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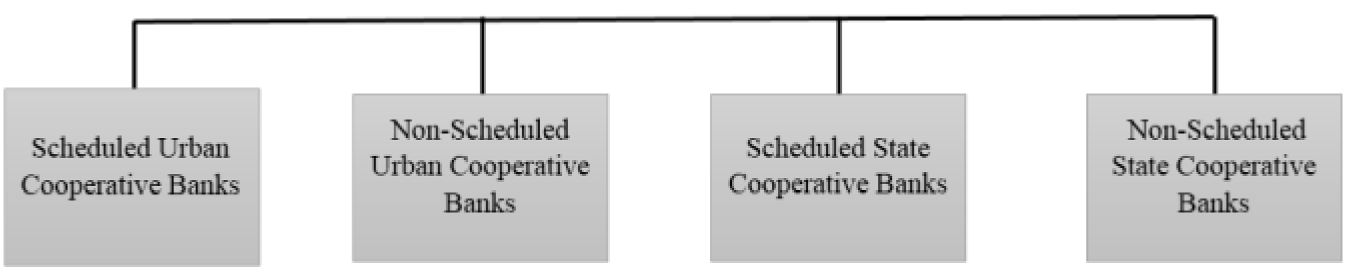
ROLE OF LENDING PRACTICES IN COOPERATIVE BANKS FAILURE

Introduction:

As per the data measured by the deposits of the customer, 83 percent of banking business is in the hands of nationalized and state banks. As per the official website of RBI banks were grouped into five categories (a) State Bank of India and its Associates; (b) Nationalized Banks; (c) Foreign Banks; (d) Regional Rural Bank; and other Scheduled commercial Banks. There are another category of the banks and are called Cooperative Banks. They are the banking institutions and work on cooperative Basis. This types of banking structure are supported by the government and they also gets financial assistance from both central as well as state government. These banks operates in Rural, Semi-Urban and Urban Areas. They work as a retail and commercial banking as to provide both Short and Long Term loans.

At present India is having 53 Scheduled Urban Co-operative banks in India. Reserve Bank of India as divided Cooperative bank into following category:



Cooperative banks work on the principle of one person-one vote as the banks are owned by their customers. In India, Cooperative banks serve an important role and are registered under the Cooperative Societies act, 1912. Though they are regulated by the Banking Regulation Act, 1949 under the Reserve Bank of India. The primary purpose of these banks is to lend short-term and long-term loans. The short-term loans are generally designed for the farmers and it is divided into three categories viz.,

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PACS (Primary Agriculture Cooperative Society), District Central Cooperatives Banks (DCCB) and State Cooperative Banks (SCB) at Village, District and State levels respectively(LAHIRI, n.d.).

The year period 1980s – 2020s saw a number of cases of a banking failure in the Indian banking system and the main cause are a poor credit management system. In the year 2019, most of the banks are either merged or are in the process of being merged. In the year 2019, the government of India has announced the merger of 10 public sector banks into four. Oriental Bank of Commerce and the United Bank of India are merged with Punjab National Bank, and Syndicate Bank will become part of Canara Bank. Where Andhra Bank and Corporation Bank will be merged Union Bank of India. The government has already merged Dena Bank with Vijaya Bank with Bank of Baroda and Allahabad Bank with the Indian Bank. Though the Indian Government has said that no commercial banks are going to shut this is merely the process of strengthening public sector banks ""(Asher, 2007).

The main cause of mergers of banks can be taken as the consolidation of the banking industry. They called it 'Unlocking potential through consolidation'. The benefits were divided into three categories viz the enhanced capacity of increase credit, strong national presence and global reach and the reduced operational cost and cost of lending. Though in spite of mergers there are scenarios of a huge banking failure in many aspects (Martin, 1977). In spite of so many mergers and acquisitions to increase the potential performance of the bank, the number of NPAs, lending failure, credit procedure failures, etc. Nationalized banks are not the only cause on i.e. majorly private and foreign banks are involved in it. The rough patch of Indian Banks has a prime role in the significant economic slowdown. Reports clearly embark on 70% NPA in the public sector and 90% of it in jointly private and foreign banks.

