

K C Chakrabarty: Technology, financial inclusion and the role of urban cooperative banks

Address by Dr K.C.Chakrabarty, Deputy Governor of the Reserve Bank of India, at the Foundation Day and Inauguration of the “Core Banking Solution Project” of the A.P. Mahesh Co-op Urban Bank Ltd., Hyderabad, 9 August 2009.

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Hon’ble Finance Minister, Govt. of Andhra Pradesh, Shri Rosaiahji; Chairman, A.P. Mahesh Co-operative Urban Bank Shri Ramesh Kumar Bung; Sr. Vice-Chairman Purshotamdas Mandhana; Vice-Chairperson Smt Pushpa Boob, Board of Directors, Senior Executives, Staff Members, Ladies and Gentlemen,

I am delighted to be here this evening amongst all of you on the occasion of the 32nd Foundation Day Celebrations of The A.P. Mahesh Cooperative Urban Bank Ltd. I would like to thank you for inviting and giving me an opportunity to share some of my views on the current pressing issues, the challenges and the opportunities in front of the urban cooperative banks today. Let me first congratulate all of you on the occasion of the Foundation Day and the technological achievement on the eve of inauguration of the Core Banking Solution Project of the bank. This single step will enable the A.P. Mahesh Cooperative Bank to serve better the needs of its traditional constituency, the middle and lower middle classes and the marginalized sections of society spread over its 30 branches – 22 in the twin cities of Hyderabad and Secunderabad and one each at Khammam, Vijayawada, Guntur, Rajahmundry, Visakhapatnam, Warangal in Andhra Pradesh, Jaipur in Rajasthan and Mumbai in Maharashtra. I am fully aware of the significance of this achievement of the bank and I do hope that it will give a new fillip to the overall growth, enhancement in efficiency and bringing excellence in the cooperative banking sector in the country.

The A.P. Mahesh Coop Bank has been a forerunner amongst urban cooperative banks (UCBs) by its performance and setting the benchmark as a good success story in the cooperative banking. The growth of the bank has been impressive as the bank has achieved the milestones of business crossing Rs.1000 crore and Core Banking Solution being rolled out across its network of 30 branches. The bank from its Primary Cooperative Society status in June, 1977 has moved from strength to strength by becoming a Scheduled Bank in October, 1996 and later a Multi State Cooperative Bank in May, 2001.

As there has been spurt in the technology adoption by the urban cooperative banks in India in recent times, thereby inducing the inclusive growth process, I felt that it would be more appropriate if I share my views on the topic “Technology, Financial Inclusion and the Role of Urban Cooperative Banks” for achieving the inclusive growth in India.

Importance of UCBs

In India, like many other countries in the world, cooperative movement started as a means of ensuring that the poorly equipped citizens have similar advantages that better placed persons were able to command. This was ensured by the pooling in of their individual resources. The principle of mutual aid, which is the basis of cooperative organisation, and the practice of thrift and self-help which sustain it, generate a feeling of self-reliance and empowerment which is of utmost importance in a democratic set up like us. I believe that these are the core objectives for which we are striving for from most of our initiatives of the various developmental projects and programmes. We recognise and are aware of their importance in the entire banking system in expanding the outreach of the system and increasing access to credit. The High Power Committee on Urban Cooperative Banks

constituted by RBI in 1999, has aptly commented that the cooperative credit endeavour was the first ever attempt at micro credit dispensation in India. The type of reach cooperative banks has in our country and the type of customized services they can offer at the local level, the potential is tremendous. But, the question is have we achieved the true potential? The answer to the question in my opinion to a certain extent is negative. The same is evident if we look at the market share of deposits and advances of the Scheduled Commercial Banks (SCBs), UCBs and RRBs. The SCBs share in the total bank deposits has been 92.1, 93.0 and 93.3 per cent in the year 2006, 2007 and 2008 as compared to UCBs 4.9, 4.2 and 3.9 per cent in the corresponding period, displaying a downward trend. The SCBs share in the total bank advances has been 93.2, 94.0 and 94.4 per cent in the year 2006, 2007 and 2008 as compared to UCBs 4.4, 3.8 and 3.4 per cent in the corresponding period, again displaying a downward trend.

