

CHAPTER 6

FINANCIAL SERVICES

Introduction

The financial sector provides the conduit for the household savings to be channelised towards productive activities. Its main function lies in enabling financial resource to be allocated for different types of business and agricultural activities. In the Union Territory of Pondicherry (UTP) banks comprise the major segment of the financial sector. Scheduled Commercial Banks(SCB) consisting of public and private sector banks (Chart 1) provide the bulk of the short term capital requirements to business and agriculture. State co-operative banks, urban co-operative banks (Chart 2) along with the non-banking financial companies (Chart 3) provide financial services. The long-term capital requirements of the state are provided by the Development Financial Institutions, and by Private Corporations who have invested in the Union Territory of Pondicherry. Inter-bank call money markets do not exist here, so all treasury operations of SCB are undertaken by their respective head offices outside Pondicherry.

The growth of the financial sector, the extent to which they have succeeded in providing the resources to propel the economy of Pondicherry and the improvements needed to be able to finance higher levels of growth in the period 2000-20 are discussed in this chapter. It consists of five sections a) an overview of the financial sector in Pondicherry, b) a review of the trends in credit delivery system and sector wise credit disbursal and c) the accessibility to credit in terms of spread of bank branches across the state vis-a-vis Tamil Nadu and other southern states d) the operation of co-operative banks e) rural credit disbursal and f) non-bank financial intermediaries.

Overview

Pondicherry economy has been growing at a fast rate in the period 1993-99 to 2000-01. While the total GSDP grew at the rate of 12.8 per cent, the service sector in Pondicherry grew at the CAGR of 10.44 per cent between 1993-94 and 1998-99. The financial sector comprising banking and finance was 8 per cent of the service sector at the beginning of the period and presently forms 12 percent. The banking sector provides the bulk of credit requirements in the Union Territory of Pondicherry. The SCBs and co-operative banks that operate throughout the state have thrived in the post-independence era.

The Second Schedule of the RBI Act 1934 lists the SCBs that consist of Commercial Banks, Regional Rural Banks (RRBs) and other Scheduled Commercial Banks, Urban Co-operative Banks

(UCB) and State Co-operative Banks (Stcob). Nationalised banks including the State Bank of India (SBI) and its associates are the major bank entities. In Pondicherry there are 3 associate banks operating out of the 7 associate banks of the SBI. Pondicherry being largely urban and semi-urban in nature does not have any RRBs. There are no foreign banks operating in the Union Territory of Pondicherry.

Co-operative credit institutions largely serve the rural sector. In terms of reach and volume of operations, co-operative credit institutions occupy an important position by providing almost 70 per cent of rural credit. Urban co-operative banks aim at mobilising savings from middle and lower income urban groups and purvey credit to the weaker sections. In Pondicherry the Co-operative banks are of two-tier structure, so there are no District Co-operative banks as in the 3-tier structure. 53 Primary Agricultural Credit Societies (PACS) are affiliated members of the Pondicherry State Co-operative Banks. Rural co-operative institutions account for 30 per cent of rural deposits and 44 per cent of outstanding loans and advances of the banking sector for agriculture and rural development.⁸

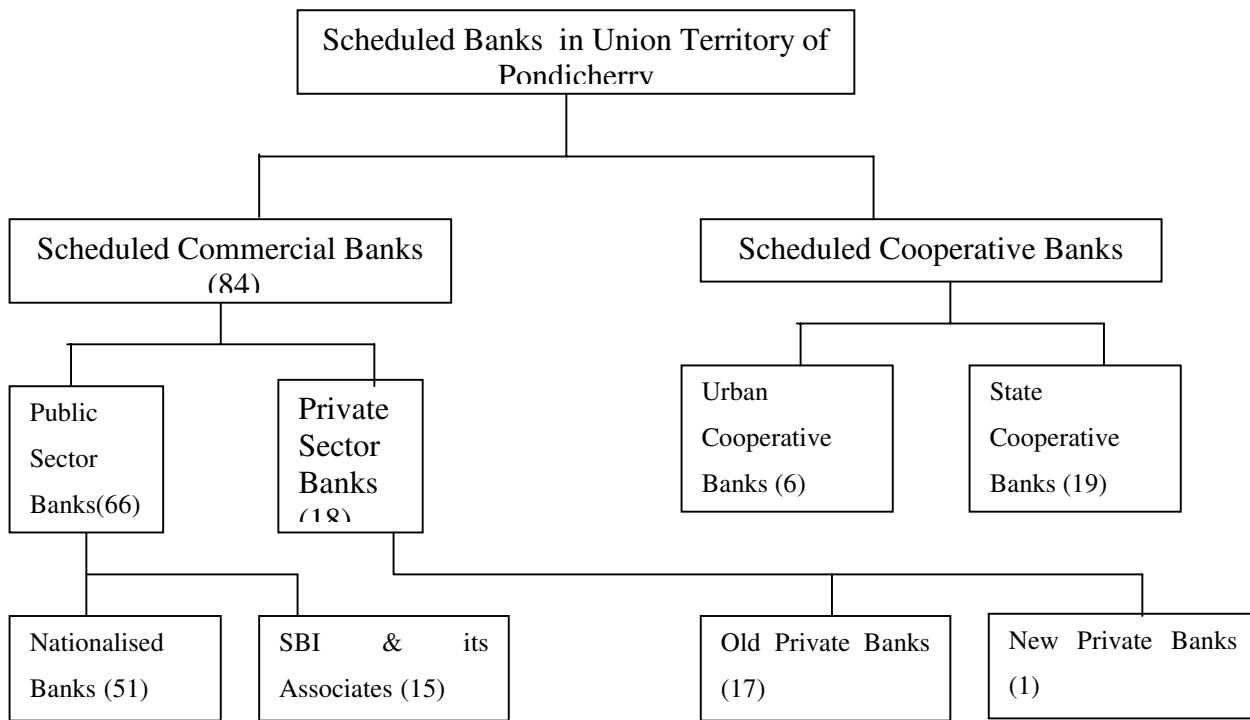
Access to Banks

In the Union Territory of Pondicherry, 34 SCBs with 84 branches are in operation. Of the 34 banks, 21 are in the public sector and all of the rest belong to old private sector except one new private bank. When banks were nationalised in 1966 the bankers had to assume the role of catalysts for economic growth through branch expansion spreading to un-banked areas and providing credit to neglected sectors of agriculture and small industries. In the Union Territory of Pondicherry the lead bank is the Indian Bank. Access to banking facilities is a significant criterion for evaluating the efficiency of the banking sector. Average population per bank in Union Territory of Pondicherry was rather high during 1969 (31,000 per branch) compared to 1996. Population per bank fell to 13,000 in 1996 and has remained more or less constant till 2001 fluctuating between 13,000 and 14,000 (Appendix 1). Population per branch in Pondicherry is very close to the national average (15,000). The states and Union Territories, which have the lowest population per branch, are Goa and Chandigarh (5,000) and Lakshwadeep (8,000) followed by Himachal Pradesh and Punjab at 9,000.

