

CHAPTER - III

RURAL BANKING SYSTEM IN INDIA

Rural sector occupies a critical place in the Indian economic system, as three out of every four Indian live in rural areas and five out of every six persons living in rural areas are dependent upon agriculture as source of income. Agriculture along with its allied activities contributes around 35 per cent to National Income. Hence, the development of agriculture would mean the development of rural masses. The rapid development of rural areas, agriculture and allied activities as a sector and various class of people residing in the country side has been the basis of policy formulation in the successive Five Year Plans of the country.

The increase in agricultural production and productivity depends on the adoption of new farm techniques and technologies. The adoption of new tools and practices depends on the the availability of larger and larger amount of funds, and this is largely influenced by the structure and operations of the financial institutions located in the country side.

India has succeeded in developing one of the largest rural banking system in the world. Various regulatory measures were taken in close succession enabling

banking system to play an effective role in economic development of country side. The two prominent measures were; firstly, the consolidation programme of Primary Agricultural Co-operative Credit Societies (PACS) so as to make them strong and viable and the policy of rural commercial bank branch expansion and its transformation from class banking to mass banking. And, secondly, the formulation of specific development programmes and action plans to facilitate the flow of bank credit to rural sector. Further, targets and sub-targets were set before, banks, so as to ensure that the credit to neglected sector (Priority sector) increases considerably¹.

Objectives

This chapter discusses the change from Single-agency to multi-agency system of rural banking in India, for providing the necessary background to the analytical study. Secondly, the structure of the of the rural banking system in the country is discussed.

Single-Agency and Multi-Agency Approaches in Rural Banking

The co-operative movement was first officially established in the country in 1904 for facilitating the development of a special institutional agency for the provision of credit for agricultural sector. GOI continued

its efforts to establish co-operative credit system as a single agency to meet the credit needs of agricultural sector. This included various concessions in the form of state contribution to share capital of co-operative credit societies, subscription to debentures of Land Development Banks, exemption from stamp duties, concessional finance from RBI/NABARD and so on. The CBs involvement in agricultural finance was very limited.

Various committees like the Agricultural Finance Sub Committee (1945), Rural Banking Enquiry Committee(1950), the All-India Rural Credit Survey Committee (1954), while emphasising that credit provided by CBs in India to agriculture was negligible, none had made any recommendations or suggestion that CBs in India should enter the agricultural and rural sector in a big way.²

The establishment of Multi institutional agencies of rural finance was the outcome of fast increasing requirements of credit for agricultural and rural development, which infact, was the result of the green revolution in the late sixties and the increasing emphasis on the development of rural sector in the Five Year Plans. These developments signified that although co-operatives were the best suited agency for providing agricultural finance, sole reliance

hence forth could not be placed on them for meeting larger credit needs. The co-operatives both organisationally and operationally found it difficult to meet the new challenges single handed, for they could not be developed uniformly in all parts of the country and strengthen financially.

The first state effort to extend commercial banking facilities in rural areas was the conversion of the Imperial Bank of India into the SBI in 1955, on the re-commendations of the A.D. Gorwala Committee in 1954. This process was carried further with the state induction of CBs in the field of rural banking under the policy of 'Social Control' over banks on the recommendations of the National Credit Council (Under the chairmanship of the Finance Minister) in 1968 to adopt the Multi-Agency Approach to meet the growing credit needs of the farmers. Further, in 1969 the All-India Rural Credit Review Committee strongly emphasised the need of CBs to enter the field of agricultural finance and this eventually led to the policy of nationalisation of 14 major CBs in July 1969 (another 6 banks were nationalised in April 1980). With this, the penetration of CBs in the rural sector began in a big way.

Further, on the recommendations of Shri M. Narasimham Working Group, RRBs were established in 1975, to serve exclusively the credit needs of the rural poor.

Hence, the change from the single agency of co-operatives to the multi-agency system of rural banking, was brought over with a view to increase the flow of rural credit and to deliver credit at the door step of the farmers.

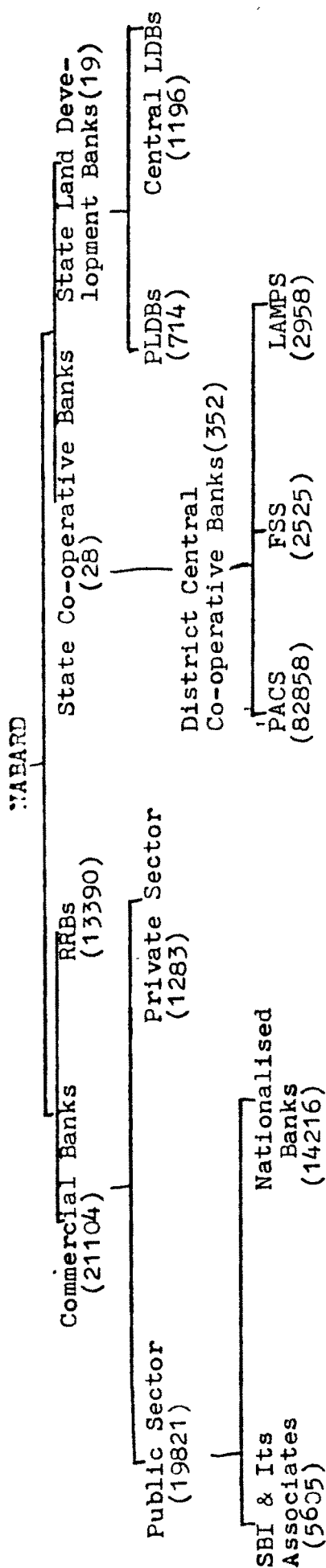
The Rural Banking Structure In India

The rural banking structure comprises of three banking institutions providing finance at the grass root level viz. Co-operatives, CBs and RRBs. Chart I presents the rural banking structure in India.

