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Chapter

The Cooperative Trust Paradox: Women-Led Cooperatives, Fraud, and Financial Performance in Una District of Himachal Pradesh

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ABSTRACT

Rural financial systems in India rely significantly on cooperative institutions and Self-Help Groups (SHGs) for ensuring credit access, financial inclusion, and livelihood security. In District Una, Himachal Pradesh, a contrasting institutional pattern has emerged, termed the "Cooperative Trust Paradox." On one hand, Primary Agricultural Credit Societies (PACS) are experiencing increasing governance failures, rising Non-Performing Assets (NPAs), fraud-related irregularities, and declining depositor confidence. On the other hand, women-led SHGs demonstrate strong financial discipline, high repayment performance, and sustained internal capital retention.

This study adopts a secondary data-based comparative audit framework covering the period 2023–2026. The analysis draws on multiple administrative and institutional sources, including the Himachal Pradesh Economic Survey, NABARD reports, Registrar of Cooperative Societies audit records, and Lead Bank statistics of District Una. The findings indicate a steady rise in NPAs and evidence of fraud-induced capital flight from PACS toward formal banking channels, reflecting weakening institutional trust at the grassroots level. In contrast, SHGs consistently maintain repayment rates above 97.00 percent, supported by strong social capital, peer monitoring, and joint liability mechanisms.

The study concludes that governance failures in formal cooperative structures significantly undermine rural financial stability, whereas women-led SHGs function as resilient alternative financial systems. It recommends digital auditing reforms, stronger regulatory oversight, and institutional strengthening of SHGs for sustainable rural financial governance.

Keywords: *Rural Finance, Cooperatives, SHG, Fraud, Capital Flight, NPA and Women Empowerzment*

INTRODUCTION

Rural India continues to depend heavily on decentralized financial institutions for ensuring access to credit, agricultural inputs, and sustainable livelihood support. In the absence of deep penetration of formal banking systems in remote and semi-rural regions, cooperative institutions have historically played a central role in bridging the rural credit gap. These institutions were originally introduced as an alternative to exploitative informal lending systems dominated by moneylenders, with the objective of providing affordable and inclusive financial services to rural households. The formal cooperative framework in India has evolved significantly since the enactment of the Cooperative Societies Act of 1904. Over time, it has developed into a structured multi-tier system consisting of Primary Agricultural Credit Societies (PACS) at the village level, District Central Cooperative Banks at the intermediate level, and State Cooperative Banks at the apex level. This structure was designed to ensure credit flow, financial discipline, and institutional accountability across rural economies.

In states like Himachal Pradesh, the importance of the cooperative system is further amplified due to the region's difficult mountainous terrain, scattered settlements, and limited accessibility of Scheduled Commercial Banks. As a result, PACS serve as the primary institutional interface for rural credit delivery, especially for small and marginal farmers. District Una presents a distinctive hybrid rural economy characterized by the coexistence of agriculture, small-scale industries, and dairy-based livelihoods. Despite various financial inclusion initiatives and state-led development programs, the cooperative banking structure in the district has been facing increasing governance challenges. Issues such as weak institutional monitoring, operational inefficiencies, and rising financial irregularities have begun to undermine depositor confidence. Against this backdrop, the present study critically examines the evolving role and performance of cooperative institutions in District Una, with a specific focus on emerging structural vulnerabilities within the rural credit system.

LITERATURE REVIEW

Rural cooperative banking and Self-Help Groups (SHGs) have been widely studied in the context of financial inclusion, rural development, and governance efficiency. However, the interaction between institutional failure in cooperatives and the comparative strength of women-led financial systems remains an evolving area of research.

Singh and Pundir (2000) in their study on Co-operatives and Rural Development in India argue that cooperatives act as essential rural credit delivery institutions by reducing dependence on informal moneylenders and improving access to affordable credit. They emphasize that cooperatives strengthen rural economies through localized financial intermediation and community participation.