⁸ Reserve Bank of India, "Report on Currency and Finance 1999 – 2000".

Scheduled Commercial Banks

Chart:1 Classification of Scheduled Bank Branches in Union Territory of Pondicherry as in 2001



Source: Prepared from data in Abstract of Statistics- Government of Pondicherry and RBI Report on Trends and Progress of Banking in India 2000-01

Table 6.1
State Wise Distribution of Scheduled Commercial Banks' offices

State/UT	1970	1980	1990	2000
Pondicherry	20	59	69	84
Tamil Nadu	1371	2814	4274	4762
India	12014	32420	60101	65521

Source: Various issues of “Report on Currency and Finance”, RBI Bulletin.

Table 6.2
No. of branches of Scheduled Commercial Banks in Union Territory of Pondicherry

	<i>Types of Scheduled Commercial Banks</i>	1980	1990	2000
1	SBI and its Associates	12	13	15
2	Nationalised banks	37	45	51
3	Public sector bank (1+2)	49	58	66
4	Other Scheduled commercial banks (PRIVATE)	10	11	18
5	All scheduled commercial banks (3+4)	59	69	84

Source: Various issues of “Report on Currency and Finance” and RBI Bulletin.

In 1969 there were only 12 branches of SCBs in Pondicherry, which rose to 59 in 1980, to 69 in 1990 and to 84 in 2000 (Table 6.2). We are however likely to see reduction in the number of private banks as well as nationalised banks in the future, as the reform measures and stringent prudential norms of income recognition guidelines are implemented by the RBI. Consolidation and mergers of weak banks with stronger ones has been on the anvil since 1992. This trend should not be construed as a reduction in the banking facility available to the people of Pondicherry. On the contrary as Information Technology is being rapidly introduced at different levels of the banking sector it is possible that internet related banking facility as well as ATMs will spread rapidly to provide easier access to banking facility in the Union Territory of Pondicherry . However, the new breed of private sector banks that have emerged in the post reform era are likely to become major players although their presence is not significantly visible now.

Deposits Mobilisation Trends and Credit Disbursal

Deposits of SCBs in Pondicherry, which include fixed deposits, current deposits, saving deposits and others such as recurring deposits totalled Rs.14.01 crore in 1970 at 1980-81 prices. This constituted 91 per cent of total deposits in the state excluding those of state Co-operative bank and urban Co-operative banks. The deposits rose to Rs.58 crore in 1980 (Table6.3). The growth of deposits was relatively moderate in the eighties. The decade of the nineties however was similar to the eighties when deposits rose by approximately 2.5 times. We find that deposits rose by 12 per cent in 2001 over the previous year. The credit-off take in the last three decades has been relatively modest and the credit-deposit ratio has been on the decline. The growth of deposits is made higher because of the large pension and average payments received from France by the French citizens. Apparently, the demand for credit in the state has not kept pace with that. The phenomenon of rising deposits without balancing growth in credit off take can perhaps be explained partly by the existence of large remittances of pension and other welfare transfers for the French citizens of

Pondicherry who continue to deposit their earnings in to commercial banks. Consequently bank deposits continue to grow.

Table 6.3
Trend and Pattern of Deposits and Credits of Scheduled Commercial Banks

Year	Different Key Indicators					Credit/Deposit Ratio
	No. Of offices	Deposits*	Credits*	Deposit* Per Office	Credit* Per Office	
1980	50	58.00	33.27	116.00	66.54	57.36
1985	63	83.31	45.23	132.23	71.80	54.30
1990	69	130.72	71.85	189.45	104.13	54.97
1995	72	189.77	79.31	263.57	110.16	41.79
2000	84	312.80	105.47	372.38	125.56	33.72
2001	84	351.08	113.51	417.96	135.13	32.33

*(Rs.in Crores)1980-81 constant prices

Source: Primary source: Reserve Bank of India Bulletins

Secondary Source: - Directorate of Economics and Statistics, Government of Pondicherry , “Abstract of Statistics” vrious issues.

Table 6.4
Compound Growth Rate of Deposits and Loans of Scheduled Commercial Banks for 10, 5 & 3 year period

Year	1990-2001	1990-1995	1996-2001	1990-1992	1993-1995	1996-1998	1999-2001
Deposits	9.64	7.58	10.79	8.09	7.56	8.79	11.33
Loans	4.55	2.39	8.33	-2.87	8.08	-0.29	10.24

Source: Computed from data (1980-81 prices) in the “Abstract of Statistics” - Directorate of Economics and Statistics, Government of Pondicherry

The credit-deposit ratio for Pondicherry follows the all India trend. The rank of Pondicherry was 16th in1991 and is 17th in 2001. (Appendix 2). Although it has remained stable in comparison to the other states, the credit-deposit ratio has been declining. Tamil Nadu has the second highest credit-deposit ratio in the country after Chandigarh Union Territory.

The rate of increase of bank deposits is an accepted criterion for measuring the growth rate of financial resources of an economy. In Pondicherry the annual compound growth rate of bank deposits of SCBs was 9.64 per cent in the decade of the nineties which is an indicator of the growth of the financial sector. The rate of growth of loans was 4.55 per cent in the same period indicating

much lower level of fund usage and this is again reflected in the marked decline in the C/D ratio throughout the last decade. There has been no shortage of financial resources in the state.

Since 1996-97 there has been steady upsurge in term deposits while savings and current deposits have stagnated. As the majority of the banks are in the public sector they are perceived to have little or no risk. Despite the recent reduction in the interest rate households continue to repose faith in banks and rush to them when the stock market is doing badly. Pondicherry has been no exception. In 1990-91 the total current deposits in the state of SCBs was Rs.36.82 crore which fell to Rs.2.66 crore in 1991-92 at the height of the boom more or less in the same way as in the rest of the country. It rose in 1992-93 to Rs.59.8 crore and grew to Rs.166 crore in 1999-2000. Other southern states also followed the same trend (Appendix 3, Graph 1). Interestingly, the term deposits in all the states continue to grow at a steady rate throughout the last decade followed by the savings deposits.

French Pensioners

There is a sizeable population of French citizens in the Union Territory of Pondicherry, it being a former French colony. These citizens of France also known as Franco-Pondicherrians were employed in the defence services as soldiers or in administrative service or in private employment in France or in French interests during the French colonial days. They now draw pensions and other welfare benefits from the French Government and their progeny and survivors who are automatically French citizens are also entitled to the benefit of these pension remittances. Apart from retirement pensions they avail disability pension for handicapped individuals and social welfare for indigent individuals as well as medical benefits, and old age pensions. The widows are entitled to one-third the pension of the retirees.

A survey conducted by the lead bank in Union Territory of Pondicherry showed that there are 1,600 households of French nationals in the state who are drawing retirement pensions for working with the French government and the French Army. Service in the French army for a minimum of 15 years enables a French citizen to receive pensions ranging from Rs.35,000 to Rs.1.5 lakh per month.⁹ The French government remits welfare transfer payments for the needy elderly indigent individuals who are French citizens in Pondicherry which ranges from 260 FF (French Francs) to 1,200 FF, which is around Rs.1,820 to Rs.8,400 per month as per the current exchange rate of Indian Rupees to French Francs. While most of these remittances are routed through the

⁹ Raji Sugumar V. "Socio-Cultural Study of the Franco –Pondicherrians" PhD thesis, Pondicherry University, 1998.

