Regional Rural Banks: Anachronistic or Aligned in the Current Schema

Gaurav Gupta

'गांव का पानी गांव में, गांव का पैसा गांव में ऋद्ध'[1]

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3.1. INTRODUCTION

With their ownership split between the Government of India, respective state governments and sponsor banks in the ratio of 50%, 15% and 35%, Regional Rural Banks (RRBs) were set up from 1975 onwards as an institution that combined the local feel and familiarity with the rural problems which the co-operatives possessed and the professionalism of commercial banks with a view to reaching the rural poor more extensively[2]. While the number of RRBs today stands at 43, with most states having one RRB each, between 1987 and 2005, each state had several smaller RRBs totalling 196 across the country.

The financial performance of RRBs over the years has been a mixed bag. Different committees and working-groups[3] have evaluated their performance and made recommendations regarding the future of RRBs. These recommendations and the subsequent action have mainly revolved around merging two or more RRBs. Recently, there has been a revival of debate around the privatization of Public Sector Banks (PSB) and RRBs[4].

Are RRBs different from commercial banks in the public and private sectors? Does the provision of finance for social objectives and financial viability go hand-in-hand? What had RRBs set out to achieve, and where do they stand today against those objectives? Is Return on Equity (ROE) a justified measure of evaluating the performance of RRBs? Is it time to write-off RRBs? These are a handful of questions this chapter attempts to discuss. Of the two financial institutions in India that operate with a primarily rural focus, i.e., Regional Rural Banks (RRBs) and Rural Co-operative Banks (RCB), this chapter focuses only on the former.

Before diving into various issues related to RRBs, a few background facts regarding rural India are considered. The farm sector in India is characterized by economically unviable small farm holdings that lead to a vicious cycle of lack of credit, low agricultural productivity, and insufficient incomes that in turn exacerbate the poor credit-worthiness of households dependent on agriculture as the primary source of income. This eventually leads to reliance on consumption-driven informal borrowing (RBI, 2019).

The focus of policymakers in India has disproportionately been on cities as drivers of growth at the expense of rural development (Chatterjee et al., 2016). However, the rural economy in India needs attention as structural transformation in India has not happened as predicted by economic theories. India's economy continues to have close to half of its population involved in Agriculture even though its share in GDP at 16% is now very small (State of Working India, 2018). Rural areas contribute half of India's GDP and employ more than two-thirds of the workforce (Chand et al., 2017). The importance of the non-farm sector has increased in rural economies over the years- its contribution up from 27% and 62% in 2005 in employment and GDP respectively to 42% and 67% in 2015 (Basole, 2017; Chand et al., 2017). The service sector (excluding construction), which is less employment intensive[5], has gained at the expense of manufacturing, whose contribution to rural non-farm employment has steadily declined from 32% in 1994 to 22% in 2010 to 17% in 2017 (Basole, 2017).

The above discussion highlights the need to focus on non-farm livelihoods in rural areas. While the National Bank for Agricultural and Rural Development (NABARD) has been working intensely with RRBs and RCBs to further the cause of livelihoods in the rural economy, as this chapter discusses, a re-doubling of efforts, especially by RRBs, would be required in the times to come for the rural economy in India to thrive. This chapter builds a strong case for further strengthening of RRBs as the main financial institution for those at the base of the pyramid and shows that while it is unfair to evaluate the performance of RRBs with the standard commercial lens, they have not performed as poorly as perceived.

3.2. PERFORMANCE OF RRBs

This section uses the standard commercial lens to evaluate the performance of RRBs. A discussion on their balance sheet composition is followed by a current year and long-term performance evaluation. The focus here is on RRBs as a group and not on individual RRBs, although a summary table with individual RRB-level performance on various parameters is provided in appendix 3.2.

3.2.1. Balance Sheet

Table 3.1 presents the combined balance sheet of all RRBs. A similar balance sheet for all PSBs is in appendix 3.1. The balance sheets of PSBs and RRBs differ mainly on two fronts: in the mix of loans and investments on the assets side and in the composition of deposits and borrowings on the liabilities side.

Investments in Statutory Liquidity Ratio (SLR) securities are above the hitherto mandated level of 18%[6] for both categories of banks, with RRBs at 31% and all PSBs at 24%. A higher Investments-to-Credit ratio for RRBs at 86% versus 54% for all PSBs signals higher risk aversion as RRBs choose to park more of their available funds/deposits in investments rather than giving more credit. This problem is especially acute for some banks that have been loss-making (current or accumulated)- refer to appendix 3.2.

RRBs are often referred to as institutions with poor credit-deposit (CD) ratios. While there is room for improvement, the CD ratio for all RRBs at 61% is not too far behind that of all PSBs in India at 64%[7]. Nonetheless, as in figure 3.1, the CD ratio of RRBs has remained in the range of 60-70% for the last 10 years. There is a huge variation in the CD ratios of different RRBs. As shown in appendix 3.2, some RRBs have CD ratios in excess of 100%, i.e., they give out more loans than they collect as deposits, and some loss-making RRBs have CD ratios less than 30%, i.e., for every ₹100 of deposits collected they are able to give out loans worth ₹30 or less.

Rural credit is a public good with multiplier effects on the rest of the economy. Rural savings escape parts of rural India with low credit-deposit ratios and are not made available for productive activities within that region/ state. Capital-adequacy norms[8] also have

Table 3.1. Aggregate Balance Sheet of RRBs (FY22)

Assets			Liabilities		
	₹ billion	Percentage		₹ billion	Percentage
Loans	**3,425**	**49%**	**Deposits**	**5,625**	**81%**
			Current accounts	120	2%
			Savings accounts	2,944	42%
			Time Deposits	2,561	37%
Investments	**2,957**	**42%**	**Borrowings**	**739**	**11%**
Deposits with sponsor banks	183	3%	NABARD	671	10%
Deposits with other banks	534	8%	Sponsor bank	39	0.6%
SLR securities	2,152	31%	Others	29	0.4%
Non-SLR securities	87	1%			
Fixed and others assets	**248**	**4%**	**Provision & other liabilities**	**197**	**3%**
Cash & cash equivalent	**334**	**5%**	**Capital**	**402**	**6%**
Cash	253	4%	Initial investment	149	2%
Call money / short notice balances	81	1%	Reserves	344	5%
			Accumulated losses	-91	-1%
TOTAL	**6,963**	**100%**	**TOTAL**	**6,963**	**100%**

Source: NABARD (2022)

