

Address by C. Rangarajan, Governor, Reserve Bank of India

on the conferment of schedule status and successful completion of Mahesh Bank, Hyderabad

1. I have great pleasure in being with you this evening and participate in the function organised to declare the A.P. Mahesh Co-operative Urban Bank Ltd. as a scheduled urban co-operative bank. It is heartening to note that the A.P. Mahesh Co-operative Urban Bank Ltd. is the first urban co-operative bank in the Southern India to acquire the scheduled status. The successive Boards of Management deserve complements for making significant strides in building up a strong capital base aggregating Rs.18.5 crore with deposits to the tune of Rs.149.7 crore and credit portfolio of Rs.85.6 crore as on 31st March 1997 and ultimately to attain scheduled status in less than two decades.

2. Andhra Pradesh has always been receptive to progressive ideas in the field of co-operation. It was due to the untiring efforts of some farsighted people of Ganjam district of the then undivided Madras province, that the Chatrapur and Parlakimidi Urban Co-operative Bank was set up as early as in 1915. At present, I understand there are 69 urban co-operative banks operating in Andhra Pradesh with a deposit base of around Rs. 650 crore.

3. Today in my address I would like to briefly touch on the importance of urban co-operative banks in the country in the context of changed banking scenario.

Urban Co-operative Banking Scenario

4. The urban co-operative banks cater primarily to the needs of lower and middle income strata of our society. Their strength is reflected in the network of outlets with 1653 urban banks and over 4951 of their offices as on 31st March 1997. Since the urban co-operative banks brought under the purview of Banking Regulation Act three decades ago, they have registered rapid progress both in terms of business and spread. The total deposit resources mobilised by the UCBs aggregated Rs.27738.40 crore and their cumulative credit stood at Rs.19086.42 crore on 30th September 1996. The UCBs capital structure was also found to be quite impressive with the owned funds aggregating Rs.4343.46 crore. Notwithstanding the impressive growth of UCBs, urban co-operative banking movement is characterised by regional imbalances. Of the 1653 banks in the country nearly 75 per cent of them are located in four States viz. Gujarat, Karnataka, Maharashtra and Tamil Nadu. Further, these four States also account for 85 per cent of the deposits and advances of UCBs. Heterogeneity is another pronounced characteristic feature of urban banking sector. While there are only 45 urban banks which have a deposit base of Rs.100 crore and above, 863 banks have deposit resources less than Rs.10 crore. As of today, 24 banks have been accorded scheduled status. Seven urban co-operative banks are operating beyond their states of registration.

Reform measures initiated by the RBI

5. RBI has initiated series of policy measures during the last 5 years. Essentially the two-pronged reforms are in regulatory and operational spheres. Pursuant to the recommendations of the Marathe Committee (1993) which examined the licensing policy of new UCBs and other related matters, RBI has been liberal in the licensing of new UCBs. The earlier dictum 'one district one bank' is no longer the determining factor for giving licences to new UCBs. The criteria for issue of licence to a new bank is based on the need for the institution and potential in the proposed centre

for mobilisation of deposits, purveying of credit and ultimately the ability to attain the viability standards within a reasonable period. As a result during the period between May 1993 and March 1997, over 412 proposals were cleared for setting up of new UCBs. Similarly, norms for issue of licences to existing UCBs have significantly been liberalised. The branch licensing policy for UCBs has undergone radical changes. Under the liberalised Branch Expansion Policy over 2070 licences were issued for opening of new branches. RBI has permitted the banks to extend their areas of operation to the entire district inclusive of rural areas in which they are registered. Well managed banks with strong deposits base could, with prior permission, operate from other States also.

6. The thrust on priority sector lending, observance of prudential exposure norms; acceptance of NRI/NRO deposits continues. Urban Co-op. Banks have been permitted to invest in public sector bonds and equity of All India Financial Institutions. UCBs could now subscribe to the units of Unit Trust of India. Recognising the existence of credit gap in the agricultural sector, the UCBs are now permitted to finance value based and other agricultural operations also. Some of the scheduled urban co-operative banks have been permitted to finance equipment leasing and hire purchase activities.

7. I am sure, all these measures will help to increase the operational efficiency of UCBs and facilitate effective participation in allround growth of the economy.

Causes of concerns

8. I may be failing in my duty if I do not dwell on some of the issues which are impeding the growth of urban bank's movement.