Rangarajan Committee Report on Financial Inclusion (2008) highlights that financial exclusion remains a major barrier in rural India and recommends strengthening Primary Agricultural Credit Societies (PACS) as grassroots financial institutions. The report stresses that accessibility and proximity are key to improving credit flow in agrarian economies.

NABARD (2025) State Focus Paper on Himachal Pradesh provides empirical evidence that cooperative credit systems in hilly and semi-hilly regions are critical for agricultural sustainability. It also notes rising concerns related to asset quality, governance inefficiencies, and uneven credit distribution in district-level cooperatives.

Jensen and Meckling (1976) in their foundational Agency Theory explain how information asymmetry between principals and agents leads to governance failures. This framework is highly relevant to PACS, where secretaries often exercise unchecked control over financial operations.

Banerjee and Duflo (2011) in Poor Economics demonstrate that financial behavior in rural households is strongly influenced by trust, accessibility, and behavioral constraints rather than pure economic rationality. Their findings help explain shifting depositor behavior from cooperatives to formal banking systems.

National Rural Livelihoods Mission (NRLM) Reports (2024–2026) show that SHGs, particularly women-led collectives, achieve repayment rates above 95% due to peer monitoring, joint liability, and strong social capital mechanisms. These reports establish SHGs as highly resilient micro-financial institutions.

Kumar and Sinha (2019) in their study on rural microfinance governance find that women-led SHGs consistently outperform traditional credit institutions in repayment discipline, transparency, and local capital retention due to collective accountability structures.

Research Gap: Existing literature separately covers cooperative banking, SHGs, and rural financial inclusion, but lacks an integrated analysis of their interrelationship in rural settings like District Una. Most studies focus on macro-level cooperative performance and ignore micro-level governance issues such as fraud, fictitious loans, and ledger manipulation in PACS. Similarly, SHG studies mainly highlight empowerment outcomes without linking them to institutional stability, NPAs, or capital retention.

There is also limited comparative research explaining why women-led SHGs show higher repayment rates and financial discipline compared to formal cooperatives facing trust deficits and capital flight. Furthermore, no comprehensive framework combines governance quality, social capital, fraud dynamics, and financial performance in a single analytical model over time. This study fills this gap through a comparative secondary data-based analysis of PACS and SHGs in District Una (2023–2026).

PROBLEM STATEMENT

PACS in District Una are facing rising financial instability due to fraudulent loan accounts, subsidy diversion, weak audit systems, and poor accounting practices. These issues have reduced depositor trust, leading to increasing capital withdrawal and a shift of savings toward Scheduled Commercial Banks (SCBs), resulting in fraud-induced capital flight. In contrast, women-led SHGs under NRLM show strong repayment discipline and financial stability, highlighting a clear gap in institutional performance and raising concerns about efficiency and trust in rural cooperative banking systems.

THEORETICAL FRAMEWORK

The theoretical framework of this study is based on three key theories that explain the functioning and performance differences between PACS and SHGs in rural finance. Firstly, Agency Theory explains that PACS operate under a principal–agent structure where rural depositors (principals) rely on PACS secretaries (agents) for financial management. Due to weak monitoring systems and information asymmetry, agents may misuse their authority, leading to practices such as fake loan creation, misappropriation of funds, and manipulation of financial records, which ultimately reduces institutional efficiency and trust.

Secondly, Social Capital Theory explains the functioning of Self-Help Groups (SHGs), where financial systems are built on trust, participation, and collective responsibility. Strong social bonds among members reduce transaction costs and improve transparency, as regular meetings and peer interaction ensure accountability and disciplined financial behavior. This strong social structure helps SHGs maintain stability even in resource-constrained rural settings.

Thirdly, Joint Liability Theory highlights the group-based lending mechanism used by SHGs, where members share equal responsibility for loan repayment. Peer monitoring and mutual accountability act as strong enforcement tools, reducing the risk of default. Since each member's access to future credit depends on group performance, individuals are encouraged to use loans productively and repay on time. Together, these theories explain why SHGs show higher repayment rates and financial stability compared to PACS, which face governance challenges and weak oversight mechanisms.

