Role of RRBS in Financial Inclusion Empirical Evidence from RRBS in Gujarat

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ABSTRACT

Regional Rural Banks (RRBs) in India have been established to spread the banking amongst rural poor, based on the recommendation of various expert committees. RRBs have special role to play in spread of banking, now known as financial inclusion, in rural and semi urban areas to include the rural mass in banking network and thereby help them the rural poor, small and marginal farmers, artisans, agricultural labors, and even small entrepreneurs.

There are three RRBs working in Gujarat namely Baroda Gujarat Gramin Bank, Dena Gujarat Gramin Bank and Saurashtra Gramin Bank, covering different parts of the state. The present study makes an attempt to analyze performance of these three RRBs in role of financial inclusion. The financial inclusion is measured in terms of (1) branch expansion measured by ratio of branch in rural and semi urban areas as well as ratio of single branch in rural area to total branches and (2) spread of credit in terms of Credit deposit ratio, taking published data of last 8 years from 2005-06 to 2012-13. The analysis of performance is made with the help of trend analysis and ANOVA. Finding shows that overall there is declining trend in terms of financial inclusion by all RRBs in Gujarat in post-merger period. The findings are in line with earlier studies.

Key words: Regional Rural Bank, financial inclusion, branch expansion, credit deposit ratio
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Financial Inclusion

The term "financial inclusion" has gained importance since the early 2000s and more so with the launch of recent ‘Jan Dhan Yojana’ by Government of India, a result of findings about financial exclusion and its direct correlation to poverty.

Financial inclusion or inclusive financing is the delivery of financial services at affordable costs to sections of disadvantaged and low-income segments of society, in contrast to financial exclusion where those services are not available or affordable. It is argued that as banking services are in the nature of public good; the availability of banking and payment services to the entire population without discrimination is the prime objective of financial inclusion public policy (Wikipedia).

Realizing the need to provide institutional credit to rural poor and save them from the ruthless clutches of unorganized sector lending the Regional Rural Banks (RRBs) were established for the first time in India way back in the year 1975 and therefore, no study on financial inclusion is complete without mention of Regional Rural Banks.

Regional Rural Banks (RRBs)

The RRBs are meant for the development of rural economy by pooling credit gap especially to the rural poor by providing credit. The main objectives of establishment of RRBs is given in the
RRBs Act of 1976 were “to develop the rural economy in 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 labourers, artisans and small entrepreneurs and for matter connected therewith and incidental thereto”.

Regional Rural Bank network in India

The RRBs were established as a part of expanding institutional credit to rural poor. Since the inception of RRBs in 1975, the growth and working of RRBs are governed by policy measures. Accordingly it is divided into three broad phases namely inception and growth phase (1975-1990), reform phase (1991-2005), and reconstruction / post merger period (2005 onwards).

The inception and growth phase showed remarkable increase in branch network. Started with modest number of 6 RRBs in the year 1975, it jumped to 40 RRBs in next year and reached to the spread 196 RRBs through 14433 branches in 372 districts by the year 1990.

It stagnated to the same number (196 RRBs ) all the years from year 1991 to 2005 with slight increase in number of branches reaching to 14484 number of branches by the year 2005 covering 523 districts. However this period called second phase, faced severe financial viability problems.

Based on various recommendations, the RRBs are restructured by merging various RRBs in the year 2005 in order to make them financially viable. In 2005-06, the Government of India initiated the process of structural consolidation of RRBs by amalgamating RRBs sponsored by the same bank within a State as per the recommendations of the Vyas Committee (2004). The amalgamated RRBs were expected to provide better customer service due to better infrastructure, computerization of branches, pooling of experienced work force, common publicity, marketing efforts etc., and also derive the benefits of a large area of operation, enhanced credit exposure limits and more diverse banking activities. As a result of the amalgamation, the number of RRBs in India was reduced from 196 to 64 as on 31st March, 2013 and in Gujarat it was reduced from 9 to 3.
Research problem

Gujarat is one of the industrially advanced states. For the sustainable progress of the state the development of rural economy is equally important. RRBs have been assigned the special role of development of rural economy by facilitating to the rural poor, the credit facilities for agriculture, trading, self-employment and so on of each religion.

Reviewing the three phases of RRBs in India, Prabha Singh et al (2009) pointed out that by the inception and expansion phase (1976 -1990) which saw rapid growth of RRBs activities; the reform phase (1991-2005) which raised the profitability of these banks at the cost of massive rural disintermediation, particularly of the targeted borrower categories and the most recent phase is of stock taking and perhaps some repositioning to strike a balance in the conundrum of ‘viability versus outreach’.

