Chapter III

Banking Sector Reforms and Agricultural Finance in India
CHAPTER-3
BANKING SECTOR REFORMS AND AGRICULTURAL FINANCE IN INDIA

3.1 Introduction

Indian economy has been marked by severe problems and uncertainties during the period 1990-91. The economy witnessed a series of difficulties like uncertain political situation, persistent fiscal imbalance, double-digit inflation, balance of payments crisis, etc. This fiscal situation, which was under strain throughout the 1980s, reached a critical situation in 1990-91 and the external payment crisis and the high rate of inflation both, reached their peak level in the middle of 1991. Growth of real GDP decelerated partly because of lower industrial growth and partly because of slowdown in agriculture. The industries were affected because of lower government investment. Non-availability of inputs due to import squeeze recession prevailed in the industrial economy due to the collapse of demand in the markets of Kuwait and Iraq in the wake of Gulf crisis, and collapse of the erstwhile Soviet Union. There was a steep fall in the country’s foreign exchange reserves to about $1 billion, equal to the value of only two 60 weeks’ imports. There was a large fiscal deficit close to 10 per cent of GDP and an unsustainable external balance with current account deficit at 3 per cent of GDP. Faced with such a crisis, India adopted reforms involving macroeconomic stabilization and structural adjustment programmes by the improving economic performance and accelerating the rate of economic growth through a transition from an inward-looking strategy to an outward-looking one and from a regime of licenses and controls to a system of incentives and price mechanism. At the core of the programme was a phased deregulation of the financial sector, along with reforms of trade and industrial policies. The banking sector reforms were part of this package. The main objective of banking sector reforms was to promote a
diversified, efficient and competitive financial system with the ultimate goal of improving the allocative efficiency of resources through operational flexibility, improved financial viability and institutional strengthening. Many of the regulatory and supervisory norms were initiated first for the commercial banks and were later extended to other types of financial intermediaries. Hence, the need of the hour was to introduce some policies to remove the above aforesaid deficiencies. In the light of above distortions, the Narasimham Committee was appointed and the Committee submitted its Report in November 1991, with detailed measures to improve the adverse situation of the banking industry. The main motive of the reforms was to improve the operational efficiency of the banks to further enhance their productivity and profitability.

3.2 BANKING SECTOR REFORMS IN INDIA

Liberalization, Privatization and Globalization have opened up new opportunities for banks to improve their operational efficiency. They relinquished their old practices and are banking on new ways to cater to the needs of their customers in a better way. The banking sector reforms in India were initiated in 1992. The objective of reforms were to strengthen the Indian banks, make them internationally competitive and encourage them to play an effective role in accelerating the process of growth. The reforms process also initiated measures for improving the productivity, efficiency and profitability of the banking system. Since independence, banking in India has evolved through four major phases namely:

1. Foundation phase from 1949 to 1969.
3.1.1 First Phase of Banking Reforms

To restore the financial health of commercial banks and to make their functioning efficient and profitable, the Government of India appointed High Level Committee called, "The Committee on Financial System" (CFS) under the Chairmanship of M. Narasimham with eight other members, which made recommendations in November 1991 (Ray and Sengupta, 2003). The recommendations of the Narasimham Committee-I in 1991 provided the blueprint for the first-generation reform of the financial sector. The period 1992-97 witnessed the laying of the foundations for reforms in the banking system (Rangarajan, 1998).

Narasimham Committee Report 1991

Banking industry has witnessed revolutionary changes as follows:

i. Introduction of capital adequacy norms and new standards of income recognition.

ii. Introduction of asset classification and provisioning norms.

iii. De-regulation of interest rates and consequent shrinkages in margins.

iv. The policy of de-licensing of branches—liberalized branch licensing policy.

v. Autonomy for banks in performance of various of their functions and operations.

vi. Merger of weaker ones with stronger ones.

vii. Introduction of various new services and entry of various alternative financial alternatives such as MF’s, GDRs, ADRs etc.,

viii. Emphasis on customer services, i.e., emphasis towards relationship banking as against transaction banking.

ix. Change in the attitude of unions and empowerment of managements to go ahead with computerization.
x. A total shift for banking operations from a matrix of parametric norms conditioned by controls. Social banking and directed operations to competitive, more autonomous and profit & productivity centered business proposition.

xi. Season changes in the legal system relating to banking.

xii. Entry of new players in private banks and foreign banks transparent guidelines or norms for entry and exit of private sector banks.

xiii. Operational freedom for banks in the areas of

1. Reserve requirements and reduction in SLR and CRR
2. Interest rate de-regulation
3. Determination of lending rates—freedom to declare PLR.
4. Freedom from consortium lending mechanism.
5. Opening of new investment avenues.
8. At least 40 per cent of advances to be in priority sector.

xiv. On the operational front, changes have come through the advent of technology.