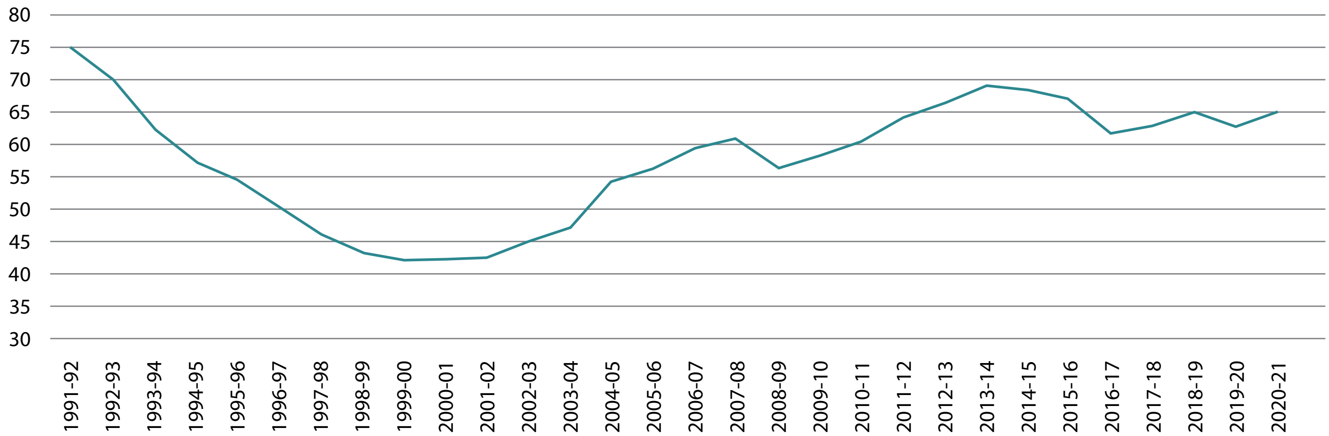

Figure 3.1. Credit-Deposit Ratio of RRBs (1992-2021)

Source: Table 58, Handbook of Statistics on the Indian Economy- RBI, 2021. Available here: https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/58T398C-637CB6A64E57AC16A8973B464104.PDF

a role to play in risk aversion by RRBs- risk weight for government securities (G-secs) is 2.5% versus 100% or more for retail lending.

For the financial year ending (FYE) 2022, RRBs placed ₹717 billion as deposits with other banks, including sponsor banks. These deposits are low-yielding assets for RRBs and act as a source of low-cost funds for the bigger banks[9].

On the liabilities side of the balance sheet, borrowings make up 11% of all liabilities for RRBs, most of which are from NABARD to facilitate targeted and subsidized lending. Overall, borrowings for all PSBs are lesser at 6% of their balance sheet. RRBs have a high share of low-cost deposits at 44%, most of which is from savings accounts at 42%. Current account deposits are minuscule at 2%, reflecting the fact that RRBs primarily cater to retail clientele in rural areas. Time deposits form 37% of all liabilities for RRBs versus 49% for all PSBs.

3.2.2. Operating Performance

A large-scale amalgamation exercise was undertaken in the early 2000s with a view to strengthening RRBs. The RRB franchise has been consistently profit-making since 1997-98, except in 2018-19 and 2019-20, owing to provisions made for pensions to their staff based on court rulings.

With a purely commercial lens, the overall performance of RRBs measured by ROE as a composite measure of return to shareholders has been unimpressive. For FYE22, RRBs delivered an ROE of 8%.

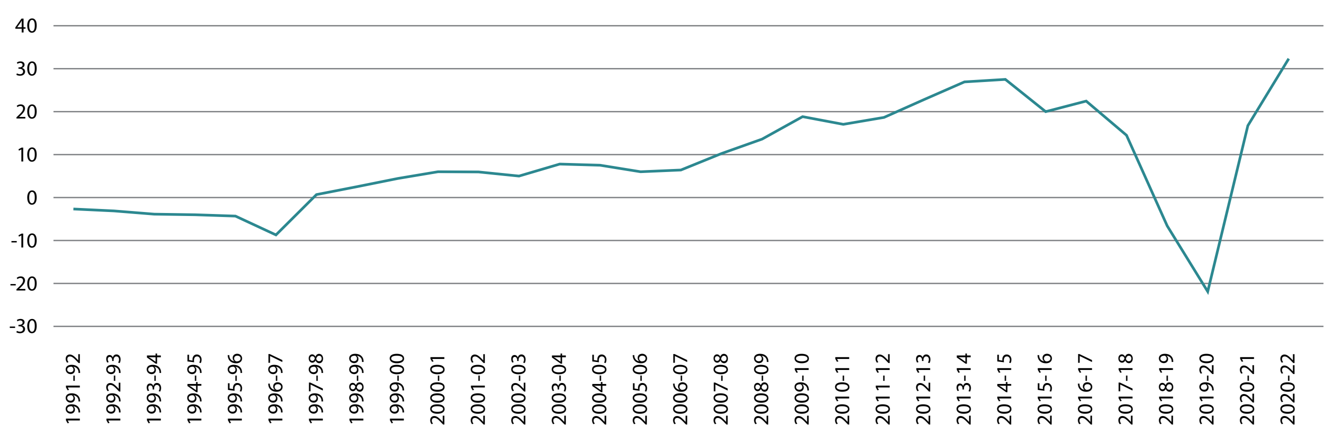

Figure 3.2. Net Profit/Loss of RRBs, in ₹billion (1992-2022)

Source: Antil (2020), Annual Report Department of Financial Services- Government of India and NABARD (2022)

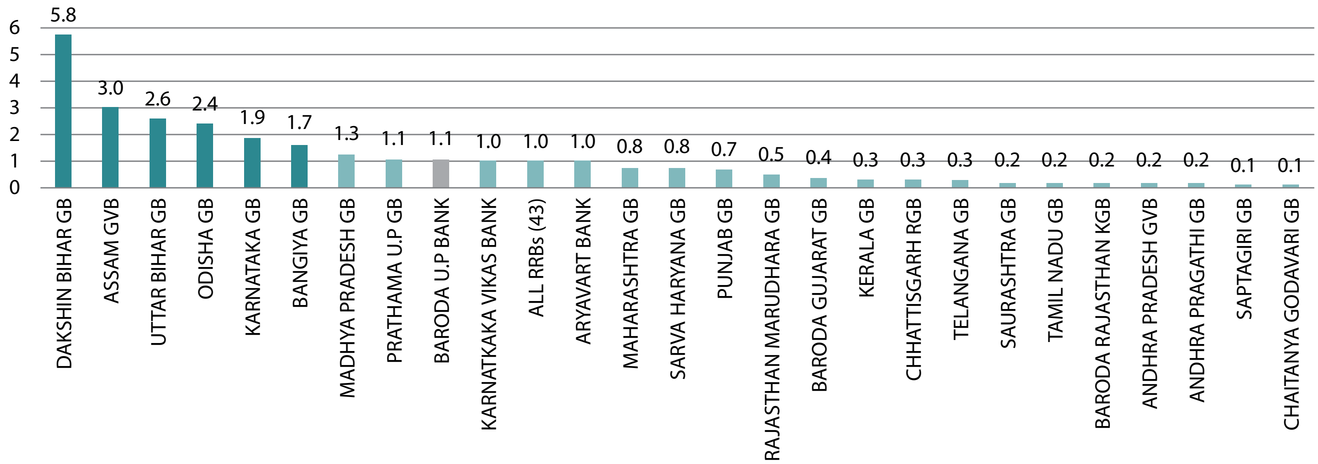

Figure 3.3. Share in NPA/Share in Loans of RRBs[11] (2022)