In this context this study intends to analyze performance of these three RRBs in role of financial inclusion. The financial inclusion is measured in terms of (1) branch expansion in rural and semi urban areas and (2) spread of credit, taking published data of last 8 years from 2005-06 to 2012-13.

Literature Review

Hemlata & Poonamsing (2009) studied on “Financial inclusion through Regional Rural Banks”. Analyzing the macro level data on RRBs related to manpower deployment, savings mobilization, credit disbursement, regional outreach, saving mobilization across regions, credit disbursed across regions, micro financing in post merger period, the study recommends that RRBs should extend their services in to unbanked areas and increase their credit deposit ratio and thereby play special role in financial inclusion.

Chidambaram (2007) noted that RRBs in India made considerable progress in deposit mobilization, credit dispensation and profit making during the period 2002-03 to 2004-05. As a result of amalgamation, RRBs were in a position to provide better customer services with better infrastructure and policies of experienced staff. He further mentions that the reform phase supplanted made a singular focus on commercial profitability for the Regional Rural Banks. In a sense, the reforms of the Regional Rural Banks were no different from the reforms of the
commercial banks. The same set of policies was implemented and the same set of standards set to calibrate their performance. Not surprisingly then, the Regional Rural Banks started aping the commercial banks in their activities - banks relocated to more promising areas; investments in government securities and PSU bonds and debentures increased while banks were hesitant to increase their loan portfolios; credit was extended mainly under non-priority sector heads so that the proportion of priority sector loans declined despite the dilution of the priority sector definition in several ways; interest rates on lending were deregulated which resulted in high interest rates charged by the Regional Rural Banks; credit to deposit ratio became less than half of the pre-reform levels indicating increased net transfer of resources from the rural poor to the urban rich; regional imbalances aggravated; and the small borrowers, the principal clients of the Regional Rural Banks were overwhelmingly sidelined. By the beginning of the present decade, the carefully built structure of rural development banking in India had all but collapsed.

Thus the above findings lead to formulation of the following hypothesis:

Ha₀: There is no significant change in terms of financial inclusion of BGGB in Gujarat

Ha₁: There is significant decline in terms of financial inclusion of BGGB in Gujarat

Hb₀: There is no significant change in terms of financial inclusion of DGGB in Gujarat

Hb₁: There is significant decline in terms of financial inclusion of DGGB in Gujarat

Hc₀: There is no significant change in terms of financial inclusion of SGB in Gujarat

Hc₁: There is significant decline in terms of financial inclusion of SGB in Gujarat

As the Banking policies of post liberalization allowed banks to focus on financial viability allowing shifting branches to profitable area, and dilute the lending to non priority sector, focus on financial viability and thereby allowing bank to park the spare fund into government securities rather than allowing more credits to most of the banks followed the similar pattern and therefore it is hypothesized as under:

Hd₀: There is no significant difference in terms of financial inclusion of three RRBs in Gujarat

Hd₁: There is significant difference in terms of financial inclusion of three RRBs in Gujarat
Framework of the Study

Taking Hundekar (1995) study as the basis, the following ratios are considered for measuring the performance of financial inclusion by RRBs in Gujarat.

A) Branch expansion policy

*Ratio of rural and semi-urban branches to total branches of the Bank.*

The RRBs are meant for only rural areas, and to know whether the particular bank is rural biased or urban-biased, the ratio of rural and semi urban branches to total branches of particular bank is analyzed.

\[
\text{Ratio of rural and semi urban branches to total branches of the bank} = \frac{\text{rural & semi- urban branches}}{\text{total branches of the bank}} \times 100
\]

*Ratio of single branches in rural centers to total branches of the Bank.*

The effectiveness of branch expansion policy of the bank may also evaluate on the basis of its performance in opening branches at the banked places or unbaked places. This can be judged by the ratio of single branches in rural centers to total branches of the bank.

\[
\text{Ratio of single branch in rural center to total branches of bank} = \frac{\text{single branches in rural center}}{\text{total branches of the bank}} \times 100
\]

B) Credit management

*Credit deposit ratio*

The ratio is obtained by dividing the total credit provided by the deposits mobilized. It indicates the extent to which the particular bank has been benefited in the form of credit expansion out of deposits generated from that bank. This ratio carried out by-

\[
\text{CDR ratio} = \frac{\text{total credit of the bank}}{\text{total deposits of the bank}} \times 100
\]
Research Methodology

The present study is based on secondary data. The relevant secondary data have been collected from the annual reports of all three RRBs in Gujarat. The study is for eight year period starting from 2005-06 to the year 2012-13. In order to analyze the data statistical tools of trend analysis and ANOVA are used with the help of SPSS Software.

