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Research Paper

A STUDY ON CO-OPERATIVE BANKING IN INDIA

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Abstract

In rural areas, the indigenous money lender continued to be the banker in need. /ince these moneylenders had virtual monopoly in supplying the credit in rural areas, the poor were o/ten subjected to exploitation with the overriding monopoly. The money lenders o/ten resorted to usurious practices like levying exorbitant rates o/ interest, demanding advance interests.

In this context, it is worthwhile to examine critically the development o/ credit structure in rural India. /ince the banging o/ this century, a number o/ experiments have been conducted on the Indian rural credit scene. The co-operatives were considered the /irst intuitional agency set up /or providing credit and other /acilities to the rural sector. A/ter economic liberalization under the new economic environment, co-operatives at all levels are making e//orts to reorient their /unctions according to the market demands. In this reared the paper examines the major problems o/ the co-operative banks and initiatives taken to overcome those problems.

INTRODUCTION

The co-operative movement, which is the largest socio-economic movement in the world, has contributed significantly to the alleviation of poverty, creation of productive employment as well as the enhancement of social integration in the country. The co-operative movement in India has taken deep roots in various sectors and is making a significant contribution towards economic development and social progress of the people.

The co-operative banking system has played a very important role in the development of the Indian economy, especially in the rural economy. The co-operative movement organized in west but the importance of such co-operative movement felt necessary for the development of India. The co-operative movement in India was started after passing of the co-operative credit Societies Act, 1904 with the main object of providing finance at lower rate of interest to agriculturist, until then, the agriculturists fulfill their financial need by borrowing from village money lenders at high rate of interest and money lenders were manipulated innocence and illiteracy of agriculturists.

Co-operative banks spared over the nation especially in rural where commercial banks are not reached. Co- operative banks are the only the kind of financial institution by which financial assistance provided by the govt. are delivered to the agriculturist of rural area. Gradually co-operative banks are started working in urban area also.

Even though the co-operative banking system is smaller when compared to the commercial banking system, its importance in the development of Indian rural economy cannot be ignored.

ORIGIN AND GROWTH OF CO-OPERATIVE BANKS

In rural areas, earlier getting the credit requirement for the agriculture and its related activities was very tough. Agriculturist were depend for their credit requirement upon unorganized money market agencies, such as money lenders, were providing credit often at exploitatively high rates of interest. At the dame time commercial banks were reluctant to enter into the field of agriculture. Because good and liquid security is the main consideration by the commercial banks. But agriculturists are not able to provide good securities. Land is the only security they can offer which is not acceptable bank advances.

Further, the repayment of loans depends on the crop and the crop is depend on the monsoon which is said to be as gamble. If the production is unprofitable or failure of agriculture may affect the repaying capacity of the borrower. Because of these reasons the commercial banks are trying to keep away from the fields of agricultural finance.

So, the co-operative banks have been taken a job of financing agriculture and its related activates in order to substitute commercial banks and unorganized money market agencies.

The co-operative banks started its activates in India in the banging of 20th century as an official effort to create a new type of institution based in the principles of co-operative organization and management, suitable for problems peculiar to Indian conditions.

Co-operative banks are become to be a part of a set of institutions which are engaged in financing rural and agricultural development. The relative importance of co-operative banks in financing agriculture and rural development has undergone some changes over the years. Till 1969, they increasingly substituted the informal sector lenders. After the nationalization of banks and creation of RRBT and NABARD, however, their relative share has somewhat declined.

WHAT IS CO-OPERATIVE BANK?

According to the International Co-operative Alliance Statement of co-operative identity, a co-operative is an autonomous association of persons united voluntarily to meet their common economic, social, and cultural needs and aspirations through a jointly-owned and democratically-controlled enterprise. Co-operatives are based on the values of self-help, self-responsibility, democracy, equality, equity and solidarity. In the tradition of their founders, co-operative members believe in the ethical values of honesty, openness, social responsibility and caring for others. The 7 co-operative principles are :

1. Voluntary and open membership
2. Democratic member control

3. Member economic participation
4. Autonomy and independence
5. Education, training and information
6. Co-operation among Co-operatives
7. Concern for Community

A co-operative bank is a financial entity which belongs to its members, who are at the same time the owners and the customers of their bank. Co-operative banks are often created by persons belonging to the same local or professional community or sharing a common interest. Co-operative banks generally provide their members with a wide range of banking and financial services (loans, deposits, banking accounts...).

