CHAPTER I

REVIEW OF CO-OPERATIVE CREDIT POLICY AND STRUCTURE

IMPORTANCE OF CREDIT FOR AGRICULTURE

Area under cultivation and productivity of land determine agricultural production. In India, area increases contributed nearly 65% and productivity increases only 35% to the total increases of agricultural output during fifties. During sixties, contribution of productivity increases to the total growth rose to 71% and that of area increases declined to only 29%. During seventies, productivity became the major source of growth of agricultural output.[1] Therefore, improvement in productivity is necessary as it provides food and other wage goods to the rising population. Moreover, it ensures a strong base for the future development of industrial sector. Agricultural sector necessitates huge capital investment for growth of its productivity. The main reason for the backwardness of indian agriculture may be attributed to the neglect of long-term credit to agricultural sector. In order to improve productivity, continuous and adequate supply of long-term investible funds becomes necessary. The provision of long-term credit is important mainly because it improves productivities of land and steps up income of cultivators over a period of time.

Utilisation of both long-term as well as short-term credit increases irrigated area, HYVs area and fertilizer consumption which in turn, cause productivity to increase. Some recent studies point[2] out that investment on irrigation or irrigation equipment would require adequate supply of long-term credit. Since the absorption of short-term credit appears to be high in irrigated areas, provision of long-term finance for buying irrigation equipment and /or investment in irrigation appears to be pre-requisite for stimulating demand for production credit. Moreover, it is observed that availability of assured irrigation plays important role in the adoption of HYV technology.

Agriculture like industry require both long-term investible funds as well as short-term funds. Agriculture sector contributes about 48%[3] of the national income as against mere 18% contributed by industrial sector. Therefore, adequate co-operative financial infrastructure with strong capital base is necessary with a view to catering to all needs of farming community. Moreover, credit disbursed should be fully utilised for productive purposes. Mis-utilisation of valuable long-term resources on large scale[4] not only affects the economic system as a whole but ultimately results in diminishing repaying capacity of borrowers. Consequently co-operative banks suffer from mounting overdue position.

CO-OPERATIVE CREDIT POLICY AND ITS CHANGING NATURE

The various studies revealed that almost the entire finance required by agriculturists was supplied by money-lenders, the part played by co-operatives being insignicant. At this stage, the Role of the R.B.I. naturally remained limited in its activities.

It was only after the Report of the All-India Rural Credit Survey Committee in 1954 that the activities of the R.B.I.showed a marked expansion in the sphere of rural credit. According to the Survey Committee,though co-operative credit proved to be inadequate as it accounted for only 3% of the total borrowings of cultivators, co-operative was the most suitable agency for the dispensation of rural credit. Co-operatives, therefore, must succeed as an effective vivels to money lenders. The Survey Committee report made severel far-reaching recommondations for an integrated development of rural credit. The main features of an integrated system of agriculture credit were:-

i) Organisation of large sized societies.

ii) Issue of crop-loans on the security of anticipated crops.

iii) Linking of credit with marketing.

iv) Construction of godwons for storeage

v) Provision of marketing facilities at mandis and district head-quarter.

vi) State partnership through contribution to the share capital of co-operative credit institutions.

vii) Administration through adequately trained and efficient personnel responsive to the needs of rural population.

POLICY OF INTEGRATED CO-OPERATIVE CREDIT

The Indian Government broadly accepted the proposale of the Rural Credit Survey Committee. Consequently, the R.B.I. was assigned the crucial role of implementing the scheme of integrated credit with a view to building-up sound co-operative credit structure which could provide timely credit to the agriculturists for the development of agriculture[5]. Moreover, with an amendmente to the R.B.I. Act in 1955, National Agricultural Credit (Long term Operations) Fund and the National Agricultural Credit (stabilization) Fund were set-up. In fact, entire recources of two funds are to be transferred to NABARD[6]. The former was to be used for (i) issuing loans for periods not exceeding 20 years to state Governments for subscribing to the share capital of Co-operative institutions (ii) advancing medium-term loans to state co-operative Banks for agriculture and other allied purposes and (iii) advancing loans for the periods not exceeding 20 years to and for the purchase of debentures of Central Land Development Bank. The latter was to be utilised for converting short-term loans into medium-term loans in circumstances into which the repayment becomes impossible owing to wide-spread natural calamities like Famine, Flood etc. Consequent upon aforesaid developments, the role of the R.B.I.shifted from that of a lender of last resort to that of an active agency not only for the promotion of a strong co-operative Credit Structure but also for enabling co-operative agencies to take a larger share in the financing of agricultural credit through appropriate measures of reform and re-organisation[7].

