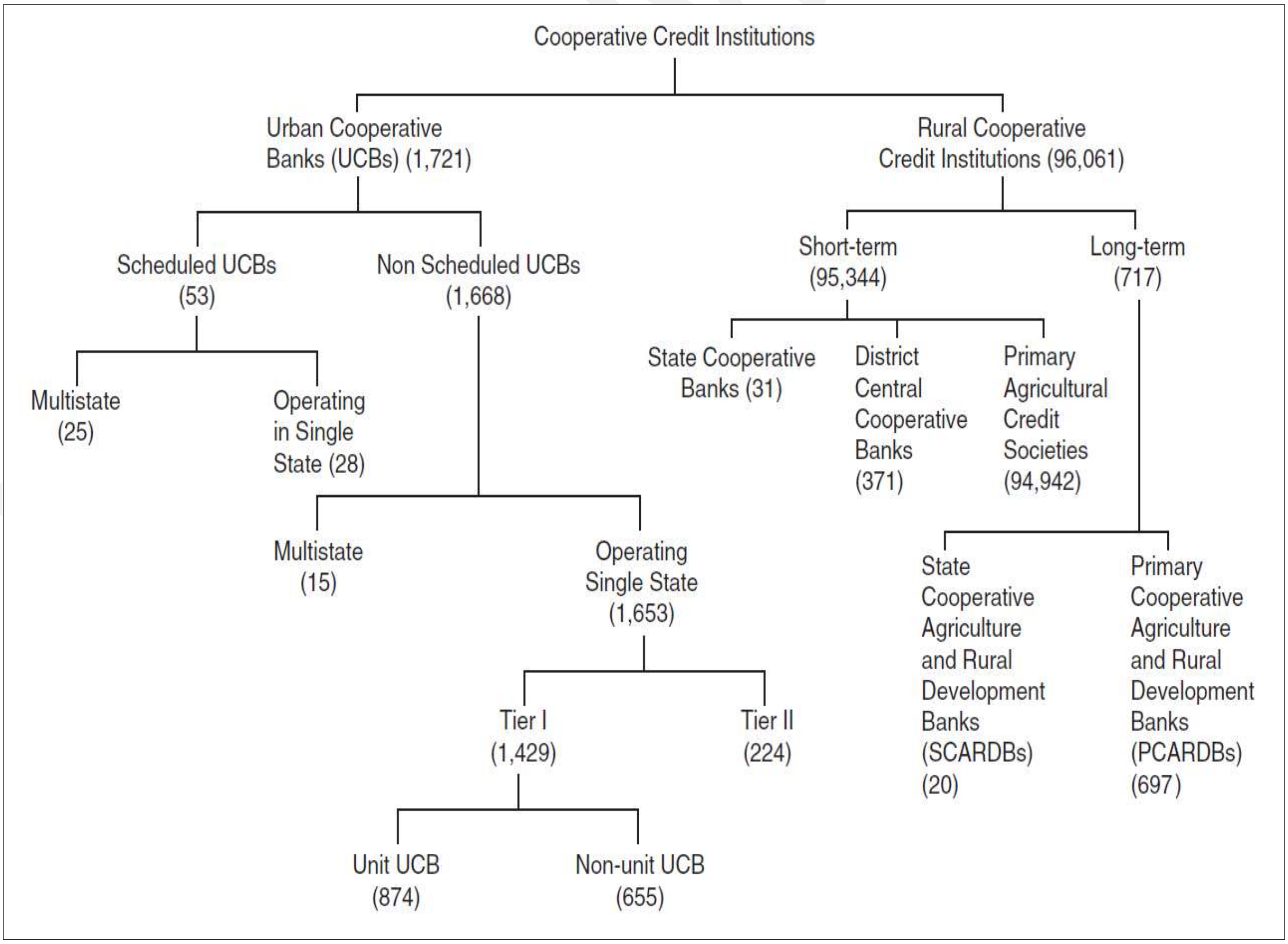
Co-operative Banking and Micro – Finance

