Twelfth Five Year Plan and Banking: Some Stray Thoughts

Dr. N. K. Thingalaya*

The Twelfth Five Plan, which would be ushered in shortly, is expected to focus on Inclusive Development. Banks have been already directed to achieve total Financial Inclusion. After sixty years of planning, it is now being increasingly realized that a large section of the population remains beyond the reach of the benefits emanating from planned development. Similarly, after over four decades of public sector banking, it is found that only 35 percent of the households could avail banking services, according to the Census 2001 data. The latest Census data as on 2011 are yet to be published.

The banking sector in India, no doubt, has witnessed paradigm shifts in its operations since 1969. It has been assigned the role of ***change agent*** in the rural sector, guiding the flow of credit to the segments, which have been accorded priority status. Regional inequalities continue to hamper economic development. It is imperative that the Regulator should adopt a long term policy for shaping the banking suitable structure.. Considering the gross inadequacy of banking facilities in the north-eastern states, the necessity of promoting a new bank to operate exclusively in these states has to be assessed. The gramin banks have to be supported through capital infusion as they can play a more effective role in reaching the unreached. There is a need to re-define the priority sectors in the context of the thrust on inclusive development.

Eliminating Regional Inequalities

For minimizing regional inequalities in the spread of bank branches particularly in the rural areas, a more effective strategic plan has to be formulated. Normally, the gramin banks are more easily accessible to the rural masses and have better compatibility than the urban-oriented big banks. But they are not big enough to cover larger areas in many states. Take the case of Uttar Pradesh, one of the BIMARU states, where all districts have the presence of gramin banks. Yet, there are a few districts with less than ten branches of gramin banks. Baghpat has 4 branches, Gautam Buddhanagar 5 and Mathura only 7 branches. While the gramin banks have 3092 branches in the state, the State Bank group has only 1712 branches. With such a pattern of branch dispersion, how long it would take to fill up the spatial gaps is anybody's guess. In Madhya Pradesh, also there are districts of this category; Betul district has only 4 branches of gramin banks, Burhanpur-7 and Sheopur 6. State Bank of India has a minor presence in terms of its service outlets in both the states compared to those of the gramin banks presently functioning in the states.

Maharashtra, the highly banked state, has glaring inadequacy of banking facilities in most of its districts outside the metropolitan area. As many as seven districts out of 35 do not have a single branch of gramin banks and another six districts have single branches, according to the latest issue of *Quarterly Statistics on Deposits and Credit of Scheduled Commercial Banks: March 2011.* Some of the less developed districts in the state have very few branches of these banks; Gadchiroli 17 branches, Washim -16 and Gondia -24. Even the agriculturally prosperous districts like Jalgaon, Kolhapur and Nasik have very poor presence of gramin banks, having single branches.

The case of Tamil Nadu, another state having a long history of banking development, is not different. There are seven districts having single branches of gramin banks and one district does not have gramin bank at all. Rural banking penetration in Tamil Nadu, when measured as the percentage of rural households in the state availing banking services according to Census

*Chairman, Academic Council, JKSHIM, Nitte.

2001, turns out to be dismally poor at 18 percent. The state has less number of rural branches compared to the neighbouring states like Andhra Pradesh, Karnataka and even Kerala, a state much smaller in size. The gramin banks generally have a better record of performance compared to other banks in the rural sector. To cite an example, in Thanjavur district, there is only one branch of a gramin bank. It has mobilised Rs.5 crore as deposits and has lent Rs.13 crore as credit as on March 2011.This is not a stray case. In the districts like Nagapattinam, Nilgiris, Perambalur, Thiruvarur Thiruchirapalli similar feature can be seen. In the last mentioned district, the lone branch of Pandyan Grama Bank, has a resource base of Rs.9 crore, while the advances outstanding are Rs.24 crore.

To cover all the unbanked villages identified by the Lead Banks and recorded in the proceedings of the State Level Bankers' Committees of all states, there is certainly the need for supplementing the efforts of all the existing banks. There is, however, no case for reviving the concept of local area banks with very small capital base. Gramin banks in their current stature have proved that rural banking could be developed as a viable proposition. They have to be encouraged to open more branches and to adopt branchless banking model wherever possible.