Moreover, V. L. Mehata Committee (1959) also made many recommendations,some of which were as below:-

i) Establishment of Primary Agricultural Credit Societies at base serving a village or a group of villages.

ii) Membership to all classes of cultivators including marginal,submarginal and tenant cultivators.

iii) Provision of adequate credit through Societies on the basis of production requirements and repaying capacity. In this way, the co-operative credit policy emphasized the rationalisation of Co-operative Credit Structure perticularly at the village level so as to ensure sufficient and smooth flow of credit to all sections of cultivators.[8]

All India Rural Credit Review Committee under the Chairmanship of Shri B.Venkatappiah also made important recommendations in July 1969. Some of the important recommendations were - The establishment of the agriculture credit board in the Reserve Bank. Setting up of small formers, development agency in each of the selected districts, the establishment of Rural Electrification Corporation, more active and higger role for the agricultural Refinance and Development Corporation alongwith the enlargement of its resources and adoption of various measures for ensuring timely and adequate flow of credit for agriculture through co-operatives and commercial banks. The committee thus prepared the ground for a multi-agency approach to agricultural finance.

Aforesaid analysis indicates that a definite policy of integrated Co-operative Credit emerged by the end of the First Plan. The policy generally held ground for about a decade in second and third plan. During third decade, a shift in policy took place towards multi-agency approach to agriculture financing with the active involvement of commercial banks in this business.[9]

MULTI-AGENCY APPROACH

In adequcy of co-operative credit constituted a major constraint in catering to the requirements of agriculture sector. Moreover, with advent of green revolution the demand for credit exceeded the supply of credit owing to following factors:-

i) The rising tempo of modernisation in Indian agriculture which necessitated large cash outlay.

ii) Growing requirements of credit for distributive trade of fertilises.

iii) A spurt in demand for credit for marketing and storage particularly after the introduction of high yielding verieties programme.

In order to meet growing requirements, a multi-agency approach to agricultural financing has been in operation since then. Under this approach, the prime objective of the R.B.I.has been to narrow down large credit gaps in the rural economy. Special institutions like R.R.B.s consequent upon the recommendations of the Banking Commission (1972) have been set-up to meet requirements of special areas. The co-operatives have the prime role in purveying credit for agricultural and allied activities for only the co-operatives posses the organisational potential to reach out to the millions of small and scattered farmers and establish grass root contacts[10].

Moreover, the co-operative network is already vast and can further be extended or strengthened with comparatively greater case and at lower cost. On the contrary, Commercial Banks' Agricultural Credit has been additive and has not helped to fill the geographical gap in the availability of credit not covered by co-operatives.[11] Moreover, RRBs partly filled the gaps left by co-operatives. Co-operatives have, therefore, dominant role in agricultural finance.

Moreover, National Bank for Agriculture and Rural

Development (NABARD) was set up on July 12, 1982 to take over the functions of ARDC and refinancing functions of the R.B.I.in relation to SCBS and RRBS.[12]

i) To provide by the way of refinance all kinds of production and investment credit to agriculture, small scale industries, articans, cottage and village industries, handicrafts and other allied economic activities.

ii) To provide loans to state Governments for periods not exceeding 20 years to enable them to subscribe the Share Capital of Co-operative Credit Societies.

iii) To augment funds for meeting its loan operations from Government of India, the World Bank and other agencies. The resources of the National Agricultural Credit (stabilisation) Fund stand transfered to the Funds of NABARD with the creation of it.

CO-OPERATIVE BANKING STRUCTURE

There are two wings of the Co-operative Credit Structure, one supplying short-term and medium-term Credit requirements and the other long-term investment credit. The Co-operatives are generally organised into a three-tier structure for short-term and medium-term credit and two-tier structure for long-term credit.

The three-tier short-term co-operative credit structure consists of the State Co-operative Banks at the apex level, Central Co-operative Banks[13] at the intermediate level i.e. district level and Primary agricultural Credit Societies at the base, serving a village or a group of villages. One of the merits of this type of structure is that PACS at village level can establish direct contact with agriculturists.

