



POST COVID FINANCIAL PERFORMANCE OF URBAN CO-OPERATIVE BANKS IN INDIA

Dr S. Baskaran* **Pavankumar G Kulkarni****

**Professor & Head, MBA Department, Dr. Ambedkar Institute of Technology, Bengaluru, India.*

***Assistant Professor, MBA Department, Nitte Meenakshi Institute of Technology, Bengaluru, India.*

Abstract

The Cooperative Credit Structure (CCS) in India is broadly made up of urban and rural cooperatives. The financial health of Urban Cooperative Banks (ucbs), numbering about 1,539, has been a matter of concern for decades, necessitating the constitution of a plethora of committees at the national and regional levels to find solutions to the countless issues hindering this sector. This article lay down various issues that urban cooperative banks UCB's are encountering due to COVID-19 pandemic and the implications so as to improve the rules and regulations wherever required to be address the negative effect on the banking sector.

Key Words: *COVID-19, Financial Health, Banking sector, Urban Co-operative Banks.*

Introduction

Cooperative banks in India have been under pressure to survive for the last few years. The subject came into the limelight after the Punjab and Maharashtra Cooperative (PMC) bank disaster, which left anxious depositors visit the branches in attempts to withdraw their money. According to report published by the Reserve Bank of India (RBI), UCB's in India have observed a decline in deposits from 6.1 % in 2019-20 to 3.5 % in 2020-21. In terms of loans and advances too, there has been a sharp decline from 8 % in 2019-20 to 0.8 % in 2020-21. By the end of March 2021, the sector comprised 1,539 UCBs and 97,006 rural cooperative banks, with a depositor base of 8.6 crore.

Diminished share in agricultural lending

Cooperative banks have played a major role in providing financial support to the rural sector. They started with an aim to promote saving and investment habits, specifically in the rural areas The RBI report noted that despite a crucial role played by the sector, its share in total agricultural lending diminished considerably over the years, from as high as 64 per cent in 1992-93 to just 11.3 per cent in 2019-20.

Most co-operative banks sit uncomfortably in the heterogeneous banking structure. While big banks continue to gain all the attention, the cooperative banks which play a significant role in credit delivery to the rural population and contribute to financial inclusion remain confined in an unglamorous state.

As on May 31, 2021, there are 1,531 urban cooperative banks (UCBs) and 97,006 rural cooperative banks, with the latter making up 65% of the total asset size of all cooperatives taken together.

Despite the crucial role played by the cooperative sector, its asset size was only around 10% compared to that of scheduled commercial banks (SCBs) at end March-2020.

NPA Rises and Losses gets bigger

The amount of gross non-performing assets (NPA) of urban co-operative banks rose to 11.3% in FY21 as against 10.8% in FY20 and 7.3% in FY19, according RBI. The financial health of rural



cooperatives too, remains fragile amid stiff competition from niche players like non-banking financial companies and small finance banks. Growth in deposits, which constitute about 90% of their total resource base, plunged in the year ended March 2020. The average growth rate in deposits fell from 13% in the first decade of consolidation drive to 8% between FY15 and FY20.

Data from RBI signals deposit deterioration trend to continue well into 2021. The UCBs reported a cumulative loss of ₹4,806 crore for FY20 as against a profit of ₹3,544 crore in FY19 mainly because of high NPAs and lower investments. The major crisis at Punjab and Maharashtra Cooperative (PMC) Bank in 2019 can be attributed to the mammoth quantum of NPAs. Secondly, the credit demand remains anaemic. After growing at an average rate of 7.8% since 2015-16, loans and advances of UCBs almost stagnated in 2019-20. The health of cooperative banks is likely to worsen in post Covid-19 days.

UCBs, like other cooperatives, depend on their members for their equity capital requirements or their internal profits to fund their growth. “Apart from this, the areas of operations for most UCBs are also restricted to the state where these UCBs are incorporated. Hence in absence of sufficient ability to grow, the scale and service offerings for most UCBs have remained constrained.

Lenient governance

For years, such banks have escaped enquiry despite failures and frauds. In FY21, for example, UCBs reported total 323 frauds, while state cooperative banks reported 482 frauds much higher than FY19. There have always been questions over who controls cooperative banks in India- states or the Centre. As banking regulations were made appropriate to cooperative banks, the RBI was able to exercise some control over them, but the regulation of the management of the cooperatives remained under the purview of states. Where state funding is involved, political embarrassments and corruption be likely to follow.

Though, the unexpected collapse of once cash-rich Punjab and Maharashtra Co-operative Bank last year forced the government to bring about legal changes. In June 2020, the government amended the laws governing cooperative banks. The power of RBI over a cooperative bank will now override the power of the state registrar of cooperatives.