The co-operative credit structure consists of two types, the one engaged in short term and medium term credit and the other in a long term credit. The short term credit structure is federal in character, based on 3 tier pattern with the apex banks at the state level, Central Co-operative Banks at the district level and co-operative credit societies at the village level. The State Co-operative Banks are the apex level institutions which finance the DCCBs. DCCBs in turn finance the co-operative

Chart I

Rural Banking Structure in India.



N.B. : 1. In some states/Union territories the SCBs directly finance the PACS and also provides directly long term loans.

2 Figures in bracket indicate the number of Institutions as on 30th June 1990. The Central LDBs data relates to 30th June 1984.

Source : 1= For commercial banks : Report on Currency and Finance, 1989-'90, Volume I : Economic Review, Published by RBI.
2 For Co-operative Banks : Important Items of Data, Credit and Non-Credit Co-operative Societies 1989-'90, Published by NABARD.

credit societies at the primary level. The long term credit structure is either Federal or unitary in character with State Co-operative Land Development Banks (SLDBs) as the apex institutions at the State Level and Primary Land Development Banks (PLDBs) or branches of SLDBs at the Taluka/block level. The GSLDB have unitary structure with branches located at the taluka level.

Thus, the field level co-operative institutions which provide credit to individual borrowers consists of (i) PACS, Providing both short term and medium term credit to their members and (ii) PLDBs or branches of SLDBs dispensing long term credit to their members.

The reorganisation programme of PACS was introduced in early sixties to make them strong and viable, following the recommendations of The Committee on Co-operative Credit (Shri V.L. Mehta as chairman) 1960. The Working Group on Co-operation constituted by the planning commission, for the Fifth Five Year Plan (1973) had observed that a PACS could become viable only if it has a minimum short term agricultural credit business of Rs. 2 lakhs. Further, it was decided by RBI in May 1976, that for the purpose of viability the coverage of villages with a gross cropped area of 2000 hectares might be considered adequate to provide a minimum short term credit potential of Rs. 2 lakhs³.

Based on the recommendations of CRAFTICARD, the NABARD has formulated a set of guide-lines for planning the future development of re-organised societies in a phased manner. As a result of the consolidation programme the number of PACS were drastically reduced over the last 15 years.

The commercial banking structure comprises of the rural branches of both public and private sector banks. SBI and its associates and nationalised banks constitute the Public Sector banks. The CBs provides both short-term and long-term loans to farmers and also finance allied activities like marketing, Processing, storage etc. in rural areas through their rural branch net work. Prior to 1969, most of the CBs branches were concentrated in urban areas, hence to increase the branch network in rural areas, RBI evolved a specific branch licansing policy. As a result, in 1989, the 57 per cent of commercial bank branches were located in rural areas as against only 22 per cent in 1969.

RRBs as new institutional agency was established in 1975, so as to meet the credit requirements of rural poor, which were neglected hither-to both by co-operatives and CBs. They combine the features of both co-operatives & CBs.

RRBs are mainly located in rural areas. The share capital of an RRB (Rs. 1 crores authorised and Rs. 25 lakhs issued), is contributed by GOI, concerned state Governments and sponsoring bank in the ratio of 50:15:35. These are scheduled commercial banks but differ from the CBs in the following way :

Firstly, the area of operation of an RRB is limited to a particular region comprising one or two districts.

Secondly, RRBs grant loans and advances only to the rural poor people and,

Lastly, the lending rates of interest of an RRB is similar to the prevailing lending rates of interest of co-operative societies in the area of operation.

As, at the end of March 1990, there were 196 RRBs, covering total of 372 districts in the country. Out of 196 RRBs, 192 have been sponsored by 26 public sector banks, 3 by 2 private sector banks, and 1 by a Co-operative bank⁴.

In our analysis, CBs data includes that of RRBs. The traditional co-operative rural credit institutions viz. SLDBs and PACS are the other two constituents of rural banking system.

At the all-India level, the state wise presence of all the 3 constituents of rural banking system is found to be existing in 18 states. These are Andhra Pradesh, Assam, Bihar, Gujarat, Haryana, Himachal Pradesh, Jammu and Kashmir, Karnataka, Kerala, Madhya Pradesh, Maharashtra, Orissa, Punjab, Rajasthan, Tamil Nadu, Tripura, Uttar-Pradesh and West Bengal.

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