United Commercial Bank, which conducts the Treasury operations for the French government in Pondicherry a number of retirees receive their pension cheques directly from France bypassing the consular office. On the average the monthly remittance is estimated to be in the range of Rs.6 to 7 crores with the minimum remittance being Rs.30,000 and the maximum as high Rs.80,000 per month. According to another estimate, the RBI is paid Rs.15 crore as foreign exchange per month. The French pensions which accumulate in the different banks of the Union Territory of Pondicherry do to some degree explain the high growth of deposits in banks.

Sector-Wise Distribution of Loans and Advances by SCBS

The pattern of sector-wise loans outstanding to different sectors of the economy in the Union Territory of Pondicherry by SCBs appears to be changing in the last decade in response to the development in the economy (Table 6.5). There is a marked decline in credit off take by agricultural / farm sector while disbursal has been growing in the manufacturing, trade¹⁰ and finance sectors. The growth in the credit disbursal to industry has risen due to the growth of the industrial activity in the Union Territory of Pondicherry. Consequently as more industrial units were set up the agricultural land has been converted to industrial use. With greater urbanisation (66.5 per cent), the profile of Pondicherry has changed remarkably. The nineties also witnessed a remarkable growth in the services sector which is included in the miscellaneous sector.¹¹

In 1990, 15.85 per cent of the total outstanding loans went to agriculture, but a decade later it came down to 9.15 per cent, although in absolute value it rose from Rs.29.42 crore in 1990 to Rs.49.50 crore in 1999-2000. On the other hand loans to industries¹² have more than doubled over the decade from Rs.91.56 crore to Rs. 227.40 crore (Table 6.5, Graph 2). The service sector (Excluding Trade & Finance) has risen by almost four times whereas trade and finance sector rose only three times.

¹⁰ Trade includes 1. Wholesale trade and 2.Retail trade.

¹¹ Miscellaneous includes a). public utilities and services such as loan to hotel and restaurant, recreation services, warehousing, agents, repairs and servicing works, etc. b).Education. c). Various types of loans to banking staffs and d). All other loans not classified elsewhere or activities not adequately described.

¹² Industry Includes:1.Mining& quarrying 2. Food 3.Beverages 4.Textiles 5. Paper& paper products 6. Leather & leather products 7. Rubber & Rubber products 8. Chemical & chemical Products 9. Petroleum, coal & nucl fuels, 10.Cement and Cement Products 10.Basic metal & metal products 11. Engineering 12. Vehicles, parts & trans equipment 13. Other industries 14. Electricity, gas and water, and 15. Construction.

Table 6.5
Sector Wise Distribution of Loans (Rs.crore at constant prices)

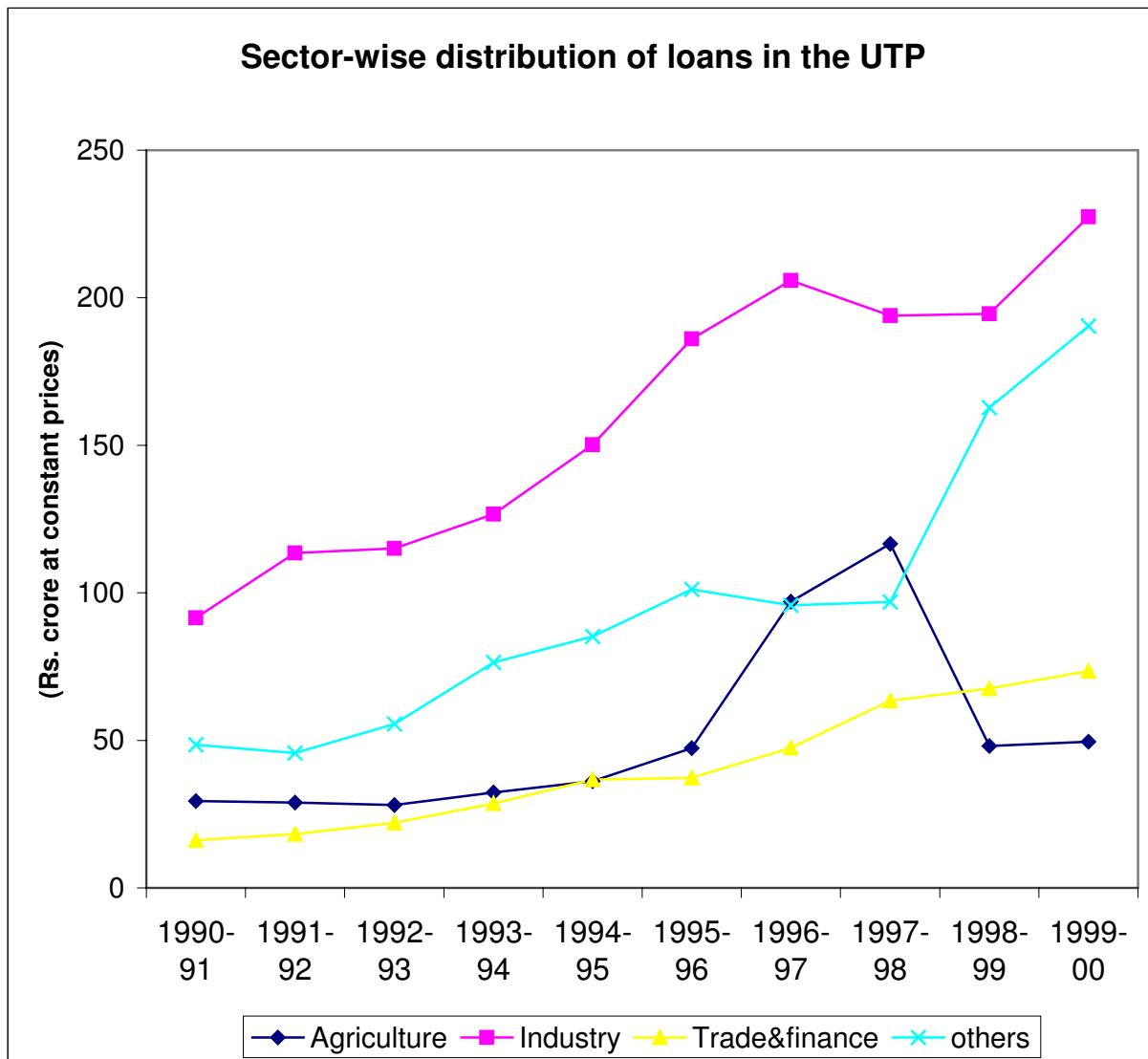
	1990-91	1991-92	1992-93	1993-94	1994-95	1995-96	1996-97	1997-98	1998-97	1999-00
Agri.	29.42 (15.9)	28.93 (14.0)	28.1 (12.7)	32.29 (12.2)	36.13 (11.7)	47.4 (12.8)	97 (21.7)	116.6 (24.8)	48.1 (10.2)	49.5 (9.2)
Indus.	91.56 (49.3)	113.5 (55.0)	115.1 (52.1)	126.6 (47.9)	150.2 (48.7)	186 (50.0)	205.8 (46.1)	193.9 (41.2)	194.5 (41.1)	227.4 (42.1)
Trade& finance	16.18 (8.7)	18.2 (8.8)	22.1 (10.0)	28.61 (10.8)	36.7 (11.9)	37.3 (10.0)	47.5 (10.7)	63.4 (13.5)	67.6 (14.3)	73.5 (13.6)
Others	48.49 (26.1)	45.71 (22.2)	55.6 (25.2)	76.4 (28.9)	85.2 (27.6)	101.2 (27.2)	95.8 (21.5)	96.9 (20.6)	162.7 (34.4)	190.4 (35.2)
Total	185.7 (100)	206.3 (100)	220.9 (100)	263.9 (100)	308.2 (100)	371.9 (100)	446.1 (100)	470.8 (100)	472.9 (100)	540.8 (100)