Unlike three-tier Credit Structure, co-operative Land Development Banks have a two-tier credit system. At the apex level in state, there is generally one State Co-operative Land Development Bank and at the district or Taluka level, there are Primary Co-operative Land Development Banks. There is no agency at the village level. Secondly in some states, there is a unitary system in which the apex bank acts as a head office with primaries as their branches. In few other states, there is a federal structure under which each primary land development bank is a legal entity. But all these primaries are federated to form the apex bank. The area of operation of the primary bank is either limited to one district or taluka. Both these systems have their own advantages as well as dis-advantages. In Maharashtra, for instance, there is a unitary type of land development banking with district as their area of operation. The following chart explains the structure of co-operative banking in India.

CHART-I

CO-OPERATIVE BANKING STRUCTURE

Agricultural Credit

- Short-term and Medium-term Credit.
  - State Co-operative Banks
    - District Central Co-operative Banks.
      - Primary Agriculture Credit Societies (At the village level)
- Long-term Credit
  - Central Co-operative Land Development Banks
    - Primary Co-operative Land Development Banks (At District/Taluka Level)

THE ROLE OF THE R.B.I.

The Role of the R.B.I.has been very important in that it took various measures mainly multi-agency approach, establishment of RRBS and NABARD and other measures for improving quality and working of co-operatives so as to facilitate adequate and smooth flow of credit to agricultural sector. The R.B.I.also provides financial accommodation to co-operatives in following ways.

A) PROVISION OF SHORT-TERM CREDIT:

The R.B.I.provides accommodation to the State Co-operative Banks in the form of rediscounts under Section 17(2)a, (b) and (bb); and advances under 17(4) a against eligible bills. Advances are also made under section 17(4) a against Government and trustee securities.

Section 17(2) (a) provides for rediscounting of promissory notes and bills arising out of bonafide commercial trade transactions maturing within 90 days.

Section 17(2) (b) provides for the rediscounting of promissory notes and bills drawn for Seasonal Agricultural Operations or Marketing of Crops, maturing within 15 months.

B) PROVISION OF MEDIUM-TERM CREDIT:

The R.B.I.grants medium-term credit to State Co-operative banks under Section 46 A 2(b) and 17(4 A) of the R.B.I.Act. The medium-term credit is granted for periods between 15 months and 5 years.

C) PROVISION OF LONG-TERM CREDIT:

The R.B.I.grants long-term credit under Section 17(4 A) as determined under section 46 A2(a), Section 46 A2(c) and Section 46 A2(D) of the R.B.I.Act.

The R.B.I.purchases the debentures floated by the State Land Development Banks by way of financing long-term loans. These loans are advanced out of the National

- Agricultural Credit (long-term) Operation Funds (now NABARD).

THE CROP-LOAN SYSTEM

The crop-loan system is accepted policy framework for the operations of the primary agricultural credit Co-operatives in the country for issuing loans for seasonal agricultural operations. The evolution of Crop-loan system owes its origin to the recommendations of Agricultural Finance Sub-Committee appointed by Govt.of India in 1944 under the Chairmanship of D.R.Gadgil. Committees appointed subsequently from time to time were responsible for several refinements brought about to the present form. Few important among them are Co-operative Planning Committee (Saraiya Committee,1945), Rural Credit Survey Committee (Gorwala Committee,1954) etc.

The system was incorporated as a basic feature in the programme of co-operative development in Second Five Year Plan. But little was achieved till 1965-66. Introduction of extension-oriented intensive crop production. Programme such as HYV etc. necessitated implementation of Crop loan system in full measure in various states.

BASIC FEATURES

Some of the basic features of crop loan system are as follows:-

a) The quantum of loan to be related to cost of cultivation of the crop.

b) The loan to be given both in cash and kind, the kind component being related to the quantum of actual kind component (improved seeds,fertilizers and insecticides) in the total inputs required for the production of particular crop.

c) The loan to be k linked with marketing of crops.