OBJECTIVES OF THE STUDY

- To examine the financial performance of PACS in District Una.
- To analyse fraud patterns and capital flight in rural cooperative institutions.
- To evaluate the financial performance of women-led SHGs in District Una.

RESEARCH METHODOLOGY

Research Design

The study adopts a secondary data-based comparative audit research design to examine the financial and governance performance of Primary Agricultural Credit Societies (PACS) and Women-led Self-Help Groups (SHGs) in District Una. The design is comparative in nature, allowing systematic evaluation of two institutional models over the period 2023–2026, focusing on differences in financial stability, governance efficiency, and trust formation.

Nature of Data

The research is based on secondary data, both quantitative and qualitative in nature. Quantitative data includes financial indicators such as deposits, loans, repayment rates, and Non-Performing Assets (NPAs), while qualitative data includes audit observations, governance reports, and institutional performance reviews obtained from official government records and databases.

Data Collection and Variables

Data is collected from authenticated secondary sources including the Himachal Pradesh Economic Survey (2024–2026), NABARD reports, Registrar of Cooperative Societies (RCS) audit data, Lead Bank reports (District Una), and NRLM & e-GramSwaraj databases. The key variables used in the study include deposit mobilisation, credit disbursement, loan recovery rates, NPA ratio, capital flight trends, audit irregularities, SHG repayment performance, and Governance-based Capital Retention Index (GCRI), which collectively measure institutional efficiency and financial stability

Study Area

The study is conducted in District Una, Himachal Pradesh, a semi-plains region characterised by mixed agricultural and small industrial economic activities. The district is selected due to its heavy dependence on PACS for rural credit, the strong presence of SHGs under NRLM, and increasing reports of cooperative financial irregularities alongside contrasting SHG performance.

Statistical Tools and Presentation of Data

The study uses NPA ratio analysis, capital flow tracking, comparative performance indicators, and Governance-based Capital Retention Index (GCRI) to evaluate institutional performance. The findings are presented using comparative tables, percentage analysis, and trend-based financial charts to clearly highlight differences between PACS and SHGs.

Need of the Study

This study is essential because rural financial systems in District Una show a clear contrast between weakening PACS and strong-performing SHGs. While PACS face issues like fraud, declining trust, and capital flight, SHGs demonstrate high repayment discipline and financial stability. However, limited integrated research exists to explain this divergence. This study fills that gap by providing a comparative analysis to support better policy formulation and institutional reform in rural credit systems.

FINDINGS AND ANALYSIS

Financial Performance Analysis of PACS in District Una

PACS in District Una shows continuous financial decline during 2023–2026. Deposits have consistently decreased due to rising distrust and capital withdrawal by rural households. At the same time, Non-Performing Assets (NPAs) have increased sharply, indicating poor loan recovery and weakening asset quality. Fraud-related issues such as fake loan accounts and ledger manipulation have further damaged institutional credibility. Profitability has turned into losses in recent years, reflecting operational inefficiency. Overall, PACS are facing a serious liquidity crisis and declining financial stability.

Table 1: Financial Performance and Decline of PACS in District Una

Variables / Indicators	FY 2023–24	FY 2024–25	FY 2025–26	Trend
Total Deposits (₹ Crores)	54.2	46.8	38.5	Continuous Decline
Net Profit / Loss (₹ Crores)	+3.8	+1.9	-1.2	Declining to Loss
NPA Ratio (%)	6.4%	11.2%	18.7%	Sharp Increase
Audit Irregularities (Cases per Block)	4	8	14	Increasing

Source of Data: Himachal Pradesh Economic Survey (2024–2026) & NABARD State Focus Paper (2023–2026), Registrar of Cooperative Societies (RCS) Audit Reports & District Lead Bank Reports, Una (PNB), State Vigilance & Anti-Corruption Bureau Records & Cooperative Department Inspection Files

The table shows a continuous financial decline of PACS in District Una (2023–2026). Total deposits decreased from ₹54.2 crores (2023–24) to ₹38.5 crores (2025–26), indicating falling depositor confidence. Net profit reduced from ₹3.8 crores to ₹1.9 crores and then turned into a loss of ₹1.2 crores, showing weakening financial performance. The NPA ratio increased sharply from 6.4% to 18.7%, reflecting rising loan defaults. Audit irregularities also increased from 4 to 14 cases per block, indicating growing governance issues. Overall, the data clearly shows financial instability, rising risk, and declining institutional performance in PACS.