Some of the innovations that have been adopted by the banks, of late are:

1. Anywhere banking through connectivity.
2. Anytime banking through ATMs.
3. Anyhow banking through tele-banking, internet banking, mobile banking,
4. continence banking, etc.
5. Plastic money.
6. Setting up of debt recovery tribunals.
3.1.2 Second Phase of Banking Reforms

By mid-1997, the RBI reported that the reforms process had started yielding results. But as observed by the NC in its second report, the improvement has arrested the deterioration of the system earlier but there is still a considerable distance to traverse. There has been improvement in several of the quantitative indices but there are many areas in which weaknesses still persist. They include customer service, technological upgradation, improvement in housekeeping in terms of reconciliation of entries and balancing of books. With the advent of liberalization measures, India appointed the Revised Narasimham Committee in 1998 for reviving the earlier reforms and to further evolve new strategies for strengthening the country’s banking system. The second report was submitted on 23rd April, 1998, which sets the pace for the second generation of banking sector reforms.

Narasimham Committee Report 1998

1. Implementation of recommendations of Narasimham committee relating to CAR, asset classification and provisioning all to be in line with international standards. The recommendations also cover such debatable issues such as narrow banking concept, reduction of Govt. stake in PSBs to 33 per cent, consolidation of banking industry by merging strong banks and independent negotiation of wages by respective banks with their unions.

2. Acquisition and mergers could easily become the call of the day affairs.

3. Strengthening bank’s recovery capabilities with the establishment of DRTs, formation of ARCs and provision under securitization and restoration of financial assets and enforcement of security interest ordinance, 2002.
4. Nationwide network of ATMs and inter-connectivity between banks recommendations of the working group on internet banking setup by RBI.

5. Capital account convertibility implementation in phases, as per the recommendations of the committee on capital account convertibility.

6. Easing of forex norms.


9. Introduction of VRS by number of PSBs resulting in reduction of flab by more than 1.00 lakh of manpower at a cost of Rs.10000 crores and an appreciable 6.19 per cent (Rs.1884 crores ) decline in the wage bill for the year 2000-02.

10. Board for financial supervisions of RBI formulating and issuing detailed guidelines for management of NPAs.

11. Introduction of corporate debt restricting mechanism by the RBI.

12. Provisions relating to setting up assets reconstruction companies for effective NPA management under the securitization and reconstruction Act.

13. Strengthening DRT base towards effective NPA management.

14. Issuance of lenders liability code by RBI proposing several stringent conditions on banks and financial institutions to remove arbitrariness in lending practice.

15. Introduction of standardized computer audit system by the RBI

16. Introduction of risk based internal audit system in banks by the RBI.

17. Dematerialization of government securities and socks.

18. Adoption of 90 days norm for recognition of loan impairment from the year ending March 31, 2004 and charging of interest at monthly rates.
20. F.I.I. investment limits in private banks up to 49 per cent over and above the 49 per cent F.D.I.
21. Easing of priority sector lending norms.
23. Second round of VRS for right sizing banks in the offing.
24. Tougher country risk norms as part of risk management systems. Implementing new capital accord issued by the Basel committee on banking supervision to be adopted by 2005.
26. Concept of "Universal banks" becoming a reality. Banks entering the insurance sector as bank assurance. Working group for harmonizing the role and operations of Development Finance Institutions (DFIs and banks).

3.1.3 The Third Phase of Banking Sector Reforms

Implementation of Basel-II norms

1. Financial liberalization tends to increase financial fragility. The "one size–fits–all approach" of Basel-I recognized only credit risk without considering market, operational and liquidity risks and was confined to a broad band categorization of credit exposures without distinguishing between differing risk profiles and risk management standards across banks, equal allocation of risk weights, and so on.

2. Basel–II norms when implemented fully are supposed to provide financial stability. It will help to focus on risk, to improve skills in measurements and managing the risks and to enhance efficiency.
3. The implementation of the "credit risk" policy principles is fraught with difficulties reviewing and monitoring of collateral in terms of appropriate valuations, maintenance of margins and shortfalls and examining sets the risk weights under Basel-I, Banks enjoy flexibility under Basel-II subject to certain prerequisites. Hence, banks should focus on approval process, administration process and controls on problem areas.

4. "Market risk" emanates from market dynamics, such as variations in interest rates, foreign exchange rates, maturity mismatches, credit spreads and equity and commodity prices, structural risks, legal restrictions, regulatory requirements, limitations of local funding or hedging markets use of non-cash market instruments such as futures and options, forwards and swaps and position taking and balance sheet flexibility.

5. Efficient liquidity planning requires the development and maintenance of various models for market risk exposures, liquidity planning under alternative scenarios, Prudential limits and liquidity review.