CROP-LOAN COMPONENTS

The R.B.I.suggested that scale of finance for each crop was to be split up into three (or four) components basdcially. 'A', 'B', and 'C'. Component 'D' was hardly adopted. Component 'A' reflects broadly the probable outlay under traditional cultivation and shall not generally exceed one-third of the average value of gross produce. Component 'B' was intended to cover the cost of chemical fertilizers and plant protection material recommended for each crop and to be disbursed in kind. Component 'C' stands corollary to component 'B' to meet cash expenditure involved in lifting fertilizers etc. and shall not exceed 50% of the value of the 'B' component but paid in cash. Component 'D' was coined as an incentive if the loan recovery is arranged through marketing co-operatives, to the extent of one-tenth of the loan amount so recovered during preceding year, but hardly adopted in practice.

In view of the operational difficulties, All India Rural Credit Review Committee (1969) recommended that the short-term co-operative credit consists of only two components viz.cash -'A' and kind -'B'. Thus the two component crop loan system has come into existence and followed widely by the all institutional agencies including co-operatives. The crop loan system sought to transform the situation in two direction.[14] First, by shifting the emphasis from real property to the crop as security, it brought in even pure tenants as potential borrowers and secondly, by relating the size of the loan to the requirements of business, it ~~ix~~ emphasise productive purpose. The integrated scheme of finance under crop loan led to a substantial increase in the flow of finance to the farmers and in a way strengthened the rural credit co-operatives by improving the economic condition of the farmers.[15]

But several field studies pointed out that the per-acre scales adopted by co-operatives are inadequate and component proportion arbitrary and do not bear any relevance either, to cost-structure or value returns.[16] Moreover, the scale of finance are not adopted on the prescribed lines in determining the credit limits. The amount of loans issued depends upon the availability of lendable resources which is normally inadequate to the co-operatives.[17]

LONG-TERM CO-OPERATIVE CREDIT POLICY

Co-operative movement was started in 1904 as money lenders dominated the rural credit scence. Initially co-operative banking of mixed 18 type was set up. However its long-term wing was not satisfactory for following reasons:-

i) Inadequacy of competent staff with co-operatives to examine title deeds of properties to be mortgaged.

ii) Short and medium term nature of its funds.

iii) Comflict of interest of banks with that of Land lords.[19]

Therefore L M B S (Land Mortgage Banks) were set up[20] consequent upon recommendations of maclagaon committee (1915).

L M B S MADE LOANS FOR

i) Redemption of land and houses of farmers

ii) Improvement of land and in methods of cultivation.

iii) Adiquidation of prior debts.

iv) Purchase of land in special case.

However, L M B S could not make progress due to limited business.

EMPHASIS ON LOANS FOR MINOR IRRIGATION

In the beginning L M B (Land Mortgages Banks) advanced loans mainly for redumption of prior debts and mortgage of land. However, after independence and with the advent of economic planning, emphasis was laid for financing capital investments in agriculture. As a result, there was a shift in emphasis in favour of loans for productive purposes in stead of those for repayment of old debts and redemption of mortgages of land.Further impetus was provided in the second and subsequent Five Year Plans which laid stress on increased agricultural production by 6 letter production methods and larger irrigation facilities. Consequently, the banks re-oriented their lending policy and accorded proiority to loans for minor irrigation and land development purposes. They even changed their names from Land Mortgage Banks to Land Development Banks (LDBS). Despite these efforts, their lending remained sporadic and scattered and did not show impressive growth. The real fillip to the lending of these banks for minor irrigation came with the establishment of Agricultural Refinance Corporation in July 1963. The corporation not only actively assisted in the formulation of area development schemes but also provided reimbursement on a liberal scale.

PRODUCTION ORIENTED SYSTEM AND EMPHASIS ON LOANS FOR PRODUCTIVE PURPOSES:

LDBS Adopted Production Oriented System of lending in 1967-68. Under this system banks agreed to advance atleast 80% of their loans for production purposes. In 1968-69 L D B S agreed that they would advance not less than 90% of loans for productive purposes of which 70%

would be for easily identifiable productive purposes. The R.B.I.broadly classified various productive purposes as: (i) Identifiable productive like digging of wells, installated of machinery like electric motors, pupp sets, tractors etc. (ii)non-identifiable productive like land improvement, land development etc. and (iii)non-productive like repayment of old debts.

The main features of production oriented system of lending are indicated below:-

i) Fixing of norms regarding cost of development for different purposes for which investment credit is tobe provided.

ii) Assessment of the repayment capacity of borrowers taking into account the cropping pattern to be adopted.

iii) Calculating the eligibility of loans with reference the repaying capacity arising out of the incremental income * expected to be generated after undertaking the proposed development subject to the outlay on the development envisaged, instead of merely on the basis of the value of security;

iv) Fixing of the period of the loan with reference to the repaying capacity of borrower in such a manner that it does not exceed the useful like of the asset created out of the loan instead of fixing a uniform period according to the purpose of the loan.