Market share of deposits

Year	% Share					
	2006R	2007R	2008P	2006R	2007R	2008P
Scheduled Commercial Banks	92.1	93.0	93.3	93.2	94.0	94.4
RRB	3.0	2.9	2.8	2.4	2.2	2.2
UCBs	4.9	4.2	3.9	4.4	3.8	3.4
Total	100.0	100.0	100.0	100.0	100.0	100.0

Uneven geographical dispersal of UCBs in few states such as Maharashtra, Gujarat, Karnataka, Andhra Pradesh and Tamil Nadu account for over 80% of urban cooperative banks presence and 75% of their total deposits. Predominant concentration of Urban Cooperative Banks in these 5 states is mainly on account of emergence of strong cooperative leadership.

UCBs normally confine their area of operation to localised geographical regions, but over a period of time, their area of operation has crossed the frontiers of districts and in some cases the states of their registration. Continuing the ideals and beliefs of cooperative pioneers, UCBs seek to bring about an alignment of human and social development with their business objectives. At present, the bigger question is can we extend or diversify the development of strong, vibrant and financially sound UCBs to the other regions of the country as well to cater to the requirements of the people at the base level and bring them under the banking fold. There is a clear indication as per the available data as mentioned earlier that a huge potential exists for the UCBs to play a more proactive role in the banking sector in the coming years.

State	No. of UCBs			No. of UCBs (% to Total)		
	End March 2006	End March 2007	End March 2008	End March 2006	End March 2007	End March 2008
1.Maharashtra & Goa	630	622	609	34.0	34.3	34.4
2.Gujarat	296	284	271	16.0	15.7	15.3
3.Karnataka	297	288	280	16.0	15.9	15.8
4.TamilNadu/ Puducherry	132	131	130	7.1	7.2	7.3
5.Andhra Pradesh	124	116	115	6.7	6.4	6.5
6.Kerala	60	60	60	3.2	3.3	3.4
7.Uttar Pradesh	77	70	70	4.2	3.9	4.0
8.West Bengal/Sikkim	51	51	49	2.8	2.8	2.8
9.Rajasthan	39	39	39	2.1	2.2	2.2
10.New Delhi	15	15	15	0.8	0.8	0.8
11.Uttarakhand		7	6	0.0	0.4	0.3
12.Haryana/Punjab /HP	16	16	16	0.9	0.9	0.9
13.Madhya Pradesh	75	60	57	4.0	3.3	3.2
14.Orissa	14	14	14	0.8	0.8	0.8
15.Assam & North East	18	17	17	1.0	0.9	1.0
16.Chhattisgarh		14	13	0.0	0.8	0.7
17.Jammu & Kashmir	4	4	4	0.2	0.2	0.2
18.Bihar & Jharkhand	5	5	5	0.3	0.3	0.3
Total	1853	1813	1770	100	100	100

@ As on June 30th, 2009 there are 1713 UCBs in the country

The potential exists, but how important a role the UCBs can play in our scheme for an inclusive growth? Why should we have more thrust on the role played by the UCBs? In a regime of planned development, sound cooperative banking movement is an instrument, which while retaining some of the advantages of decentralisation and local initiative, will yet serve willingly and readily the overall purposes and directives of the developmental plans of the government in the identified sectors. It is an indispensable instrument of planned economic action in a democracy. The client profile of UCBs today predominantly comprise of priority sector segments viz. Small business establishments, SSIs, retail traders, professionals, self-employed persons and SRTOs, etc. who would not normally find it easy to have access to large commercial banks. In urban areas, however, there are a number of underbanked people like artisans, labourers, small business men, retailers, etc. of smaller means who find it difficult to organise themselves in keeping with the requirements of modern times. It is highly desirable on social as well as on economic grounds, that members of this

class should be enabled to be brought into the banking fold and the UCBs certainly can take a lead into this.