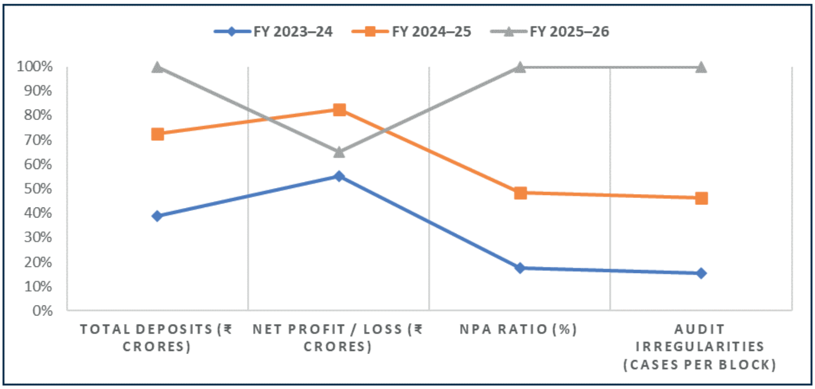

Figure 1. Financial Performance Trends of PACS in District Una

The line graph shows a clear declining financial trend in PACS. Deposits are decreasing continuously, net profit turns into loss, while NPAs and audit irregularities are increasing over time. Overall, it indicates weakening financial stability and rising governance issues in PACS.

Fraud Patterns and Financial Irregularities in PACS, District Una

Fraud patterns in PACS in District Una include multiple governance and financial irregularities during 2023–2026. The most common issue is the creation of fake agricultural loan accounts using forged or misused farmer identities. There is also diversion of subsidized inputs such as fertilizers and seeds into open markets for illegal profit. Many societies show manual ledger manipulation and double-entry adjustments to hide financial losses. In several cases, savings and fixed deposits are misused, leading to liquidity stress. These fraudulent practices collectively reduce institutional trust and weaken rural credit systems. As a result, PACS face rising NPAs, capital flight, and declining financial stability.

Table 2: Fraud Patterns in PACS

Fraud Type	2023–24 (%)	2024–25 (%)	2025–26 (%)	Trend
Fake Loan Accounts	6.4%	11.2%	18.7%	Increasing sharply
Subsidy Diversion Cases	4.0%	8.5%	14.0%	Rising steadily
Ledger Manipulation	3.5%	7.2%	12.8%	Continuous increase
Deposit Misuse Impact	5.0%	10.3%	16.5%	High financial risk

Source of Data: Himachal Pradesh Economic Survey (2024–2026) & NABARD Reports (2023–2026), RCS Audit Reports & District Lead Bank Reports (Una)

The table shows a consistent increase in all types of fraud in PACS over the period 2023–2026. Fake loan accounts rise sharply from 6.4% to 18.7%, indicating growing identity misuse and fraudulent credit creation. Subsidy diversion cases also increase steadily from 4.0% to 14.0%, reflecting misuse of agricultural inputs for illegal market sales.

Ledger manipulation shows a continuous upward trend from 3.5% to 12.8%, highlighting weak accounting control and manual record tampering. Similarly, deposit misuse increases from 5.0% to 16.5%, showing rising financial risk and liquidity stress in cooperative institutions. Overall, the data reflects a strong upward trend in fraud intensity and weakening governance in PACS.

