
A STUDY ON THE FINANCIAL PERFORMANCE IN LIEU OF THE CAPITAL ADEQUACY IN REGIONAL RURAL BANKS WITH SPECIAL REFERENCE TO THE MADHYA PRADESH

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Abstract

The decade of 1990s was a turning point for the Indian banking business. It observed a full change in the manner banking was carried out in India. It has developed into a stable and powerful financial entity, with a primacy of place in providing funding for the country. In short, finance is regarded as the life blood of a banking enterprise. This is because in the modern money-oriented economy, finance is one of the basic requirements of all kinds of financial activities. Financial Performance is concerned with the managerial decisions that result in the acquisition and financing of short term and long term credits for the bank.

Here it deals with the conditions that require choose of specific assets and the choose of specific problem of size and development of an organisation. The study deals with the capital adequacy in regional rural banks of Madhya Pradesh in terms of deposits, disbursement, growth, profitability. In short, it deals with arrangement of funds and their effective utilization in the banks.

Key Words: Financial Performance, Capital Adequacy, Deposits, Disbursement, Growth, Profitability.

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INTRODUCTION

In present era of globalization and privatization (GDP) of India is expanded at the rate of 7.7 percent, Agriculture has started occupies a top position in Indian policy-making not only because of its contribution to GDP but also because of the large percentage of the population that is still dependent on the sector for its livelihood. The growth in population and wealth has stimulated demand to the extent that domestic production has not always been able to keep up and there is increasing speculation that the Indian economy may be overheating leading to inflation. However, the banking sector has witnessed a huge growth in the recent years. Despite such a growth, the credit flow by banks to the rural and agricultural sectors remains dismal, which, more or less, has resulted in financial exclusion of the rural masses. Regional rural banks have to play up major

role to finance and provide landings to agriculture sector at diminishing rate of interest in order to grow the economy and GDP. It requires better financial management of the RRBs.

This study concentrates on the principles of bank management of assets and liabilities. The study has an applied feel to it as it mainly focuses on the microeconomic problems of financial performance and capital adequacy of banking firms. The study helps financial management reduce the misuse of funds, **Proper estimation of total financial requirements, Proper mobilization, Proper utilization of finance, Maintaining proper cash flow, Increase efficiency, Reduce cost of capital** and maximize the profit in long run of RRBs.

Capital adequacy ratio shows the capital strength of the bank. CAR is a signal of soundness of the financial position of the bank. This ratio shows the bank's ability to face the worst period by paying its debts from its capital in case of huge Nonperforming assets, and less chances of the bank's financial distress. This ratio is used to protect depositors and promote the stability and efficiency of financial systems around the world.

REVIEW OF LITERATURE

Naz, Huma and Parihar, Sarita in their Research Study "Role of Regional Rural Banks in Jammu and Kashmir" (2014) discovered that the establishment of the Regional Rural Banks has been the landmark in the history of rural banking. This research is based on the role of banks in providing facilities and sources to India backwardness and its farmers.

Yellaiaha, Dr C., Sudhakaraiyah, Dr.G.and Venkateswarlu,M. in their study "Progress and Amalgamation of Regional rural Banks In India-An Overview" (2014) found that in spite of rapid expansion of branches of commercial banks and increase in the membership of Primary Agricultural Credit Societies (PACS), still a large gap exists in the rural credit between demand and supply of credit both in terms of functional needs and adequate geographical coverage in different regions of the country. Therefore, it is felt that these credit institutions neither in their present form of functioning nor with any possible adoption or reorganization, would be able to fill the kind of credit gap which existed in the rural economy of the country.

Bhandari, Govinda Prasad. In his Research Paper "Productivity Analysis of Public Sector Banks And The Regional Rural Banks In India" (2014). The study is an attempt to understand the comparative productivity picture of Public Sector Banks (PSBs) and the Regional Rural Banks

(RRBs) in India. The study unveils that PSBs position is better in branch productivity, staff productivity, employee and branch-wise income and expenditure in comparison to Regional Rural Banks in the country.

Singh, Kuldeep. In his research paper “**Performance Evaluation Of Regional Rural Banks**” (2014) found that “The institution of Regional Rural Banks (RRBs) was created to meet the excess demand for institutional credit in the rural areas, particularly among the economically and socially marginalized sections. Although the cooperative banks and the commercial banks had reasonable records in terms of geographical coverage and disbursement of credit, in terms of population groups the cooperative banks were dominated by the rural rich, while the commercial banks had a clear urban bias.