Source: Author's calculations based on NABARD (2022)

For the year-ending March 2022, overall NPA levels were at 9.15%. NPAs, however, were concentrated mainly in a few RRBs. Figure 3.3 shows the ratio of each RRB's share in NPA and share in loans. Banks in Bihar, Assam and Odisha contribute more than twice to overall RRB NPAs than they do to overall gross loans of RRBs. Besides agriculture, NPAs are high in MSME and education loans. In the state with the highest contribution of 24.3% to NPAs of RRBs, i.e., Bihar[10], NPAs in all categories of loans are high for the two RRBs operating there-agricultural loans at 55% and 24%, MSME loans at 64% and 25%, education loans at 55% and 60% and housing loans at 5.5% and 26%.

3.2.3. Yields on Loans and Rates Paid on Deposits

Considering that their borrowers have lower credit-worthiness compared with the majorly urban clientele of other banks in India owing to less secure livelihoods, lower average incomes, and high levels of NPAs, contrary to what one might expect them to do, RRBs charge relatively lower interest rates as shown in figure 3.4. Between FY20 and FY22, the maximum difference between yields from investments mainly in risk-free government securities and much riskier loans, mainly to individuals, was 271 basis points in FY21.

On the other hand, in line with the extant regulations applicable to all banks, including RRBs though the threshold criteria are different for RRBs and other scheduled commercial banks, the pricing of deposits is biased[12] against the poor and small savers in rural India. For example, in FY22, the average cost of deposits for RRBs was 4.11%. Net of inflation, these rates are low (or negative), especiallyin the context that for savers in rural India deposits are the primary instruments of saving.

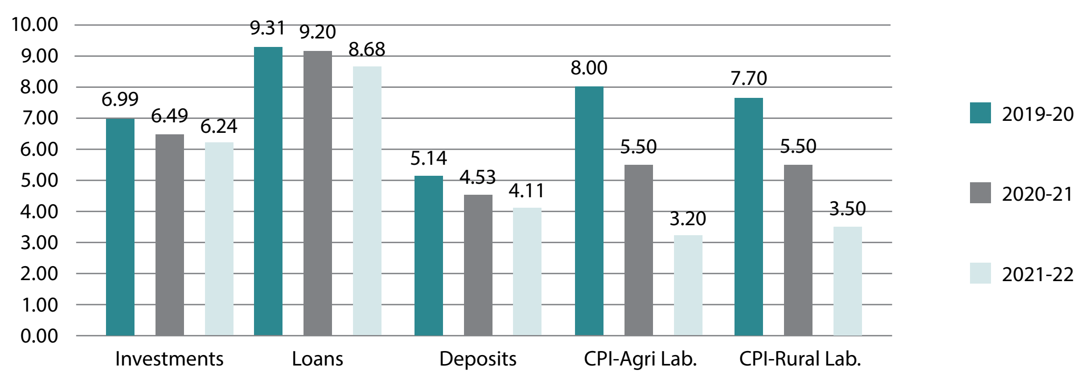

Figure 3.4. Pricing of Loans and Deposits and Rural Inflation (2020-22)

Source: NABARD (2022) and Economic Survey (2022).

3.3. CONSTRAINTS FACING RRBs

The analysis in the previous section is incomplete without a discussion on the difficult operating environment and the several constraints which are unique to RRBs.

RRBs suffer in terms of both the economies of scale and scope. The operations of an RRB are restricted to a specific state and, as is discussed in the next section, are primarily focused on the rural agricultural economy, which in India's case has not done well for several decades, barring a few instances of states led by the Green and White revolutions (Economic Survey 2016; OECD/ ICRIER 2018). Their directed credit portfolios do not enjoy the diversification necessary for a bank to mitigate credit risk. Political influence (Cole, 2008)and risks from frequent natural disasters exacerbate the difficult operating environment. Pricing and credit subsidy are highly distorted in favour of short-term credit, implying limited scope for productivity-enhancing investments by borrowers (RBI, 2019).

Compared to a commercial bank, RRBs' operations are purely domestic, lending is extensively balance sheet consuming, and there is limited scope for cross-selling other products that can generate fee/other income. For the banking sector in India, off-balance-sheet assets[13], which generate non-interest income and have lower capital requirements compared to on-balance-sheet products, are more than 100% of the value of on-balance-sheet assets. For RRBs[14], the percentage of off-balance-sheet products, if at all, is less than 1% of on-balance-sheets assets.

RRBs deal in simple lending products and have limited inter-linkages with the rest of the domestic or international banking sector. Yet RRBs are subjected to capital requirements at par with other commercial banks[15]. Retail lending is the sine qua non for RRBs in rural areas, and lending to this segment attracts 100% or more risk-weighting versus investments in G-Secs at 2.5%.

Considering their involvement on the Boards of Directors of RRBs, owners take little interest in the running and oversight of operations. Government of India has not nominated independent directors on the boards of RRBs. Even in the case of some of the well-performing RRBs, State Government nominee directors have not attended a single board meeting throughout the entire financial year. The Chairman of the Board is also the senior most executive of the bank and is deputed from the sponsor bank along with a small team of other senior officers.

Dependence on sponsor banks is high and bordering on being exploitative. A case in point is the reliance of PSBs on RRBs to meet their PSL targets by the purchase of Priority Sector Lending Certificates (PSLC). The credit risk of this over-achievement of PSL targets is entirely borne by RRBs in the case of the sale of PSLC.

RRBs below a certain threshold level of profitability[16] and capital are not allowed to offer internet and mobile banking (Tankha, 2015). Even the clientele of RRBs is not necessarily very tech-friendly, so migration of transactions to low-cost channels is challenging with a view to reducing operational costs.

Health of RRBs depends on the vagaries of nature, and the geography they operate in also plays a key role in their fortunes. Risk cost and poverty profile of regions/ states of operation are positively related, i.e., relatively less-well-performing RRBs are in states with higher levels of poverty.