Co-operative Banking

- A co-operative bank is a financial entity that belongs to its members, who are at the same time, owners and customers of their bank.
- These individuals share common cultural, economic and social interests who voluntarily form this association, which turns into an establishment of a co-operative bank.
- Co-operative banks fill in the gaps of banking needs of small and medium income groups which are not adequately met through by the public and private sector banks.
- The co-operative banking system supplements the efforts of the commercial banks in mobilising savings and meeting the credit needs of the local population.
- It functions with the rule of "one member one vote" and on "no profit no loss basis".
- The co-operative sector consists of urban co-operative banks and rural co-operative credit institutions.
- The **rural** co-operative credit institutions is segmented as follows:

Short term:	Long term:
• State co-operative banks • District central co-operative banks • Primary agricultural credit societies (PACS)	• State co-operative agricultural and rural development banks • Primary co-operative agricultural and rural development banks

- The size of co-operative banks is relatively smaller than that of commercial banks.



- **Urban co-operative banks**
    - UCBs mobilise savings from the middle and low income urban groups and supply credit to the weaker sections.
    - They cater to the needs of small borrowers in the non-agricultural sector.
    - The UCBs are varied and heterogeneous in terms of geographical spread, size, strength, levels of professionalism, and performance.
    - UCBs major source of funds are the bank deposits.
    - The UCBs are regulated by three authorities: central government (in case the bank has multi state presence), state governments and RBI.
    - UCBs are mostly engaged in retail banking.
    - Around 80% of UCBs are concentrated in 5 states, namely, Maharashtra, Gujarat, Karnataka, Andhra Pradesh and Tamil Nadu.
- **Rural co-operative credit institutions**
    - The main **objective** of rural co-operative credit institutions is rural development and sustainability
    - These rural co-operative banks receive refinance facility from NABARD
    - The **characteristics** are as follows:
        - Separate legal entity
        - Voluntary association
        - No personal motive
        - State authority
        - Democratic administration
    - The **need** of such an institution is:
        - Promotes rural development
        - Alternative source of credit
        - Promotes productive borrowing
        - Best suited for socio-economic conditions of Indian villages
        - Encourages more agriculture produce that leads to more export and hence, more GDP
        - Significantly improves the quality and quantity of agricultural produce
        - Makes people understand the importance of savings and investment
        - Creates decent jobs
        - Women empowerment
    - The **structure** of rural co-operative is explained in detail below:
        - Short – term credit
            - ✓ TIER 1 (Apex) – **State Co-operative Banks**
                - SCBs are the apex institutions co-ordinating and regulating the working of central co-operative banks (CCBs).
                - They form the upper tier of short term credit structure dispensing mainly short and medium term credit.
                - They can lend money to CCBs and PACSs but, not directly to farmers.
                - They function as "balancing centres" for the CCBs by making available the surplus funds of some CCBs as CCBs are not allowed to borrow or lend among themselves.
                - RBI uses SCBs as a gateway to lend credit to co-operative societies.
                - Supervised by **NABARD**
            - ✓ TIER 2 (Middle) – **(District) Central Co-operative Banks**
                - It is a co-operative bank operating at the district level in various parts of India.
                - It was established to provide banking to the rural locality for the agricultural sector with their bank branches primarily established in rural and semi-urban areas.
                - They channelize funds from SCBs to PACSs.