Source: Money and Banking CMIE , October 1998-2001. Figures in brackets are percentages

The manufacturing industries sector was booming in the last decade and this trend is likely to remain in the future (see Graph 2). It is also necessary to identify areas of the growth for the future. As per our discussions with local officials the government has identified tourism as major source of revenue, and this sector is also already growing rapidly (see Graph 2). This expansion is perhaps due to the pro-active policy of the Union Territory government. The credit off take exhibited by the loans disbursed by SCBs to the service sector especially after 1997-98 are indicative of the likely trend in the future.

Loans received by the Trade and Finance and others sector have shot up from 34.8 per cent in 1990-91 to 48.8 per cent ten years later. The thrust area of growth in Pondicherry is the services sector and credit disbursal figures of the past decade bear witness to it. This also reiterates the view that the momentum of growth is inherent in the tertiary sector, already experiencing a growth rate of almost 20 per cent in the last decade. Deliberate policy to support the rural sector through NABARD's refinance strategy and targeting of self help groups will reduce hardships for those associated with agriculture and allied activities.

Graph 2.



Source: Calculated from data in CMIE Centre for Monitoring Indian Economy. Money & Banking October – 2000

Innovations

Housing Finance

Discussions with officials from the lead bank and other commercial banks revealed that banks which provide loans and advances to medium and small-scale industries often faced

problems of poor recovery leading to mounting non-performing assets.¹³ Hence banks have been facing increased amount of defaults and non-repayments of loans. Nationalised Banks instructed their regional and local branches to diversify their customer base and business focus.

The increasing pressure on banks to raise efficiency level through reduced non-performing assets has forced managers to be far more cautious in their lending. Deposits are now being shifted to Treasury Bill investment for lower but safe return. The nationalised banks looking for new avenues of business found the housing sector loans to salary earners as an untapped avenue of lending and a rich potential market for growth in Pondicherry. It is observed that banks in Pondicherry are shifting their loans and advances into the housing sector. Pondicherry is rapidly growing in its urban stature as more and more non-agricultural activities are undertaken. Banks are competing with housing finance companies to provide housing loans to salary earners. This scheme was introduced in November 2001 and it has helped many banks to turn the corner in Pondicherry.

Banks are offering housing loan within the range of 11.5 per cent to 10 per cent of interest to all types of salary earners working in both the government & private sector. This is a much lower interest rate than the range of 14 per cent to 16 per cent charged by housing finance companies. The procedures with regard to documentation for granting loans has been simplified and lead time for loan processing has been reduced. So far Rs.8 crore housing loans have been disbursed since the inception of the scheme in 2001. The annual size of their business is expected to be Rs.40 to 50 crore. The shift of business focus is expected to raise profits for the nationalised banks and usher greater profitability and efficiency. The advantage of this new business policy lies in the ability of the bank managers to coerce the borrowers of housing finance to repay promptly or be socially ostracised by colleagues where the salary earner is employed. Bank mangers are increasingly finding that housing finance is a lucrative business solution to the shrinking bottom line.

Information Technology

The financial sector reform of the nineties and the opening up of the economy and integration with global markets have facilitated faster automation of banks procedures through computerisation.

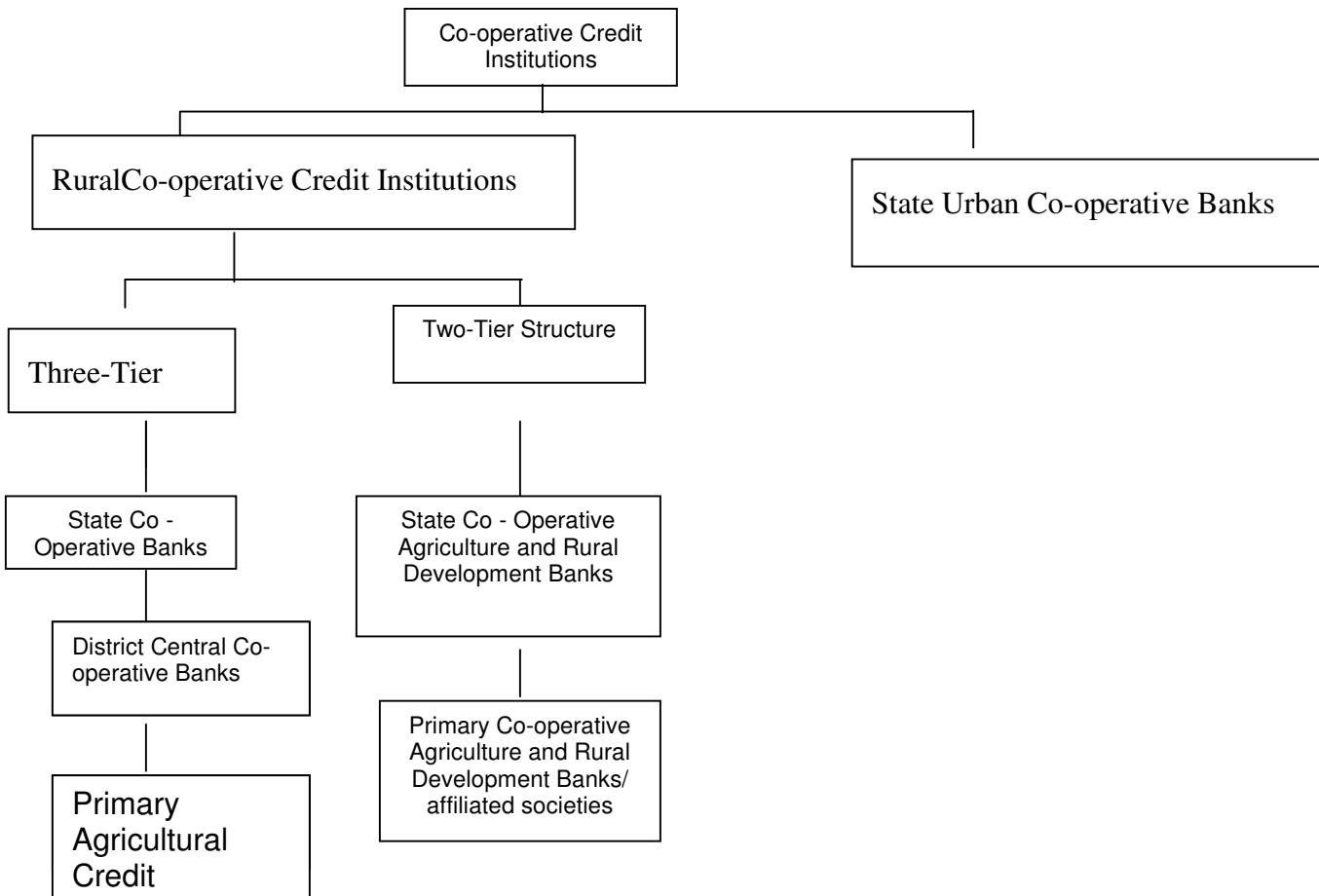
¹³ Prior to Dec 1992, an asset was classified as Non Performing Asset if the amounts due remained 'Past due' for more than two quarters. With effect from March 31, 2001 an advance has to be classified as NPA , if interest and /or instalment of principal remain over due for a period of more than 180 days in respect of a term loan. For moving towards international best practices and to ensure greater transparency, the intention to adopt the 90 day norms for recognition of loan impairment from the year ending March 31, 2004 was announced in the statement on monetary and credit policy for the year 2001-2002.(Source: RBI Report on Trends and Progress of Banking in India 2000-01).