3.4. WHY ARE RRBs IMPORTANT?

3.4.1. The Focus of RRBs is Mainly on Rural India

Almost 70% and 90% of all RRB branches are in rural and rural and semi-urban areas combined respectively (table 3.2). RRBs contribute to 14% of

Table 3.2. Branches by Bank-type[17] and Area (March 2022)

	Rural	Semi-urban	Urban	Metropolitan	Total
PSB	28,845	24,123	18,744	18,452	90,164
PVB	7,862	12,036	8,225	10,649	38,772
SFB	1,036	2,150,	1,488	1,117	5,791
RRB	15,425	4,837	1,636	438	22,336
LAB	8	42	17	14	81
Payments	33	293	325	70	721
Total	53,209	43,481	30,435	30,740	1,57,865

Source: RBI's database on Indian economy/ Bank Branch Statistics (Quarterly/ Bank-wise and Population Group-wise Number of FunctioningOffices of Commercial Banks). Available here- https://dbie.rbi.org.in/DBIE/dbie.rbi?site=publications all bank branches in India and to 29% of all bank branches in rural India. PSBs with 55% share are clear leaders in the share of branches in rural and rural and semi-urban combined. Next, with a 21% share, each private sector banks (PVBs) and RRBs have almost the same number of branches in rural and semi-urban combined. However, PVBs are focused more on semi-urban and RRBs more on rural areas.

3.4.2. RRBs are an Important Institution for the Financial Inclusion of the Rural Poor

RRBs are the primary publicly-owned institution driving the financial inclusion of the rural poor. As in table 3.3, RRBs carry higher targets[18] with respect to social priorities compared to other classes of banks, i.e., commercial and small finance banks (SFB). Commercial banks have a target of 40% of their advances (Adjusted Net Bank Credit- ANBC) to PSL, whereas SFBs and RRBs both carry a target of 75%. Both Commercial Banks and SFBs carry lower targets for lending to the weaker sections.

What further differentiates RRBs from other banks is that their actual achievement of PSL targets is way higher than the minimum requirement. Achievement for FY22 stood above 90%, 46% and 79% for overall PSL, direct advances to agriculture and weaker sections respectively. No other institution comes close to this achievement of RRBs.

3.4.3. RRBs Perform Better Than Other Categories of Banks in Rural Areas and Aspirational Districts

RRBs have a deeper reach in rural areas and aspirational districts and perform better on this front compared to PSBs, PVBs and SFBs. RRBs contribute to 3.1% of total bank loans outstanding in India and a much higher 10.4% of total bank loans outstanding in aspirational districts. Considering only rural areas, from tables 3.4 and 3.5, the share of RRBs of total bank outstanding in all districts is 21% and in aspirational districts is 30%.

Aspirational districts contribute to 11.1% and 16.8% of all lending in rural areas by SCBs (ex-RRBs) and RRBs respectively. PVBs and SFBs have low or negligible shares and, clearly, the focus of RRBs on rural and hitherto deprived regions is much more. It must, however, be noted that SFBs as a category of institutions are relatively new and came into existence only in 2015[19].

Looking at district-level[20] data from RBI, of the 713 districts covered, in 111 districts, the share of RRBs in total bank lending was higher than that of PSBs- RRBs had lent ₹641 billion in comparison with ₹182 billion by PSBs. In the 23 aspirational districts of these 111, RRBs had lent ₹138 billion in comparison with ₹76.4 billion by PSBs.

RRBs and PSBs have shares of 22% and 42% in the total number of borrower accounts. The same numbers for PVBs and SFBs stand at 32% and 3% respectively. If one looks at total lending, the share of RRBs and PSBs is 21% and 60% respectively, clearly indicating the small borrower focus of RRBs. On the other hand, the share of private sector banks and SFBs in overall lending (in rural areas) is 18% and 1%, much lower than their shares in the number of accounts. Average outstanding per borrower account for RRBs is ₹115,472, whereas that for PSBs is 54% higher at ₹177,880.

As far as savings are concerned, RRBs have a 17% share[21] in total deposits of ₹18 trillion of all scheduled commercial banks from rural India

Table 3.3. Targets for Social Priorities (as of March 2022)

	Commercial Banks	SFB	RRB	Achievement- FY22
Priority sector adv to total adv.	40%	75%	75%	90.1%
Direct agri adv to total adv.	18%	18%	18%	46.4%
Small & marginal farmers (within agri)^	9%	9%	9%	26.8%
Micro-enterprises	7.5%	7.5%	7.5%	12.0%
Weaker section adv to total adv. @	11%	11%	15%	78.9%

^ Targets till FY22 | @ Targets for Domestic Commercial Banks and SFBs till FY22 |adv.- advances

Source: https://m.rbi.org.in/scripts/BS_ViewMasDirections.aspx?id=11959#Targets

Table 3.4. Share of Banks in Rural Areas, All Districts (March 2021)

Rural areas only All districts	Accounts (million)	Limit (₹ billion)	Outstanding (₹ billion)	Limit per acct. (₹ '000)	O/s per acct. (₹ '000)	Limit utilisation (%)	Share in accts. (%)	Share in o/s (%)
FB	0.1	55	24	631	276	44%	0.1%	0.2%
PVB	28.3	2,783	1,948	98	69	70%	32.4%	18.0%
PSB	36.5	9,517	6,489	261	178	68%	41.7%	60.0%
RRB	19.6	2,794	2,266	142	115	81%	22.4%	20.9%
SFB	3.0	134	91	44	30	68%	3.4%	0.8%
Total	87.5	15,283	10,817	175	124	71%	100.0%	100.0%

Source: RBI, Basic Statistical Returns-1

Table 3.5. Share of Banks in Rural Areas, Only Aspirational Districts (March 2021)

Rural areas only Aspirational districts	Accounts (million)	Limit (₹ billion)	Outstanding (₹ billion)	Limit per acct. (₹ '000)	O/s per acct. (₹ '000)	Limit utilisation (%)	Share in accts. (%)	Share in o/s (%)
FB	0.002	0.2	0.2	114	110	96%	0.02%	0.02%
PVB	2.4	259	167	108	70	65%	20.9%	13.1%
PSB	4.7	872	718	184	151	82%	41.4%	56.0%
RRB	3.7	454	380	123	102	84%	32.4%	29.6%
SFB	0.6	23	16	39	27	68%	5.3%	1.2%
Total	11.4	1,609	1,281	141	112	80%	100.0%	100.0%

Source: RBI, Basic Statistical Returns-1

3.4.4. RRBs Have a Higher Share in Lending to the Weaker Sections

State-specific comparison of the performance of RRBs with other banks using State-level Bankers' Committee (SLBC)[22] data from West Bengal (WB)[23], Uttar Pradesh (UP)[24], Andhra Pradesh (AP)[25] and Gujarat (GJ)[26] provides a comparison of RRBs with other banks and further demonstrates the role played by RRBs as an institution of the poor. For each of the states in table 3.6, where available, the first two columns provide the state-specific share of all categories of banks in borrower accounts as well as in amounts borrowed.One can consistently note that RRBs are an important institution for those in agriculture and those who belong to the weaker sections of society. RRBs share of lending to MSMEs is low. For weaker sections, RRBs provide 14.2%, 26.4%, 18.5% and 6.5% of all credit made available to them in WB, UP, AP and GJ respectively.

