FINANCING AGRICULTURE BY INSTITUTIONAL SOURCES

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ABSTRACT

Agriculture is the first culture that man learnt to practice as a means of living and a way of life. The adoption of new technology has given rise to increasing demand for farm credit which is the key factor in, and life blood of agriculture development. The bulk of the loans for agriculture in the developing countries originates in the informal sector and probably is not less than five times the outstanding of institutional credit. So there is a need to discuss on the concept of institutionalization of agricultural credit.

Keywords: Institutional Credit, Agriculture, Credit, Rural development, Small and Marginal farmers, commercial banks, RRBs, Cooperatives.

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INTRODUCTION

Credit is the temporary transfer of purchasing power. It is the external source of capital for investment. There is a strong, though often latent, demand for agricultural credit in the developing world. It must be stressed that credit, though often necessary, is only one instrument for promoting agricultural development. In general, the demand for credit depends on the level of economic development of a country and the structure of its agricultural economy.

Provision of adequate institutional credit to support the modern technology and augmentation of agricultural productivity and production is the basic aim of the country's agricultural credit policy. All production activities require for their sustenance some degree of credit, the amount and duration of which depends on the length of the production cycle. Keeping this in view there is a need to institutionalize the agricultural credit.

OBJECTIVES OF THE STUDY

The rural credit market appears to be confronted with a paradox. The informal sources of finance, be they local money lenders, landlords, traders, etc., charge more than 20% rate of interest, often keep land as collateral against loan and have a very high recovery rate. On the other hand, rural financial institutions (RFIs) charge almost half of this interest rate, do not take land as collateral for most of the crop loans, and still face high defaults. Where and how rural financial institutions have gone wrong? From the reports of several committees and Task forces on rural credit, it appears that the RFIs, with the sole objective of eliminating informal finance through moneylenders, have always been allowing leniency in their financial policies. The result is that while informal finance still holds significance in the rural areas1, the RFIs, especially cooperatives are heading towards a state of financial unsustainability.

The main factors behind financial unsustainability of the RFIs are stated to be overwhelming overdues or non-performing assets, high transaction cost, low financial margins and regulated interest rates. Consequent upon these, the RFIs have failed to accumulate enough resource-base and are unable to mobilize speedy disbursement of credit in the rural areas. There are also other problems that RFIs have failed to tackle with. These relate to inequality in the distribution of credit among various classes of people and regions, untimely delivery of credit and cumbersome procedures and formalities to transact credit. All these are major cause of concern. Therefore, it is recommended that the RFIs should be strengthened to accelerate the flow of credit to meet the credit demands of the agricultural sector and bring overall development in the rural economy. In this context, it would be worthwhile to explore various policy and institutional measures that have been taken so far for a speedy and timely delivery of credit to the agricultural sector. Before this, it will be useful to examine the magnitude of overdues in the agricultural sector that are likely to be written off. The present study is a step in this direction.

DATA BASE

As the present study requires secondary data for evaluating the objectives envisaged in the study. Secondary data were collected from the published reports of State and Central Governments, Annual Reports of various commercial banks, and reports and publications of RBI such as Report on Currency and Finance, Report on Trend and Progress of Banking in India, World Bank Report etc.,

INSTITUTIONALISATION OF AGRICULTURAL CREDIT

Though the source of credit for agriculture can be divided on various bases like period-wise, purpose-wise, security-wise but it can be divided into Institutional and Non-institutional sources of credit on the basis of creditor.

INSTITUTIONAL ARRANGEMENTS

Agricultural credit is disbursed through a multiagency network consisting of Commercial Banks (CBs), Regional Rural Banks (RRBs) and Cooperatives. There are approximately 100,000 village-level Primary Agricultural Credit Societies (PACS), 368 District Central Cooperative banks (DCCBs) with 12,858 branches and 30 State Cooperative Banks (SCBs) with 953 branches providing primarily short- and medium term agricultural credit in India. The long-term cooperative structure consists of 19 State Cooperative Agricultural and Rural Development Banks (SCARDBs), with 2609 operational units as on 31 March 2005 comprising 788 branches and 772 Primary Agricultural and Rural Development Banks (PA&RDBs) with 1049 branches.

AGRICULTURAL CREDIT: DISCERNIBLE TRENDS

In India a multi-agency approach comprising co-operative banks, scheduled commercial banks and RRBs has been followed for purveying credit to agricultural sector. The policy of agricultural credit is guided mainly by the considerations of ensuring adequate and timely availability of credit at reasonable rates through the expansion of institutional framework, its outreach and scale as also by way of directed lending. Over time, spectacular progress has been achieved in terms of the scale and outreach of institutional framework for agricultural credit. The source wise and creditor wise credit availability to the agricultural sector in different time periods in India is presented in the following table.