6. Operational risk from inadequate or failed internal process, people or system or from external events such as natural disasters, enemy attacks, failure of IT infrastructure, frauds by employees/ vendors or rogue traders is systemic. The establishment of an operational risk framework is essential. This includes control processes, development of operational risk measurement modeling methodologies, management reporting system and governance mechanisms, including review of the procedures and developments in core banking and business policy.⁵
3.2 AGRICULTURAL FINANCE IN INDIA

Agriculture is the backbone of Indian economy. The prosperity of the country depends upon the agriculture sector. In the Indian economy agriculture contributes one-third of the national income. Sixty percent of the export directly or indirectly originates from agriculture. Therefore, a need arises to provide credit to all those farmers who require it. Even if we look into the expenditure pattern of the farmer families, they have hardly any savings to fall back on. Therefore, credit enables the farmer to advantageously use seeds, fertilizers, irrigation, machinery, etc. Farmers have to invariably search for source, which supplies adequate farm credit. The source of agriculture finance can be divided into two categories, institutional finance and non-institutional finance. Institutional finance consists of cooperatives, scheduled Commercial Banks and Regional Rural Banks. Among Co-operatives Primary Agriculture Credit Societies (PACs) provide mainly short and medium term loans; whereas Primary Co-operative Agricultural and Rural Development Banks (PCARDBs) provide long term loans for the agriculture. The Commercial Banks including Regional Rural Banks (RRBs) provide both short and medium-term loans for agriculture and allied activities. The National Bank for Agriculture and Rural Development (NABARD) is the apex institute at the national level for agricultural credit and provides refinance assistance to the above agencies.

3.2.1 Need for Agricultural Credit

Agricultural credit is the key factor to accelerate agricultural development in India. The credit needs of the farmers are of three kinds. Firstly, farmers need short term credit to finance agricultural operations like purchase of seeds, pesticides and fertilizers. Secondly, they need medium term credit for purchase of ploughs, agricultural equipments, tractors and other implements to cultivate their lands with the help of modern implements. Thirdly
they need it for long-term agricultural development such as improvement of land, construction of boundaries and horticulture. To raise agricultural production, they will have to borrow still more credit and more credit is always needed where there is distribution of the rights on the land. It is thus in the interest of agriculture and general progress, that credit shall be available to farmers in adequate amount and at appropriate costs. As prof. John D. Black has very rightly said; “if we are all concerned about increasing total agricultural output in the shorter time, we must provide credit first and foremost. This will enable farmers to buy more labor saving equipments, more seeds and fertilizers and wells as well as other channels of irrigation and purchase of land”. Farmers also need loans for non-agricultural purpose such as repayment of old debts, construction of building and repairs to houses, acquisition of consumer durables, payment of land revenue and meeting expenditure on social customs and litigations. The most important factor regarding the development of Indian agriculture is non-availability of adequate, timely and cheap finance needed by agriculturists for the purchases of farm inputs and tools. With the introduction of modern technology in agriculture, credit plays a vital role. Before the advent of the planning era in 1951, agriculture credit was largely provided by informal channels such as moneylenders, traders, relatives and friends.

3.2.2 Sources of Agricultural Credit

Credit holds a unique position in the economic development of the country. It is an important input to achieve the directive of the Five Year Plans. It is also essential for giving energy to the idle assets. For rural people, the ‘credit’ means finance from some sources to run the business of agriculture. Prof. G.D.H. Cole has said “Credit is purchasing power not derived from income but created by financial institution either as an asset to
ideal income holding depositors in the banks or as a net addition to the total amount of purchasing power.”

The present system of agricultural credit consists of two sectors—the institutional and the non-institutional. The non-institutional sector consists mainly of the professional moneylenders, landlords, traders, commission agents and the farmer’s relatives and friends. The institutional sectors comprise Co-operative Banks, Commercial Banks and the Regional Rural Banks. According to the All India Rural Credit Survey Report 1954, the sources of the credit in the rural areas can be divided into 9 categories, viz; government co-operatives, relatives, landlords, agriculturists, moneylenders, professional moneylenders, traders and commission agents, commercial banks and others. All borrowings from governments through various departments under various schemes such as grow more food campaign and schemes for the rehabilitation of displaced persons. The Land Improvement Loans Act and the Agriculturists Loan Act have been accounted as from government borrowing from different types of co-operative institutions such as primary credit societies, marketing societies, central co-operative banks and land development banks which are treated as borrowings from co-operatives. Interest free loans given by the relatives are treated as loans from the relatives loans bearing interest from a relative are classified as loan from one or the other of the approximate agency such as the agriculturists, moneylenders, professional moneylenders etc. According to the business of relative, loans are classified as the loans from landlords when loans were given by landlords to their own tenants. If a cultivator receives a loan from a landlord, of whom he is not a tenant when such a loan is not recorded as from a landlord but under the appropriate agency, according to the business of the landlord. An agriculturist moneylender is defined as one whose major profession is agriculture and whose money
lending business is comparatively of minor importance. The category of professional moneylender is defined to include all those who earn a substantial part of their income from money lending and who cannot be classified as agriculturist moneylenders. No distinction has been made between professional moneylenders living in towns and those living in the rural areas. Borrowings from the persons who are in the main trades, commission agents, etc. are treated as borrowings from traders and commission agents. Borrowings from all banks scheduled and non-scheduled are classified as borrowings from agencies other than the above mentioned are kept under others.¹³

