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DEVELOPMENT OF AGRICULTURAL BANKS IN INDIA

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ABSTRACT

During Independence there was extremely low productivity per hectare and per worker. However, the previous trend of stagnant agriculture was completely changed due to the introduction of economic planning since 1950-51 and with special emphasis on agricultural development, particularly after 1962. Though industry has been playing an important role in Indian economy, still the contribution of agriculture in the development of Indian economy cannot be denied.

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INTRODUCTION

Finance in agriculture is as important as development of technologies. Technical inputs can be purchased and used by farmers only if sufficient money (funds) is available with farmers. Most of the times farmers suffer from the problem of inadequate financial state. This situation leads to borrowing from an easy and comfortable source. Professional money lenders were the only source of credit to agriculture till 1935. They used to charge unduly exorbitant rates of interest and follow serious practices while giving loans and recovering them. As a result, farmers were heavily burdened with debts and many of them are left with perpetuated debts. There were widespread discontents among farmers against these practices and there were instances of riots also. With the passing of Reserve Bank of India Act 1934, District Central Cooperative Banks and Land Development Banks, agricultural credit received impetus and there were improvements in agricultural credit. A powerful alternative agency came into being through the initiative of the government.

Key words: Importance Of Agriculture Finance, Role Of Agriculture Finance, Status Of Agriculture Finance, Strategy To Improve Agriculture Finance.

IMPORTANCE OF AGRICULTURE FINANCE

Agricultural production in this country depends upon millions of small farmers. Their intensity, effort and efficiency have helped in raising yields per acre. Finance in agriculture act as a key to farmers. But farmers‟ money is always inadequate and he needs outside finance or credit. Because of inadequate financial resources and absence of timely credit facilities at reasonable rates, many of the farmers, are unable to go in for improved seeds and manures or to introduce better methods or techniques. The farming community must be kept informed about the various sources of agriculture finance. Agricultural finance possesses its usefulness to the farmers, lenders and extension workers. The knowledge of lending institutions, their legal and regulatory environment helps in selecting the appropriate lender who can adequately provide the credit with terms and related services needed to finance the farm business.

ROLE OF AGRICULTURE FINANCE

Agriculture plays a crucial role in the development of the Indian economy. It accounts for about 19 per cent of GDP and about two thirds of the population is dependent on this sector. Agricultural finance is a subset of rural finance dedicated to financing agricultural related activities such as input supply, production, distribution, wholesale, processing and marketing. Financial service providers face distinct challenges when dealing with this sector. For example, the seasonal nature of production and the dependence on biological processes and natural resources leave producers subject to events beyond their control such as droughts, floods or diseases. The modern agriculture has increased the use of inputs specially for seed, fertilizers, irrigational water, machineries and implements, which has increased demand for agricultural credit. The adoption of modern technology, which is capital intensive, has commercialized agricultural production in India. Besides, the farmers‟ income is seasonal while his working expenses are spread over time. In addition, farmer's inadequate savings require the uses of more credit to meet the increasing capital requirements. Furthermore, credit is a unique resource, since it provides the opportunity to use additional inputs and capital items now and to pay for them from future earnings. The rural population in India suffers from a great deal of indebtedness and is subject to exploitation in the credit market due to high interest rates and the lack of convenient access to credit. Rural households need credit for investing in agriculture and smoothening out seasonal fluctuations in earnings. Since cash flows and savings in rural areas for the majority of households are small, rural households typically tend to rely on credit. Rural households need access to financial institutions that can provide them with credit at lower rates and at reasonable terms than the traditional money-lender and thereby help them avoid debt-traps that are common in rural India. Timely and adequate agricultural credit is important for the increase in fixed and working capital for farmers. In order to provide sufficient credit to the farmers, many institutional and non-institutional agencies are working. Under institutional agencies cooperative, commercial, regional rural banks and different Government organizations are supplying credit to the needy farmers on priority basis.