Table 3.6. Share of banks for Priority Sector Loans for select states (as of March 2021)

WB	Total advances		Agriculture		MSME		Weaker sections		Minority		SC/ST	
	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount
PSBs	26.5%	57.5%	32.7%	53.9%	42.8%	57.4%	35.5%	48.2%	18.3%	54.2%	15.0%	41.1%
PVBs	50.2%	35.2%	29.4%	21.6%	37.4%	38.0%	42.4%	31.3%	69.1%	38.1%	66.4%	40.1%
SFB	4.0%	0.6%	3.4%	1.3%	4.9%	0.4%	5.3%	3.3%	4.1%	1.2%	6.5%	2.6%
RRBs	5.8%	2.6%	9.7%	12.7%	14.1%	3.5%	6.0%	14.2%	5.2%	6.3%	8.0%	10.4%
Co-ops	13.5%	4.0%	24.7%	10.6%	0.9%	0.6%	10.8%	3.1%	3.4%	0.3%	4.2%	5.7%

Table 3.6. Share of banks for Priority Sector Loans for select states (as of March 2021)

UP	Total advances		Agriculture		MSME		Weaker sections		Minority		SC/ST	
	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount
PSBs	-	62.8%	50.4%	60.0%	-	68.4%	-	59.4%	39.0%	69.3%	-	-
PVBs	-	26.0%	8.0%	9.2%	-	27.7%	-	12.2%	28.4%	14.0%	-	-
SFB	-	0.7%	3.5%	0.5%	-	0.4%	-	2.1%	4.2%	0.8%	-	-
RRBs	-	8.4%	28.7%	25.2%	-	3.5%	-	26.4%	28.4%	15.9%	-	-
Co-ops	-	2.1%	9.4%	5.1%	-	0.0%	-	0.0%	0.0%	0.0%	-	-

AP	Total advances		Agriculture		MSME		Weaker sections		Minority		SC/ST	
	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount
PSBs	55.2%	68.6%	58.7%	63.8%	70.1%	61.7%	-	73.5%	-	64.3%	-	73.3%
PVBs	15.4%	18.7%	4.7%	9.8%	8.1%	33.8%	-	6.9%	-	11.1%	-	5.8%
SFB	1.3%	0.2%	1.4%	0.2%	0.2%	0.2%	-	0.1%	-	0.2%	-	0.1%
RRBs	15.3%	7.4%	19.1%	15.8%	20.9%	4.2%	-	18.5%	-	18.8%	-	15.3%
Co-ops	12.9%	5.0%	16.0%	10.3%	0.7%	0.1%	-	1.0%	-	5.7%	-	5.6%

GJ	Total advances		Agriculture		MSME		Weaker sections		Minority		SC/ST	
	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount	A/c (#)	Amount
PSBs	28.6%	47.0%	37.3%	49.9%	48.4%	41.4%	38.4%	57.5%	36.8%	49.7%	49.1%	72.2%
PVBs	50.6%	46.7%	22.0%	23.3%	40.4%	55.8%	28.5%	19.8%	31.6%	40.5%	25.1%	14.6%
SFB	8.1%	1.1%	8.8%	1.9%	7.3%	1.6%	18.3%	5.2%	28.6%	6.3%	19.5%	4.8%
RRBs	3.7%	1.5%	9.4%	7.5%	2.2%	0.6%	6.1%	6.5%	2.1%	2.4%	2.7%	3.8%
Co-ops	8.9%	3.6%	22.5%	17.3%	1.7%	0.5%	8.8%	11.1%	0.9%	1.1%	3.6%	4.6%

Source: SLBC documents

3.4.5. Higher Proportion of Loans to Exclusively Women-Member SHGs

Under the SHG-Bank Linkage program, till March 2022, Commercial Banks, RRBs and Co-operative Banks have together linked 11.9 million SHGs with savings balances of ₹307 billion, ₹138 billion, and ₹27 billion respectively. Of these 11.9 million SHGs, 6.7 million are credit-linked, with a total of ₹ 1.5 trillion in credit.

RRBs have a share of approximately 30% number of SHGs linked, savings mobilization and credit provided to SHGs. Slightly less than 10% of all loans given by RRBs are to exclusively women-member SHGs. RRBs also have the lowest % of NPAs in their SHG credit portfolio at 3.14% (table 3.7). In their SHG portfolio, 96% of all mobilized savings and 98% of all credit provided by RRBs is to exclusively women SHGs. The same figures for Commercial Banks stand at 86% and 93% and for Co-operatives are at 92% and 96%.

Table 3.7. Share of Banks[27] in SHG Savings and Credit (as of March 2022)

All SHGs	Share in savings		Share in loans		NPA
	No. of SHGs	Amount	No. of SHGs	Amount	% of SHG loans
Commercial banks	57.9%	65.0%	62.0%	68.0%	3.23%
RRBs	30.1%	29.2%	30.1%	26.1%	3.14%
Co-operative banks	12.0%	5.8%	7.9%	5.9%	13.29%
Total	100.0%	100.0%	100.0%	100.0%	3.80%

Source: NABARD, Status of Microfinance in India (2021-22)

Table 3.8. ROE of RRBs (FYE2022)

	No. of RRBs	Total Profits (₹ billion)	Total Owned Funds (₹ billion)	Average ROE	Cumulative Average ROE
>= 25%	2	2.0	6.9	28.5%	
>= 20% & < 25%	4	10.8	45.8	23.7%	24.3%
>= 15% & < 20%	4	11.4	67.2	16.9%	20.2%
>= 10% & < 15%	7	9.5	75.2	12.6%	17.3%
>= 0% & < 10%	17	7.5	183.8	4.1%	10.9%
Negative ROE	9	-9.0	23.0	-39.1%	8.0%
All RRBs	43	32.2	401.8	8.0%	

Source: Author's calculations based on NABARD (2022)

3.5. RRBs PERFORMANCE: A LONG-TERM VIEW

In the context of the recent revival of debate around the privatization of PSBs in general and of RRBs in particular, the purpose of this section is to highlight that RRBs should not be brushed aside as a category of unsuccessful institutions. Some RRBs with a small amount of infused capital have generated a surplus multiple times of the funds invested. Given the leverage in the banking business, this creates huge multiplier effects on the local/ regional rural economies.

In an earlier section, it was highlighted that in FY22, RRBs generated an ROE of 8%, which is low. This overall number, however, masks the huge variation in profitability of individual banks and the overall performance is pulled down by a few RRBs in areas/ states that have high poverty levels, a high proportion of landless labour in agriculture and are prone to frequent natural disasters. Table 3.8 breaks down the performance of RRBs into different categories of ROE. The top performing 10 and 17 RRBs generated an average ROE of 20.2% and 17.3% respectively in FY22. Barring the 9 loss-making RRBs in FY22, 34 RRBs generated an overall ROE of 10.9% in FY22. This, by no means, can be classified as poor performance, given the constraints that RRBs operate under.

