to ₹ 26490.81 crore as on 31 March 2011 registering an increase of 41.10% . Borrowings viz-a-viz the gross loan outstanding constituted 26.8% as against 22.7% in the previous year.

Uses of Funds

The uses of funds of RRBs comprise of investments and loans and advances.

1. Investments

The investment of RRBs increased from ₹ 79379.16 crore as on 31 March 2010 to ₹ 86510.44 crore as on 31 March 2011 registering an increase of 8.98%. SLR investments amounted to ₹ 45022 crore where as non-SLR investments stood at ₹ 41488 crore. The Investment Deposit Ratio (IDR) of RRBs progressively declined over the years from 72% as on 31.3.2001 to 52.04 % as on 31 March 2011.

2. Loans & Advances

During the year the loans outstanding increased by ₹ 16098.33 crore to ₹ 98917.43 crore as on 31 March 2011 registering a growth rate of 19.4% over the previous year. Meghalaya Rural Bank recorded the highest growth rate of 35% during the year 2010-11.

3. Loans Issued

Total loans issued by RRBs during the year increased to ₹ 71724.19 crore from ₹ 56079.24 crore during the previous year registering a growth of 27.90%. Samastipur KGB reported highest growth rate of 123% during 2010-11 followed by Andhra Pradesh GVB at 112%.

Working Results

1. Profitability

75 RRBs (out of 82 RRBs) have earned profit (before tax) to the extent of ₹ 2420.75 crore during the year 2010-2011. The profit was marginally lower than the previous year. After payment of Income Tax of ₹ 634.22 crore, the net profit aggregated to ₹ 1786.53 crore. The remaining 7 RRBs incurred loss to the tune of ₹ 71.32 crore.

2. Accumulated Losses

As on 31 March 2011, 23 of the 82 RRBs continued to have accumulated losses to the tune of ₹ 1532.39 crore as against ₹ 1775.06 crore (27 RRBs) as on 31 March 2010. The accumulated loss decreased by ₹ 242.67 crore during the year under review.

3. Non-performing Assets (NPA)

The Gross NPA of RRBs stood at ₹ 3712 crore as on 31.03.2011 (i.e.3.75%). The percentage of Net NPA of RRBs has shown an increase from 1.8% to 2.05% during the year. The data revealed that 15 RRBs had gross NPA percentage of less than 2%, whereas 33 RRBs had it above 5%.

4. Recovery Performance

There has been an improvement in the recovery percentage during 2009-10 from 80.09% as on 30 June 2009 to 81.18% as on 30 June 2010. The aggregate overdue, however, increased by ₹ 934 crore to ₹ 9805 crore as on 30 June 2010.

5. Credit Deposit Ratio

The aggregate CDR of RRBs increased over the years from 57.10% as on 31 March 2010 to 59.51% as on 31 March 2011. Eight of the RRBs reported CDR of more than 100%.

6. Productivity of Branch and Staff

The branch productivity increased to ₹ 16.57 crore in 2010-11 from ₹ 14.72 crore in 2009-10 with a growth of 12.57%. Similarly, staff productivity in 2010-11 increased to ₹ 3.78 crore from ₹ 3.70 crore in 2009-10 with a growth of 2.16%.

Policy Initiatives during the Year 2010-2011

1. Capital Infusion for improving CRAR

Consequent upon the decision taken in the Finance Minister’s Review Meeting of RRBs dated 18.08.2009, a Committee was constituted by Government of India, Ministry of Finance, Department of Financial Services under the Chairmanship of Dr. K.C. Chakrabarty, Deputy Governor, Reserve Bank of India, to examine the financials of RRBs with reference to CRAR and suggest a roadmap for achieving a CRAR of 9% by March 2012. As per Dr. K.C. Chakarbarty Committee Report recapitalization to 40 selected RRBs in 21 states was started in 2010-11. The recapitalization amount is to be shared by the stake holders in proportion of their shareholding i.e. 50%, 35% and 15% by Central Government, concerned sponsor banks and State Government. As per approved scheme, the release of Central Government share is subject to proportionate share by the Central Government, concerned sponsor banks and State Government. A sum of ₹ 66.49 crore was released to 5 RRBs during 2010-11.

Accepting the recommendations of the committee, the GOI along with other shareholders decided to recapitalize the RRBs by infusing funds to the extent of ₹ 2200 Crore. The implementation is already underway and is expected to be completed during 2012-13.

2. Regional Rural Bank Service Regulations 2010

Based on the recommendations of Amaresh Kumar Committee, the GOI issued the RRB Service Regulations 2010.

3. Regional Rural Bank Appointment and Promotion Rules 2010

GOI also notified the RRB Appointment and Promotion Rules 2010**,** in July 2010.