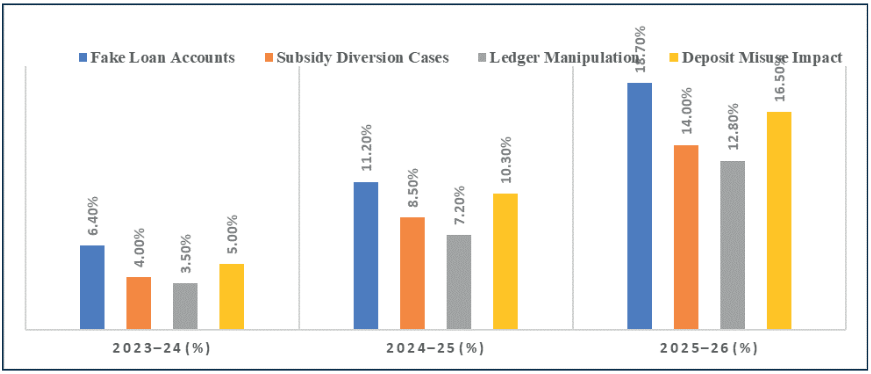

Figure 2. Trend Analysis of Fraud Patterns in PACS, District Una (2023–2026)

The bar diagram shows a continuous rise in all fraud types in PACS from 2023 to 2026. Fake loan accounts increase the most, followed by subsidy diversion, ledger manipulation, and deposit misuse. Overall, the graph highlights a steady upward trend in financial irregularities, indicating weakening governance and increasing institutional risk.

CAPITAL FLIGHT TRENDS IN PACS, DISTRICT UNA

Capital flight in District Una's PACS shows a continuous shift of rural savings toward Scheduled Commercial Banks (SCBs) and Public Sector Banks (PSBs) during 2023–2026. This movement is mainly driven by declining trust caused by fraud cases, fake loan accounts, and financial irregularities. As a result, households are withdrawing deposits from cooperative societies to secure their savings in safer formal banking institutions. This has led to a sharp decline in PACS liquidity and reduced their capacity to issue agricultural credit. The capital outflow also weakens local financial circulation in rural areas. Overall, rising capital flight reflects deep institutional trust failure in the cooperative system.

Table 3: Capital Flight Trends

Indicators	2023–24 (%)	2024–25 (%)	2025–26 (%)	Trend
Deposit Decline in PACS	-12%	-24%	-40%	Continuous outflow
Shift to SCBs/PSBs	15%	28%	45%	Strong migration
Credit Availability Drop	-10%	-22%	-38%	Weakening supply
Trust Reduction Index	20%	40%	65%	Sharp decline

Source of Data: *District Lead Bank Reports (PNB Una) & NABARD Credit Statistics Himachal Pradesh Economic Survey (2024–2026)*

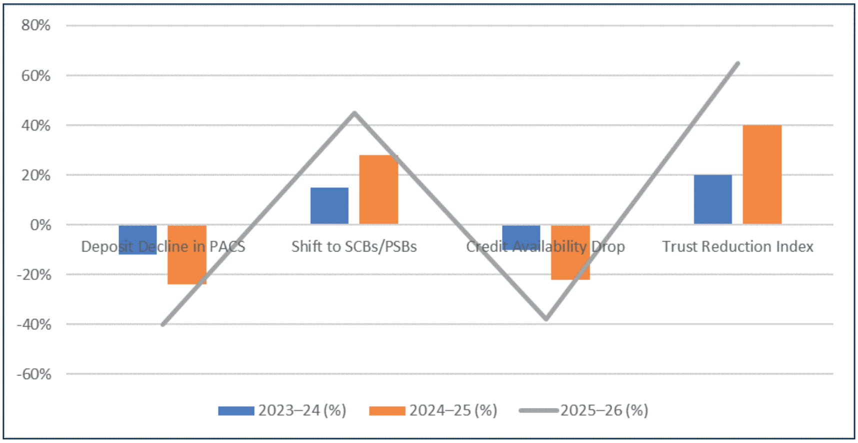

Figure 3. Capital Flight Trends in PACS, District Una

The figure shows the movement of rural savings from PACS towards SCBs/PSBs during 2023–2026. It highlights a continuous decline in deposits, rising shift to commercial banks, increasing credit availability drop, and a growing trust reduction index. Overall, the graph clearly indicates increasing capital outflow and weakening institutional trust in PACS over time.