Co-operative banks differ from stockholder banks by their organization, their goals, their values and their governance. In most countries, they are supervised and controlled by banking authorities and have to respect prudential banking regulations, which put them at a level playing field with stockholder banks. Depending on countries, this control and supervision can be implemented directly by state entities or delegated to a co-operative federation or central body.

Even if their organizational rules can vary according to their respective national legislations, co-operative banks share common features :

Customer's owned entities: in a co-operative bank, the needs of the customers meet the needs of the owners, as co-operative bank members are both. As a consequence, the first aim of a co-operative bank is not to maximise profit but to provide the best possible products and services to its members. Some co-operative banks only operate with their members but most of them also admit non-member clients to benefit from their banking and financial services.

Democratic member control: co-operative banks are owned and controlled by their members, who democratically elect the board of directors. Members usually have equal voting rights, according to the co-operative principle of "one person, one vote".

Profit allocation : in a co-operative bank, a significant part of the yearly profit, benefits or surplus is usually allocated to constitute reserves. A part of this profit can also be distributed to the co-operative members, with legal or statutory limitations in most cases. Profit is usually allocated to members either through a patronage dividend, which is related to the use of the co-operative's products and services by each member, or through an interest or a dividend, which is related to the number of shares subscribed by each member.

Co-operative banks are deeply rooted inside local areas and communities. They are involved in local development and contribute to the sustainable development of their communities, as their members and management board usually belong to the communities in which they exercise their activities. By increasing banking access in areas or markets where other banks are less present - SMEs, farmers in rural areas, middle or low income households in urban areas - co-operative banks reduce banking exclusion and foster the economic ability of millions of people. They play an influential role on the economic growth in the countries in which they work in and increase the efficiency of the international financial system. Their specific form of enterprise, relying on the above-mentioned principles of organization, has proven successful both in developed and developing countries. Co-operative banks in a vast country like India is of great significance because :

· It is an organization for the poor , illiterate and unskilled people
· It is an institution of mutual help and sharing
· It softens the class conflicts and reduces the social cleavages
· It reduces the bureaucratic evils and follies of political factions
· It overcomes the constraints of agricultural development
· It creates conducive environment for small and cottage industries

STRUCTURE OFCO-OPERATIVE BANKS

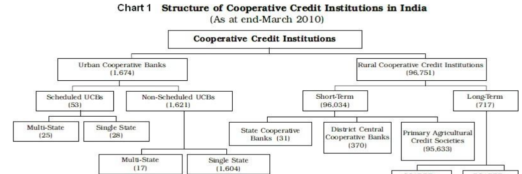
Different types of co-operative credit institutions are functioning in India. They can be classified as (i) Urban co-operative banks (UCB'S) and (ii) Rural Co-operative Credit Institutions. The Urban co-operative banks consist of a single tier, viz. primary co-operative banks. The rural co-operative credit institutions either short term or long term commonly known as short term co-operative credit structures.

The short term co-operative banking structure is pyramidal or federal in character, with three tier linkages between state, district and village level institutions. At the base that is, at the village level, the primary credit societies function upon which the whole co-operative credit is based. At the district level, the district or central co-operative banks function as a federation of primary agricultural societies and at the state level , the apex or state co-operative banks are established . The district or central co-operative banks are federated to the state co-operative banks. The apex or state co-operative banks are colossally linked with the National Agriculture and Rural Development (NABARD). Short tern co-operative credit structure provides crop and other working capital loans primarily for short tern purposes to formers and rural artisans.

The long term co-operative credit structure, comparing the state co-operative Agriculture and Rural Development Banks(NABARD) at the state level and the primary Co-operative Agriculture Rural Development Banks (PACARDB's) at the district , provides medium and long term loans fir making investments in agriculture, rural industries and housing . SCARDB'S and PCARDB are the names substituted for primary and state land development banks, respectively.

The organization structure of co-operative credit institution is presented in chart1 which reveals that co-operative banking has a more widespread and extended network in the rural sector than in the urban sector.