Role of RBI – efforts to ensure sustainable growth and functioning of UCBs

While the cooperative banking sector had shown spectacular growth during the 1990's exhibiting substantial potential for sustained growth, there were also concerns regarding inherent weakness of some of the entities over the years resulting in erosion of public confidence and causing concern to the regulators as also to the sector at large. Various Committees and Task Force set up over the years, notably the Committee headed by Shri K. Madhava Rao on UCBs and Shri Jagdish Capoor on the rural cooperatives Task Force on Urban Cooperative Banks have also recommended for enabling all the stakeholders to work together for a strong vibrant and stable system. It is in this critical context that, the Reserve Bank committed itself to strengthening the sector and to protect the depositors' interests. The Reserve Bank's Vision Document for UCBs brought out in March 2005 with the objective of maintaining the viability and competitiveness of the cooperative sector. The document also envisaged:

- Putting in place a mechanism to address the problems of dual control,
- Putting in place a consultative arrangement for identifying weak but potentially viable entities and nurturing them back to health, if need be through a process of consolidation, and
- To identify unviable entities in the sector and provide them an exit path.

To address these issues, RBI felt the need to have more effective interaction with the State Government to address some of the systemic issues hindering the growth and functioning of the cooperative banks. In view of this, RBI has signed Memorandum of Understanding (MoU) with 26 States so far, which provides the basis for constitution of Task Force for Urban Cooperative Banks (TAFUCB), the forum for consultative decision making process. The various TAFUCB meetings across the States have generated the desired effects and have helped in strengthening of the UCB sector as a whole.

RBI's role in empowering UCBs

In order to empower the cooperative banks in their commercial / managerial functioning, RBI in its MOUs with the State Governments has committed to facilitate the development of human resources and skills and to provide assistance in IT initiatives undertaken by the UCBs. The UCBs here have to take a lead and play a more pro-active role in order to utilise the services and assistance provided by the Reserve Bank to make themselves more competitive by bringing efficiency in their functioning. This has to be achieved through cultivating Capital Adequacy and NPA Provisioning Standards; better Corporate Governance; introducing Professional Management and following best practices in Banking operations.

Role of technology

The use of technology in expanding the banking outreach has been an area of focus for the Reserve Bank. Technological innovation has not only enabled a broader reach for consumer banking and financial services, but has enhanced its capacity for continued and inclusive growth. Banks and financial institutions rely on gathering, processing, analyzing information in order to improve its service and meet the expectations of customers. Banks have been quick to realize and adopt technology in a big way. The visible benefits of IT in day-to-day banking in India are quite well known. The "Anywhere Banking" through Core Banking Systems, "Anytime Banking" through new, 24/7/365 delivery channels such as Automated

Teller Machines (ATMs), and Net and Mobile Banking, etc. are also increasingly becoming an integral part of the services provided by the UCBs. In addition, IT has enabled the efficient, accurate and timely management of the increased transaction volume that comes with a larger customer base.

Another important aspect with regard to technology implementation for internal purpose in UCBs is the Management Information System (MIS). The MIS reports so generated help the top management as an effective risk management and a strategic decision making tool.

Use of IT reduces the costs of financial transactions, improves the allocation of financial resources, and increases the competitiveness and efficiency of financial institutions. Most importantly, it enables to take any product or service to the general masses. The challenge now lies in taking greater advantage of new technologies and information-based systems and expanding the coverage of the Indian banking and financial system to under-served markets in rural and semi-urban areas. The use of Smart Card technology, mobile ATMs, coverage of post offices under electronic payments networks in remote areas could play significant role in providing financial services to unbanked and underbanked people. Today, we all should understand that poor people are bankable and there is tremendous potential for the business growth of financial institutions by providing banking services to them. What we need right now is the appropriate business delivery model which will facilitate taking the banking services to the doorsteps of the people at a lesser cost. The technology based solution would go a long way for achieving inclusive growth in India.

India is experiencing an explosion in the use of mobile communication technology. Mobile phone users now belong to all strata of society, spread across metropolitan, urban, semi-urban and rural centres. Banks and financial service providers can leverage the advantage by reaching out to people through this medium for providing various financial and banking services. The mobile phone can function as a multi-application smart card, thus making banking services available to virtually every mobile phone owner. This holds substantial promise as the delivery vehicle of the future – there is huge potential and an exciting opportunity. However, the expansion of such capabilities must be accompanied by a minimum level of essential security features and continued compliance with established covenants and international standards relating to privacy of customer transactions in order to enhance the customers' confidence in the mobile and internet banking by controlling the fraudulent transactions.