Findings and Discussion of the Study

Table 1: Findings of the Study

<table>
<thead>
<tr>
<th>RBB (Ratio of Rural and Semi-urban Branches to total branches of RRB)</th>
<th>RSB (Ratio of Single Rural Branch to total branches of RRB)</th>
<th>CDR (Credit deposit Ratio)</th>
<th>Performance in terms of Financial Inclusion</th>
</tr>
</thead>
<tbody>
<tr>
<td>Trend Analysis</td>
<td>R² /actual trend</td>
<td>R² /actual trend</td>
<td>R² /actual trend</td>
</tr>
<tr>
<td>BGGB</td>
<td>- (Graph 1)</td>
<td>0.942*/ Downward (Graph 2)</td>
<td>0.674** / Downward (Graph 3)</td>
</tr>
<tr>
<td>DGGB</td>
<td>0.895**/ 2nd degree poly. (Graph 4)</td>
<td>0.963*/ 2nd degree poly. (Graph 5)</td>
<td>- (Graph 6)</td>
</tr>
<tr>
<td>SGB (Chart 3)</td>
<td>0.758*/ Downward (Graph 7)</td>
<td>0.967*/ Downward (Graph 8)</td>
<td>- (Graph 9)</td>
</tr>
<tr>
<td>ANOVA</td>
<td>No significant difference</td>
<td>No significant difference</td>
<td>Significant difference (Table 2.1 to 2.3)</td>
</tr>
</tbody>
</table>

- BGGB & DGGB is lower than SGB
No significant Difference in BGGB and DGGB

* Significant at 0.05 level; ** significant at 0.01 level *** significant at 0.001 level
1. **Branch Expansion:**

As shown in Table-1 both the ratios related to branch expansion in unbanked/ rural area namely (1) Ratio of rural and semi urban branch to total branch of RRB and (2) Ratio of single branch in rural area to total branches in the bank show downward ratio for BGGB and SGB whereas the same for DGGB show 2\textsuperscript{nd} degree polynomial trend. Further ANOVA analysis show that for both the ratios there is no significant difference among three RRBs, meaning the all the three RRBs in Gujarat are showing decline in branch expansion in unbanked area which counter serves the social objective of RRBs of financial inclusion.

2. **Credit Management:**

In case of Credit deposit Ratio (CDR), it shows downward trend for BGGB and no pattern /trend is found for SGB and DGGB. The further analysis by ANOVA shows that there is a significant difference in this ratio of three RRBs. The post hoc analysis shows that there is significant difference in CDR of three banks. From Table-1 we found that CDR is significantly lower in BGGB than SGB, similarly, it is significantly lower in DGGB than SGB while there is no significant difference between BGGB and DGGB for credit deposit ratio.

The above findings lead to reject the null hypothesis and accept alternate hypothesis that there is no significant improvement in financial inclusion by BGGB, DGGB and SGB.

This can be attributed mainly to policy related to RRBs to treat RRBs in similar line to commercial banks with a single focus on financial profitability.

**Suggestions**

**At Bank level:**

1. All the three RRBs shall evolve strategy at Bank level like embracing technology, collaboration with branches of commercial banks, post office, micro finance groups to extend the outreach in unbanked area in cost effective manner.
2. Taking SGB’s case the other two RRBs namely BGGB and DGGB should try to improve credit deposits ratio. Low Credit deposit ratio is a matter of concern for bank. Bank shall
evolve strategies to increase CDR up to 70 to 80%. The extension of outreach to unbanked area a suggested in point no. 1 shall thereby help to improve the C/D ratio also.

Policy level:

On the basis of above findings following suggestions are offered for formulating a rural banking policy it is hoped that these suggestions will go a long way in improve working of RRBs:

1. RRBs branch should be allowed to finance within a block rather than a few villages. This will increase its business and include healthy competition amongst rural branches of other banks.
2. RRBs staff should have technical knowledge of agriculture, rural crafts and artisans as well understanding rural credit system and environment with aptitude for working in rural areas. For this purpose RRBs should provide training to their staff according to requirements and recruit only those persons who are capable to do work according to above requirements. These personnel should use regional language in dealing with customers.
3. Any credit program launched for weaker sections should have consumption credit component enabling them to be away from the money lender. This will also stop diversion of loan amount to unproductive program.
4. With credit and savings scheme RRBs should be involved in group liability, insurance against risk and productive employment to generate income for landless labourers and poor rural women. Self-help groups (SHGs) may be helpful for providing credit facilities to individuals. These SHGs which work devotedly for the rural people should also be involved in every stage of the project cycle i.e. from project identification beneficiary selection, appraisal right up to the evaluation stage.
5. RRBs are facing competition with rural branches of commercial banks. Commercial banks work in the same area of operation and provide services to big farmers. Generally these banks do not provide loans to small and marginal farmers, rural artisans and landless labourers. To avoid unnecessary competition, RBI and sponsor banks should make a policy for transfer of business from rural branches of commercial banks to RRBs. This process would have two fold benefits. On the one hand, it will provide business of
rich farmers to RRBs to increase the profit and on the other hand, avoid wasteful competition with commercial banks.