This has led to reducing operational costs enhancing quality of customer service in the medium term. The technology adoption and absorption has so far revolved around two basic themes: Retail Banking and Corporate Banking. The former has leaned more on basic technology infrastructure. The challenge for Indian banks is the principle of “all banks to all people” and “banking at the nearest bank”. It is imperative therefore to integrate retail-corporate model into the rural-urban co-development paradigm. High level of customer service, timeliness, efficiency and risk management can be enhanced if infrastructure is upgraded smoothly. However, inter bank connectivity through Public Switching Telephone Network (PSTN) and network communication, through VSAT is an essential step to achieve this goal. The two major areas where retail banking can grow rapidly at the customer interface level are the Automatic Teller Machine (ATM) and the Credit Card.

Banks under increasing pressure to improve their profit performance through efficient credit disbursal and lower cost of operation are now closing uneconomic branches and investing in Automatic Teller Machines (ATMs) to provide teller service at a much lower cost. The annual maintenance cost per unit of ATM is in the range of Rs.30,000 to Rs.10,000 apart from the initial installation cost. A minimum 10,000 card holders per ATM will make this investment profitable. Since ATMs serve both the purpose of payout and receipt of cash it can reduce the operational costs substantially. So far there are 13 ATMs installed by 3 public sector banks including SBI & one new private sector bank in Pondicherry. The installation of ATMs must be accompanied by a parallel programme of educating customers about the convenience of 24 hours access to cash and cheque deposit facility. Banking operation without human interface has to be popularised for its success.

Credit cards which have gained considerable popularity in metropolitan cities are accepted at only a limited number of retail showrooms and three star hotels in Pondicherry. It is visualised that credit cards will become a major instrument of bank transactions. The lead bank in Pondicherry is offering overdraft facility through credit cards at 7 centres including Pondicherry.

Chart 2: Organizational Structure of the Co-operative Credit Institutions
Co-operative Banks



State Co-operative Banks

Co-operative credit institutions occupy an important position in the financial system of the economy in terms of their reach, volume of operations and the purpose they serve. The organisational structure of co-operative credit institutions is given in Chart 2. Rural co-operative banks play a pivotal role in the rural credit delivery system. This section surveys the Urban Cooperative Bank and State Co-operative Bank which are the two types of Co-operative banks operating in the Union Territory of Pondicherry providing up to 5 per cent of the total bank credit in the region.

In the Union Territory of Pondicherry the co-operative banks are organised on the two-tier structure. The primary credit societies are members of the State Co-operative Bank of Pondicherry; there are no District Co-operative Banks in Pondicherry. The Pondicherry State Co-operative Bank

started functioning in October 1958 and was registered under the Co-operative Society Act, 1904. It received license from RBI in 1994 and the scheduled status in 1995 coming under the purview of the Banking Regulation Act 1949. It is statutorily inspected by the NABARD. The Bank started operations with a share capital of Rs.0.06 crore and working capital of Rs.0.117 crore, which have now grown to Rs.4.63 crore and Rs.142 crore respectively. The major contribution of the share capital is from the affiliated societies and the state government; the working capital consists of reserves, deposits and loans from the state government and NABARD. The Bank is managed by the Administrator appointed under the Pondicherry Co-operative Societies Act 1972. The present Administrator of the bank is the Registrar of Co-operative Societies, Pondicherry.

At present there are 19 branches of the Pondicherry State Co-operative Bank, of which four are in the outlying region of the city. There are 53 primary credit societies, whose activities range from agriculture to spinning, weaving, sugar mills and fisheries. The Bank provides various types of loans:

- Seasonal agricultural operations,
- Working capital loans to Weavers Co-operative Society,
- Loans for farm and non-farm sectors,
- Cash credit limits to Co-operative Societies including the Co-operative Sugar Mills and Spinning Mills,
- Conversion of short term agricultural loans given on account of natural calamities into medium term loans.

The Bank also issued a term loan to Co-op. Spinning Mill at Karaikal under consortium arrangement to the extent of Rs.470.00 lakhs. The total loans outstanding as on 31st March 2001 amounted to Rs.6,251.98 lakh. Table 6.6 gives the sectoral deployment of advances from 31st March 1997 to 31st March 2001.

As there was no significant growth of outstanding loans and advances in the past 3 years several new schemes to diversity business opportunities for the Bank were initiated, such as a) House Mortgage Loan, (b) Agricultural Jewel Loan to agriculturists with lower rate of interest @ 13 per cent p.a. (c) Personal Computer Loan to individuals, and (d) Loans to the public on Government Servant Surety. These new schemes have turned out to be popular and thus broadened the scope of issuing more loans in the future. The Bank has further framed Subsidiary Rules for

providing a) cash credit to businessman, (b) cash credit to agriculturists and has also taken steps for relaxing/amending various Subsidiary Rules for increasing outstanding loans.

