

**A Research Project on  
Cooperative Banks (DCCBs/ UCBs) and Risk Management in the Post Covid-  
19- A Study of Select Cooperative Banks of Pune, Ahmednagar, Satara &  
Mumbai**

**Research Team**

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**EXECUTIVE SUMMARY**

Cooperative institutions provide an alternative approach to financial inclusion in India through their geographic and demographic outreach to the urban and rural populace. During 2019-20, the cooperative sector, however, faced certain financial challenges. Episodes of frauds during the year affected the asset quality and profitability of urban cooperative banks (UCBs). During 2020-21 so far, uncertainties related to COVID-19 have affected the operations of this sector, as they did for the other financial institutions. Despite these weaknesses, this period also witnessed steering of reforms in the form of setting up of an umbrella organisation that will ease funding constraints to these banks, and amendment to the Banking Regulation Act which addressed the vexing issue of dual regulatory control. At end-March 2020, the sector consisted of 1,539 UCBs and 97,006 rural cooperative banks. Rural cooperatives make up 65 per cent of the total asset size of all cooperatives taken together. Despite the crucial role played by the sector, its asset size was only around 10 per cent compared to that of SCBs at end March-2020. Out of the 1539 UCBs there are 54 Scheduled UCBs which control share of 47% of assets, in the UCB sector. The financial soundness of the sector had been a concern over the years. Considerable initiatives have been taken to bring capacity building and adoption of technology. These initiatives notwithstanding, several structural issues confronted the sector such as dual regulation by the Reserve Bank and the Central/State governments, inability to combine the principles of cooperation with professionalism, lack of avenues to raise additional capital, the need of technological upgradation and more recently, incidences of frauds. The enactment of the Banking Regulation (Amendment) Act, 2020 was expected to address some of these problems.

## **Background of this Amendment:**

Under the Indian Constitution, cooperation is a state subject covered under the seventh schedule. During the mid-1960s, as demands for extension of the deposit insurance scheme to cooperative banks became more vocal and pressing, banking laws were made applicable to these banks so that the Reserve Bank may be able to exercise some control over them. This led to the dual control of the sector in which the Registrar of Cooperative Societies (RCS) or the Central Registrar of Cooperative Societies (CRCS) were empowered to look after their incorporation, registration, management, recovery, audit, supersession of Board of Directors and liquidation. The Reserve Bank was vested with regulatory oversight on banking activities of UCBs, State Cooperative Banks (StCBs) and District Central Cooperative Banks (DCCBs). The Reserve Bank was also entrusted with the supervision of UCBs. Reserve Bank's regulatory and supervisory powers were, however, limited in many ways, which affected its ability to take prompt corrective actions in case of irregularities. The amendment to the BR Act, 1949 seeks to protect the interests of depositors and strengthen cooperative banks by improving governance and oversight by the Reserve Bank, while enabling better access to capital. The amendment, which was notified on September 29, 2020 came into force for UCBs with retrospective effect i.e. from June 29, 2020. The amendment also provides the Reserve Bank extensive powers to supersede the management of the urban cooperative bank in consultation with the state government concerned. These measures are intended to protect the interest of the depositors while ensuring proper management and without causing any disruption to the financial system. These amendments are likely to improve the management and financial performance of cooperative banks and enable the Reserve Bank to regulate them more effectively.

## **Performance**

Growth in deposits, that constitute 90 per cent of the total resource base of UCBs, decelerated in 2019-20 after a revival in the previous year. Since 2017-18, the deposit deceleration in UCBs was starker than in SCBs, pointing to the difficulties faced by UCBs in raising resources. In FY'20 the deposit growth in UCBs was @ 3.50% compared to 6.10% in FY'19. Supervisory data available with the Reserve Bank suggest 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 GNPA ratio of UCBs again

surpassed that of SCBs. The rise in NPAs may partly be attributable to stagnant growth in loans and advances and weak balance sheets. At end-March 2020, more than 95 per cent of UCBs maintained CRAR above the statutory requirement of 9%. Historically, UCBs have had higher level of NPAs than SCBs. Since 2015-16, however, this position reversed, with the asset quality review (AQR) resulting in greater NPA recognition in SCBs, while asset impairment of UCBs inched up gradually over time.

### **Profitability**

The overall operating profit of UCBs took a major hit in 2019-20 as their interest income that constitutes around 89 per cent of total income, declined for the second consecutive year due to deceleration in investments and high growth of NPAs. This was accompanied by an increase in interest and non-interest expenditure. These factors combined with higher provisioning for contingencies – which more than doubled during the year – resulted in net losses in the consolidated balance sheet. The decline was mainly driven by the SUCBs, although marginal profits of NSUCBs provided a silver lining.

In Maharashtra: There are 494 UCBs present in all the 36 districts of the state, represented through 6620 branches, backed with 6767 ATMs. The total deposit as 31.3.2020 stands at Rs 314210 cr and Total Advances, as on 31.3.2020 is at Rs 193136 cr in Maharashtra.

Immediate Concerns: The unearthing of a fraud in a major UCB during 2019-20 affected Coop Banking sector's asset quality and profitability, with ripple effects on other related banks. Although the spill over was largely contained, this episode brought to the fore the systemic risks stemming from a low capital base, weak corporate governance, slower adoption of new technology and inadequate systems of checks and balances. In this light, the government and the Reserve Bank have undertaken several measures to improve governance and oversight of cooperative banking system. Last year Central government also established a Cooperation ministry to impart more guidance and address legal issues stemming out from multiple state functioning of UCBs.

Impact of Covid-19 Pandemic: Covid 19 has presented more problems for them. One of the most stringent lockdown in world was imposed in India in order to arrest the impact of the pandemic. Economic activity was brought to a complete halt for close to 8 weeks. It raised massive challenges for the Banking sector to reach out to the customers, challenges for the customers to reach to

Banks. It created transactional difficulties and logistic nightmares. With an already not so comfortable immediate background of challenges (as described in earlier paras), the Cooperative Banks anticipated the impact of pandemic with wariness, and took mitigating measures. So given their existing challenges it was to be seen as to how these cooperative Banks met the challenges of the pandemic, both during the pandemic and in the immediate aftermath of the pandemic. Given their overwhelming contribution to financial inclusion and massive reach, however, the need to strengthen the sector and render it self-sustaining cannot be over-emphasised in the interests of the communities they serve.

### **Scope of the Research**

Maharashtra has been badly affected by COVID-19. The Banks in general have been put to severe stress. Cooperative Banks even more so because of the reasons of inherent weakness as elaborated above. There is an urgent need to observe how different Coop Bank managements have reacted to the new RBI guidelines/Govt guidelines, audit norms and also the repayment stress created due to the pandemic. It is also needed to know what actions are being taken to source new business, implement new technology. There is a need to study the various operational measures, which highlights the risk management taken by the cooperative Banks. The study attempts towards better understanding of their current functioning, understand the gaps if any, which will help the concerned in formulating further policy guidelines. It would also help understand the need for any specific assistance which may be required for this sector in area of fund raising, providing relief on stressed assets etc.