There is also a counter-question that if banks were really efficient then why the government is merging them with other banks? The possible reason might be the alarming rise of bad loans in the banks. The traditional role of a bank is to lend money and the creation of its assets. Due to various factors like the instable economic environment, rapidly change in the interest rates, an increase in the inside loan can be the prime reason for banking slowdown. This paper deals with the history of cooperative banks and the comparative study of tier wise distribution of UCBs, banking structure of UCBs, NPA of UCBs, State-wise distribution of UCBs and selected bank-wise financial parameters.

The present paper is to study the major factors driving lending practices. This research gives significant literature for insight to borrowers. This paper also gives information regarding the benefit of potential informed decisions and making optimal outcomes out of it. The objective of this paper is to study the main factors of lending practices and the reason of failing cooperative banks. To find the objective we have conducted a case study research. This paper also used direct observation, unstructured interviews, and a review of various documents and data available online. In our present study, we considered PMC cooperative banks as our case study and reviewed lending practices of the top 10 cooperative banks. This study is useful for researchers, policymakers, investors, and students of the relevant discipline.

Theoretical Background:

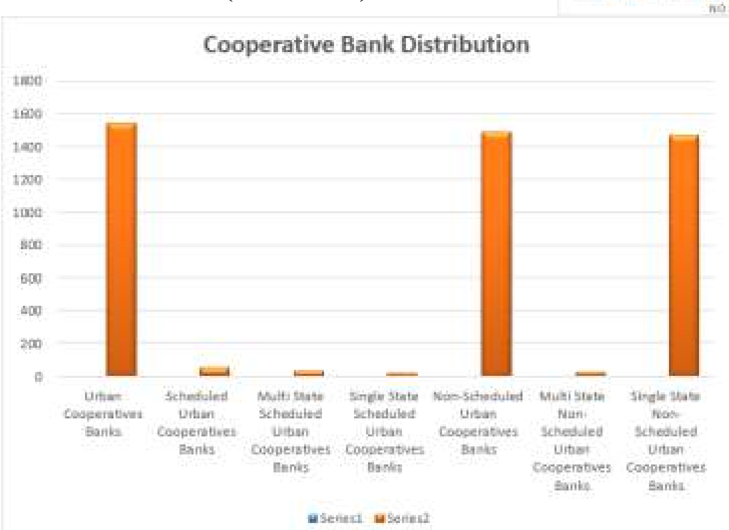
Firm Level Analysis

In general terms, we also call lending and 'financing' which generally means to lend money or property to the other party in order to get it repaid with some additional money called interest. In lending practices involved two parties' lenders and borrowers performing their certain and specific roles throughout the procedure. There is no specific quantitative measurement to access the quality of bank management, there are certain regulatory and rating agencies with which the data is been analyzed (Siems, 1992).

In the market, various types of loan options are available to bank financing for small business or working capital management, for management of asset and types of machinery, credit card financing, mortgage, or some other personal use ——'(Lu & Whidbee, 2013). Along with different types of loans there are which has its own conditions and implications, and the involved factors are; the amount of loan, Assets pledged, the term of the loan, expansion of business, etc.

The cooperative banks offers loan at lower yield on their capital than comparison to other nationalized and private sectors banks –(Lind, 2005) . The lending procedure involve minimum loan rate of 10.75% with minimum amount of 10000 which can maximize up to 3.5 Lakh with interest rate of 12.25%. The interest charges are annual basis and require a minimum documentation process by the consumers. Also, the processing charges are at minimal or not at all, the repayment period is of up to 60 months. Most people apply for a loan are between the ages brackets of 21 to 60 years. The necessary condition is the person should be a resident in India and having a clean history with a good repayment record.

Figure 1.1 Structure of Cooperative bank and division (2018-2019)



Data Source: Time-Series Publication. Official Reserve bank Website. RBIs data warehouse. (Accessed on 11-02-2020)

In the above figure, we can clearly see that out of total 96.5% of banks are Non-Scheduled urban Cooperative banks and 98% of which is Single State Non- Scheduled Urban Cooperatives Banks. Hence the number of scheduled urban cooperative banks is less than the total cooperative banks. At the top of the banking system, we have a reserve bank of India. The geographical coverage of the cooperative banking system has been increased tremendously, though more than 95% of them are Non-Scheduled UCBs (Sathye, 2003). As the Non-Scheduled banks do not follow the rules made by the RBI, they are not included in the second schedule of RBI, Non-Scheduled bank are not allowed to borrow money from RBI, and Non-schedules banks can deposit this amount with themselves.