Table 6.6

Particulars	1996-97	1997-98	1998-99	99-2000	2000-01
1. S.T. Loan (Agr 1)	850.81	935.61	991.51	692.40	619.98
2. M.T. Loan (Agr 1)	77.68	64.96	65.35	40.77	32.52
3. S.T. Loan (Others)	44.92	43.66	148.20	39.44	40.00
4. M.T. Loan (Others)	805.93	772.14	696.71	857.09	1045.52
5. L.T. Loan (others)	476.30	459.34	324.95	207.45	198.52
6. C.C (Weavers)	497.61	706.17	787.66	792.01	865.67
7. C.C (Consumers)	248.96	139.59	132.59	89.00	87.68
8. C.C (Others + O.D)	206.15	185.06	219.55	220.09	277.68
9. Salary Earners Soc.	682.54	558.90	933.25	983.84	837.98
10. Transport Loans	59.07	55.81	33.53	25.79	19.35
11. Jewel Loans	526.66	570.04	477.75	379.35	379.48
12. NFS (SSI Units Loans)	35.68	37.32	38.85	38.27	34.50
13. Loan on Deposits	260.21	107.22	137.23	119.29	185.10
14. Sugar Mills	416.84	881.20	910.14	1457.08	1321.96
15. Spinning Mills	344.10	280.70	35.86	151.87	305.98
Total	5533.46	5798.09	6248.13	6,093.74	6,251.98

Source: Note on the Working of the Pondicherry State Co-operative Bank Limited , March 2001 prepared by themselves

Loans to agricultural activities both short term and medium term are on the decline while loans and advances for non-farm activities have increased for the Bank from Rs 8.1crore to Rs10.5 crore. The loans to salary earners have doubled in the span of 5 years of 1996-2001. The Sugar mills have increased their cash credit off take by three fold in the same time period. The Sugar mill industry, despite downturn globally, seems to be picking up in the Union Territory of Pondicherry in terms of its credit requirements. On the other hand there is a sharp fall in the cash credit availed by the consumers cooperative societies. A similar trend is also visible in loans to Transport Owners Society and to members for purchase of jewellery.

Table 6.7
Some Key Indicators (Rs.crore)

		1998-99	1999-2000	2000-2001
1.	Deposit per employee	0.3961	0.4980	0.5075
2.	Advance per employee	0.2961	0.2874	0.2949
3.	Non – Interest income as percentage to total income	1.46	1.60	1.21
4.	Establishment expenses as percentage to total expenses	24.19	25.54	22.75
5.	Profit as percentage to working capital	1.1	0.78	1.08
6.	Establishment expenses as percentage to working capital	2.5	2.4	2.5
7.	Cost of management as percentage to working capital	3.3	3.2	3.1

Source: The Pondicherry State Co-operative Bank Ltd 43rd Annual Report 2000-2001

The Pondicherry State Co-operative Bank which has been in operation for more than four decades, has been through periods of uncertain business. We note that it has had negative earnings in the eighties and nineties. The recent surge of failures of cooperative banks highlight the need to restructure their regulatory guidelines keeping in view their intrinsic character. Their functioning and constraints in operation have been examined by a High Power Committee (HPC), a Task Force and an Expert Group to devise ways to improve their efficiency and make the credit delivery system more viable. The State Cooperative Bank of Pondicherry notwithstanding its earlier records has become profitable in the last three years of its operations. However, profit as a percentage of working capital has been less than 2 per cent, while establishment expenses as percentage of working capital is more than 2 per cent and cost of management as percentage of working capital is more than 3 per cent. These indicate that there is scope for increasing the efficiency of operations through more economic use of working capital.

Table 6.8
Trend and Pattern of Different Assets of State Co-Operative Bank (Rs.crore)[^]

Year	Deposit				Total Deposits	Loans	Profit &loss credit balance**	Interest recoverable (assets) – Interest Payable (liabilities)*
	Fixed	Current	Saving	Others				
1980	2.034 (65.55)	0.337 (10.86)	0.720 (23.21)	0.012 (0.38)	3.102 (100)	2.806	0.027 (0.81)	0.067 (2.01)
1985	1.864 (58.96)	0.429 (13.55)	0.869 (27.47)	0.0004 (0.01)	3.162 (100)	3.276	0.022 (0.42)	-0.003 (-0.06)
1990	9.080 (79.47)	0.757 (6.62)	1.589 (13.91)	0	11.426 (100)	9.810	0.255 (2.24)	0.120 (1.05)
1995	9.911 (72.52)	1.487 (10.88)	2.269 (16.60)	0	13.667 (100)	10.679	0.111 (0.94)	-0.001 (-0.01)
2000	15.125 (69.60)	2.503 (11.52)	4.104 (18.89)	0	21.733 (100)	11.609	0.220 (1.75)	5.36 (42.72)
2001	13.665 (63.77)	2.941 (13.73)	4.821 (22.50)	0	21.427 (100)	11.450	0.304 (2.44)	5.63 (45.24)

Source: Table prepared from data in various issues of “Abstract of Statistics”- Government of Pondicherry (1980-81 constant prices).

Note :- ^1980-81 Price ** Profit &loss credit balance as a percentage of Loans to cooperative Society * Interest recoverable (assets) – Interest Payable (liabilities) as a percentage of Loans to Cooperative Society and Individuals assets) in the “Abstract of Statistics”- Government of Pondicherry (1980-81 series)

Urban Co-operative Bank

Urban Co-operative Banks (UCBs), aim at mobilising savings from the middle and low-income urban groups and purvey credit towards the weaker sections. The major part of credit from UCBs is channelised towards priority sector segments. The Union Territory of Pondicherry which consists of a sizeable urban and semi-urban population has UCBs operating within it territory.

The trend of various financial indicators of UCBs in the Union Territory of Pondicherry is presented in Table 6.9. The deposit mobilised by UCBs was only Rs.0.39 crore in 1980 which went up to Rs.7.11 crore in 2001. The major part of deposits at present comes from fixed deposits followed by saving deposits and current deposits. The share of fixed deposits in total deposits has increased over the years. The difference between interest recoverable and interest payable as a percentage of Loans remains less than 1 per cent, which is an indicator of weak returns earned by

UCBs. There is an urgent need for the UCBs to improve the interest earning capacity and to identify other sources of income to improve their financial position.

The financial fragility of these banks could be partly traced to the increased competition among banks after reforms in the nineties and to the interdependence between financial institution through inter-institution exposure and payment settlement channels. The UCBs appear to be exhibiting traits of weakness as they were found to be incurring losses in several years after 1995. Corrective steps need be taken to strengthen the cooperative credit delivery system in the urban areas of Pondicherry.

Urban Cooperative Banks in Pondicherry are at present exhibiting features of weakness. Those which are sick should be closed down or amalgamated with stronger ones. Weak banks having imprudent lending norms are a hazard to the financial health of the entire region as financial instability is contagious and endemic.

Policy Initiatives of Rural Credit Disbursal

Major policy initiatives at the national level relating to co-operative credit institutions and rural credit system since 2000-2001 include the launch of new tranche of Rural Infrastructural Development Fund (RIDF), enhancement of KCC (Kissan Credit Card), formation of Self Help Groups (SHG) and micro credit. Prudential and operational norms relating to UCBS have been changed significantly.