STATUS OF AGRICULTURE FINANCE

Credit in conjunction with modern agricultural technologies has ushered in the agricultural development across Indian regions. The liberal credit supply by the lending institutions enabled

rapid infrastructural growth across and thereby improved the farm level credit absorption capacity. Although credit has played vital role in agricultural development yet regional and farm-category wise disparity has also taken place. Infact, some of the states with better natural resource base have progressed well while some others lagged far behind. Likewise, some farmers with better resource endowments and access to financial and other institutions have marched faster while others could not do so. Furthermore, multiplicity of lending institutions together with the liberal deployment of credit through various ongoing schemes including micro-financing have saved rural dwellers from the clutches of money lenders. Yet, non-institutional credit agents still survive as they follow the canons of financing

STRATEGY TO IMPROVE AGRICULTURE FINANCE

The achievement of targets in the agricultural sector which covers production of food and essential raw material like cotton, jute and oilseeds, ought not to be allowed to suffer for want of adequate credit. However, specific items of productive work and rates of interest need to be considered as an integral part of the Plan. For providing these facilities all the existing agencies like money lenders, commercial banks, cooperatives and the State have to be integrated and harnessed to a common purpose. Such a comprehensive approach is essential for ensuring the best use of all the available resources of the nation.

I. Setting The Scene

There is a heavy demand for investment capital and sustainable financial services for rural areas and agricultural activities necessary for global growth and food security. In particular, smallholder households and enterprises in developing countries lack the required investment capital and access to financial services, thereby resulting in low agricultural productivity and efficiency with attendant low incomes and high losses. Tackling this challenge requires significant investment on many fronts. Agriculture and its many associated value addition agribusinesses and services must play a crucial role in order to meet the 17 new global Sustainable Development Goals (SDGs), including their important goals and targets toward ending hunger, poverty and reducing inequality by 2030. The SDG investment required is estimated at more than $4 trillion annually. Current investment in SDG-related areas leaves an annual financing gap of $2-3 trillion per year of which agriculture, water, climate change and

related agricultural and rural infrastructure make up a majority (SchmidtTraub and Sachs, 2015). Global public goods are an important part of financing sustainable development but the private sector is clearly important. In context, Official Development Assistance (ODA) provided about $135 billion in 2013, and global capital stock is valued at more than $200 trillion. Due to the nature of the sector, and despite many efforts by the public and private sectors and private capital that exists, meeting the heavy demand for agricultural investment capital and providing sustainable financial services for rural areas and agriculture has proven to be extremely difficult (Third International Conference on Financing for Development 2015).

II. Understanding Demand, Driving Innovation: Smallholder Households and Financial Services:

Working to build the evidence base on smallholder households, the Consultative Group to Assist the Poor has been conducting financial diaries, national surveys, and sectoral segmentations in a number of markets. This research was designed to provide a data-rich and deep understanding of the demand for financial services by smallholder households. It is based on a careful analysis of smallholder household livelihoods, as well as an accurate depiction of their agricultural and financial lives. The purpose of the landscaping paper was to provide background for this demand-side research, drawing on existing literature and recent developments in both financial inclusion in general, and smallholder finance in particular. It is intended to orient the smallholder financial diaries and national surveys, and other demand-side research with this client group into the larger ecosystem and long history of related research and experience. It is known that smallholders' lives generally center on agriculture, yet many of their livelihoods are dependent upon a variety of economic activities and sources of income. How they perceive their agricultural and non-agricultural activities in their daily life and future plans shapes their demand for financial tools and the trends for the future. For example, as more family members migrate to the cities or abroad, the demand for transfers and mobile technology increases relative to agriculture finance.