6. Separate credit plan for excluded Regions: The committee recommends that RRBs operating in predominantly tribal areas and having high levels of exclusion may prepare annual credit plans having a separate components for excluded groups, which would integrate credit provision with promotional assistance such as agricultural services and BDSs for the farm and non-farm sectors respectively including entrepreneurship development and formation and strengthening of producer’s organizations like dairy cooperatives, refinance and promotional support may be provided by NABARD to RRBs on a large scale for implementation of this credit plans.

7. Minimum benchmark of credit-deposits ratio of 60 percent needs to be insisted upon for each bank/RRB in every rural district of the country to ensure adequate credit flow to the rural and semi urban sectors.

Contribution of the study

The result is in line with earlier studies by Hemlata & Poonamsing (2009), Chidambaram (2007) and Singh et al (2009). Thus, this study supports the earlier study empirically and contributes to the present literature on RRBs in India.

Conclusion

RRBs were opened with serving social objective. It has all the more important role to play in today’s market economy for financial inclusion. New initiatives like micro finance or Jan Dhan Yojana are well come steps but at the same time Government of India must take policy measures to strengthen the already deep rooted institutions like RRBs to play more effective role in financial inclusion and thereby lead the nation to sustainable economic development.

Appendix

Graph 1 : Trend of RBB of BGGB   Graph 2 : Trend of RBB of DGGB   Graph 3 : Trend of RBB of SGB
Graph 4: Trend of RSB of BGGB  
Graph 5: Trend of RSB of DGGB  
Graph 6: Trend of RSB of SGB

Graph 7: Trend of CDR of BGGB  
Graph 8: Trend of CDR of DGGB  
Graph 9: Trend of CDR of SGB

Table-2.1 Summary: Credit Deposit Ratio

<table>
<thead>
<tr>
<th>Groups</th>
<th>Count</th>
<th>Sum</th>
<th>Average</th>
<th>Variance</th>
</tr>
</thead>
<tbody>
<tr>
<td>BGGB</td>
<td>8</td>
<td>345.9979</td>
<td>43.24973</td>
<td>22.89823</td>
</tr>
<tr>
<td>DGGB</td>
<td>8</td>
<td>360.785</td>
<td>45.09812</td>
<td>21.75823</td>
</tr>
<tr>
<td>SGB</td>
<td>8</td>
<td>551.7737</td>
<td>68.97172</td>
<td>24.31712</td>
</tr>
</tbody>
</table>
Table 2.2 ANOVA : Credit Deposit Ratio

<table>
<thead>
<tr>
<th>Source of Variation</th>
<th>SS</th>
<th>df</th>
<th>MS</th>
<th>F</th>
<th>P-value</th>
<th>F crit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Between Groups</td>
<td>3293.295</td>
<td>2</td>
<td>1646.648</td>
<td>71.621</td>
<td>.000</td>
<td>3.4668</td>
</tr>
<tr>
<td>Within Groups</td>
<td>482.815</td>
<td>21</td>
<td>22.991</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>3776.110</td>
<td>23</td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Table 2.3 Multiple comparisons : Credit Deposit Ratio

<table>
<thead>
<tr>
<th>(I)Bank</th>
<th>(J)Bank</th>
<th>Mean Difference (I-J)</th>
<th>Std. Error</th>
<th>Sig.</th>
</tr>
</thead>
<tbody>
<tr>
<td>BGGB</td>
<td>DGGB</td>
<td>-1.848390225</td>
<td>2.397456664</td>
<td>0.724492</td>
</tr>
<tr>
<td>BGGB</td>
<td>SGB</td>
<td>-25.72198584</td>
<td>2.397456664</td>
<td>0.000</td>
</tr>
<tr>
<td>DGGB</td>
<td>SGB</td>
<td>-23.87359562</td>
<td>2.397456664</td>
<td>0.000</td>
</tr>
</tbody>
</table>

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