4. Technology Innovation through Core Banking Solutions (CBS)

The RRBs were required to ensure that their branches are put on CBS platform so that they can provide hassle free and any where banking services to their clients. 80 RRBs have since been fully migrated to CBS as on 30m September 2011. NABARD is providing financial assistance to identified 28 weak RRBs to the extent of 40% for core banking solution from Financial Inclusion Technology Funds (FITF) and rest of the cost will be shared by the Sponsor Bank (50%) and the RRB (10%)

5. Financial Inclusion

As envisaged by the Government of India, RRBs as a group have become a strong intermediary for financial inclusion in rural areas by opening a large number of “No frills” accounts and by financing under General Credit Card (GCC), as per RBI guidelines. Total number of accounts stood at ₹ 1310.17 lakhs in March 2011 which was ₹ 1188.67 lakhs in March 2010.

6. Interest Subvention to RRBs

The continuance of the interest subvention scheme was announced in the Union budget 2010-11. Interest subvention of 1.5% per annum was available to RRBs for deploying their own funds for crop loan up to ₹ 3 lakhs per farmer, provided the ultimate borrower get such loans at 7% interest per annum. An additional subvention of 2% was announced during the year to those farmers who repaid crop loans promptly within one year of disbursement. Thus, the interest paid on crop loans by such farmers was effectively at the rate of 5%.

Problems (Weakness) of RRBs

Although RRBs had a rapid expansion of branch network and increase in volume of business, these institutions went through a very difficult evolutionary process due to the following problems.

1. Very limited area of operations
2. High risk due to exposure only to the target group
3. Public perception that RRBs are poor man's banks
4. Mounting losses due to non-viable level of operations in branches located at resource-poor areas.
5. Switch over to narrow investment banking as a turn-over strategy
6. Heavy reliance on sponsor banks for investment avenues with low returns barring exceptions, step-motherly treatment from sponsor banks.
7. Chairman of RRBs under the direction of Regional Managers appointed as Board of Directors by sponsor banks
8. Burden of government subsidy schemes and inadequate knowledge of customers leading to low quality assets
9. Unionized staff with low commitment to profit orientation and functional efficiency.
10. Inadequate skills in treasury management for profit orientation

11. Inadequate exposure and skills to innovate products limiting the lending portfolios
12. Inadequate effort to achieve desired levels of excellence in staff competence for managing the affairs and business as an independent entity
13. Serious undermining of the Board by compulsions to look up to sponsor banks, GOI, NABARD and RBI for most decisions.
14. RRB hampered by an across the board ban on recruitment of staff.

SUGGESTIONS (RECOMMENDATIONS) FOR IMROVEMENT OF RRBs

1. Government should encourage and support banks to take appropriate steps in rural development.
2. Efforts should be made to ensure that the non-interest cost of credit to small borrowers is kept as low as possible.
3. Policy should be made by government for opening more branches in weaker and remote areas of state.
4. Productivity can be improved by controlling the costs and increasing the income.
5. To participation cost, subsidy should be adjusted towards the end of the transaction for which loan assistance is sanctioned.
6. Government should take firm action against the defaulters and shouldn't make popular announcements like waiving of loans.
7. The RRBs have to make an important change in their decision making with regard to their investments.
8. The RRBs have to be very careful and reduce the operating expenses, because it has been found from our study that these expenses have increased the total expenditure of the banks.
9. The RRBs have to give due preference to the micro-credit scheme and encourage in the formation of self help group.
10. Cooperative societies may be allowed to sponsor or co-sponsor with commercial banks in the establishment of the RRB.
11. A uniform pattern of interest rate structure should be devised for the rural financial agencies.
12. The RRB must strengthen effective credit administration by way of credit appraisal, monitoring the progress of loans and their efficient recovery.
13. The credit policy of the RRB should be based on the group approach of financing rural activities.
14. The RRB may relax their procedure for lending and make them easier for village borrowers.

CONCLUSION

To conclude, the rapid expansion of RRB has helped in reducing substantially the regional disparities in respect of banking facilities in India. The efforts made by RRB in branch expansion, deposit mobilization, rural development and credit deployment in weaker section of rural areas are appreciable. RRB successfully achieve its objectives like to take banking to door steps of rural households particularly in banking deprived rural area, to avail easy and cheaper credit to weaker rural section who are dependent on private lenders, to encourage rural savings for productive activities, to generate employment in rural areas and to bring down the cost of purveying credit in rural areas. Thus RRB is providing the strongest banking network. Government should take some effective remedial steps to make Rural Banks viable.

Regional Rural Banks plays a key role as an important vehicle of credit delivery in rural areas with the objective of credit dispersal to small, marginal farmers & socio economically weaker section of population for the development of agriculture, trade and industry .But still its commercial viability has been questioned due to its limited business flexibility, smaller size of loan & high risk in loan & advances. Rural banks need to remove lack of transparency in their operation which leads to unequal relationship between banker and customer. Banking staff should interact more with their customers to overcome this problem. Banks should open their branches in areas where customers are not able to avail banking facilities. In this competitive era, RRBs have to concentrate on speedy, qualitative and secure banking services to retain existing customers and attract potential customers.

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