The concept of Potential Linked Credit Plan (PLP), introduced by NABARD can be used to judge credit requirements in Pondicherry. The estimated credit flow in the UT of Pondicherry during the Tenth Five Year Plan period (2002-2007) in terms of potential available and likely to be developed aggregate to Rs.1,193.30 crore. The estimated credit requirements in expected to increase from Rs.1,92.78 crore during 2002-03 to Rs.308.66 crore during 2006-07. The projected amount under the PLP for 2002-03 is Rs.198.72 crore, which represents a 9.95 per cent increase above the PLP projection of 2001-02. A sizeable share amounting to 38.6 percent has been allocated to Non-Farm Sector followed by 'Other Priority Sector' (25.9 per cent) and Crop Loans (20.4 per cent). Storage and Marketyard and Minor Irrigation accounted for 3.5 percent and 3.3 per cent, respectively followed by Dairy Development (3.2 per cent), Farm Mechanisation (2.4 per cent) and Fisheries (1.0 per cent). The share of remaining activities accounts for less than 1 per cent each. (Appendix 4).

Table 6.9
Trend and Pattern of Different Assets of Urban Co-Operative Bank (Rs.crore)

Year	Deposit				Total Deposits	Loans	Profit & loss credit balance	Spread Interest (assets) – Interest (liabilities)
	Fixed	Current	Saving	Others				
1980	0.321 (81.19)	0.004 (0.89)	0.071 (17.92)	0	0.395 (100)	0.356	0.003 **(0.69)	0.005 *(1.20)
1985	0.622 (76.88)	0.017 (2.15)	0.170 (20.98)	0	0.810 (100)	0.861	0.023 **(2.59)	0.031 *(3.51)
1990	0.750 (34.23)	0.051 (2.34)	0.483 (22.03)	0.907 (41.40)	2.191 (100)	1.505	0.073 **(4.82)	-0.040 *(2.66)
1995	0.183 (21.23)	0.028 (3.30)	0.556 (64.40)	0.096 (11.08)	0.863 (100)	2.098	0.026 **(1.25)	-0.005 *(0.26)
2000	5.834 (84.72)	0.156 (2.27)	0.896 (13.01)	0	6.887 (100)	4.879	0.119 **(2.44)	-0.022 *(0.45)
2001	5.947 (83.60)	0.131 (1.83)	1.036 (14.57)	0	7.114 (100)	5.965	0.233 **(3.90)	0.037 *(0.63)

Source: Table prepared from data in “Abstract of Statistics” - Government of Pondicherry (1980-81 prices)

^ : 1980-81prices. ** Profit &loss credit balance as a percentage of Loans (assets). * Interest (assets) – Interest (liabilities) as a percentage of loans (assets). Figure in brackets are percentages of total

However, the flow of Ground Level Credit disbursement to non-farm sectors of 1997-98 during the Ninth Five Year Plan was 49.6 per cent. Term loans for minor irrigation, farm mechanisation and dairy development attracted a higher allocation than proposed for the Tenth plan; the shares being 4.57 per cent, 5.57 per cent and 4.6 per cent, respectively. The other activities including land development, plantation and agriculture, poultry and fisheries attracted less than 17 per cent of total disbursement (Appendix 5).

Of the six blocks in the Union Territory of Pondicherry Reddiarpalayam Block account for (35.2 per cent) of the total PLP projection for the year 2002-2003 followed by Karaikal (20.4 per cent), Villainur (17.3 per cent), Karikalampakkam (16.5 per cent), Mahe (6.1 per cent) and Yanam (4.5 per cent).

The credit-deposit ratio of rural sector banks was 49.4 per cent at the end of March 2001. Efforts are on to raise it to sixty percent. The recovery performance has been declining and stands at to 52 per cent (June 2001) as against 60.3 per cent in 1996.

The Union Budget 2001-02, provided for an increase of the corpus of Rural Infrastructure Development Fund (RIDF) VII from Rs.4,500 crore during 2000-01 to Rs.5,000 crore 2001-02. To help the state, the rate of interest charged on RIDF lending has been reduced from 11.5 per cent to 10.5 per cent. The KCC scheme which turned out to be very successful as its popularity among farmers indicates has been further stimulated by banks being authorized to provide personal insurance package to the KCC holders up to a maximum of Rs.50,000. The premium burden being shared by card issuing institutions. KCC scheme introduced in 1999 at UTP is popular among both farmers and issuing bankers. Farmers have the flexibility to avail of production credit and also avoid procedural delays in getting credit sanctioned. At present 1,700 KCC have been issued for the disbursal of loans and the card is valid for 3 years. Furthermore, to ensure that small and medium farmers are not denied access to KCC facility, NABARD in consultation with the RBI disposed with the floor limit of Rs.5,000 earlier suggested for coverage under the scheme. The loans dispersed under KCC scheme were also brought under the Rashtriya Krishi Bima Yojana of the General Insurance Corporations and personal accident insurance cover of Rs.50,000 for death and Rs.25,000 for disability from 2001-02 would be provided to KCC holders.

Micro-Finance-Informal Credit Delivery System

The Self Help Groups (SHG), which constitute an informal credit delivery system, are now increasingly recognized as an effective mechanism for reaching a large number of un-banked sections of the rural poor. The SHGs have been formed to help banks in reducing transaction costs and risk and also to improve recovery performance. The micro-finance groups in UTP include SHG and CMG (Credit Management Groups). CMG organized by M.S.Swaminathan Research Foundation (MSSRF) participate in research oriented farming, dairying, goat rearing, fisheries and allied activities. The profile of micro finance existing in Pondicherry is given below.

Table 6.10
The Micro Finance profile in the UTP is as presented below

Total number of blocks in the UTP	6
No. of blocks where SHGs exist	6
Total number of blocks where SHGs are credit linked	3
No. of NGOs in the UTP	50
No. of NGOs participating in linkage programme	3 (M.S.Swaminathan Research Foundation, CERD and Mangalam Society)
No. of additional NGOs to be roped in during the year	2
Total No. of Bank branches in the UTP (Rural and Semi-Urban)	Com.Banks : 41 Coop. Banks: 14
Of which : No. of branches participating in linkage programme	Com.Banks : 17 Coop. Banks : Nil
No. of additional branches proposed to be roped in	Com. Banks : 6 Coop. Banks : 7
No. of Govt./other agencies participating	3 (Women Development Corporation, Krishi Vigyan Kendra & PONLAIT)
No. of Govt./other agencies likely to participate	5 (District Rural Development Agency / BDO, Agriculture, Animal Husbandry, Fisheries and Social Welfare)

Source: Potential Linked Credit Plan, Union Territory of Pondicherry, X Five Year Plan Period with Blockwise Projections for 2002-03..

Non-Banking Financial Companies

Non-Banking Financial Companies undertake a wide spectrum of financial activities ranging from hire purchase and leasing to pure investments. NBFCs are, in terms of the Section 45-I(f) read with Section 45-I(c) of the RBI Act.1934 as amended in 1997, involved in the principal business of receiving deposits and engaging themselves in lending, investments in securities, hire purchase finance or equipment leasing. There are broadly 8 types of NBFCs: (1) equipment leasing companies, (2) loan companies, (3)hire purchase companies, (4)investment companies, (5)mutual benefit companies(Nidhis), (6)Miscellaneous non-banking companies(Chit funds), (7)residuary finance companies and (8)housing finance companies.