BORROWING OF CULTIVATORS FORM DIFFERENT CREDIT AGENCIES

Credit Agency	Proportional in total borrowings in per cent 1951-52	1971-72	1995-96	2005-2006	2010-2011
A. INSTITUTIONAL CREDIT (1 TO 3)	**7.3**	**31.7**	**75.0**	**61.1**	**68.8**
1. Government	3.1	7.1	5.0	4.6	1.5
2. Co-operative Society/ Banks	3.3	22.0	40.0	30.2	24.9
3. Commercial Banks & Rural Banks	0.9	2.6	30.0	26.3	25.1
B. NON-INSTITUTIONAL CREDIT (4 TO 7)	**92.7**	**68.3**	**25.0**	**38.9**	**29.7**
4. Moneylenders	69.7	36.1	7.0	26.8	21.9
5. Traders	5.5	8.4	5.0	5.2	3.6
6. Relatives and friends	14.2	13.1	3.0	1.5	0.4
7. Landlords and others	3.3	10.7	10.0	5.4	3.8
TOTAL (A+B)	**100.0**	**100.0**	**100.0**	**100.0**	**100.0**

Source : 1. All India Credit and Investment Survey,
2. All India Debt and Investment Survey and NSSO.
3. Economic Survey

The structure of agricultural credit revealed by the cited table confirms the grip of non-institutional sources in 1951 and 71 and institutional sources in 1981. We can observe the clear hold of institutional sources by 1995-96. Though the institutional sources lost its share by 2005-06 but recovered soon by 2010-11. Among institutional sources co-operatives societies' share is as high as commercial banks and other rural banks. By 2010-11, the share of commercial banks rose to 25.1 which is highest among institutional sources followed by co-operatives with 24.9 per cent.

The share of non-institutional sources is decreasing drastically. It was very high at 92.7 in 1951-52 but sharply declined to 36.8 per cent. Once again it raised its share against institutional sources in 2005-06, but gradually losing its domination again. It contributes 29.7 per cent in 2010. Among non-institutional sources, moneylenders share is very high right from the beginning. In 2010 moneylenders share alone is 73 per cent, whereas the share of traders and landlords is almost same and constant over the period. The percentage of relatives and friends is losing drastically and by 2010 its share is negligible. Some of the major discernible trends are as follows:

● Over time the public sector banks have made commendable progress in terms of putting in place a wide banking network, particularly in the aftermath of nationalisation of banks. The number of offices of public sector banks increased rapidly from 8,262 in June 1969 to 68,355 by March 2005.

● One of the major achievements in the post-independent India has been widening the spread of institutional machinery for credit and decline in the role of non-institutional sources, notwithstanding some reversal in the trend observed particularly in the 1990s.

Institutional credit to Agriculture

(Rs. Crores

year	Cooperative banks	per cent	RRBs	Per cent	Commercial Banks	Per cent	Total	Per cent Increase
1991-92	5800	52	596	5	4806	43	11202	27
1992-93	9378	62	831	5	4960	33	15169	35
1993-94	10117	61	997	6	5400	33	16494	9
1994-95	9406	50	1083	6	8255	44	18744	14
1995-96	10479	48	1381	6	10172	46	22032	18
1996-97	11944	45	1684	6	12783	48	26411	20
1997-98	14085	44	2040	6	15831	50	31956	21
1998-99	15916	43	2538	7	18441	50	36897	15
1999-00	18363	40	3172	7	24733	53	46268	25
2000-01	20801	39	4219	8	27807	53	52827	14
2001-02	23604	38	4854	8	33587	54	62045	17
2002-03	23716	34	6070	9	39774	57	69560	12
2003-04	26959	31	7581	9	52441	60	86981	25
2004-05	31424	25	12404	10	81481	65	125309	44
2005-06	39404	22	15223	8	125859	70	180486	44
2006-07	33987	24	15170	10	100999	67	150156	49
2007-08	35875	20	17987	10	128876	70	182738	51
2008-09	36165	19	19325	10	132761	71	188251	53
2009-10	32871	18	23984	13	121879	69	178734	----

Source : Economic Survey and NABARD various issues.

● The share of institutional credit, which was little over 7 per cent in 1951, increased manifold to over 68 per cent in 2010, reflecting concomitantly a remarkable decline in the share of non institutional credit from around 93 per cent to about 30 per cent during the same period. However, the latest NSSO Survey reveals that the share of non-institutional credit has taken a reverse swing which is a cause of concern.