        - Also, it's another important function is to provide loans to PACSs (or also individuals).
        - Their three primary sources of funds are: share capital and reserves; deposits from the public; loans from SCBs
        - Supervised by **NABARD**
      - ✓ TIER 3 (Grass root) – **Primary Agricultural Credit Societies (PACSs)**
        - They are the grass root level arms of short term co-operative credit structure.
        - PACSs directly deal with individual farmers, provide short and medium term credit, supply agricultural inputs.
        - Also arrange for marketing of produce of its members through the co-operative marketing society.
        - PACSs is possibly the largest rural financial systems in the world.
        - They are dependent on the finance provided by CCBs.
        - The financial health of PACSs has deteriorated. To improve this situation, NABARD provides financial support for computerisation, human resource development and so on.
    - ▪ Long – term credit
      - ✓ This structure provides medium and long term loans for **mechanisation**, **animal husbandry, and redeeming farmer's lands, improving farmer's lands, crop loans, gold loans, rural industries and housing.**
      - ✓ UPPER TIER – **State Co-operative Agricultural and Rural Development Banks (SCARDBs)**
        - Dispenses investment credit.
        - Predominantly dependent on borrowings for financial resources.
      - ✓ LOWER TIER – **Primary Co-operative Agricultural and Rural Development Banks (PCARDBs)**
        - Heavily dependent on borrowings.
        - It is formed at taluk levels.
        - Main plan is to increase agricultural productivity in the country.
  - The **challenges** faced by rural co-operative credit institutions are as follows:
    - ▪ Inadequate funds
      - ✓ Limited working capital that is insufficient to perform any course of action.
      - ✓ So, lack of resources and weak funds base acts as a barrier to meet the credit requirements of indigents.
    - ▪ Availability of agricultural loans only
      - ✓ Co-operative societies fail to provide financial support to every department.
      - ✓ The credit services are only limited to agricultural operations.
      - ✓ Credit societies overlook the other financial needs of farmers.
    - ▪ Political intrusion
      - ✓ Members of the co-operative society become victims of the politician's tactics.
      - ✓ They misuse the co-operatives for their advantage and to inflate the vote bank.
      - ✓ They clench onto co-operatives like a leech, affecting their productivity.
    - ▪ Mixed intentions
      - ✓ There are instances where people become members for personal gain.
      - ✓ It not only violates the original goal of "mutual help", but also creates clash between private interests and interest of the co-operative society.
- **Regional Rural Banks (RRBs)**
  - After nationalisation in 1969, there was an increase in confidence of the public regarding banking system of the country, but due to cultural and logistical issues, it was difficult for commercial banks to lend to farmers and complete their needs.
  - So RRBs are basically banking organisation for local level operations across the states in India.

- They are conceived as low cost institutions, having rural ethos, a negligible local fee and pro poor focus.
- Provides essential banking and financial services to the rural areas.
- Main purpose is to mobilise resources from the rural areas and grant loans to needy and marginal farmers and artisans.
- RBI regulates the banking system of RRBs but NABARD is responsible for overall supervision and inspection of RRBs.
- RRBs are owned by:
  - Central govt. = 50%
  - State govt. = 15%
  - Sponsor bank = 35%
- Role of RRBs is as follows:
  - Identify the financial needs of rural areas.
  - Making financial credit available to the weaker section of society who had little / no access to cheaper loans and had to depend on cruel private money lenders.
  - Generating employment opportunities in rural areas.
  - Taking the banking services to the doorstep of rural masses.
  - Granting loans to:
    - ✓ Small, marginal farmers; agricultural labourers.
    - ✓ Artisans, small entrepreneurs and persons of small means who are engaged in trade, commerce, industry or other productive activities within its area of operation.
- Problems faced by RRBs are as follows:
  - Inadequate fund:
    - ✓ Poor rural people are not able to save anything due to poverty and low income.
    - ✓ This low level of savings create problems for RRBs to collect sufficient funds from them.
    - ✓ Dependent on NABARD to provide finance for further operation.
  - High over dues:
    - ✓ Poor recovery of loans, insufficient and untrained staff, poor marketing facilities, improper channel of recovery system.
  - Regional imbalance:
    - ✓ Concentration of branches in specific states and districts, overlooking the need to branch out to a more diverse area.
  - Lack of proper coordination:
    - ✓ There is communication gap and inefficient discussions between RRBs and other financial institutions like NABARD, commercial banks etc.
    - ✓ This has badly affected the performance of RRBs.