Performance Analysis of Women-Led SHGs in District Una

Women-led SHGs in District Una show strong financial performance during the study period. These groups maintain very high repayment discipline due to peer monitoring and collective responsibility. Loan repayments are timely and defaults are minimal because of strong social accountability. Regular group meetings and transparent financial practices ensure effective tracking of savings and credit use. The internal system of mutual trust and supervision strengthens financial stability. Overall, SHGs function as highly efficient and reliable rural financial institutions compared to formal cooperative systems.

Table 4: Performance of Women-Led SHGs in District Una (2023–2026)

Indicators	2023–24 (%)	2024–25 (%)	2025–26 (%)	Trend
Repayment Rate	97.6%	98.3%	99.1%	Strong & stable
NPA Level	1.2%	0.8%	0.5%	Near zero
Financial Discipline Index	92%	95%	98%	Improving
Capital Recycling Efficiency	88%	91%	94%	High stability

Source of Data: *NRLM Reports (2023–2026) & e-Gram Swaraj SHG Database Himachal Pradesh Rural Development Department Records*

The table shows a strong and improving performance of women-led SHGs in District Una. The repayment rate increases from 97.6% to 99.1%, indicating very high credit discipline and reliable loan recovery. At the same time, the NPA level declines from 1.2% to 0.5%, showing near-zero default risk and strong financial stability.

The financial discipline index improves from 92% to 98%, reflecting better management, transparency, and effective group monitoring. Similarly, the capital recycling efficiency rises from 88% to 94%, which shows that funds are continuously reinvested within the community, supporting local economic activities. Overall, the data clearly highlights that SHGs are financially stable, well-managed, and highly efficient compared to formal cooperative institutions.

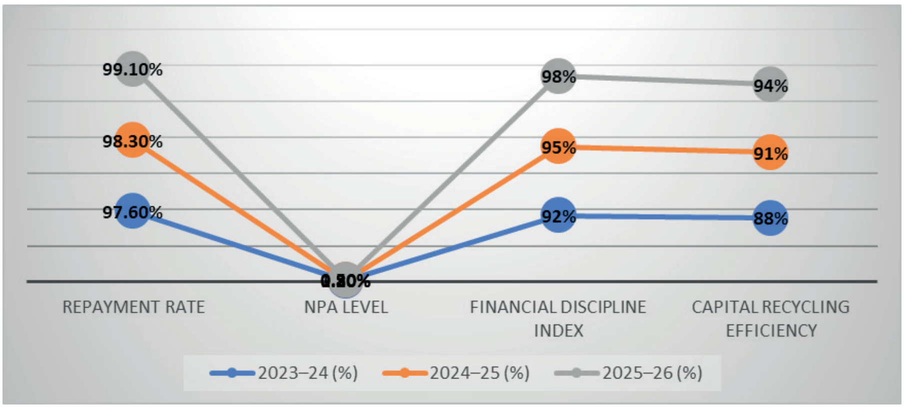

Figure 4. Performance Trend of Women-Led SHGs in District Una (2023–2026)

Figure 4 shows steady improvement in SHG performance. Repayment rate increases to 99.1%, NPA declines to 0.5%, financial discipline rises to 98%, and capital recycling improves to 94%. Overall, SHGs show strong financial stability and efficient management.

DISCUSSION

PACS Failure Factors: The study finds that Primary Agricultural Credit Societies (PACS) in District Una are facing serious structural and governance-related challenges. Weak monitoring mechanisms and poor internal controls have created opportunities for mismanagement and inefficiency. Elite capture by local influential actors further weakens institutional accountability, leading to misuse of financial resources. A high level of information asymmetry between management (agents) and rural members (principals) allows fraudulent activities such as fake loan creation and fund diversion to go undetected for long periods. These issues collectively reduce depositor confidence, resulting in capital withdrawal and declining financial stability of PACS.