Figure 1.2 Tier Wise Distribution of UCBs of last three year

Data Source: Time-Series Publication. Official Reserve bank Website. RBIs data warehouse. (Accessed on 11-02-2020)

Table 1.1 Showing the Tier-Wise Distribution of UCBSs

Table 1.1 Showing the Tier-Wise Distribution of UCBS

Year	Tier	No. of UCBs	Percentage	Deposits	Percentage	Advances	Percentage	Total Assets	Percentage
2018-2019	I	917	59.39	43,587.80	9.00	25,075.80	8.28	54,591.25	9.11
	II	627	40.61	440,728.05	91.00	277,941.96	91.72	544,622.47	90.89
	All UCBs	1,544	100.00	484,315.85	100.00	303,017.76	100.00	599,213.72	100.00
2017-2018	I	1,071	69.05	593.20	12.99	335.98	11.98	737.55	13.10
	II	480	30.95	3,971.86	87.01	2,469.03	88.02	4,894.23	86.90
	All UCBs	1,551	100.00	4,565.07	100.00	2,805.01	100.00	5,631.79	100.00
2016-2017	I	1,083	69.33	603.31	13.60	317.81	12.17	744.97	13.80
	II	479	30.67	3,831.38	86.40	2,294.43	87.83	4,654.06	86.20
	All UCBs	1,562	100.00	4,434.68	100.00	2,612.25	100.00	5,399.03	100.00
2015-2016	I	1,104	70.14	504	12.85	291	11.86	625.99	13.08
	II	470	29.86	3,418	87.15	2,159	88.14	4,158.05	86.92
	All UCBs	1,574	100.00	3,922	100.00	2,450	100.00	4,784.04	100.00
2014-2015	I	1,132	71.69	543.00	15.29	328.87	14.66	668.03	15.35
	II	447	28.31	3008.34	84.71	1914.42	85.34	3683.95	84.65
	All UCBs	1,579	100.00	3551.34	100.00	2243.29	100.00	4351.97	100.00

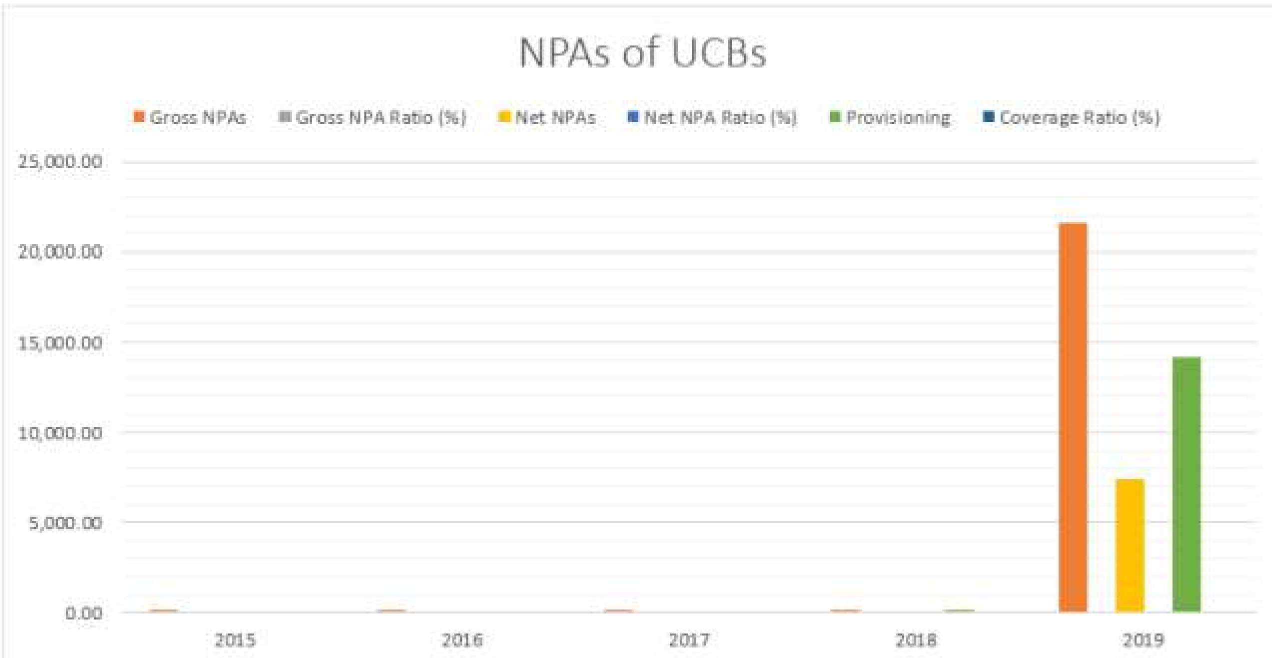
Data Source: Time-Series Publication. Official Reserve bank Website. RBIs data warehouse.