- **Grameen Banks**
  - The word "grameen" is made of the word "gram" or "village", and it means "of the village".
  - They give small loans called "microcredit" or "grameen credit" to poor people without any collateral.
  - Grameen bank is owned 90% by borrowers of the bank and 10% by govt.
  - The system of the bank is based on the idea that many poor people have skills, but cannot use these skills without some money.
  - 97% of the bank loans go to women.
  - **How does it work?**
    - Groups of 5 prospective borrowers are formed.
    - Only 2 out of 5 are eligible for receiving a loan.
    - The group is observed for a month to check if they are conforming to the rules of the bank.
    - Only when those 2 people repay principal amount + interest over a period of 50 weeks, do the other 3 become eligible for loan themselves.
    - So the system works on mutual trust, and it's a collective responsibility to make sure individual records are clear.

        - Grameen bank does not take people to court if they are unable to repay the amount.
    - **Interest rates: (**All interests are simple interest**)**
        - 20% for income generating loans
        - 8% for housing loans
        - 5% for student loans
        - 0% for struggling members of society (beggars)
    - **Objectives**:
        - Extend banking facilities to poor.
        - Eliminate exploitation of poor by private money lenders.
        - Create opportunities for self – employment.
        - Bring the disadvantaged, mostly women from the poorest households to become self – sufficient.
        - Change the vicious circle of: "low income, low saving, low investment" to virtuous circle of: "low income, injection of credit, investment, more income, more savings, more investment".
    - **16 Decisions: (**16 ways in which the poor can improve their lives**)**
        - 1 - We shall follow 4 principles of grameen bank - discipline, unity, courage and hard work.
        - 2 - We shall bring prosperity to our families.
        - 3 - We shall not live in broken houses.
        - 4 - We shall grow vegetables all year around.
        - 5 - We shall plant as many as seeds as possible in plantation season.
        - 6 - We shall plan to keep our families small.
        - 7 - We shall educate our children.
        - 8 - We shall always keep our environment clean.
        - 9 - We shall build and use latrines.
        - 10 - We shall drink water from tubewells.
        - 11 - We shall not take dowry for son's marriage; we shall not give dowry for daughter's marriage.
        - 12 - We shall always be ready to help each other.
        - 13 - We shall not inflict injustice on anyone.
        - 14 - We shall take part in all social activities.
        - 15 - We shall look after our health.
        - 16 - We shall not practice child marriage.
    - **Difference between conventional banking and grameen banking**:

Conventional Banking	Grameen Banking
Based on collateral	Collateral – free
Main objective is to maximise profit	Main objective is to get financial services to poor, especially women
Locate themselves in urban / business districts	Locate themselves in rural areas and cover as many villages as possible
Interests are usually compounded quarterly	Interests are simple interests

- **Swayam Krishi Sangam (SKS)**
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- **Bandhan Bank**
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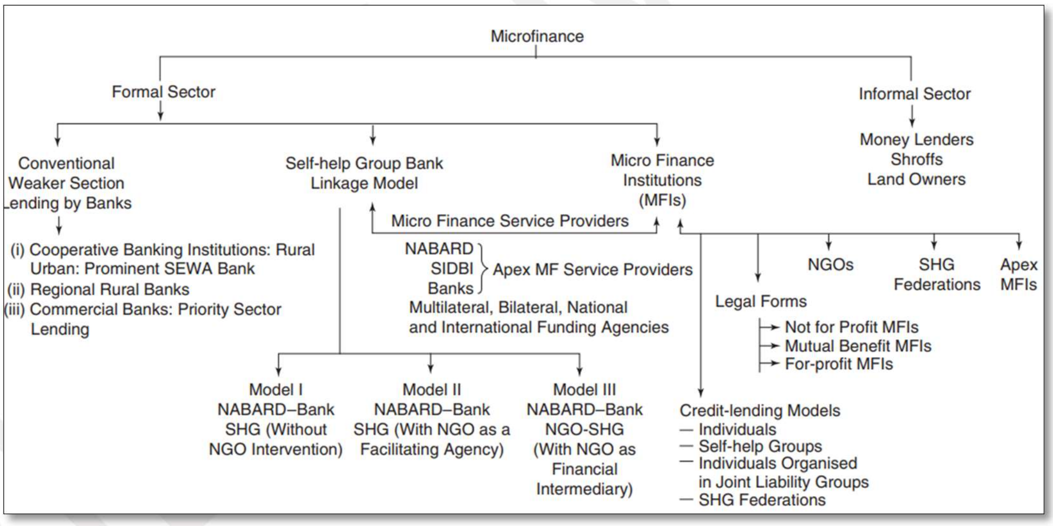
Micro – Financing