Chart 1 **Structure of Cooperative Credit Institutions in India**
(As at end-March 2010)



SCARDBs: State Co-operative Agriculture and Rural Development Banks
PCARDBs: Primary Co-operative Agriculture and Rural Development Banks

The co-operative credit structure consists of 98425 institutions with district urban and rural sectors. The urban sector has 1674 co-operative banks (with 53 scheduled banks) and 96751 rural co-operative credit institutions. The rural credit institutions are again divided into short term and long term credit instantiations. The short term credit institutions consists of state co-operative banks numbering 31, central co-operative banks numbering 370 and primary agriculture credit societies numbering 95633 and the long term institutions consist of 20 state banks agriculture and rural development banks 697 primary agriculture and rural development banks.

ROLE OFRBI

For commercial banks, the RBI is a lender of last resort, but for co-operative banks, it is the lender of first resort which provides financial resources in the form of contribution to the initial capital (through state Government.), working capital, and refinance. The role of supersedes its regulatory role of the RBI can be in respect of these banks. The main role assigned to the RBI by all India Rural credit Survey Committee in building up the Co-operative Credit organization are:

· To active as a collaborator in drawing up schemes of development with government of India and state governments.

· To act as the provider of finance first to the stat governments for contribution to the share capital of co-operative credit institutions at various levels and secondly, to the co-operative credit structure itself to meet its requirements of short-term , medium term and long-term finance.

To meet the financial obligations, two funds were set up under the RBI Act the National Agricultural Credit (long term operations) fund and the National Agricultural Credit (Stabilization) fund with contribution from the RBI every Year .

Co-operative banks are subject primarily to the control, audit, supervision and periodic inspection of the co-operative department of the state government under the co-operative Societies Act , but less rigorously, by RBI under the Banking Regulation Act. The RBI and the state government. Lay down rules for investment of the loan policy of co-operative banks.

MAJOR PROBLEMS OF THE CO-OPERATIVE BANKS

As in the case of commercial banks, the quantitative growth of co-operative banks has not been accompanied by a qualitative growth. There have always been a number of weaknesses in their performance. Many of these weaknesses are identified as follows:

1 The vital link in the co-operative credit system, namely, the PAC's, themselves remain very weak. They find difficult to satisfy tenants and small farmers credit needs fully.

2 Still co-operative banks are supplying only a small portion of the total needs of the farmers, which means that the farmers are still depends on village money lenders rather than co-operative banks.

3 Most primary societies are unable to meet fully even the production oriented credit needs of the farmers.

4 These banks still not became independent in financial resources. They depend very heavily still on government, RBI, NABARD for refinancing facilities. They have yet not been able to become self reliant in respect of resources through deposit mobilization.

5 They suffer from infrastructural weakness and structural flows. They do not look like banks and do not inspire confidence in the potential members, depositors and borrowers.

6 Overdues at all levels are increasing alarmingly, indicating the failure of the co-operative credit institutions and they have not been able to ensure adequate and timely credit for the borrowing farmers.

7 They suffer from to much officialistion and politiasation that prevented them from developing steadily as a self reliant and resilient credit system.

8 There are many regulators for them, but still there are many lacunea in their regulation.

9 They have been resorting to unethical practices.

10 They suffer from dangerously low or weak quality of loan assets, and from highly unsatisfactory recovery of loans.

INITIATIVES TAKEN TO STRENGTHEN THE DEVELOPMENT OFCO-OPERATIVE BANKS:

For the improvements of co-operative banks Government and RBI have framed many committees time to time to study the challenges and opportunities of the co-operative banks. One among them is Khusro Committee. A Committee headed by an economist, A.M. Khusro, that conducted an appraisal of the agricultural credit system in India. Several observations and recommendations were made in its report in 1989 are as follows:

1. The committee recommitted that there should be two categories of lending rates for agriculture, for small and marginal farmers, interest rate concession should be 1.5 per cent on the loans and on their deposits 1.5 percent higher interest should be given. Higher rate of interest should be charged for other farmers with ceiling interest rate of 15.5 percent.

2. National Co-operative Bank of India should be setup for acting as balancing centre for co-operative credit at the apex level in the country.

3. The committee also recommended for establishment of Agricultural and Rural Infrastructure Development Corporation in the eastern regions of the country comprising the States of Bihar, Orissa, West Bengal and North Eastern States. This corporation evolves a strategy for increasing agricultural lending through building up of necessary forward and backward linkages and formulating location specific projects/schemes for accelerating transformation of agriculture.