Strengthening the Gramin Banks

Since their inception in 1975, the gramin banks have passed through different stages of expectations and distractions. During the initial stage, there was unplanned expansion raising the hopes and aspirations of planners and the prospective-users. During the next stage, their complacent under-performance and financial instability created dis-satisfaction among the owners. At the third stage, the introduction of Financial Sector Reforms, almost denounced them as un-remunerative appendages in the 90s. Finally the process of consolidation initiated by the Government of India since 2005, changed their fortunes completely. Through a process of mergers at the state level, their number was reduced from 196 to 82, enlarging their areas of operation. With this, their bottom-lines have expanded and they are able to wipe out the accumulated losses in many cases. Some of them have earned higher volume of profits compared to some of the old generation banks of the private sector.

There appears to be a move now to introduce a second round of mergers. The objective virtually is to reduce their number only. ***Considering the role the gramin banks are expected to play in enhancing Financial Inclusion, it is not desirable to tinker with the structure of gramin banks at this juncture.*** They have already passed though difficult days and are now in a position to flex their muscles. In Andhra Pradesh, for example, where the micro-finance institutions have found their Waterloo, the five gramin banks continue to expand their business as usual. Andhra Pragathi Grameena Bank among them has 393 computerised branches, handling 31.10 lakh deposit accounts and servicing 10.30 lakh borrowing accounts. As on September 2011, it handles a total business of Rs.9092 crore. Andhra Pradesh Grameena Vikas Bank has 524 branches in the state, having a total business of over Rs.7000 crore. The other three banks also are quite strong and are capable of reaching out to the unreached at relatively lower cost. There is no point in merging them, which may lead to some dislocations in their operations.

It is necessary that the gramin banks have to be strengthened by infusing more capital into their capital base. They must be groomed to become super markets selling all financial products, using IT-enabled process. They can become more than a robust substitute for the microfinance institutions, which are operating with huge over-head costs. The feasibility of partly privatisation of their capital of the more profitable gramin banks may be explored.

Redefining the Priority Sectors

The priority sectors, invented in 1968, have become over the years, an omni-bus carrying all type of passengers. Its contents have increased substantially, while the basis adopted for prescribing sectoral targets has not moved beyond its arbitrariness. In the original scheme of things, sectoral targets were fixed for the banks uniformly, without taking into account their branch composition. Later, at the political level, it was insisted upon each bank to attain the sectoral targets in each state, where it operated.

Perhaps, un-concerned with these policy-directed sectoral targets, at the district level, under the Lead Bank Scheme, the Lead Banks are directed to formulate district credit plans. NABARD was entrusted with the task of preparing Potential Linked Credit Plans for all the districts. These exercises in credit planning are carried out religiously in all the 622 districts. They are monitored periodically at the meetings of the District Consultative Committees. Over the years, these credit planning exercises have become form-filling rituals generating voluminous data, bank-wise, branch-wise, taluk-wise and scheme-wise.

There are hardly any records available to indicate whether these plan documents are used for any analysis at the Rural Planning and Credit Department at the Reserve Bank of India. Sectoral targets implicitly remain intact, bank-wise, state-wise and district-wise. Some fresh thinking on this is necessary.

Since power shortage in the country is assuming alarming situation, credit facilities given for installation of solar power may be brought under the priority sector lending. Credit facilities could be provided to the Below Poverty Line families under the Differential Rate of Interest scheme (call it ***Darkness Removal Initiatives***, if necessary) for installing solar power system for domestic lighting. The amount of loan required per family for installing solar power system with two bulbs may be around Rs 13,000 only. Banks have to be directed to ensure that at least one per cent of their total advances are lent for this purpose, preferably in the rural areas, where electricity has not reached. As the over all target is to provide power through renewable sources to 2.43 crore BPL households, this scheme can play a crucial role in banishing darkness for a large number of poor households in rural areas. The electricity boards cannot provide electricity to all remote villages, even over the next two decades, considering their inherent problems of inadequate generation and inefficient distribution. Extending credit to the poor households at the concessional rate of 4 per cent would enable most of them to opt for solar power installation. And this loan may not erode drastically the total profits of banks, as only one per cent of their total advances are expected to be earmarked for this purpose.