OBJECTIVES OF THE STUDY

1. To determine and analyze the relationship between Regional Rural Bank performance and capital adequacy.
2. To make suggestions or the improvement in the Financial Management in RRBs of Madhya Pradesh.

HYPOTHESIS

H₀₁: There is no significant relationship between Regional Rural Bank’s Performance and Capital Adequacy.

H₁₁: There is a significant relationship between Regional Rural Bank’s Performance and Capital Adequacy.

RESEARCH METHODOLOGY

Research may be deductive or inductive. Deductive research approach begins with the development of a theory or hypothesis and later a development of a strategy to test it in a context to verify or reject its claims

SECONDARY DATA

To test the hypotheses secondary data have been collected and compiled together to conclude the results. To test the objectives following secondary data were taken from the Bank Reports separately from Madhyanchal Gramin Bank, Central M.P. Gramn Bank and Narmada Jhabua Gramin Bank. For this study four years data have been calculated (2011-12 to 2014-15) as on March Ending Year. To test the first objective, for the measurement of banks’ performance the following parameters were taken such as; loan disbursement, deposits, recovery, growth, profitability and capital adequacy.

RESULTS & FINDINGS

Table 1.1: Descriptive Statistics On Regional Rural Bank’s Performance and Capital Adequacy

	Mean	Std. Deviation	N
Capital Adequacy	37.2975	6.22607	4
RRBanks’ Performance	723.9275	92.15462	4

Table 1.2: Correlations On Regional Rural Bank’s Performance and Capital Adequacy

		Capital Adequacy	Banks’ Performance
Pearson Correlation	Capital Adequacy	1.000	.932
	Banks’ Performance	.932	1.000
Sig. (1-tailed)	Capital Adequacy	.	.003
	Banks’ Performance	.003	.
N	Capital Adequacy	4	4
	Banks’ Performance	4	4

Above table shows the correlations and it is evident from this table that Pearson’s correlation coefficient between RRBs’ Performance and Capital Adequacy is 0.932 which is significant since the significant value (p- value) 0.003 is less than 0.05. Therefore, we may conclude that there is

significant association between RRBs' Performance and Capital Adequacy. Furthermore, since the value of correlation coefficient r suggests a strong positive correlation, we can use a regression analysis to Model the relationship between the variables.

Table 1.3: Model Summary^b On Regional Rural Bank's Performance and Capital Adequacy

Model	R	R Square	Adjusted R Square	Std. Error of the Estimate	Change Statistics				
					R Square Change	F Change	df1	df2	Sig. F Change
1	.932 ^a	.868	.802	2.76797	.868	13.178	1	2	.003

a. Predictors: (Constant), Banks' Performance

b. Dependent Variable: Capital Adequacy

Table 1.4: ANOVA^a On Regional Rural Bank's Performance and Capital Adequacy

Model	Sum of Squares	Df	Mean Square	F	Sig.
1 Regression	100.968	1	100.968	13.178	.068 ^b
Residual	15.323	2	7.662		
Total	116.292	3			