### 3.2.3 Agricultural Credit System before Independence

Two committees set up by the Government of India in 1945 had recommended on the working of the co-operative credit institutions. The Agricultural Finance Subcommittee of the Policy Committee on Agriculture, Forestry and Fisheries 1945, emphasized the role of the co-operative agencies in financing agriculture. The Co-operative Planning Committee was set up in 1945 to draw up a co-operative plan for the country had recommended that the existing three-tier cooperative institutions should be suitably strengthened and provided with the necessary share capital and finance. Thus, at the time of independence, finance was being advanced to agriculturists by the government in the form of loans and grants through the co-operative credit agencies and to a very small extent by commercial banks. But all these accounted only for 7.3 percent of the total credit needs of agriculture which was then estimated to be between Rs. 500 crores to Rs. 800 crores. A major portion of these credit needs continued to be met by the private moneylenders (RBI, 1954).²⁴ Pattern of supply of agricultural credit at the time of independence and the borrowings from each agency to the total borrowings of cultivators can be seen in the following Table-3.1 and Figure-3.1. As Table 3.1 reveals, the striking
feature is the dominance of the institutional credit sector which accounts for 7.3 per cent.

Among the non-institutional agencies, agricultural moneylenders are leading in the supply of credit (24.9 per cent) followed by landlords (1.5 per cent), professional moneylenders (44.8 per cent), relatives & friends 14.2 per cent and others (1.8 per cent). In the case of institutional agencies, government stood in first place followed by Co-operatives and Commercial banks. Agency-wise credit structure is presented in Figure 3.1.

<table>
<thead>
<tr>
<th>Credit Agencies</th>
<th>Percentage Share</th>
</tr>
</thead>
<tbody>
<tr>
<td>Government</td>
<td>3.3</td>
</tr>
<tr>
<td>Co-operatives</td>
<td>3.1</td>
</tr>
<tr>
<td>Commercial banks</td>
<td>0.9</td>
</tr>
<tr>
<td><strong>All institutional agencies</strong></td>
<td><strong>7.3</strong></td>
</tr>
<tr>
<td>Landlords</td>
<td>1.5</td>
</tr>
<tr>
<td>Agro-moneylenders</td>
<td>24.9</td>
</tr>
<tr>
<td>Professional moneylenders</td>
<td>44.8</td>
</tr>
<tr>
<td>Trader &amp; Commission agents</td>
<td>5.5</td>
</tr>
<tr>
<td>Relatives &amp; friends</td>
<td>14.2</td>
</tr>
<tr>
<td>Others</td>
<td>1.8</td>
</tr>
<tr>
<td><strong>All non-institutional agencies</strong></td>
<td><strong>92.7</strong></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>100.0</strong></td>
</tr>
</tbody>
</table>

3.2.4 Agricultural Credit System During Post-Independence Era

In July 1966, the Reserve Bank of India set up the All India Rural Credit Review Committee to undertake a comprehensive review of the agricultural credit system and submitted its Report in 1969. The Committee made several recommendations. It suggested a dynamic role to the ARDC. During this period, due to the changes in the agricultural scenario of the country, especially the introduction of new agricultural strategy in cultivation i.e. green revolution, it demanded a larger share of credit from institutional agencies and the co-operatives were not able to meet this increased demand. Thus, the committee recommended inducting the commercial banks to supplement the effort of co-operatives in the form of Multi-agency approach. The All India Rural Credit Review Committee emphasized that the requirement of the agricultural sector was so large and diverse that the commercial and co-operative banks can both play a mutually complementary role without getting into conflict with each other (RBI, 1966). On the other hand, there was a growing concern over the pattern of distribution of bank credit and
some conscious efforts to alter it by inducing a greater flow of finance for small-scale industry and, at the same time, by arming the Reserve Bank of India with direct powers of intervention over the managerial affairs of commercial banks (Ghosh, 1979). This concern was required to be reconciled with the framework of the commercial banking system through the policy of social controls. Based on the suggestions of various study groups, the Banking Laws (Amendment) Bill 1967 was introduced in the LokSabha on December 23, 1967. With this Amendment, ‘social control’ on banks was instituted. The basic objective of the social control policy was to ensure, in the immediate future, an equitable and purposeful distribution of credit, within the resources available, keeping in view the relative priorities of development needs (GoI, 1967). The major instrument, for achieving this policy, was the establishment of National Credit Council at the all India level with the objective of “assessment of the demand for bank credit from various sectors of the economy” and “determining priorities for grant of loans and advances for investment, having regard to the availability of resources and requirements of the priority sectors, in particular agriculture, small scale industries and exports (Ghosh, 1979). The National Credit Council found that not even 1 percent of India’s villages were served by commercial banks. It also noted that while industry, accounted for a mere 15 percent of national income, its share in commercial bank credit was nearly 67 per cent, but on the other hand, agriculture that contributed 50 percent of GDP virtually got nothing from banks (Shah, 2007). Thus, the commercial banks were mandated to achieve certain targets and sub-targets under priority sector lending. Direct finance to agriculture and allied activities is to reach at certain specified levels over a period of time.
3.2.5 First Generation Banking Reforms and Agricultural Credit:

