



## TWENTY-FIVE YEARS OF CO-OPERATIVE RURAL BANKS

In March 1989, the Co-operative Rural Banks (CRBs) celebrate their 25th anniversary. In early 1964, when this scheme was inaugurated by the People's Bank it was considered an adventurous move, and there had been widespread scepticism about its success even within the Bank. Yet the CRBs steered their way through to withstand these challenges, and also proved to be a true partner in rural development in many ways (See paper by Dr. Nimal Sanderatne, pages 15-17).

In this Special Report, the concept of CRBs, its evolution, strengths, challenges and some clues for their future direction are discussed by a team with specialised experience and background of this area. It is hoped that these articles would provide a closer insight into the origins and progress of the CRBs, their contribution to the development of the country in general and to the rural sector in particular.

### A Profile of CRBs

The rural sector occupies an important position in the Sri Lankan economy. As much as 75 percent of Sri Lanka's population lives in the rural sector which provides them with food, shelter, and employment opportunities and the basic means of livelihood. Its contribution to the GDP, export earnings, and also to

the capital formation of the country cannot be underestimated. Moreover, the vastly untapped development potential in this sector, together with the social obligations to uplift the living standards of the rural population makes this sector all the more important in the development process. It is in this context that the significance of the commemoration of the 25th anniversary of the CRBs should be viewed.

The last 25 years have recorded dramatic changes in the country's social fabric and witnessed many changes in the Sri Lankan economy and resultantly in the banking system of the country. Naturally, CRBs also had to face these socio-economic undercurrents and perhaps change their ways to suit the situation. Whether these institutions have been successful in this process is an open question. Yet, the fact that they have been able to sustain themselves and continue to grow may in itself be considered an achievement. A cursory look at the evolution and the growth of the CRBs shows a steep and sustainable increase in the number of banking outlets, and also their business turnover. The growth in number of CRB branches, as depicted in the Graph, which moved at a rather cautious space until 1973, accelerated thereafter to reach 968 branches operating in various parts of the country

by 1988. Of these about 282 were full-fledged CRBs, while the balance 686 were special branches providing limited operations. How many of these branches are really rural? Given the complexities in the definition, of what is rural and what is not, this kind of assessment may not be easy. However, it was found that about 13.8 percent of the 968 branches were located in predominantly backward, rural districts like Moneragala, Hambantota and Mullativu. (See Table on P.14). Another 45.9 % of the branches were located in rural districts like Badulla, Kegalle and Kurunegala. The next category of districts include those once having a bigger urban fringe, such as Gampaha, Kalutara, and Jaffna. About 33.7 percent of the branches fell into this group of districts, while the Colombo district alone constituted 6.4 percent of the CRB branches.

Of course, this kind of classification may appear to be rather crude, but it gives a relative positioning of districts and the concentration CRB branches into each category of districts. It should be noted that even within these districts the CRBs may tend to concentrate into more urbanized areas than towards the real rural hinterland. An important inference one could make from such a classification would be that quite a substantial number of CRB branches are still located in the urban areas and not exclusively in the rural areas.

Another important performance indicator of the CRBs has been deposits collection. The deposits volume of CRBs grew from a meagre Rs.496,360 in 1965 to Rs. 1.83 billion in 1988. The average growth rate of CRB deposits has been closer to 50 percent per annum which is far in excess of the average rate of growth of deposits of the country. In this sense, CRBs have been a remarkably effective deposit mobilizer. They have been equally competitive in both tremendously under-banked rural areas, as well as highly over-banked rural areas. For instance about 10 percent of their total deposits have come from the Colombo district alone; while another 41 percent of these deposits have come from the districts of Gampaha, Kalutara, Galle, Jaffna and Kandy. All these districts have reached relatively higher levels of sophistication in terms of the standards of facilities offered and the spread of banking habits which made these districts and their depositors more exposed to competitive commercial banking sources.

Another interesting feature of the deposit mobilization scheme of the CRBs has been that the bulk of the depositors are small savers whose deposits range from between Rs.25 to Rs.500. In this sense the market niche of the CRBs has been the small time depositor, whose average balances of savings deposits has been around Rs.700. By September 1988, the CRBs had deposit accounts amounting to 2.34 million. In this sense the market niche of the CRBs has generally been those depositors who are not entertained by the commercial banking system of the country. The fact that even non-members of the CRBs are eligible to open deposit accounts makes CRB deposit mobilization schemes much more effective. The maintenance of a large number of small accounts is in fact a relatively non-rewarding exercise, if not for the relatively low administration cost of the CRB operations. It is precisely this low administration cost of maintenance of deposit accounts that has made CRBs so fiercely competitive in the mobilization of rural deposits.