EMPHASIS ON DIVERSIFICATION OF LOANS

Emergence of various Institutions, particularly commercial banks and regional rural banks in a multi-agency set up in the field of rural credit dwindled scope for development of minor irrigation in certain areas (like Andhra Pradesh, Gujarath and Tamil Nadu) Consequently, loaning operations of many L D B S declined. In November, 1973, the R.B.I.suggested the new lines of investmental available to banks. Moreover, the Madhava Das Committee(1975) recommended that each Central L D B should build up a portfolio of viable and diversified pattern of schemes. In 1978, Shri Ramkrishnayya Deputy Governor of R.B.I.also referred to the need ~~o~~for diversified lending policy for L.D.B.S.Under diversified lending policy, L D B S propose to finance dairy farming, poultary farming, piggery, sheep rearing, fisheries, sericulture, gobar gas plants, Construction of godowns and cold storage plants, processing of farm producer agro-based small industries, market ~~h~~ yards, agro-service centres, rural and cottage industries and rural artisans etc., which are so essential for integrated rural development. Therefore banks become L D B S from L M B S. Now they have to change over as A D B S (Agricultural Development Banks).

* * *

: REFERENCES :

1 Mrs.R.A.Thite:Performance of Indian Agriculture Unpublished Seminar Paper (M.Phil.) 1984-85, P.5

2 K.Subbarao: Institutional Credit and Adoption of New Technology, Indian Journal of Agricultural Economics, Jan.-March, 1980, P.80-81.

3 The share of agriculture in gross domestic product, has fallen significantly from 48% in 1960-61 to about 41½% in 1970-71 (when valued at 1960-61 Prices) and from 41½% to less than 40% in 1981-82 (when valued at 1970-71 Prices)
K.N.Raj : Some observations on Economic growth in India Economic and Political Weekly, Oct.13,1984 P.1802.

4 Mis-utilisation of credit has been quite massive in Maharashtra over last 20 years leading ultimately to stagnation in the agriculture sector, Economic and Political Weekly, September 7,1974 P.1527.

5 R.B.I : 'Role of the R.B.I.in the Sphere of Rural Credit,' R.B.I. Bombay, 1980. P.5.

6 R.B.I : 'Report on Currency and Finance', 1981-82, P.198-199.

7 R.B.I: Role of the R.B.I.in the Sphere of Rural Credit, R.B.I.,Bombay 1980. P.6.

8 W.C.Shrishrimal, 'Co-operative Credit in Planning era, progress, problems and Impact', in book co-operation and the dynamics of change, Chinchankar and Namjoshi: Somaiya Publishing Pvt., Ltd., Bombay, 1977. P.185.

9. W.C.Shrishrimal, Op.Cit. P.186.

10 Kamath Working Group on Multi-Agency Approach in Agricultural Financing, R.B.I.Report on trend and progress of Banking in India, 1977-78. P.38-39.

11 Report of the Review Committee on Regional Rural Banks, R.B.I, 1978, P.32.

12 R.B.I. 'Report on Currency and Finance', 1981-82 P.198-199.

13 The term 'Central' is used because of the fact that these banks are at the middle level of the co-operative credit structure.

14 Gokhale Institute Studies No.64: Writing and speeches of Professor D.R.Gadgil on Co-operation, Orient Longman Limited, Bombay, 1975, P.105.

15 C.K.Dalaya and R.S.Sabnis: Co-operation in Maharashtra Centre for the study of Social Change, Bombay, 1973, P.~~28~~ 15.

16 U.Venkateswarlu and Bhalerao, 'Validating Scale and Components of Co-operative short-term credit through Bulk-Line Cost Concept', Indian Co-operative Review, July 1984, P.3.

17 Indian Co-operative Review, January 1984, P.242.

18 Mixed Banking is that banking under which banks make both short term as well as long term loans.

19 Conflict of interest was due to the fact that the banks wanted to assist in the redemption of mortgages where as the landlords wanted to persist in their retention.

20 The first L M B in India was established in the Punjab in 1920. It was followed by another L M B in Madras in 1925.

* * *