The total capital infused in RRBs by all owners from 1975 to 2022 is ₹148.8 billion. Using this, through their operations over the years, RRBs have been able to accumulate ₹253 billion of incremental reserves. Thus, the total capital available for lending business, i.e., Total or Net Owned Funds, is ₹401.8 billion.

Table 3.9 presents a simple picture of the long-term performance of the 43 RRBs that exist today. RRBs have been classified into 3 buckets according to the absolute amount of capital infused in each of them, i.e., ₹0-1 billion, ₹1-5 billion and more than ₹5 billion each. The other two key variables in this table include the absolute amount of capital infused by RRBs owners and the ratio of net owned funds to infused capital. This ratio measures how much a rupee of investment by owners has grown into and is now available as total capital to the bank for carrying out its business. For all RRBs, this ratio stands at 2.7 after considering the latest round of investment of ₹64.9 billion in FY22.

Almost 50% (21 out of 43) of all RRBs are in the less than ₹1 billion bucket of infused capital. These 21 banks have totally had ₹9.17 billion, that is 6%, of all capital infused in the 43 RRBs of ₹148.8 billion. In this category, the best-performing bank,i.e., Chaitanya Godavari Bank in Andhra Pradesh, with a ratio of Net Owned Funds to Infused Capital at 103.2, now has a total available capital base of ₹7.7 billion against an investment of merely ₹74 million by all its owners.

The problem with respect to the poor financial performance of RRBs, if any, lies in a handful of banks and states. Most of the poor-performing RRBs are in the last bucket, with each bank having received more than ₹5 billion of capital. These 9 institutions have consumed 70% of all capital infused in RRBs from 1975 till 2022. To summarize, the well-performing institutions have required very small amounts of investment by the owners and only where problems have persisted because of geography, political institutions and overall growth/ development-related issues which are beyond the direct influence of RRBs, the owners have had to infuse more capital to keep the banks in business. The entire RRB franchise, therefore, cannot be labelled as poor performing.

Table 3.9. Ratio of Net Owned Funds to Infused Capital (2022)

Capital buckets	Regional Rural Bank	Ratio of Net Owned Funds to Infused Capital	Infused Capital (₹ million)	% Total Infused Capital
₹ 0-1 billion	Chaitanya Godavari GB	103.2	74	
	Telangana GB	84.9	181	
	Andhra Pragathi GB	75.4	423	
	Meghalaya RB	72.6	26	
	Saptagiri GB	65.3	178	
	Karnataka Vikas GB	51.1	240	
	Andhra Pradesh GVB	51.1	941	
	Punjab GB	46.8	254	
	Sarva Haryana GB	38.6	463	
	Tamil Nadu GB	35.1	470	
	Prathama U.P GB	34.2	605	
	Saurashtra GB	26.4	245	
	Himachal Pradesh GB	9.8	154	
	Puduvai Bharathiyar GB	6.0	135	
	Baroda Gujarat GB	6.0	783	
	Mizoram RB	5.1	547	
	Uttar Banga KGB	2.1	908	
	Arunachal Pradesh RB	0.7	601	
	Nagaland RB	0.2	237	
	Manipur RB	0.2	731	
	J&K GB	0.1	972	
	Total		**9,167**	**6%**
₹ 1-5 billion	Karnataka GB	18.0	1,176	
	Baroda U.P. Bank	11.7	2,079	
	Aryavart Bank	8.8	2,631	
	Baroda Rajasthan KGB	6.7	3,093	
	Rajasthan Marudhara GB	4.8	1,819	
	Tripura GB	4.6	2,656	
	Chhattisgarh RGB	4.5	2,159	
	Maharashtra GB	2.1	3,126	
	Jharkhand RGB	1.9	2,508	
	Uttarakhand GB	1.7	1,531	
	Assam GVB	0.7	4,767	
	Paschim Banga GB	0.2	4,898	
	Ellaquai Dehati Bank	-0.0	2,938	
	Total		**35,382**	**24%**
> ₹ 5 billion	Kerala GB	2.4	6,359	
	Madhya Pradesh GB	0.8	12,780	
	Dakshin Bihar GB	0.7	10,537	
	Uttar Bihar GB	0.4	14,456	
	Bangiya GVB	0.4	15,069	
	Madhyanchal GB	0.4	8,758	
	Odisha GB	0.2	14,092	
	Utkal GB	0.1	14,487	
	Vidharbha Konkan GB	-0.2	7,713	
	Total		**104,252**	**70%**
	All RBBs		148,801	

Source: Author's calculations based on NABARD (2022)

3.6. THE ROAD AHEAD: POLICY RECOMMENDATIONS

RRBs should continue to focus on a double bottom line instead of just on profits. As the above analysis has demonstrated, several individual RRBs have managed to fulfil and overachieve their financial inclusion obligations as well as remain profitable to fund future growth.

Individual RRBs have spent decades in their respective geography of operation. Instead of continuing to depend on sponsor banks, individual RRBs should focus on becoming independent and become leaders and guide other institutions on rural lending in their specific states/ regions.

RRBs, as well as NABARD, should think about augmenting their contributions by further focusing and developing capabilities to increase lending towards the rural non-farm economy. Lending to PSUs operating in the state should be routed through RRBs- at least some share. As part of compensation for their contributions to the local rural economies, RRBs should have accounts of local bodies as well as get a share of state governments' business.

Even though their clientele may not be as tech-friendly as the urban clientele, RRBs should be given the freedom to offer basic facilities such as mobile and internet banking. In the times to come, they will face stiff competition from SFBs and Payments Banks, who will be targeting the assets and liabilities side of their business respectively. Both these types of banks do not face the same stringent constraints as the RRBs do and are also free to expand in all parts of the country.

Setting up an umbrella entity for RRBs on the lines of the proposed National Federation of Urban Co-operative Banks and Credit Societies Ltd. could help RRBs lower costs by consolidating operations processing. This would bring in the much-needed economies of scale given the small-ticket nature of RRBs' business on both the assets and liabilities side of the business. This umbrella entity could also act as a common internet and mobile banking provider for the clientele of RRBs.

Finally, RRBs as an institution need more liberal support from the owners- in capital contribution where required as well as in the strengthening of their Boards. Private sector initiative on lines similar to RRBs has already failed, i.e., local area banks. For the poor, un(der)-served and financially excluded, the private sector cannot be the only ray of hope. As the analysis in this chapter has shown, these publicly owned institutions may not have addressed all the challenges, but they have surely contributed in the right direction. The future holds promise for the rural economy, and RRBs can be influential partners in this journey of transformation. It may be too soon for the government to give up on RRBs and steer them towards possible privatization. The Kiss of Death Can Wait.