4. The present crop insurance scheme is deficient in its operation and its work should be done by statutory crop Insurance Corporation. It also recommended for setting up of export committee of insurance expert, agricultural economists and actuaries.

5. Common legal framework should be devised for recovery of dues. For this purpose State level tribunals for adjudication, i.e., determining the case legally should be established.

6. Merger of Regional Rural Banks (RRBs) with the respective sponsoring banks.

GOVT. OF INDIA REVIVAL PACKAGE FOR STCCS (VAIDYANATHAN COMMITTEE)

The Government of India (GoI) is committed to increasing the flow of credit to agriculture, especially to small and marginal farmers. The short term rural co-operative credit structure (CCS), which should play a central role in this respect, is unable to do so. This structure is severely impaired financially and institutionally. Its share in total credit flow to agriculture has been declining. Concerned at this state of affairs, the GoI had set up a special Task Force in August 2004 under the Chairmanship of Prof.A.Vaidyanathan to suggest an implementable action plan for reviving the CCS. The Task Force submitted its report to the GoI on 04 February 2005. The Government, after due consideration, accepted their recommendations in principle. The recommendations are now being implemented.

The package is aimed at reviving the short-term rural co-operative credit structure (STCCS) and make it a well-managed and vibrant medium to serve the credit needs of rural India, especially the small and marginal farmers. It seeks to

· Provide financial assistance to bring the system to an acceptable level of health;

· Introduce legal and institutional reforms necessary for their democratic, self reliant and efficient functioning; and

· Take measures to improve the quality of management. It is to be emphasised that all three components are equally important and should be treated and implemented as an integrated package.

Financial assistance under the package would cover accumulated losses in the CCS. This however, does not mean writing off of the loans which are yet to be repaid by the borrowers. The co-operatives will have to continue to make efforts to recover these loans and thereby improve their financial health further.

Emphasis is already being laid on building up strong human resource base in the co-operative sector. Efforts are being to lay greater emphasis to promote professionalisation in the management and training of the co-operative personnel so as to enable them to man the various post in the co-operative organization. The training and the evaluation programs are being restructured on scientific lines after capturing the core elements of the information technology and management information system. It is being recognized that only highly professionalized management cadre and trained co-operative personnel would be able to face the competitive challenges from the private sector. Keeping this aspect in view the various training programs are being extended by VAMNICOM and other ICMS with a focus on professionalisation in management and efficiency of co-operative personnel.

CONCLUSION

Credit is one of the crucial inputs for propelling the growth of agriculture. For the past few decades, institutional finance is coming in a big way to help the Indian farmer in increasing the productivity and production. All Rural Financial Institutions have played a crucial role and the role of Co-operatives was laudable till the end of 20th century as the largest purveyor of agricultural credit. However, with the liberalization and the reforms that had swept the banking industry in the past decade and half had diminished their leadership position and made the way for the new players to fill the gap. The share of the co-operatives in agriculture which used to be around 70% even in late '90s had slipped down to less than 30% due mainly to inertia to keep pace with the changes and efforts not matching with those of competitors especially from Commercial Banks of Public and Private sectors.

Due to stiff competition co-operative banks are facing serious challenges at this juncture. The enhanced role of the banking sector in Indian economy and the increasing levels of competition have placed numerous demands on co-operatives. Globalization has also resulted in improved risk management practices. In such circumstances, the co-operatives shall have to shoulder greater responsibilities:

1. To step up their network of services to ensure sustainable growth in agriculture production
2. Generate potentials for rural employment in view of shifting policy of the government.

The co-operative banks have to face the latest challenge in the form of technology adoption. Ironically to mention, many co-operative banks do not even have computers in many of their branches. Presently, the role of co-operatives, no longer remains confined to their traditional activities, but expanded to new economic ventures as in the case of other enterprises in the public or the private sector. It is high time for the co-operative banks to understand the changing environment in banking and rise with suitable strategies to meet the future confidently. The revival package offered by the GOI is to rejuvenate the rural co-operative credit structure. The co-operatives which are the beneficiaries of the financial package, should therefore, utilize it effectively, change according to the present days' requirement and offer according to the customers expectations so as to withstand the competition.