In June 1991, the Government of India announced a new economic policy effecting major policy changes designed to correct the macro economic imbalances and effect structural adjustment so as to bring about a more competitive system and promote efficiency in the real sectors of the economy. Financial sector reform is a necessary concomitant of trade and industrial policy liberalization and in fact is critically important. Hence, in August 1991, the Ministry of Finance appointed Narasimham Committee on financial systems to examine all aspects relating to the structure, organization, functions and procedures of the financial system. The Committee submitted its Report in November 1991.

The Committee has observed that between 1969 and 1990, of the total increase of over 51,000 offices, as many as 33,600 were in the rural areas and over 7,900 in the semi-urban areas making for a total of over 80 per cent. Further, the increase in rural deposits as a proportion of the total increased from 3 per cent to 15 per cent. The advance to agriculture which stood at 5 per cent in 1969 has increased to 18 per cent of the aggregate credit as prescribed by RBI guidelines on priority sector lending. In purely quantitative terms this expansion must be regarded as a successful fulfillment of the objectives of the directed credit programme of RBI and government. Fixation of targets for specific sector lending was essentially the means to achieve the broader goals of credit allocation but over the years, the means appear to have become ends in themselves. The desire to attain credit targets has meant inadequate attention to 135 qualitative aspects of lending and a consequent rise in loan delinquencies. Over the years, competitive populism has affected banking and credit operations. The phenomenon of loan melas was quite contrary to the principles of professional appraisal of bank credit needs. There was hardly a serious
appraisal of credit need potential, productive capacity or provision for effective post-credit supervision. Loan waivers have added an additional element of politicization of banking apart from the severe damage to the concept of credit discipline by encouraging defaults. Altogether, the proportion of the infected agricultural credit is estimated to be as high as over 20 per cent. The Committee therefore proposed that directed credit programmes should cover are defined priority sector consisting of the small and marginal farmers also. The credit target for this redefined priority sector should be fixed at 10 per cent of the aggregate bank credit. For the credit flow to agriculture the Committee suggested the institution of a preferential refinance scheme by RBI as under:

I. A reorganization of the banking structure which would consist of i) three or four large banks (including SBI) which would become international in character. ii) eight to ten national banks with a network of branches throughout the country engaged in general or universal banking. iii) Local banks whose operations would be generally confined to a specific region, and iv) rural banks including RRBs whose operations would be confined to the rural areas and whose business would be predominantly engaged in financing agriculture and allied activities.

II. To abolish the branch licensing with a view that the banking system substantially extended its branch network over rural areas and successfully achieved an increase in banking density.

III. To evolve a rural banking structure which could confine effectively the advantages of the local character of RRBs and the financial strength and organizational and managerial skills of the commercial banks. The committee suggested that the sponsor banks should segregate the operations of their rural branches through the
formation of one or more subsidiaries depending on the size, administrative convenience and business assessment of each sponsor bank. Each subsidiary should have a compact area of operations. These subsidiaries of the national banks should be treated at par with the RRBs in regard to the cash reserve and statutory liquidity requirements and refinance facilities from NABARD with a view to improving the viability of rural operations. Regarding the merger of RRBs with their sponsor banks, the committee left it to the option of the banks concerned.20

3.2.6 Second Generation Banking Reforms and Agricultural Credit:

In India since the formal announcement of the first initiative of financial sector reforms in the Union Budget of 1991-92 to the Second Report of the Narasimham Committee in 1998 a considerable ground has been covered in putting in place a financial system which can meet the requirements of a more competitive and open economy.21 In 1997, RBI set up a high level committee to suggest measures for improving the credit delivery system as well as simplifying the procedures for agricultural credit. The Committee submitted its Report on 21 April 1998. The Committee in its Report has made several suggestions to improve the flow of credit to the agricultural sector besides identifying the constraints faced by commercial banks in providing adequate and timely credit to the rural sector (RBI, 1997).22 A summary of the recommendations are listed below:

i. All banks should examine their systems and make suitable modifications to simplify the documentation covering loan agreements.

ii. While appraising credit proposals, attention should be paid to the evaluation of the income stream of the borrower taking into account the track record of credibility,
capacity as well as technical viability of the proposal. His repayment capacity should be assessed on the basis of aggregate household income and to ensure quick disbursement of loans at least 90 per cent of agricultural loan applications should be decided at the branch level.