APPENDICES

APPENDIX A.3.1. Balance Sheet of All PSBs (FY21)

Assets			Liabilities		
	₹ billion	Percentage		₹ billion	Percentage
Loans	**63,488**	**54%**	**Deposits**	**99,008**	**84%**
			Current accounts	6,845	6%
			Savings accounts	34,629	30%
			Time Deposits	57,534	49%
Investments	**34,009**	**29%**	**Borrowings**	**7,189**	**6%**
Deposits with other banks		0%			
SLR securities	27,900	24%			
Non-SLR securities	6,109	5%			
Fixed and others assets	**8,489**	**7%**	**Provision & other liabilities**	**4,033**	**3%**
Cash & cash equivalent	**11,329**	**10%**	**Capital**	**7,085**	**6%**
Cash	5,391	5%	Initial investment	593	1%
Call money / short notice balances	5,937	5%	Reserves	6,491	6%
			Accumulated losses		
TOTAL	**1,17,314**	**100%**	**TOTAL**	**1,17,314**	**100%**

Source: RBI, Report on Trend and Progress of Banking in India (2021)

APPENDIX A.3.2. RRB Level Summary of Performance- Key Statistics

Regional Rural Bank	Infused Capital (₹ million)	Gross Loans (₹ million)	Net Profit-FY22 (₹ million)	Net Owned Funds to Infused Capital	Share in Infused Capital	Gross NPA	Share in Loans (%)	Share in NPA (%)	Share in NPA/ Share in Loans	CD-ratio (%)	ROE
Chaitanya Godavari GB	74	73,933	1,623	103.2	0.1%	0.91%	2.04	0.20	0.10	101	21.1%
Telangana GB	181	1,12,729	3,732	84.9	0.1%	2.39%	3.11	0.81	0.26	100	24.3%
Andhra Pragathi GB	423	2,01,294	4,169	75.4	0.3%	1.47%	5.55	0.89	0.16	104	13.1%
Meghalaya RB	26	9,469	226	72.6	0.0%	7.62%	0.26	0.22	0.83	27	12.0%
Saptagiri GB	178	71,467	2,010	65.3	0.1%	1.29%	1.97	0.28	0.14	77	17.3%
Karnataka Vikas GB	240	13,109	319	51.1	0.2%	9.37%	3.61	3.70	1.02	72	2.6%
Andhra Pradesh GVB	941	2,39,549	8,138	51.1	0.6%	1.74%	6.60	1.25	0.19	87	16.9%
Punjab GB	254	87,121	1,086	46.8	0.2%	6.61%	2.40	1.74	0.72	67	9.1%
Sarva Haryana GB	463	1,18,348	1,407	38.6	0.3%	7.19%	3.26	2.56	0.79	59	7.9%
Tamil Nadu GB	470	1,56,173	2,293	35.1	0.3%	1.89%	4.30	0.89	0.21	90	13.9%
Prathama U.P GB	605	1,73,350	605	34.2	0.4%	9.99%	4.78	5.22	1.09	70	2.9%
Saurashtra GB	245	55,976	1,850	26.4	0.2%	2.19%	1.54	0.37	0.24	72	28.6%

Karnataka GB	1,176	2,43,218	475	18.0	0.8%	17.26%	6.70	12.65	1.89	71	2.2%
Baroda U.P. Bank	2,079	20,811	629	11.7	1.4%	9.78%	5.73	6.13	1.07	37	2.6%
Himachal Pradesh GB	154	28,043	46	9.8	0.1%	5.74%	0.77	0.48	0.63	37	3.0%
Aryavart Bank	2,631	2,02,135	627	8.8	1.8%	8.81%	5.57	5.36	0.96	63	2.7%
Baroda Rajasthan KGB	3,093	1,83,312	5,020	6.7	2.1%	1.77%	5.05	0.98	0.19	80	24.1%
Puduvai Bharathiyar GB	135	9,330	103	6.0	0.1%	2.07%	0.26	0.06	0.23	89	12.7%
Baroda Gujarat GB	783	58,543	292	6.0	0.5%	3.57%	1.61	0.63	0.39	53	6.2%
Mizoram RB	547	25,103	494	5.1	0.4%	5.29%	0.69	0.40	0.58	59	17.6%
Rajasthan Marudhara GB	1,819	1,02,597	954	4.8	1.2%	4.61%	2.83	1.43	0.50	64	11.0%
Tripura GB	2,656	28,124	1,431	4.6	1.8%	6.78%	0.78	0.57	0.74	36	11.7%
Chhattisgarh RGB	2,159	52,111	275	4.5	1.5%	2.56%	1.44	0.40	0.28	37	2.8%
Kerala GB	6,359	1,92,791	1,241	2.4	4.3%	3.08%	5.31	1.79	0.34	85	8.1%
Uttar Banga KGB	908	27,677	451	2.1	0.6%	6.15%	0.76	0.51	0.67	72	23.7%
Maharashtra GB	3,126	80,290	51	2.1	2.1%	7.19%	2.21	1.74	0.79	53	0.8%
Jharkhand RGB	2,508	40,068	733	1.9	1.7%	6.42%	1.10	0.78	0.70	43	15.5%
Uttarakhand GB	1,531	27,908	68	1.7	1.0%	7.21%	0.77	0.61	0.79	41	2.7%
Madhya Pradesh GB	12,780	12,242	-1,253	0.8	8.6%	11.74%	3.36	4.32	1.28	69	-12.9%
Arunachal Pradesh RB	601	2,573	123	0.7	0.4%	3.86%	0.07	0.03	0.42	23	28.1%
Dakshin Bihar GB	10,537	1,05,787	-2,986	0.7	7.1%	52.74%	2.92	16.81	5.77	40	-39.3%
Assam GVB	4,767	50,441	0	0.7	3.2%	27.74%	1.39	4.22	3.03	37	0.0%
Uttar Bihar GB	14,456	1,04,202	-877	0.4	9.7%	23.95%	2.87	7.52	2.62	54	-14.3%
Bangiya GVB	15,069	74,756	286	0.4	10.1%	15.18%	2.06	3.42	1.66	37	5.1%
Madhyanchal GB	8,758	32,236	327	0.4	5.9%	17.90%	0.89	1.74	1.96	30	10.4%
Nagaland RB	237	430	-10	0.2	0.2%	1.93%	0.01	0.00	0.21	34	-23.1%
Manipur RB	731	2,221	-35	0.2	0.5%	17.55%	0.06	0.12	1.92	48	-27.0%
Paschim Banga GB	4,898	34,395	-996	0.2	3.3%	10.42%	0.95	1.08	1.14	55	-116.6%
Odisha GB	14,092	62,040	49	0.2	9.5%	22.29%	1.71	4.17	2.44	38	2.1%
J & K GB	972	28,786	-274	0.1	0.7%	5.28%	0.79	0.46	0.58	59	-224.3%
Utkal GB	14,487	31,010	23	0.1	9.7%	21.79%	0.85	2.04	2.38	35	3.1%
Ellaquai Dehati Bank	2,938	5,658	-340	-0.0	2.0%	14.53%	0.16	0.25	1.59	40	
Vidharbha Konkan GB	7,713	32,124	-2,203	-0.2	5.2%	12.40%	0.89	1.20	1.36	54	-143.8%
All RRBs	1,48,801	36,28,380	32,185	2.7	100%	9.15%	100	100	1	61	8%