- **Definition**
    - Micro – finance is defined as financial services such as savings account, insurance funds, and credit provided to poor and low income clients so as to help them increase their income, and thereby improving their standard of living.

- **Goals, Features, Working**
    - Goals:
        - Micro finance services are provided to low income groups; or unemployed individuals because these are the people who are trapped in poverty and are not able to do business with traditional financial institutions.
        - It allows these people to take on small businesses; and not be exploited by private money lenders.
        - Many micro finance institutions focus on helping women in particular.
    - Features:
        - Loan given without security
        - Loans to those people below poverty line
        - Members of SHGs benefit from micro finance
        - Terms and conditions offered to poor people are decided by NGOs
        - The goal of micro – finance is to ultimately give impoverished people an opportunity to become self – sufficient
    - Working:
        - It's working ethic unlike typical financing institutions where the lender is concerned with the borrower having enough collateral to over the loan; micro – financing institutions focus on helping the borrower / entrepreneur succeed.
        - It provides large number of services such as:
            - ✓ Providing the basics – bank cheques, savings account etc.
            - ✓ Start-up capital for small business entrepreneurs.
            - ✓ Educational programmes that teach about investing, loans etc.
- **Institutions**



- **Advantages and Disadvantages of Micro – finance**
    - Advantages are as follows:
        - 1. Women have benefitted.
        - 2. Reduces social exclusion.
        - 3. Prevents illegal and immoral lenders to take advantage.
        - 4. Gives people easy access to credit.
        - 5. Allows people to provide better for their families.
        - 6. Creates possibility for future investment.
        - 7. Encourages people to save.
    - Disadvantages are as follows:
        - 1. MFIs deal with low volume of money.
        - 2. They provide loans against no collateral, so the risk of non-payment can arise.

- 3. Their bad debts are often quite high.
- 4. They cannot service more than a certain number of customers.
- 5. Over-dependence on the banking system for funding.
- 6. Their interest rates are higher as compared to mainstream banks.
- 7. Absence of governance structure.
- 8. Many operational, attitudinal and policy level constraints.