● Notwithstanding their wide network, co-operative banks, particularly since the 1990s have lost their dominant position to commercial banks. The share of co-operative banks (22 per cent) during 2005-06 was less than half of what it was in 1992-93 (62 per cent), while the share of commercial banks (33 to 68 per cent) including RRBs (5 to 10 per cent) almost doubled during the above period.

● The efforts to increase the flow of credit to agriculture seems to have yielded better results in the recent period as the total institutional credit to agriculture recorded a growth of around 23 per cent during 1995-96 to 2008-09 from little over 14 per cent during 1991-92 to 2008-09. In terms of total credit to agriculture, the commercial banks recorded a considerable growth (from around 43 per cent to about 69 per cent), while cooperative banks registered a fall (over 52 per cent to over 18 per cent) during the above period. There is a considerable increase in RRBs from five percent to 13 per cent.

However, the growth of direct finance to agriculture and allied activities witnessed a decline in the 1990s3 (12 per cent) as compared to the 1980s (14 per cent) and 1970s (around 16 per cent). Furthermore, a comparative analysis of direct credit to agriculture and allied activities during 1980s and since 1990s reveals the fact that the average share of long-term credit in the total direct finance has not only been much lower but has also decelerated (from over 38 per cent to around 36 per cent), which could have dampening effect on the agricultural investment for future growth process.

● The disaggregated picture as per size-wise distribution of credit reveals that the growth of direct finance to small and marginal farmers witnessed a marked deceleration from about 24 per cent in the 1980s to little over 13 per cent during the 1990s.

RECENT POLICY INITIATIVES

There are many rural infrastructure projects which have been started but are lying incomplete for want of resources. They represent a major loss of potential income and employment to rural population." Rural Infrastructure Development Fund (RIDF) was set up in NABARD4. Since then, 11 tranches of allocations have been made towards the Fund. Commercial banks make contributions towards the Fund on account of the shortfalls in their priority/agriculture sector lending. The scope of RIDF has been widened to enable utilisation of loan by Panchayati Raj Institutions (PRIs), Self-Help Groups (SHGs), Non-Government Organisations (NGOs), etc., since 1999-2000.

The Fund has continued with additional corpus being announced every year in the Union Budget. The RIDF XI was announced in the Union Budget for 2005-06 with an allocation of Rs.8,000 crore making a total corpus of Rs.78,300 crore. RIDF XI accorded special emphasis for setting up of Village Knowledge Centres by providing Rs.100 crore out of the corpus of Rs.78,300 crore.

Two innovations, viz., micro-finance and Kisan Credit Card Scheme (KCCS) have emerged as the major policy developments in addressing the infirmities associated with the distributional aspects of credit in the recent years. The KCCS has emerged as the most effective mode of credit delivery to agriculture in terms of the timeliness, hassle-free operations as also adequacy of credit with minimum of transaction costs and documentation. Around 59.09 million KCCs were issued till end-March 2006. The cooperative banks (51.5 per cent) had a major share followed by commercial banks (36.9 per cent) and RRBs (11.6 per cent).

CONCLUDING OBSERVATIONS

The co-operative credit structure needs revamping to improve efficiency of the credit delivery system in rural areas. In case of co-operatives, the Vaidyanathan Committee concluded that having regard to its outreach and potential, recapitalisation could be undertaken so that the credit channels for agricultural credit which are presently choked could be declogged. The Committee has, however, made it clear that recapitalisation should only be considered if it is preceded by legal and institutional reforms by State Governments aimed at making co-operatives democratic and vibrant institutions running as per sound business practices, governance standards and regulated at the upper tiers by the RBI.

Merging and revamping of RRBs that are predominantly located in tribal/backward regions is seen as a potentially significant institutional arrangement for financing the hitherto unreached population. Such an exercise is currently on and the State Governments and Sponsor Banks have to come together and cooperate in this area. The experience of micro finance proved that the "poor are bankable" and they can and do save in a variety of ways and the creative harnessing of such savings is a key success factor.

Policy making bodies have an important role in creating the enabling environment and putting appropriate policies and interventions in position, which enable rapid up scaling of efforts consistent with prudential practices.

In the process, ensuring the quality of SHGs warrants priority attention, State Governments have to make critical assessment of the manpower and skill sets available with them for forming, and nurturing groups and handholding and maintaining them over time. There is a need to study the best practices in the area and evolve a policy by learning from them.

All the rural financial institutions – Commercial banks, cooperatives and Regional Rural Banks have used components of mobile banking as an innovative way to provide low-cost savings and lending services to very poor clients. This practice has greatly reduced transaction costs for both the lenders and borrowers.

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