Source: Author's calculations based on NABARD (2022)

APPENDIX A.3.3. Market Share of Banks (Rural and Semi-Urban Areas)

Rural + semi-urban All districts	Accounts (million)	Limit (₹ billion)	Outstanding (₹ billion)	Limit per acct. (₹ '000)	O/s per acct. (₹ '000)	Limit utilisation (%)	Share in accts. (%)	Share in o/s (%)
FB	0.3	173	103	646	383	59%	0.2%	0.4%
PVB	52.6	9,330	6,527	177	124	70%	32.3%	25.1%
PSB	73.1	21,224	15,804	291	216	74%	44.9%	60.9%
RRB	25.6	3,735	3,080	146	121	82%	15.7%	11.9%
SFB	11.3	645	451	57	40	70%	7.0%	1.7%
Total	162.9	35,128	25,965	216	159	74%	100.0%	100.0%

Rural + semi-urban Aspirational districts	Accounts (million)	Limit (₹ billion)	Outstanding (₹ billion)	Limit per acct. (₹ '000)	O/s per acct. (₹ '000)	Limit utilisation (%)	Share in accts. (%)	Share in o/s (%)
FB	0.02	5	3	326	182	56%	0.1%	0.1%
PVB	5.5	849	607	155	111	71%	26.3%	20.8%
PSB	9.2	2,187	1,768	237	192	81%	44.2%	60.5%
RRB	4.6	589	494	128	107	84%	22.1%	16.9%
SFB	1.5	73	52	47	33	70%	7.4%	1.8%
Total	20.9%	3,704	2,923	178	140	79%	100.0%	100.0%

Source: RBI, Basic Statistical Returns-1

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END NOTES

1. Reproduced from the Report of the Agricultural Credit Review Committee- also known as Khusro Committee, 1989.
2. https://rbidocs.rbi.org.in/rdocs/Publications/PDFs/6OPERATIONSANDPERFORMANCEC128869813DB453EBC97A32BE448E781.PDF
3. https://rbidocs.rbi.org.in/rdocs/content/PDFs/78971.pdf
4. https://www.ncaer.org/events/IPF-2022/Paper-2-IPF-2022-PoonamGuptaandArvindPanagariya.pdf and https://rbidocs.rbi.org.in/rdocs/Bulletin/PDFs/02_PPSB18082022EA8FD038503549209E1450595170EFFD.PDF
5. Employment intensity of a sector is defined as its percentage contribution to overall employment divided by its percentage contribution to overall GDP.
6. Source: https://www.rbi.org.in/ and https://rbidocs.rbi.org.in/rdocs/PublicationsPDFs/44TF2910755D03B4ECFA38E07F37FD1BB42.PDF
7. Please note that the aggregate financials for RRBs are for the financial year ending March 2022 while those for all PSBs are as of the financial year ending March 2021.
8. https://www.nabard.org/auth/writereaddata/file/Report%20of%20the%20Working%20Group%20on%20RBS.pdf
9. The CRR and SLR requirements for such excess deposits which are further invested with other banks fall on RRBs alone. Refer to exempted categories here:https://www.rbi.org.in/Scripts/BS_ViewMasCirculardetails.aspx?id=9905
10. What is curious in the case of one of these banks in Bihar, i.e., Uttar Bihar Gramin Bank, is that the average amount of education loan given at ₹263,447 is 127% higher than the average housing loan at ₹115,979.
11. GB refers to Gramin Bank, GVB refers to Gramin Vikas Bank, and KGB refers to Kshetriya Gramin Bank.
12. As per RBI's Master Directions on Interest Rate on Deposits (updated as on September 16, 2022), RRBs are free to provide differential rates of interest on savings bank balances above ₹ 0.1 million as well as on bulk term deposits (defined as term deposits above ₹1.5 million). As an example, Baroda Rajasthan Kshetriya Gramin Bank offers higher rates for higher balances that can be only maintained by the richer classes, i.e., for savings account balances above ₹2.5 million and one-time deposits above ₹20 million which goes against the basic premise of RRBs as an institution of the poor. Rates available here: https://www.brkgb.com/interest-rate-deposits.html
13. Appendix Table IV.2, Report on Trend and Progress of Banking in India, Dec 2021. Available here: https://www.rbi.org.in/Scripts/AnnualPublications.aspx?head=Trend%20and%20Progress%20of%20Banking%20in%20India
14. Source: Annual reports of individual RRBs
15. It must be noted, however, that RRBs are 35% owned by sponsor banks which operate in global financial markets or geographies and are required to comply with the Basel norms.
16. RBI Master Directions on Internet Banking Facility for Customers of Regional Rural Banks. Available here: https://www.rbi.org.in/Scripts/BS_CircularIndexDisplay.aspx?Id=10128
17. PSB = Public sector banks, PVB = Private sector banks, SFB = Small finance banks, LAB = Local area banks, Payments = Payments banks
18. RBI Master Directions on Priority Sector Lending-Targets and Classification (updated as of 2nd August 2022). Available here: https://m.rbi.org.in/scripts/BS_ViewMasDirections.aspx?id=11959
19. While data for urban, rural and aspirational districts have not been analysed separately and over time for SFBs, they have the highest proportion, i.e., 95% of small borrower accounts with credit limits less than ₹ 0.2 million. This is the highest among all bank groups including RRBs. The average amount outstanding per account in Table 3.4 isthe lowest for SFBs, in line with their originas MFIs and PSL mandate that is similar to that for RRBs (A. Neti, Inclusive Finance India Report 2021).
20. Basic Statistical Returns-1 returns for March 2021 filed by banks with RBI
21. Basic Statistical Returns -2 returns for March 2022 filed by banks with RBI
22. It must be noted here that SBLC data, though made available on the internet, is available as scanned copies of paper documents and not provided in a user-friendly format for most states.
23. https://slbcbengal.pnbindia.in/pdf/156th_SLBC_Agenda_Notes.pdf
24. http://www.slbcup.com/Agenda/SLBC%20Booklet%20March%202022.pdf
25. https://www.slbcap.nic.in/pages/SLBC%20Meetings/219%20%20Agenda.pdf
26. https://slbcgujarat.in/wp-content/uploads/2022/06/173-SLBC-Agenda_Final.pdf
27. As far as direct exposure to microfinance is concerned, banks have the highest share among all lender categories, including MFIs, and this has been growing consistently since 2018 (N. Srinivasan, Inclusive Finance India Report 2021).