III. Digital Financial Services: Developments in Serving Smallholder Farmers

A number of private-sector actors and other stakeholders are experimenting with digital financial services ("DFS"), particularly those enabled by mobile phones, to overcome the specific

challenges of serving smallholder farmers and their families. Buoyed by the relative success of DFS in the non-agricultural context, a range of DFS deployments have been launched in recent years aimed at extending financial services to smallholders. The efforts are still nascent and the challenges plentiful. Nonetheless, there is widespread interest in exploring the potential of DFS to overcome a number of traditional economic and cultural barriers that currently limit smallholder use of formal financial services.

a. Agricultural Credit

Credit is critical to agricultural finance, whether to purchase inputs (seeds, fertilizer), tools, or to cover ongoing operational costs prior to harvest time. Yet for smallholders, credit is relatively rarely drawn from financial institutions. The cost of assessment of the client risks and transactions costs of providing loans by conventional means is too high for most financial institutions.

b. Insurance Insurance

can reduce the negative impacts of crop failure and livestock illness. It may also improve a farmer's ability to access credit and willingness to invest in labor and inputs. There are several types of agriculture-related insurance, including weather index insurance (for example, drought, excessive rain), area yield, livestock mortality, and price insurance. The operational costs of making and receiving payments for insurance, issuing payouts and verification often make the costs prohibitive for smallholders. As such, insurance providers innovated using index insurance for weather risks coupled with mobile registration and payments.

c. Payments

There is a fast-growing trend in mobile money transfers. Where available, some smallholder farmers are customers of a digital payment provider and make transfers and/or payments outside of their agricultural activities. There are also newly-developed platforms that enable organizations and government agencies to make payments for specific agricultural purposes, including for fertilizer and seed subsidies. The use of electronic vouchers using mobile phones can reach considerable scale, such as with Zoona in East Africa where more than 1 million e-

vouchers were issued to smallholders. In Nigeria, 8 million farmers received fertilizer vouchers that can be redeemed by mobile phone.

IV. Financing to Support Women in the Agricultural Sector

Women often have limited control and ownership over large assets such as land. They also lack the ability to post hard collateral for loans. In addition, the literature points out that women have limited opportunities to develop human and social capital. Indeed, they face constraints in accessing training and capacity building and membership in producer organizations. These unique challenges make access to finance a much bigger challenge for women compared to men in the agricultural sector. Some of the constraints for women that are the most difficult to address are not financial, nor can they be addressed simply through economic or market opportunities. Cultural issues and constraints such as the purdah (female seclusion) system in rural Islamic areas can have an overwhelming influence on the role that women can play. The challenge for financial service providers is to understand the varied interests and cultures and, together with the target group, adapt culturally appropriate products and services to meet those interests. The research on this topic reviews the existing literature and summarizes the key issues and challenges regarding the access of women to financial services in the agricultural sector. Research and experience so far demonstrate that there is a business case to be made for closing the financing gap between men and women in agriculture. Research also highlights some examples of various private and public initiatives that aim to achieve greater economic growth in agriculture by closing this gender gap

V. New Trends in Financing Agricultural Value Chains – Promising Practices and Emerging Recommendations for Policy Development

Analysis of an entire value chain means that important opportunities and constraints that may not be apparent when considering single production systems or chain layers in isolation can now be identified and analyzed. Recent studies show that looking at the entire value chain (rather than just parts of it) offers better insights. This enables an understanding of both financing within a value chain and financing that is tailored to fit a value chain (Miller and Jones 2010). A number of trends have had significant influence on emerging market economies. These are fundamentally altering the way in which agribusiness cooperates with the financial sector

including: value addition, the emergence of supermarkets, and agro-industries emerging as a major source of income and livelihood development. In sum, value chains are ever more important to the understanding of agricultural markets. Producers that are left out of value chains run the risk of being marginalized in terms of prices and market integration. Financing requirements, above all the small units in the rural non-farm sector, have typical patterns. These small processing units may operate out of the home premises or in small village based and family-operated facilities. They usually operate on high ratios of operating costs to fixed assets. Liquid resources are needed to pre-finance the procurement of produce during harvesting periods.

Improve financial institutions' understanding of the agricultural markets and their capacity to assess business opportunities. This implies a shift towards a value chain approach, which considers the collective set of actors and processes over the entire value chain when making financing decisions. This approach would allow financial institutions to acquire knowledge from input providers, traders, processors, wholesalers and other value chain actors as well as informal service providers who hold a unique informational advantage due to their direct business engagement within the value chain. Financial institutions can also take advantage of the current unprecedented availability of quantitative data to form market intelligence for agricultural finance, which enables significant cost savings before moving to the qualitative analysis of product design.