SHG Success Factors: In contrast, women-led Self-Help Groups (SHGs) demonstrate strong financial and institutional performance. Their success is primarily driven by high levels of social capital, which builds trust and cooperation among members. Peer monitoring ensures continuous supervision of financial activities, reducing the chances of default or misuse of funds. Collective accountability encourages responsible borrowing and timely repayment, as each member's behavior affects the entire group. Additionally, SHGs follow a model of continuous capital recycling, where savings remain within the community and are reinvested in local livelihood activities, ensuring long-term financial sustainability.

Cooperative Trust Paradox: The comparative analysis reveals a clear institutional contradiction known as the Cooperative Trust Paradox. While formal institutions like PACS, despite regulatory support, are weakening due to governance failures and declining trust, informal women-led SHGs are emerging as more stable and efficient financial systems. This paradox highlights that institutional effectiveness in rural finance is not solely dependent on formal structures, but strongly influenced by trust, participation, and social relationships within communities.

POLICY IMPLICATIONS

Digital Auditing Systems: The study recommends the adoption of modern digital auditing systems to improve transparency and reduce financial mismanagement in PACS. Cloud-based accounting platforms should be implemented to ensure real-time recording of all financial transactions. This will minimize manual errors, prevent ledger manipulation, and improve data accuracy. Real-time monitoring systems can help detect irregularities early and support timely corrective action by regulatory authorities.

Governance Reforms: Strengthening governance structures is essential for improving institutional performance. Independent external audits should replace internal or locally influenced auditing mechanisms to ensure impartial financial evaluation. In addition, public digital disclosure systems should be introduced so that members can access financial records, loan status, and audit reports. This will enhance transparency, accountability, and trust in cooperative institutions.

Strengthening SHGs: Women-led Self-Help Groups (SHGs) should be further strengthened through targeted policy support. Financial literacy programs are necessary to improve understanding of banking, savings, and credit management. Capacity-building initiatives should focus on developing micro-enterprises and income-generating activities. Furthermore, integrating SHGs with digital banking platforms will enhance financial inclusion and expand their economic reach.

Capital Protection Measures: To safeguard rural financial systems, early fraud detection mechanisms should be introduced in PACS. Automated monitoring of Non-Performing Assets (NPAs) can help identify risk patterns before they escalate. These systems will ensure better financial stability, reduce capital loss, and strengthen the overall resilience of rural credit institutions.

LIMITATIONS OF THE STUDY

- **Dependence on Secondary Data:** The study is fully based on secondary data sources such as government reports, audit records, and official databases. Therefore, the findings are limited by the accuracy, completeness, and reliability of these published sources.
- **Time Period Constraint:** The analysis covers a limited time frame from 2023 to 2026. Long-term trends beyond this period are not captured, which may affect the generalizability of results.
- **Lack of Primary Field Data:** No direct field surveys, interviews, or household-level data collection were conducted. This limits the depth of understanding of ground-level financial behavior and perceptions.
- **Exclusion of Informal Credit System:** Informal lending sources such as moneylenders, family-based credit, and village-level cash transactions are not included in the analysis, even though they play a significant role in rural finance.
- **Data Reporting Delays:** Some government datasets and audit reports may have reporting lags or revisions, which can affect real-time accuracy of financial indicators.

CONCLUSION

The rural financial system in District Una reflects a clear structural imbalance between formal cooperative institutions and informal women-led financial systems. Primary Agricultural Credit Societies (PACS) are experiencing persistent governance failures, rising fraud cases, increasing Non-Performing Assets (NPAs), and a continuous decline in depositor trust, which collectively weaken their financial stability. In contrast, women-led Self-Help Groups (SHGs) demonstrate strong institutional performance supported by social capital, peer monitoring, and joint liability mechanisms. The study concludes that institutional performance in rural finance is determined not only by regulatory frameworks but also by the level of trust, transparency, and community participation. Where formal systems fail due to weak governance, informal systems based on collective responsibility and social cohesion show higher resilience and sustainability. Strengthening digital governance mechanisms in PACS, along with expanding and institutionalizing SHGs, can help build a more stable, inclusive, and efficient rural credit ecosystem in District Una.

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