iii. Advocates the building up of an appropriate return-oriented liquid savings product into the loan to provide a cushion during lean periods.

iv. The Committee advised that the system of disbursing agricultural loans partly in cash and partly in kind may be dispensed with.

v. The Committees suggested for the setting up of dedicated recovery teams by the state government and also educate the borrowers through rurally oriented field publicity campaigns.

vi. Recommended that RBI or any other agency may not prescribe margin, security, unit cost etc., which should be left to the discretion of the lending banker.

vii. Proposed a substantial modification in the 'service area approach' that freedom should be given to the borrowers to choose any branch of a commercial bank for credit requirements and to banks to operate outside their 'service area'.

viii. Further recommended to introduce annual composite cash credit limit for all agricultural borrowing families.

ix. The Committee also advised to discontinue the practice of taking 'No Dues Certificate' from borrowers. It proposed designing specific loan products to meet the demands of the borrowers in the non-farm sector i.e., increased non-farm activities with farm activities to supplement their income.

x. The Committee pointed out that the agricultural credit portfolios of commercial banks comprise two sets of borrowers. One linked to government subsidy schemes
where cases are sponsored by government agencies and sanctioned by banks and
the other identified by banks directly. Recoveries in respect of the former are 30 per
cent while in respect of the latter are 80 per cent plus. The Committee
recommended a systematic review of the subsidy linked lending and favoured
replacement by an alternative method of lending without subsidy and on the basis
of commercial decision of banks.

The Advisory Committee on Flow of Credit to Agriculture and Related Activities
from the Banking System (2004), under the chairmanship of Prof. Vijay Shankar Vyas
recommended that RRBs should continue but they should be restructured into viable
financial institutions, simultaneously retaining their regional character and rural focus. The
alterations initiated in stages would ultimately result in 20 state-level RRBs. The
Government of India, as part of its strategy to boost agriculture production, announced a
package to double the flow of institutional credit to agriculture within three years starting
2004-05. Consequently, targets were set and the programme was implemented during the
period 2004-05 to 2006-07. NABARD and RBI were vested with the responsibility of
overseeing the implementation of the programme. There were notable inter-agency and an
inter-district variation with regard to year of achievement of the doubling of agriculture
credit as well as in terms of ‘number of times’ the target was achieved. In all the states, the
commercial banks fared better than the RRBs and Co-operatives. At all India level,
institutional credit flow through the scheduled commercial banks increased from
Rs.25,255.93 crores as by June end 2003 to Rs.1,15,265.86 crores by the end of June 2007,
registering a compound annual growth rate (CAGR) at 47 per cent. During the same
period, the number of accounts increased from 70.07 lakhs to 155.37 lakhs and registered
an a CAGR of 22.15 per cent. Similarly, the average loan per account increased from Rs.
36040 to Rs. 74189 during the period 2003-07. Thus, the growth in credit flow between 2003 and 2007 resulted in both credit widening (increased accounts) as well as credit deepening (increased loan per account). At state level, credit widening and deepening varied substantially. The credit widening was more conspicuous in Maharashtra as the annual growth in number of accounts was 40 per cent and the average loan size increased at 10 per cent only. Madhya Pradesh followed similar trend. In the remaining three states (Tamil Nadu, Rajasthan and Uttar Pradesh), the growth in credit flow followed the all India trend and the contribution of widening and deepening to the credit flow was almost equal. In Uttar Pradesh and Rajasthan, the share of RRBs declined drastically while that of Co-operatives declined in all the states, except in Rajasthan. The Report has further suggested that there is a need to orient agriculture credit policies in a manner that is more conducive for the marginal and small farmers, tenant farmers, share croppers and oral lessees in accessing credit from formal institutions.23

3.2.7 Agricultural Credit Structure in India: Pre and Post Reform Period:

Agriculture is the most important sector of the Indian economy from the perspective of poverty alleviation and employment generation. Agriculture provides employment to around 60 percent of the total work force in the country. It Accounts for about 13 percent of India’s national income at present.24 The agriculture carried on customarily by poor, small and marginal farmers and weaker sections of the society, has faced the key problem of finance. Indian Government accentuated on directed credit programmes as an important policy which provided administered allocation of credit to priority sectors at concessional interest rates. The idea behind this policy was that, without government interference through directed credit programmes, banks funding could not be
channelized to those activities which are of high social return or those categories of credit-worthy people who are marginalized in the credit market.²⁵