In order to enhance the deployment of technology in UCBs, a Group was constituted to examine the various areas where IT support could be provided by the Reserve Bank of India. Based on the recommendations of the Working Group which looked into ways of supporting IT initiatives of the UCBs, IDRBT is being asked to facilitate UCBs availing of Core Banking Platform on an Application Service Provider (ASP) model. With this, the UCBs will be able to put in place cost-effective, modern technology so as to render better customer service and sound regulatory compliance.

Challenges before UCBs

The success of cooperatives ultimately depends upon their ability to perform their duties and fulfill the expectations of their members. The loyalties of the members can be retained not on the basis of monopoly, agreements or under duress but on the strength of the goodwill secured by rendering service. Banking Cooperatives are sometimes organised and administered by those who lack both the qualifications and the experience necessary for the job. This factor alone accounts for a large number of cooperatives' failures and the uneven development of the movement, in the country. The importance of efficient management cannot, therefore, be over emphasised.

Functioning in a highly technologically advanced banking environment in the country is in itself a challenge and an opportunity for the UCBs to upgrade to a computerized environment

so as to focus on more business opportunities and render better customer service. These technological platforms provide an impetus for growth. The role of training and educating not only the staff but also the customers about the various technology based banking and financial services also plays an important part here. Being a movement essentially dependent on the ability of persons in humble walks of life, who are often amateurs in the handling of business operations, the need for training and education is greater to optimally utilise the technological platform. RBI is also trying to facilitate the imparting of training to the key players responsible for the growth of UCBs. To improve the professional skills and as part of the commitment made in the MoUs with the State Govts., free of cost training courses for Directors, CEOs and other officials of UCBs are being conducted by the Reserve Bank at regional locations and in local languages for the convenience of banks. As of now, 1307 directors have been given training apart from 1004 CEOs, 2078 officials and 341 liquidators/administrators/auditors including Chartered Accountants.

Financial inclusion for an inclusive growth

Traditionally, we have seen and observed that the poor have not been welcomed to the banking fold by the banks and financial institutions with a misconception that they are not bankable and there is no business opportunity in offering services to the under-privileged and poor people in the semi-urban rural and slum-dwellers in the metropolitan cities. Banks and financial institutions had been till recent times financially excluding these people on the pretext that:

- They have no or few assets,
- They have nothing to offer as collateral,
- They have no business experiences,
- They cannot be trained for availing financial services,
- They have no credit history, and
- They cannot understand the nuances of banking due to illiteracy or less education.

Given the belief that Credit is a Human Right as advocated by Nobel Laureate Professor Muhammad Yunus, and the poor can overcome poverty by generating their own employment and income, we have to develop a financial system which takes care of the needs of the poor on an urgent basis. Access to affordable financial services – especially credit and insurance – enlarges livelihood opportunities and empowers the poor to take charge of their lives. Such empowerment aids social growth and sustainable growth of the economy. Apart from these benefits, Financial Inclusion imparts formal identity, provides access to the payments system and to savings safety net like deposit insurance.

Today, we need to understand that Financial Inclusion is critical for achieving inclusive growth in the country. To achieve that, we have to expand our scope of financial inclusion initiatives to reach out to people at the grass-root level. We may consider achieving that in three ways:

- Through State-driven intervention by way of statutory enactments (for instance, the US example of the Community Reinvestment Act; and in France making it a statutory right to have a bank account).
- Through voluntary effort by the banking community by evolving various strategies to bring within the ambit of the banking sector the large strata of society, and more importantly;
- Creating a demand by the people themselves to pull the banks, financial institutions and other service providers towards them to offer banking and financial services at a competitive and affordable rate. This will go a long way in not only financially

including and empowering the people but also as an avenue of providing excellent business opportunities for the financial market payers.

Generally, we associate the term Financial Inclusion with our initiatives of bringing poor people in the rural areas into the banking fold; however, we have to realize that there are still a large number of people in the urban area who are financially excluded. They have the need for availing the various types of banking services, especially the savings and money remittance services. This section of financially excluded people in the urban areas provides a good opportunity for the UCBs to step in and fill this void. This is a challenge and a big opportunity for the UCBs at the same time; and I reiterate that if UCBs are not able to grab this excellent opportunity, new institutions will come up to fill this void and UCBs will lose a good business opportunity.