Bureaucratisation of co-operative sector

9. The UCBs as they are conceived, must be run on democratic lines so that they truly function as people's institutions. The Brahama Prakash Committee dwelling on this vexatious issue has strongly recommended autonomy for the co-operative institutions and minimising the role of Government officials in the governance of these institutions. I am indeed delighted to note that the Andhra Pradesh Government has taken a lead in legislating the Andhra Pradesh Mutually Aided Co-operative Societies Act, 1995, in granting greater degree of freedom to the co-operatives. This may be followed by the other States so that, among others, the posting of officials on deputation from various departments to the top management of the co-operative banks could be replaced by professional managers.

Weak banks

10. Existence of a large number of weak UCBs has become constant cause of anxiety for RBI. Of the 1653 UCBs as on 31 March 1997, 222 banks have been declared as weak on account of erosion of capital base and part of deposits, unsustainable level of non-performing assets, accumulated losses and non-attainment of viability standards. I may clarify here that the weakness of banks is not a sudden occurrence but the end result of a gradual process of financial deterioration coupled with ineffective management. Hence the weakness has to be identified at the incipient stage itself by the Boards of Management so as to bring about a turn around in the banks' financial position before the malady corrodes the vitals of the institutions. Except in States like Maharashtra and Gujarat, the State Level Review Committees constituted to review the weak banks and formulate the rehabilitation packages, have been quite inactive. Unless a well defined time bound revival plan for a weak bank is prepared and followed by the State/Local Level Review Committees, the extreme steps of winding up/liquidating these institutions may have to be taken.

Professionalising the management

11. Another weak link in urban co-operative banking sector is lack of professionalism. In a competitive financial milieu, where the customers look for innovative products and efficient service, the UCBs cannot insulate themselves from the rising demands of their clientele. They must, therefore, scout for professionals to man the junior and middle levels in management cadres and simultaneously, impart training to all cadres of staff. RBI at its College of Agricultural Banking, Pune has regularly been providing training to the middle and top management of UCBs on various facets of banking. RBI Regional Offices have also been extending faculty support for the training establishments run by UCBs/Federations.

Internal control systems and audit

12. Another related area which has been engaging our attention is the ineffective internal control and audit systems prevailing in UCBs. Over a period of time, the existing systems and procedures have come under severe strain because of multiplicity of factors such as expansion of branches, growth of volume of operations and diversification of business. As you are aware, a weak internal control mechanism is a potential source for perpetration of frauds, the issue cannot be ignored any longer. Sensing the imperative need for strengthening the internal control system, RBI has from time to time issuing detailed guidelines for activating internal control machinery in UCBs. Recognising the felt need for a thorough revamp of existing audit systems prevalent in UCBs, RBI has, in the recent past, appointed a Committee under the Chairmanship of Shri Uday M. Chitale, a prominent Chartered Accountant, for reviewing the audit systems in UCBs and suggesting appropriate model. The Committee has strongly recommended for induction of professionals to carry out the audit of UCBs as the latter are distinctly different from other co-operative institutions. The Committee, among others, suggested for commissioning Chartered Accountants to carry out statutory audit of large size urban banks with deposits over Rs.25 crore. RBI has accepted the Committee's recommendations and advised the State Governments for expeditious implementation of the recommendations.

Technological upgradation

13. The question of absorption of computers in UCBs has also assumed significant importance in the backdrop of financial sector reforms. Although RBI has advised the UCBs with working capital over Rs.5 crore to mechanise their operations, many UCBs are still to register visible progress in this direction. As technological upgradation is sine qua non for a bank's survival in a competitive environment, any delay in computerising the operations of UCBs will only retard their growth. I am happy that Mahesh Co-operative Urban Bank has already successfully completed total automation of eleven branches.

14. The Indian banking and financial system has been undergoing some significant changes in the recent years. The aim of the financial sector reform that is currently under way is to create a system that is both viable and efficient. With the reductions in the reserve requirements, the lendable resources of banks have expanded. They have also greater freedom to determine interest rates. Banks are operating in a more competitive environment and therefore the need to take care of customer requirements has become more urgent. The urban co-operative banks are an integral part of our financial system. They meet a felt need. They have a local touch and meet the requirements of small and medium borrowers. It is however important that they remain financially sound. Efficiency is not a function of size. Small and medium size banks can be efficient and customer friendly as Mahesh Co-operative Bank has shown. The urban co-operative banks must prove the adage "small is beautiful".