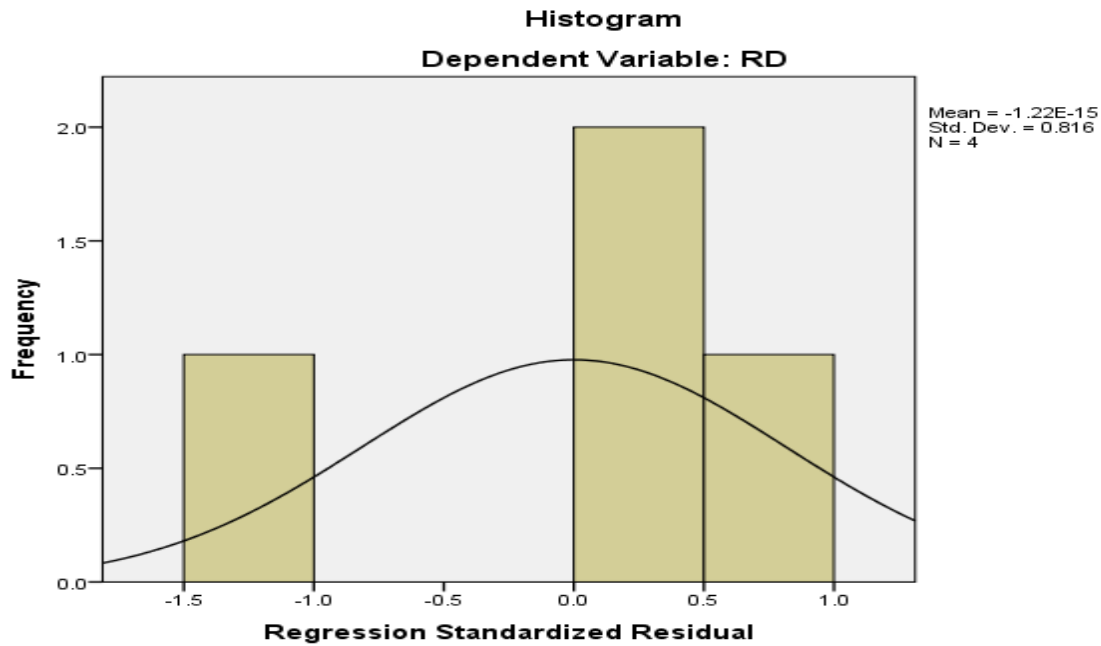
a. Dependent Variable: Capital Adequacy

b. Predictors: (Constant), Banks' Performance

Table 1.5: Coefficients^a On Regional Rural Bank's Performance and Capital Adequacy

Model	Unstandardized Coefficients		Standardized Coefficients	T	Sig.	95.0% Confidence Interval for B	
	B	Std. Error				Beta	Lower Bound
1 (Constant)	8.276	12.630		-.655	.580	-62.618	46.066
Banks' Performance	.063	.017	.932	3.630	.068	-.012	.138

a. Dependent Variable: Capital Adequacy



Histogram 1.1 On Regional Rural Bank’s Performance and Capital Adequacy

Over all model summary shows the value of linear correlation coefficient $R=0.932$, it is the linear correlation coefficient between observed and model predicted values of the dependent variable, Its large value indicates a strong relationship. R^2 the coefficient of determination is the squared value of the multiple correlation coefficient. Adjusted $R^2=0.868$, R^2 change is also 0.802 and these values are significant which shows that overall strength of association is noteworthy. The coefficient of determination R^2 is 0.802; therefore, 80.2% of the variation in Capital Adequacy is explained by Regional Rural banks’ growth, recovery, profitability, loan disbursement rate and deposits. ANOVA is used to exhibit model’s ability to explain any variation in the dependent variable. ANOVA table exhibits that the hypothesis that all model coefficients are 0 is rejected at 1% as well as 5% level of significance which means that the model coefficients differ significantly from zero. In other words we can say that there exists enough evidence to conclude that slope of population regression line is not zero and hence, RRBs’ Performance is useful as predictor of Capital Adequacy. From the table of coefficients, the regression equation can be obtained as

Capital Adequacy= 7.094 + .530* RRB’s Performance

The findings concluded that the performance which includes profitability, deposits, disbursement of regional rural Banks’ performance is the way and an attempt to meet the capital adequacy.

Similar studies were conducted by many researchers on capital adequacy which is the best determinant in giving the input in measuring the financial performance of banks. Business grows mainly by taking risk as greater the risk, higher the profit and hence the entity must strike a trade-off between the two. Risk is the potentiality that both the expected and unexpected events may have an adverse impact on the bank's capital and earnings. While the expected losses are generally taken care of by suitable pricing methodology, the unexpected losses, both on account of individual exposure and the whole portfolio in entirety, is to be borne by the bank itself and hence is to be taken care of by the requisite capital. Hence the need for suitable capital structure and sufficient Capital Adequacy requirements is felt (Raghavan, 2004). Capital is essential and critical to the perpetual continuity of a bank as a going concern. A minimum amount of capital is required to ensure safety and soundness of the bank and also to build trust and confidence of the customers. A bank with a sound capital position is able to pursue business opportunities more effectively and has more time and flexibility to deal with problems arising from unexpected losses thus achieving increased profitability (Athanasoglou et al., 2005). A Study by Hassan (2001) examined the performance of Islamic banks' worldwide during 1994-2001. Variety of internal and external banking characteristics were used to predict profitability and the result indicated high capital lead to high profitability. Abreu (2002) found that well capitalized banks face lower expected bankruptcy costs and thus lower funding costs and this resulted into better profitability. Stiroh (2002) assessed the potential benefits from the diversification of activities and increasing reliance on non-interest income. The result of this present study suggested that banks' performance in terms of deposits, borrowings, profitability, loan disbursement, recovery have the greatest impact on banks' capital with regard to the capital adequacy.