RBI and financial inclusion

RBI has been giving adequate attention and has stepped in whenever it felt that the banking community as a whole has missed out or not given the desired attention to certain areas. This is the reason why the Reserve Bank is placing a lot of emphasis on financial inclusion. In India, the focus of the financial inclusion at present has been confined to ensuring a bare minimum access to a savings bank account without frills with a limited overdraft facility to all. RBI has framed guidelines with a view to achieving greater financial inclusion, to make available a basic banking “no frills” account either with nil or very minimum balances as well as charges that would make such accounts accessible to vast sections of the population. The nature and number of transactions in such accounts would be restricted and made known to customers in advance in a transparent manner. Efforts are being made so that all banks give wide publicity to the facility of such no frills account to ensure greater financial inclusion. Banks and financial institutions have to take a lead here for achieving our objective of reaching out to people.

In order to ensure that persons belonging to low income group both in urban and rural areas do not face difficulty in opening the bank accounts due to the procedural hassles, we have simplified the KYC procedure for opening accounts for people who intend to keep balances not exceeding rupees fifty thousand (Rs. 50,000/-) in all their accounts taken together and the total credit in all the accounts taken together is not expected to exceed rupees one lakh (Rs.1,00,000/-) in a year.

Cooperative banks and regional rural banks being local level institutions are well suited for achieving financial inclusion. Being local institutions they are ideally suited for achieving Financial Inclusion. The use of IT solutions for providing banking facilities at people’s doorsteps holds the potential for scalability of the Financial Inclusion initiatives. Many Pilot projects have been initiated in various States using smart cards for opening bank accounts with bio-metric identification. Here, the link to mobile or hand held connecting device ensures that the transactions are recorded in the bank’s books on real time basis. The outcome of these Pilot projects has been promising. However, we have to now ensure that the gains and lessons from these Pilot projects are translated into an achievable, affordable and implementable plans on a pan India basis to leverage the benefits of inclusive growth, otherwise all our hard work in recent years would fizzle out without many tangible benefits.

Conclusion

Today, our focus should be to simplify the technology which can operate on any platform. The technology solution to the business needs should be user-friendly without much third-party or IT vendor intervention or support requirement for operating the same. In this context, the banks need to redesign their business strategies to incorporate specific plans to promote financial inclusion of low income group treating it both a business opportunity as well as a social responsibility. We can achieve our goal of inclusive growth if all the available

resources including technology and expertise available with the banks, the support of the government, the optimum utilization of the Micro Finance Institutions (MFIs), NGOs and Self Help Groups are geared towards including more and more people under the banking net. Initially, it may appear that taking banking to the sections constituting “the bottom of the pyramid” may not be profitable but as various study conducted reveals that even the relatively low margins on high volumes can be a profitable proposition. Banks therefore need to work out their appropriate business delivery models and financial products to cater to the needs of the people.

It is important that banks should give wide publicity to the facility of no-frills account. Banking services need to be “marketed” to connect with large population segments and these may be justifiable promotional costs.

Mobile phones, POS terminals, “simple to use” cash dispensing and collecting machines akin to ATMs, etc. with operating instructions and commands in vernacular language would greatly facilitate the financial inclusion of the semi-urban populace at an affordable cost, and cooperative banks with a local touch and feel can address these issues in a big way.

The Reserve Bank’s endeavour has been to strengthen the UCBs so that they run on sound principles without posing any systemic problems. Our focus is also geared towards facilitating the process of computerization in UCBs, especially those who are not yet computerized to enable them to take advantage of technology to increase business opportunities, improve customer service and increasing the coverage of its services. Financial Inclusion as a holistic benchmark of a country’s advancement and its commitment to meet the aspirations of its disadvantaged franchisee is a “Goal” to pursue by all the concerned players. All of us, the RBI, the banks and financial institutions, the fringe players facilitating the financial inclusion process have to work hard for the sustainable inclusive growth, both social and economical. We indeed have an important role to play and contribute towards the development of this great nation.

I am sure The A.P. Mahesh Cooperative Urban Bank’s technological initiatives will go a long way in contributing to our goal of achieving 100 per cent inclusive growth in India. I wish you all the best for all your future endeavours and initiatives.

Thank you.