Unlike other banks, cooperative banks have not been otherwise the cause of current economic circumstances. Credit unions are generally conservative for the lending practices and the restricted financial policies of regulatory authorities (Crear, 2009). Traditionally these banks were centered on communities, localities and other small workers group. The majority of services rendered by these are saving & current accounts, deposit lockers, loan and mortgage(Thomson, 1991). In a study, more than half of the existing consumers agree to refer the banks to their friends and family. Also, the financial performance of UCBs is improved by 2010-11, though there are some pitfalls in the state, district and rural cooperative banks. The financial performance of long term loans was found weaker than compared to short term loans (Gupta & Jain, 2012). This is to note that though the concept of issuing loan has widened considerably but the incorporation of UCB essentially lend to small borrowers and small business. These have centered on the analysis of monetary feasibility and credit value of money lending organizations so as to anticipate corporate disappointments and the nascent rate of these institutions(Chander, 2010). The recent change in the UCBs involves a developmental role in making it economically viable. Though the dual nature of UCBs is to be rationalized, as the regulations for long term and short term loan is different in aspects of regulatory powers "" (Asher, 2007). As per the consideration regarding the performance of the lending process of cooperative banks, the likelihood of failure was affected by the banking organizational structure. According to research in the case of de novo banks that are part of single-bank holding companies are more likely to fail as compare to the de novo banks of multi-bank holding companies. Interestingly, the capital level of do not play a key role in the failure of banks rather than de novo, independent or multi-bank holding company '(Lu &

Whidbee, 2013).

NPAs of UCBs

The Non-Performing Assets of banking institutions are generally that loans and advances which are in default or missed, in general terms, we call it debts but in case of banks these situations are referred to as Non-Performing Assets. This situation generally arises when the borrower defaults in his obligations. In the past decade the NPAs of all sectors of banks has been increased exponentially (Kavitha & Muthumeenakshi, 2017). The reason behind this could be the weak implication of regulations by RBI, disbursement of loan to insolvent or in default customers, or the banks are unable to recover the amount disbursed by them. The principle of co-operative banks are not to go for profit maximization. Also higher the average ratio of working funds in banks depicts the better situations(Chander, 2010).



Data Source: Time-Series Publication. Official Reserve bank Website. RBIs data warehouse. (Accessed on 11-02-2020)

The inefficiencies of banks in maintaining the deficiency of NPAs directly impact the solvency ratio of the banks. Especially in the case of Cooperative banks where the prime intention is not to maximizes profit. In the above figure, we can see that till FY 2018-19 the Gross NPA is less than 200 billion, wherein the case of FY 2019-20 the gross NPA is 21559 billion which is 108.5 times more than the previous. This data draws the attention towards the significantly weaker position almost in all the dimensions.

Banks in above case has a lot of options to exercise in order to recover its NPAs and the major takeaway could regularly update its lending policy, to frequently remind the borrowers, further it can be divided into various sub-standards i.e. doubtful NPAs and loss assets, depending upon duration and possibility of repayment, and should also have an option of taking possession of a collateral security (Chakrabarti, 2011). In a study conducted in Pakistan, it has been concluded that the increase in deposits boost up the earning of the banks and an increase in cash reserves is inversely proportional to the earnings of the banks. Also, high NPAs results decrease in earnings of banks ——— (Arif & Nauman Anees, 2012).