The other side of the coin of the CRB operations is the loans and advances. The CRBs have right from the beginning set as its objective catering to the overall financial needs of the rural sector of this country. In order to achieve this goal a comprehensive package was designed to include, various possible credit needs such as agriculture industry, consumption, housing, rural electrification etc. In the first few years of operation of the CRBs, these advances have always been in excess of their deposits, with the difference between advances and deposits being regularly provided by the People's Bank. This process continued until 1975, after which year the deposit levels began increasing at a faster rate than advances. There have been many reasons for this development (See articles on CRB investments). Yet the credit promotion of the CRBs has not been as effective as their deposit mobilization operations and this has become a blind spot in their services to the rural sector.

There have been many criticisms levelled against the CRBs for their inability to plough back CRB funds to the rural sector itself. Although the problem of extraction of surpluses by the banking system has been raised on many public platforms it has neither been adequately studied nor properly, discussed. Some of the questions that have often been evad-

ed by the surplus extraction school include:

- (i) how clear are we about the demarcation of boundaries of rural areas vis-a-vis urban areas?
- (ii) how many of the so-called rural depositors are really rural, and how much of their savings consist of the total savings of the Rural banks?
- (iii) what are the expectations of the rural savers?
- (iv) what is the real size of the credit gap in the rural sector, and what causes have prevented prospective borrowers from coming to the CRBs?

#### Classification of Advances.

A purpose-wise classification of CRB advances presents a few interesting features. The low exposure of the CRBs to finance the working capital requirements of direct production related economic activities is the most interesting of them all. The direct production related economic activities in the rural sector include small farming, animal husbandry, rural industry etc. which provides the livelihood for the rural majority. However, advances to agriculture and related operations by the CRBs consist of a meagre 15.3 percent of their total outstanding loans, while the advances to the industrial sector cover a marginal 4.9 percent of the total loans. Secondly, over the years the growth rates of advances to this sector seem to have been occurring at a pace very much disproportionate to their relative performance in the Sri Lankan economy.

A sector that has been adequately covered in the credit operations of the CRBs portfolio has gone into the sector of housing, in 1988. The importance of this sector in the credit disbursement of the CRBs has been quite consistent during the past few years. The relatively high exposure of CRB loans to this sector synergises with the recent upsurge in the investments on housing in the country. On the other hand, from the point of view of the borrowers, housing loans have become the most easily obtainable credit type available in the CRBs.

Pawn brokering has become the single most important credit type offered by the CRBs in the eyes of the borrowers. This category of borrowings has become

attractive because of its absence of formalities and timeliness of operations. As much as 50 percent of the total advances of Rs.764 million consisted of pawn brokering and the use of this facility continued to grow despite the suspension of pawn brokering operations in quite a large number of CRBs in various parts of the country.

The market place of the CRBs and the external influences on its investment climate have been quite turbulent during more recent times. This includes the virtual removal of the state patronage and shelter from the Co-operative Movement, the re-introduction of the operations of the free market forces in banking operations and the institution of a few competitive arrangements such as RRDBs, TCCS based Rural Banks, and the appointment of Agency banking outlets popularly known as PNNs, which have made the business of CRBs much more challenging than ever. These new challenges have influenced the CRBs to rethink their age old approaches to business, and conventional linkages with outside bodies. (For an overview and possible future directions for the CRBs, see paper by Mr. M.W.Panditha, pages 9 - 13).

The approaches to business operations of the CRBs covers a very wide area. Some of the integral parts of its coverage includes the organizational structure, management styles, systems and procedures etc. some of which are discussed in a separate paper (See paper by Sunil Wijesinghe). The linkages of the CRBs even include, its relationship with the People's Bank — their creator; the MPCSS; the State-through the Department of Co-operative Development; and other institutions.

There have been many committees set up to report on their coordination and studies carried out on these linkages. The suggestions of these various committees in a rhetorical sense boils down to a variety of options ranging from separation, to consolidation to regroupings and in extreme cases to winding up. However, in a very broad sense, the CRBs seem to need a re-structuring of one type or another. Such a restructuring would engulf not only its linkages with the outside world environment but also with those components that are internal to the CRBs.

U.V.