Effect of Geographical Concentration

The UCBs carry three types of concentration risk: (a) geographical, (b) sectoral and (c) loan size-wise. At the end of March 2021, out of 1,539 UCBs, Maharashtra and Gujarat housed 712 (46 per cent) of them. These two States accounted for nearly 70 per cent of the total UCB branches in the country. In terms of business (deposits + advances), the two States commanded as high as 3/4th of the all-India UCB business. These States have been brutally attacked by Covid-19.

A akin pattern can be seen in Karnataka and Tamil Nadu states representing 25 % of the total UCBs and 10.5 % of the total business. Therefore, it is quite likely that in these 4 geographically neighbouring States, the business, profitability and competence parameters of the UCBs must have been critically under pressure. At March-end 2021, almost a 1/3rd of the total advances by the UCBs were outstanding against MSMEs, a sector which has been badly affected by the lockdowns. Their recovery will necessitate recapitalisation by the State, return of the migrant workforce, restoration of demand and supply, and above all, quick and widespread vaccination. Moreover, the sector is in the



cups of a major structural and compositional ‘churning’ in the post-lockdown period. It will take significant time for the sector to make a comeback, after accounting for the economic time lost. Combined with the exposure to agriculture and housing, the total outstanding of the UCBs stood at over 43 per cent of the total advances.

Initiative from Central Bank:

In February 2021, The Reserve Bank of India has appointed yet another national committee, headed by a former RBI Deputy Governor, NS Vishwanathan, to articulate “operative measures for rapid treatment and resolution of UCBs and also measure their potential for consolidation in the sector”. The group was also tasked with investigating the need for differential regulations and charting out potential acceptable activities for the UCBs with a view to enhancing their resilience.

This was preceded by the central bank acquiring full-scale supervisory authority over the UCBs through an amendment to the Banking Regulation Act, 1949 in September 2020. However, these amendments have not gone down well with the Maharashtra government (the State with the highest number of UCBs). The Maharashtra government has constituted a State-level committee under its Minister for Revenue to protect the interests of cooperative banks in the State.

The way forward

New amendments giving the central bank more regulatory and supervisory freedom will probably support the UCBs to function in a well-organized manner which will not only create them future-ready, but will stem the repeated disruptions in banking activities through failures that cause pain on millions of depositors. In addition, with the reduction of ‘dual’ control, the RBI will be able to regulate UCBs more directly and efficiently. Consequently, a lot of the rigmarole and legal challenges will also reduce.

The growing changes in the financial sector combining and integrating micro finance, FinTech companies, payment gateways, social platforms, e-commerce companies and NBFCs confront the sustained presence of the UCBs, which are mainly small in size, lack professional management and have geographically fewer diversified operations.

Most of the unit banks could be sold to those new generation banks who require to get better their footprint, if need be, by a Deposit Insurance and Credit Guarantee Corporation, monetary bail-out. The financially sound ones having a diversified geographical presence, beyond a threshold balance sheet size, need to be converted into small finance banks.

Conclusion

There is a hope that the new ministry will help resolve problems in cooperative banking even as many suspect it to be a political move. “The ministry, along with recent RBI reforms shall improve the functioning of UCBs and could further deepen the cooperative model across other states. Further, there is an imperative need to reconsider the appeal or otherwise of having a genre of banks creating uncertainty and doubts in the minds of depositors and obliging the regulators to carry out with disparity treatment. The question is not who controls the UCBs; if the Urban Cooperative Banks can manage themselves effectively and efficiently; there will be increasing freedom for them.



References

1. Article on “Urban cooperative banks in ICU, post Covid.” published in The Business Line on 27th July 2021:
2. <https://www.thehindubusinessline.com/opinion/urban-co-op-banks-in-icu-post-covid/article35566094.ece>.
3. Report of the Expert Committee on Urban Co-operative Banks Published by Reserve Bank of India on 23rd Aug 2021 .
4. <https://www.rbi.org.in/Scripts/PublicationReportDetails.aspx?UrlPage=&ID=1185>
5. Article on “Explained: why cooperative banks in India are struggling” published in the times of India on 11th July 2021.
6. <https://timesofindia.indiatimes.com/business/india-business/explained-why-cooperative-banks-in-india-are-struggling/articleshow/84321360.cms>.
7. Article on “Sress in Urban cooperative banks Amid covid -19 prompted banking regulation ordinance” published in Bloomsberg on 16th September 2020.
8. <https://www.bloomberquint.com/economy-finance/stress-in-urban-cooperative-banks-amid-covid-19-prompted-banking-regulation-ordinance-nirmala-sitharaman>.