Given this diversity NBFCs cater to a wide range of demands for many types of loans. The salient characteristic of NBFCs is their non formality. Documentation for availing of loans is

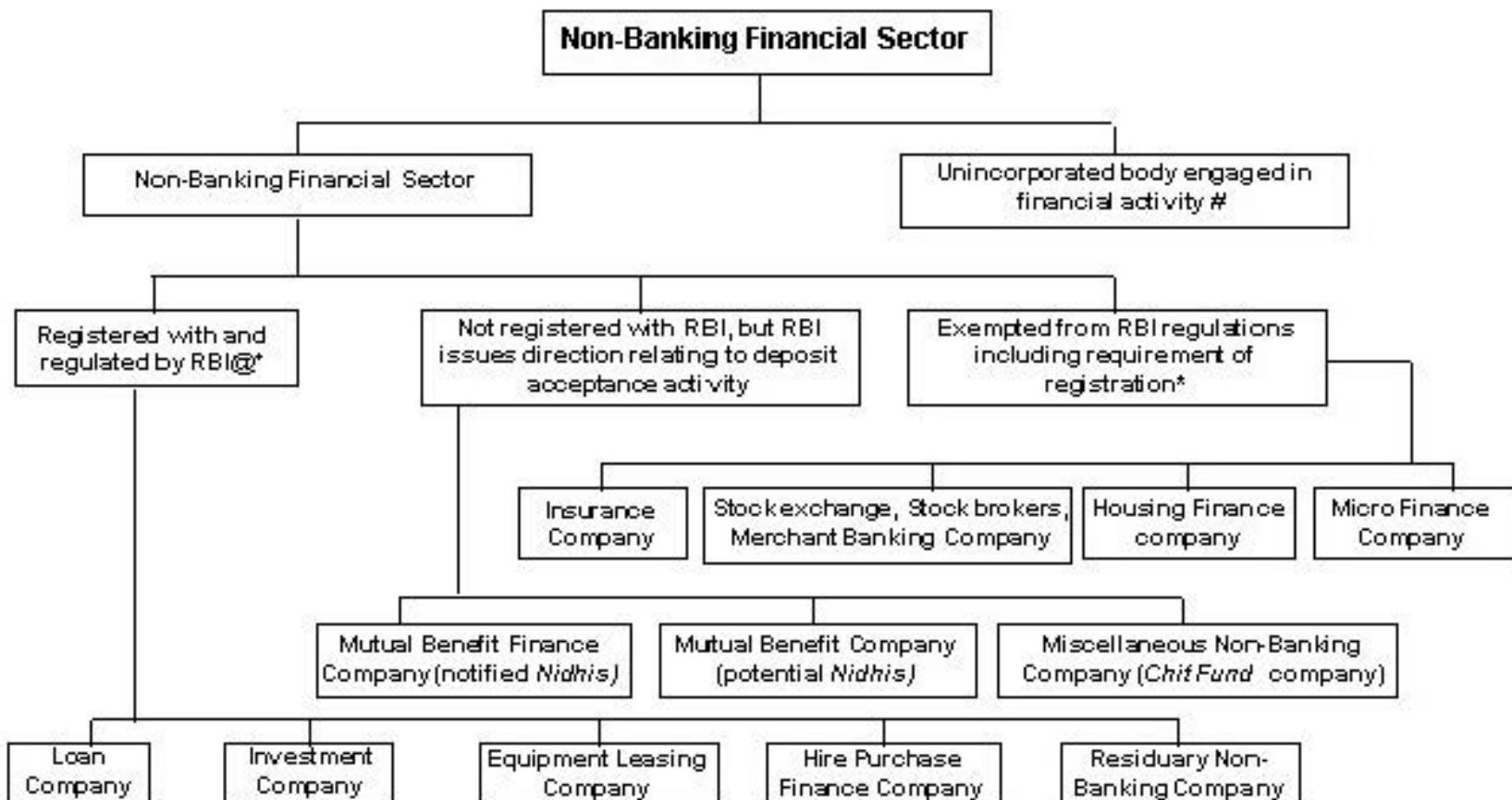
simple in contrast to that in relation to SCBs. The convenience of easy processing and quick loan sanctions draws the relatively less sophisticated public towards them. A large number of companies depend on direct contract through agents who are sometimes family or community members. The NBFCs in Pondicherry therefore are rather popular among the small traders and businessmen, lorry and bus operators and middle income groups, for jewellery purchase, commercial vehicles and consumer durables etc.

Supervision of NBFCs

The supervisory framework for NBFCs is based on three criteria, viz., (a) the size of NBFC, (b) the type of activity performed, and (c) the acceptance or otherwise of public deposits. Towards this end, a four-pronged supervisory strategy comprising (a) on-site inspection based on CAMELS (capital, assets, management, earnings, liquidity, systems and procedures) methodology, (b) computerised off-site surveillance through periodic control returns, (c) an effective market intelligence network, and (d) a system of submission of exception reports by auditors of NBFCs, has been put in place. The regulation and supervision is comprehensive for companies accepting or holding public deposits to ensure protection of the interests of depositors.

In the Union Territory of Pondicherry although as per records 51 NBFCs were registered and operating, the primary survey revealed that only 31 were actually operational of which only 21 firms responded to the survey. These firms were operating as Nidhis or Mutual benefit funds. While 57 per cent of these were partnership firms 19 per cent were private limited companies. Only 4.7 per cent were public limited, the rest were sole ownership enterprises. The client base of these NBFCs consists of mostly small traders, and businessmen, lorry and bus operators and the middle income group. The NBFCs revealed that they had in all 61,794 customers: among them 87.5 per cent were depositors and only 12.5 per cent were borrowers. The balance is obviously skewed against the borrowers. The survey revealed that only 42 per cent of the clients were perceived to be good in terms of credit worthiness and 33 per cent were fair which implies that the residual were likely to be become defaulters.

Chart 3.1 : Components of the Non-Banking Financial Sector



- # Unincorporated bodies can not receive deposits except from relatives as specified in section 45-S of the Reserve Bank of India Act and such institutions as specified under section 46(6)(iv) of the Act, if such bodies are engaged wholly or partly in any of the activity specified in clause (c) of section 46(I) of the Act, or its principal business is that of receiving deposits or lending in any manner.
- @ Primary Dealers are registered with Reserve Bank of India (RBI) and regulated by RBI as such, irrespective of whether they accept public deposits or not.
- * As they are regulated by other regulatory authorities.
- + NBFCs who accept public deposits are subject to a regulatory framework prescribed for the purpose.

The comprehensive regulatory structures evolved by RBI would mitigate the fragility of the operational environment. The entry norm of Rs.25 lakh as minimum net owned funds in chapter III B, III C and V of the RBI Act in 1999 will streamline the NBFCs operations. However, small operators at the rural level will continue to thrive or go underground. This is because the rural people are not aware of conditions like Certificate of Registration that have to be complied with before any NBFC can accept deposits from the public.