CONCLUSION

It has been evident from the study of regional rural banks' performance that regarding deposits Madhyanchal Gramin Bank has mobilized aggregating Rs. 61357 lacs (13.1%) during the year which is 72% of M.O.U target. Deposits being the important source for banking business, intensive thrust for expanding the stable base of deposits was given, focusing on public deposits which registered a growth of Rs. 567.24 crore (13%). As regards as loans and advances-out standings total advances of the bank grew from Rs. 178805 lacs to Rs. 205899 lacs during the year of 2013-2014, net growth registering of Rs. 27094 lacs in absolute terms and 15.15% in percentage terms. In the same manner in the Central M.P Gramin Bank, the per branch deposit

and per employee deposit increased to 1238 lacs in 2014-15 and Rs.344 lacs as against last year 2013-14.

Under the loan disbursement the regional rural banks have fulfilled its commitment to increase priority sector advances and simultaneously continued disbursement under non priority sector advances also to increase yield on advances and to ensure overall development of the service area. The Central M.P Gramin Bank is continuing its policy of extending adequate credit facilities for development of Agriculture, upliftment of rural poor. In compliance of Central Government new directives, bank have revised and simplified the KCC scheme to make it farmers friendly. Bank has extended KCC facility upto Rs. 3.00 lacs at concessional interest @ Rs. 146358 lacs in 2014-15 and in 2013-2014 it was 158362. The share of agriculture and allied activities during the year 2014-15 is Rs. 156446 which is 83.24% of total loan disbursement of Rs. 187993. Bank is playing a meaningful role in rural/agriculture development through credit disbursal under Government sponsored schemes like Swarna Jayanti Gram Swarojgar Yojna, Antyavasya Scheme, Khadi & Village Industries, Minor Irrigation etc. It will help in removing economic imbalances in society and shows bank's commitment towards growth of rural economy and creation of employment in rural areas. During the financial year 2014-15, to extend credit facility to economically weaker section of the society, bank has linked 1688 Self Help Groups and disbursed loan of Rs. 294-97 lac under NABARD Scheme. This bank has fulfilled its commitment to increase Priority Sector advances and simultaneously continued disbursement under Non Priority Sector advances also to increase yield on advances and to ensure over all development of the service area.

It has been revealed from the above table that the recovery performance of priority sector in Narmada Jhabua Gramin Bank is a slightly variate as in 2011-12 it was 84.37% but in 2012-13 it was reduced to 83.44%. But again it was increased to 85.73% in 2013-14 and again reduced to 84.38% in 2014-15. Hence, it was concluded that performance is much better and deviate from 1-2 % does not matter. So this variable shows the performance of banks in the good parameters. In the same way in non priority sector the percentage of recovery performance was 82.67% in 2011-12 but it was increased by 2 point something percentage in 2013-14 but in 2014-15 it was reduced to 65.04%. In this sector there was much deviation in the recovery due to increasing interest rate depending on the market scenario and also some restricted guidelines in providing the time limit to customers.

SUGGESTIONS & RECOMMENDATIONS

In the light of the findings of the study, the following suggestions are made for improving the performance of the regional rural banks.

- From the findings it is revealed that the bank has adequate capital in terms of total assets. Therefore it is suggested to the banks that they should increase more profits in lieu of the loan disbursement, borrowings, investment in different avenues and also should reduce the liabilities from outside from the customers' perspective.
- In compiling of the data some fluctuations were observed so, it is recommended to the banks they should attract more customers to open their account so that profit per employee may be increased.
- The rural Banks should provide its employees incentives or benefits according to their performances based on the increase of customers and retain them for a long time. This is the best method for retaining their employees and also sustaining the number of customers. Training and development should provide to them so that they can learn to retain their customers and also at the same time they are able to maintain customer relationship management.
- To increase the profit, Banks should reduce their NPAs so that the profitability should be assessed at the fixed point.
- The extent of nonperforming loans in a financial institution's loan portfolio is often considered the best leading indicator of the institution's financial performance. A low ratio of nonperforming loans to the total outstanding loan portfolio is often correlated with low financial expenses and higher profitability. A low nonperforming loan portfolio also necessitates a lower spread for the financial institution between the interest it pays on its deposits and the interest it charges on its loans, thereby benefiting its customers.

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