- **Self Help Groups (SHGs)**
  - SHG is a registered / unregistered group of 15-20 members.
  - They have relatively homogenous social and economic background.
  - They have voluntarily come together to save a small amount of money to a common fund and which meets their emergency needs on a mutual help basis.
  - This common fund might not be sufficient enough to lend to borrowers, so they seek financing from external organisations such as banks.
  - A large number of SHGs have women as their members.
  - Women have a tendency to save money, and are more concerned about their family future and kids; they get adjusted in a group easily; borrow small amounts and repay regularly and sincerely.
  - SHGs are widely viewed as better managers of money, more transparent and accountable than most other community groups.
  - So, micro-finance is used by SHG to meet survival needs, diversify their basket of income generating activities, meet working capital requirements in traditional activities and set up micro-enterprises.
  - **Goals** of SHG:
    - 1. Overcome the problem of lack of collateral.
    - 2. Building blocks of rural poor.
    - 3. Provide platform to discuss social issues.
    - 4. Financial inclusion.
    - 5. Banking literacy.
    - 6. Good impact on housing and health.
    - 7. Help women become self – reliant.
    - 8. Timely loans with reasonable interest rates.
- **NGOs**
  - Non-govt. organisations (NGOs) are key players in micro-finance sector.
  - They are the promoters of concept of SHGs.
  - They conduct workshops, seminars, and training programmes to create awareness among SHGs.
  - They also help SHGs to establish a connection with banks.
  - NGOs can also act as financial intermediary, like borrow bulk funds from banks and lending them to SHGs.
  - NGOs help a lot in rural and agricultural development.
  - **Features** of NGOs:
    - Driven by social values and humanitarian principles.
    - Committed to upliftment of underprivileged.
    - Contributes significantly in reducing poverty, discrimination and social exclusion.
    - Effective non-political link between govt. and people.
    - Vital role in formation of SHGs.
    - Promotes micro-finance.
  - **Challenges** faced by NGOs:
    - 1. Lack of long-term strategic planning
      - ✓ Most of the projects are short term, and these activities are one time shots.
      - ✓ It blurs the public image of NGO.
    - 2. Poor co-operation with mass media
      - ✓ Rely on journalists, and expect them to cover their activities and show up for event.
      - ✓ Need to have their own PR manager.

- 3. Lack of funds
    - ✓ Simply wait for donations, or previous supporters to contact them.
    - ✓ Need to actively spread word and take the first step towards taking donation.
- 4. Lack of commitment
    - ✓ Not many people actually want to work for NGOs, they aren't persistent enough or simply are joining to get certificate.
    - ✓ NGOs should not rely on one person, but rather keep looking out for different people to recruit.
- 5. Politization of NGOs
    - ✓ Local politicians or civic workers are major hindrance to NGOs.
    - ✓ They use them as some sort of "weapon" for their political agenda, and threaten NGOs, with de-registration.
- 6. Unwillingness to cooperate with each other
    - ✓ Many times, NGOs have egocentric leaders and council which leads to internal disputes and NGOs failure.
- 7. Lack of professional experience of working in particular area
    - ✓ NGOs have a lot of young workers, and not enough funds to give them a professional training.
    - ✓ Such a scenario works against NGOs as they are not able to direct the young enthusiastic people in the correct way.
- 8. Lack of credibility
    - ✓ Many NGOs come and go, after minting a lot of money. This reduces donor's trust in NGOs.
    - ✓ Once NGOs credibility goes down, it is very difficult to get funds from outside leading to NGO's failure.
- 9. Not being able to get enough people to support NGOs
    - ✓ They struggle to market themselves, and are generally bad at campaigning.
    - ✓ With the lack of awareness, NGOs find it difficult to get enough supporters.
- 10. Not being able to recruit morally and ethically strong people for the NGOs
    - ✓ Sometimes, NGOs needs to work in extremely rural and dirty areas. In such cases, people who are selfless and want to really help the community are required.
    - ✓ Such people are difficult to find, hence leads to many project failures.
- 11. Misuse of funds
    - ✓ Some NGOs try to get funds in illegal and immoral manners, and use them for hidden political agendas.
    - ✓ Such NGOs reflect badly on those NGOs who are working with dedication and commitment.
- 12. Lack of dedicated leadership
    - ✓ Most NGOs have leaders who are old. Such a leadership and style of functioning does not align with young enthusiastic people who often get frustrated and leave.
    - ✓ These young people in fact come up with new ideas, initiatives and innovation.
- 13. Unfinished projects
    - ✓ With no long term planning, sometimes, even projects go unfinished. This is due to internal conflicts or lack of trained personnel.
    - ✓ It is important for NGOs to successfully complete their projects in order to keep their good reputation and maintain work enthusiasm in their people.