In India, the directed credit policies have been used for promoting agriculture and small-scale industry. Agriculture has been targeted because it is a risky activity and agricultural households are credit rationed by the formal sector (Swaminathan, 1991²⁶; Kochar, 1997²⁷). In addition, the availability of concessional credit augments the usage of quality inputs and encourages investment on machinery, irrigation and new technology to increase agricultural productivity. Thus, commercial and co-operative banks were directed to enlarge their rural branch networks and strengthen their lending to agriculture. Lending to priority sector became an important component of bank lending after the nationalization. With the increasing credit needs for farming operations, specific lending targets were fixed for each major bank and by March 1990, it was recommended to increase the proportion of direct agricultural lending to 18 percent of net bank credit. However, rural directed credit programme has not been a success, especially in terms of allocation of resources, cost-effectiveness and access to credit to farmers. Various researches have established different reasons for the failure. Katula and Gulati, Rao, Binswanger and Khandker found that the agricultural lending rates set by the government were lower than commercial and industrial rates, and hence, commercial banks could not cover the cost of their agricultural loan from profit arising from other operations. This led to cross-subsidization of the agricultural operations (Katula and Gulati 1992²⁸; Rao 1994²⁹; Binswanger and Khandker 1995³⁰). Moreover, the objective to achieve quantitative targets, ignoring qualitative aspects and mounting overdues, created a threat to the viability of financial institutions. Further, the disbursal of loans without assessing the feasibility, capability and entrepreneurial experience of borrowers led the banks to incur losses due to the widespread problem of
fungibility and poor repayment of the loan.\textsuperscript{31} Naastepad also concluded in his study that the effectiveness of directed credit programmes in stimulating investment, raising growth and reducing poverty was always a matter of dispute.\textsuperscript{32} One of the World Bank's study also supported that directed credit was inferior to a market-based allocation of resources in achieving growth and redistributive objectives (World Bank 1989\textsuperscript{33}; Odedokun1996\textsuperscript{34}). Therefore, the focus of India's financial reforms has been on the phasing-out of its directed credit programmes.\textsuperscript{35} Several Committees have been constituted to suggest ways to increase the availability of institutional credit to the rural areas.

These includes:

- The Expert Committee on Rural Credit (Chairperson: V.S. Vyas).
- Committee on Agricultural Credit through Commercial Banks (Chairperson: R.V.Gupta)
- Committee on Co-operatives (Chairperson: Vikhepatil).
- Advisory Committee on Flow of Credit Agriculture (Chairperson: V.S.Vyas).
- Task Force on Revival of Co-operative Credit Institutions (Chairperson: A.Vidhyanadhan).

The government has accepted and implemented several of their suggestions.\textsuperscript{36}

The structure of agricultural credit system of India comprises government of India and Reserve Bank of India\textsuperscript{37} at apex and wide network of commercial banks, Co-operatives and Regional Rural Banks. Rural Co-operative Credit institution consist two tier long-term credit structure and three-tire short-term credit structure. Long-term credit structure consists at state level state co-operative agriculture and rural development bank and at village level, there are primary co-operative agriculture and rural development banks.
Short-term credit structure consists of state Co-operative Banks at state level, District Central Co-operative Banks at district level and Primary Agricultural Credit Societies at village level. Among the institutional sources, primary agricultural credit societies are the most important source of credit. Private moneylenders and agri-input dealers are also important sources of credit for the farmers. Non-institutional loans are obtained by farmers from commission agents, moneylenders, relatives and friends. Among these the commission agents and moneylenders are the dominating source of credit. On an average, commission agents and moneylenders provide more than 95 per cent of the non-institutional credit to agriculture. Interest charged by them is very high. The changing scenario of Indian Agricultural Credit in the course of three decades is presented in Table 3.2. The table 3.2 informs us that during early green revolution period (1971) non-institutional credit agencies were leading with 68.3 per cent and institutional credit was 31.7 per cent. Where as in exact reforms period (1991) institutional credit agencies were emerged as 66.3 per cent and non-institutional credit agencies were 30.6 per cent. Here we have to congratulate the state contribution was significant. Furthermore, during 2011 year, again, non-institutional agencies had taken a little spike of 37.7 per cent and institutional agencies were 60.6 per cent. By all means, institutional credit agencies were took leadership role in financing farming community in India, which was a positive and healthy step towards farmer’s welfare in India. The agricultural credit structure is presented in figure 3.2.
Table 3.2
Agricultural credit structure in India: 1971-2011

