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India's big co-operative banks facing trust-deficit; struggle to survive

At one point, co-operative banks used to be the preferred banking institutions for people in rural areas to meet their financial requirements. These institutions commanded the trust of the local communities. But, on account of widening trust-deficit and competition from stronger industry rivals, these entities are now struggling to survive; they have seen a sharp erosion in business in recent years.

Among them, urban cooperative banks (UCBs), the bigger ones in the cooperative banking universe, have seen a sharper decline in their loan growth and deposit growth in recent years. The collapse of UCBs like Punjab and Maharashtra Cooperative Bank (PMC Bank) has added to the customers' distrust.

According to RBI's report on Trend and Progress of Banking in India, the deposits of UCBs grew by 3.5 per cent in 2019-20 compared with 6.1 per cent in 2018-19 while loans and advances grew by just 0.8 per cent in 2019-20 compared with 8 per cent in 2018-19. The borrowings grew by just 4.9 per cent in FY20 compared with 39.2 per cent in FY19 while the reserves and surplus contracted by 9.2 per cent compared with a growth of 5.6 per cent in the previous fiscal year.

"Governance standards and inability to raise capital at market rates are weak points for co-operative banks," said Sanjay Agarwal, senior director at CARE Ratings.

Falling business

Growth in deposits, which constitute 90 per cent of the total resource base of UCBs, decelerated in 2019-20 after a revival in the previous year. The average growth rate of deposits declined from 13.1 per cent in the first decade of the consolidation drive to 8 per cent during 2014-15 to 2019-20, in line with the growth in balance sheet size.

Since 2017-18, the deposit deceleration in UCBs was starker than in SCBs, pointing to the difficulties faced by UCBs in raising resources. The deposit deceleration was led by Scheduled UCBs. Supervisory data available with the Reserve Bank suggest the continuation of deceleration well into 2020-21.

After growing at an average rate of 7.8 per cent from 2015-16 till the previous year, loans and advances of UCBs almost stagnated in 2019-20, reflecting anaemic credit demand, the RBI said. The marginal credit expansion was mainly driven by non-scheduled UCBs, while credit from SUCBs contracted. Although deposit growth slumped, low credit demand contained borrowings from market and SCBs, the RBI said.

The asset quality too worsened. In 2019-20, the asset quality of both SUCBs (scheduled UCBs) and NSUCBs (non-scheduled) deteriorated, with the latter recording a larger increase in the GNPA ratio. The rise in NPAs may partly be attributable to the stagnant growth in loans and advances and weak balance sheets, the RBI said. During 2019-20, 4.8 per cent of NSUCBs had CRARs less than 9 per cent as opposed to 3.7 per cent in the previous year, while the corresponding figure for SUCBs remained around 7.4 per cent.

"Co-operatives banks used to help unbanked sections of India to access formal banking services. But with mainstream banks engaging with all category of customers aggressively through digital channels, the relevance of cooperatives has come down," Agarwal said.

Rivals pose threat

In recent years, as UCBs faced competition from other niche players like small finance banks and non-banking financial companies (NBFCs), and also had to reaffirm their credibility to depositors, their balance sheet growth has moderated, the RBI said. SFBs offer higher interest rates and better technology to customers which cooperative banks cannot match.

India has a total of 98,545 cooperative banks, of which 1,539 are UCBs. Of this, 54 are scheduled UCBs and 1,485 unscheduled banks. Of the 97,006 rural cooperative banks, the majority are primary agriculture credit societies—95,995 and 363 district cooperative banks and 33 state cooperative banks.

Rural co-operatives make up 65 per cent of the total asset size of all co-operatives taken together, the RBI said. At the end of March, 2020, the UCBs have total advance of Rs 3.05 lakh crore and deposits of Rs 5.01 lakh crore.

The Reserve Bank liberalised the licensing policy for UCBs in 1993, resulting in proliferation in their number in the country. Nearly one-third of the newly licensed UCBs, however, became financially unsound within a short period, the RBI said.

The Reserve Bank's Vision Document 2005 reversed the liberal licensing policy while envisaging a multi-layered regulatory and supervisory strategy aimed at shoring up their viability. This included merger or amalgamation of weak but viable UCBs with stronger ones and closure of the unviable ones.

Since 2003, 385 UCBs have had their licences cancelled or withdrawn, or have been merged with stronger ones, the RBI said. However, despite the fall in the number of UCBs, their combined asset size continuously increased, underscoring the improvement in their financial position and effectiveness of the consolidation drive. Beginning in 2004-05, UCBs have undergone 136 mergers till March 2020, with Maharashtra accounting for more than half of them, the RBI said.

RBI tightens scrutiny

As the cooperative banks have suffered from corporate governance issues and dual regulation, the central bank has been tightening its grip on these banks. The last big bank collapse in the cooperative sector was PMC Bank which plunged into a crisis following financial irregularities and careless lending. The RBI, which superseded the bank's board in September 2019, is yet to work out a resolution for the lender.

As Moneycontrol reported [in an earlier story](#), in 2020, the RBI has issued a total of 106 directives to co-operative banks either restricting their business operations or extending the period of existing directions. About 60 of them were in the second half of the year. In other cases, the regulator imposed a monetary penalty. Even in the cases of three banks where licences were withdrawn, the RBI had imposed business restrictions previously. Three licences were cancelled. These are Karad Janata Sahakari Bank, CKP Co-operative Bank in Maharashtra and the Mapusa Urban Co-operative Bank of Goa.

The list of co-operative banks which have been under the closer watch of the regulator (where directions have been issued) is long and includes lenders from across the states. A large number of them were from Maharashtra. The names include The Needs of Life Co-operative Bank, Mumbai, The City Cooperative Bank, Dr. Shivajirao Patil Nilangekar Urban Co-operative Bank Ltd, Bhagyodaya Friends Urban Co-OP Bank, Shivam Sahakari Cooperative Bank and so on. In 2020, the regulator cracked the whip on Tamil Nadu-based Thiruvaikuntam Coop Bank, West Bengal-based Kolikata Mahila Coop Bank, Mudhol Cooperative Bank, Hindu Cooperative Bank, Punjab and Sikar Urban Cooperative bank among others.

"Frequent failures of cooperative banks have created a trust deficit among borrowers," said Agarwal of CARE.

With SFBs gaining ground and competition from SCBs taking a toll on their market, the UCBs will have tough days ahead in terms of survival and new business acquisition.