VI. Innovations and Emerging Trends in Agricultural Insurances

a. Risk and Response Agriculture is a risky business and farmers face a host of market and production risks that make their incomes volatile from year to year. These risks include yield losses due to bad weather, pests and diseases; post-harvest losses during storage and transport; and unexpectedly low market prices. Traditional risk management arrangements frequently fail to provide an adequate safety net for the poor. They are also limited in their ability to manage catastrophic risks that affect many farmers within a region at the same time (for example, regional droughts or floods). Covariant risks are also a problem for financial institutions and input suppliers, since they can be faced with widespread defaults on loans and unpaid bills

b. Index-based Insurance Index-based insurance (IBI) grew out of the need to overcome the perverse incentive problems that have plagued traditional forms of crop insurance. Like private crop insurance, index insurance seeks to provide cover against specific perils. However, in this case, contracts are written against events defined and recorded at regional levels rather than at individual farm levels (for example, a drought recorded at a local weather station, or a low official crop yield estimate for a district or county). In order to serve as agricultural insurance, the index should be defined against events that are highly correlated on the downside with regional agricultural production or income. For example, an insured event might be that rainfall during a critical period of the growing season falls 70 percent or more below normal. Index-based insurance faces a number of challenges that hinder scaling up:

• **Demand problem** – all insurance programs face general demand problems from uncertainty of the product or need, as well as specific problems related to the index nature of the product. Relatively few farmers seem willing to purchase IBI products. Few IBI schemes for farmers have achieved scale without being heavily subsidized and/or the insurance being made compulsory (for example, for public bank borrowers in India). Two reasons suggested for this weak demand are: a) farmers have other ways of managing risk that may seem to be less costly than insurance, and b) farmers may not have the liquidity to pay the insurance premium at the beginning of the farming season, particularly poorer farmers. Better-off farmers also probably have more options than poor farmers, including in years with calamities.

• **Index problem** – A fundamental requirement for IBI is the availability of an index that correlates highly with the agricultural risk to be insured, and for which there is a suitable and reliable database to perform actuarial calculations and objectively determine when an insured event has occurred. The index also needs sufficient spatial granulation to minimize basis risk. These can be daunting requirements in countries and regions with limited weather stations, or where the data are unreliable or released too late to be useful for determining payouts. Technological advances are rapidly reducing the cost of adding secure weather stations, and in some countries, private firms now offer weather station services for a fee (for example, in India). However, there are greater problems in that additional weather stations add to the cost of developing and marketing insurance contracts. New weather stations come without site-specific

historical records and require the calculation of "synthetic" datasets behind them based on the triangulation of existing historical weather data. There has been a lot of recent innovation in developing indices that can be assessed remotely with satellites, such as cloud cover, vegetative cover, or soil moisture content for a given region during critical agricultural periods. Such data are sometimes linked to a bio-physical model that relates the remotely sensed data to the agricultural losses to be insured

• **Distribution problem** – There are serious difficulties and costs in marketing index insurance to large numbers of smallholders, as well as in collecting premiums and making payments. Few private insurers have the required distribution networks in rural areas in developing countries. Therefore, they often work through an intermediary with an existing network of their own (for example, a microfinance institution, bank, input dealer, agro-processor, or NGO), or they work with groups of farmers that can be insured as single entities (for example, through farmer associations and mutual funds). For example, Fresh Co in Kenya, SFS in the Philippines, and Pioneer and NWK Agri Services in Zambia, all use private input dealers to market their insurance. Examples of the aggregator approach are the Zambian National Farmers' Union in Zambia (which arranges insurance for groups of its members), and Agroasemex in Mexico which reinsures farmers' self insurance funds.

Reference: 1. Date Collected through Electronic (Internet).