Table 1.2 showing NPA of top 10 cooperative banks

In crores

SL. N0.	Name of the Banks (Rank-Wise)	31-03-19	31-03-18	Status	Change in Percentage
1.	Saraswat Banks	61.74	31.73	Increase	+94.58
2.	Cosmos Bank	155.3	177.38	Decrease	-12.45
3.	SVS Bank	971.74	912.91	Increase	+06.44
4.	Punjab and Maharashtra Cooperative Bank	137.77	98.33	Increase	+40.11
5.	Abhyudaya Cooperative Bank	505.56	485.2	Increase	+04.20
6.	TJSB Sahakari Bank	44.14	41.87	Increase	+10.31
7.	Bharat Cooperative Bank	253.24	187.73	Increase	+35.16
8.	Janata Sahakari Bank	187.73	394.88	Decrease	-52.46
9.	NKGSB Cooperative Bank	200.80	317.16	Decrease	-36.69
10.	Apna Sahakari Bank Ltd	147.87	58.90	Increase	+151.05

Data Source: Official Annual Reports of respective Cooperative Banks (Accessed on 17-02-2020)

Above is the NPA status of top urban helpful banks indicating the opening NPAs and the closing NPAs and the particular change in the rate in the equivalent. Out of 10, just 3 NPAs reveal the diminishing in NPAs rest each of the 7 Banks has expanded NPA. Most of the banks portray the circumstance of more misfortune and the biggest increment in NPA is more than 150 %. It is a common phenomenon that increase in the deposit ibn the banks will gradually increase the performance and it is inversely proportional to NPAs (Shastri, Tripathi, & Ali, 2011)———(Arif & Nauman Anees, 2012; Shastri et al., 2011).

Table: 1.3 Rank and Percentile coefficient

Point	*31-Mar-19*	*Rank*	*Percent*
3	971.74	1	100.00%
5	505.56	2	88.80%
7	253.24	3	77.70%
9	200.8	4	66.60%
8	187.73	5	55.50%
2	155.3	6	44.40%
10	147.87	7	33.30%
4	137.77	8	22.20%
1	61.74	9	11.10%
6	44.14	10	0.00%

The substantial fallacy regarding Non-Performing Assets including the misconception that banks earn more by investing in non-banking activities or not performing the traditional activity (DeYoung & Torna, 2013). The recent failure of Punjab and Cooperative bank is due to the alarming numbers of unrecovered loans which are the ultimate result of incomplete and liberal lending policies. Banking failure occurs due to the quality of management of banks fails and inefficiency in the presently available policies (Jacobson & Roszbach, 2003; Siems, 1992). Thus a bank has to deal jointly with both liquidity risk and credit risk in the banks this could increase the bank stability (Imbierowicz & Rauch, 2014).

Conclusion:

Lending policies of cooperative banks is a major challenge and responsibility for banking failure. This study investigates the lending policies at the level of cooperative banks in India. We critically examined the literature review, the latest published data, and the primary data collected from the database of RBI and official websites of respective banks. We analyzed the same by using data tabulation techniques, statistical smoothening and rank, and percentile coefficient. The results show that more than 70% of the existing cooperative banks have NPAs increasing with an average rate of 48.88% every year.

The regulatory body is imposing the restrictions only feasible to apply i.e. sec 35(a) of banking regulation act on the top owners, which can barred banks from issuing more loans of renewal of old loans. The increase in the figures of corporative banks is alarming in numbers. The failure of corporative banks is due to small capita base (as UCBs can start from 25 lakhs), less liquidity ratio and lineal lending policies. The biggest challenge is that the Cooperative banks are audited by the State Government and RBI inspects the data once in a year which needs to be altered and RBI should be granted with more Power to regulate the cooperative banks. The busting of cooperative banks are running from 2001 i.e. from Ahmedabad Madhavpura Mercantile cooperative bank to Punjab and Maharashtra Cooperative Bank. During the period of time, more than 200 banks have reached the verge of liquidations. We have seen that the NPA of PMC has proliferated to 108th times of its preceding previous years NPAs.

The solution of failure in lending practices could be that, to provide the urban Cooperative Banks the power of converting themselves into small financing companies. To allow the RBI to provide more authority over the regulatory of UCBs. This possible measures could retain the downfall in the current situation of UCBs and can decrease the chances of failing.

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