Financial inclusion would be operationally more meaningful, if the DRI lending scheme is adopted to extend credit to the hitherto unreached poor rural households, who cannot hope to get the benefit of electricity for decades. Instead of retaining the DRI scheme as an ineffective scheme in their ledgers, the banks can channelise it for rural electrification. Since the loan component is small and interest rate is low, the BPL households can get the advantages of solar light at an affordable cost. Brighter light at home brings not only happiness. It would provide the facility for the school going children to read after sun set. Its contribution to the welfare of the family is invaluable.

A few aberrations have crept into the coverage of priority sector during the last few years. Apparently to enlarge the coverage of priority sector credit, some indirect advances also are brought into the ambit of priority sectors. One such example is that of the advances made by banks to microfinance institutions for on-lending to the poor borrowers. Their lendings to the small borrowers at interest rates ranging from 30 percent are certainly against the very spirit of priority credit. The powerful lobby of the mFIs and

that of their angel investors have made this feasible, with the tacit consent of the regulator. A re-thinking on this aspect is long overdue.

It is reported that the Reserve Bank of India has constituted a committee "to re-examine the existing classification and suggest revised guidelines with regard to priority sector lending classification and related issues". Like the committees set up in the past, this committee also may suggest some cosmetic changes, without going into fundamental issue relating to the very basis of fixing the sectoral targets. The arbitrariness in target fixation is likely to continue. This aspect needs to be examined afresh.

A New Bank for the North-East

Banking facilities are grossly inadequate in the eight states in the north-east. One of the committees appointed by the Reserve Bank of India has identified 36 districts out of 59 districts in this region as Financially Excluded Districts in 2005. Population per branch was considered as the yard stick for this purpose, as a rough indicator of the inadequacy of banking facilities.. Districts where the rural and semi-urban per branch population is more than 19272 and their corresponding credit gap is more than 95 percent are considered as Financially Excluded Districts.

The Reserve Bank of India was considering for more than a couple of years, the need for granting new licences for banks in the private sector. Though the conditions for granting licences were specified, so far no new bank has been given any licence. Considering the geographic peculiarities of the region, the feasibility of promoting a bank for operating exclusively in this region may be considered. The incentive for this bank could be that 15 percent of their branches could be located anywhere in the metropolitan and urban centres. Initially, this bank can be permitted to open 100 branches in this region, while it can open five branches in any metropolitan centre. When the total number of branches exceeds 200, its entitlement for metropolitan branches would go up to 12 percent and when the total number goes beyond 500, it can have 15 percent of metropolitan branches.

It may be noted that there need not be any apprehension about the viability of such a bank confined to this region. Assam Gramin Vikash Bank has 362 branches operating in 25 districts of Assam state alone. Out of them only 13 branches are urban branches. It handles a total business of Rs.4376 crore and its net profit is Rs.35.37 crore as on March 2011. Without having exposure to big advances and without having outlets in metropolitan centres, if this bank could be managed profitably, the new bank with branches in metropolitan centres could be financially more viable.

In view of the inadequacy of infrastructure facilities in the entire region, the state governments have to bestow their attention on improving the basic infrastructure facilities in their states. One way of assisting the new bank to open its branches in the rural areas, the state governments may construct Panchayath Bhawans in the villages on a selective basis, where space could be provided to the bank to accommodate its branches. The Government of Jharkhand has already started such a project, constructing multi-purpose Panchayath Bhawans in most of the villages. It has indicated that space would be provided for the rural branches in these Bhawans free of rent for one year. It has also indicated that for ensuring the viability of the new branches, it would keep a deposit of Rs.10 to Rs.15 lakh in the new branches. This is certainly a gesture of significance, if it is really implemented. Details of the progress made so far are not readily available.

Banking development cannot take place in isolation. The state and the central governments have to create the necessary conditions conducive for development. In the Twelfth Five year Plan, the Government of India may have to allocate sufficient funds for rapid development of the infra structure facilities in this

region. The disturbed political situation has to be changed into one amenable to development. More investments on creating basic amenities and generating employment opportunities would help the banking sector to fulfill their task of reaching out to the unreached

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