<table>
<thead>
<tr>
<th>Credit Agencies</th>
<th>1971</th>
<th>1991</th>
<th>2011</th>
</tr>
</thead>
<tbody>
<tr>
<td>Co-operative and Commercial Banks</td>
<td>24.4</td>
<td>58.8</td>
<td>52.8</td>
</tr>
<tr>
<td>Government and other Formal Sources</td>
<td>7.3</td>
<td>7.5</td>
<td>7.8</td>
</tr>
<tr>
<td><strong>All institutional agencies</strong></td>
<td>31.7</td>
<td>66.3</td>
<td>60.6</td>
</tr>
<tr>
<td>Professional and Agricultural moneylenders</td>
<td>36.1</td>
<td>17.5</td>
<td>18.2</td>
</tr>
<tr>
<td>Traders</td>
<td>8.4</td>
<td>2.2</td>
<td>4.8</td>
</tr>
<tr>
<td>Land lords</td>
<td>8.6</td>
<td>4.0</td>
<td>5.7</td>
</tr>
<tr>
<td>Relatives and friends</td>
<td>13.1</td>
<td>4.6</td>
<td>4.4</td>
</tr>
<tr>
<td>Other sources</td>
<td>2.1</td>
<td>2.3</td>
<td>4.6</td>
</tr>
<tr>
<td><strong>All non-institutional agencies</strong></td>
<td><strong>68.3</strong></td>
<td><strong>30.6</strong></td>
<td><strong>37.7</strong></td>
</tr>
<tr>
<td>Sources not specified</td>
<td>0.0</td>
<td>3.1</td>
<td>1.7</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td>100</td>
<td>100</td>
<td>100</td>
</tr>
</tbody>
</table>

Source: 1. All-India Rural Credit Survey 1971.
2. All India Debt and Investment Survey 1991.

Figure 3.2
Agricultural Credit Structure in India: 1971-2011
3.2.8 Progress of Institutional Credit in the Post Reform Period in India:

The main institutional agencies for providing agricultural credit are (1) Co-operatives (2) Commercial Banks. (3) Regional Rural Banks (4) National Bank for Agriculture and Rural Development (NABARD) and (5) Reserve Bank of India. The first three are field level agencies which are refinanced to the necessary extent by NABARD as the apex institution at national level. RBI is the Central Bank of the country and has, therefore, a crucial role in monitoring the supply of agricultural credit as a part of its overall monetary and credit policy. The progress of institutional credit in the post reform period in India is presented in table 3.3.

Table 3.3.
Disbursement of Institutional Credit for Agricultural Loans issued from 2000-01 to 2011-12. (Rs.Crores)

<table>
<thead>
<tr>
<th>Year</th>
<th>Co-operatives</th>
<th>Regional Rural Banks</th>
<th>Commercial Banks</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000-01</td>
<td>27295</td>
<td>3966</td>
<td>16440</td>
<td>47701</td>
</tr>
<tr>
<td>2001-02</td>
<td>30569</td>
<td>4546</td>
<td>18638</td>
<td>53573</td>
</tr>
<tr>
<td>2002-03</td>
<td>34040</td>
<td>5879</td>
<td>25256</td>
<td>65175</td>
</tr>
<tr>
<td>2003-04</td>
<td>40049</td>
<td>7175</td>
<td>36203</td>
<td>83427</td>
</tr>
<tr>
<td>2004-05</td>
<td>45009</td>
<td>11927</td>
<td>48367</td>
<td>105303</td>
</tr>
<tr>
<td>2005-06</td>
<td>48123</td>
<td>15300</td>
<td>80599</td>
<td>144022</td>
</tr>
<tr>
<td>2006-07</td>
<td>54019</td>
<td>20228</td>
<td>115266</td>
<td>189513</td>
</tr>
<tr>
<td>2007-08</td>
<td>57643</td>
<td>23838</td>
<td>1134720</td>
<td>1216201</td>
</tr>
<tr>
<td>2008-09</td>
<td>58787</td>
<td>26499</td>
<td>160690</td>
<td>245976</td>
</tr>
<tr>
<td>2009-10</td>
<td>74938</td>
<td>34640</td>
<td>188253</td>
<td>297831</td>
</tr>
<tr>
<td>2010-11</td>
<td>-</td>
<td>43965</td>
<td>222792</td>
<td>266759</td>
</tr>
<tr>
<td>2011-12</td>
<td>-</td>
<td>53058</td>
<td>312877</td>
<td>365935</td>
</tr>
<tr>
<td>Total</td>
<td>470472</td>
<td>2360101</td>
<td>2510121</td>
<td>3081416</td>
</tr>
<tr>
<td>%Share</td>
<td>15.26</td>
<td>76.59</td>
<td>8.15</td>
<td>100.00</td>
</tr>
</tbody>
</table>


It is observed from the table 3.3 that the increase of institutional credit in the post reform period is impressive. The shares of percent were 15.26 per cent, 8.15 per cent and 76.59 per cent for Co-operatives, Regional Rural Banks and Commercial Banks.
respectively. The participation of Co-operatives in farm financing increased by 2.74 times, Regional Rural Banks 19.03 times and that of Commercial Banks 11.08 times. The credit issued by Co-operatives increased from Rs. 27295 crores in 2000-01 to Rs 74938 crores in 2009-10. The Regional Rural Banks loans issued increased from Rs. 3966 crores in 2000-01 to Rs.53058 crores in 2011-12. The agriculture loans issued by Commercial Banks increased from Rs. 16440 in 2000-01 to 312877 crores in 2011-12. The total institutional credit issued for agriculture loans increased from Rs. 47701 in 2000-01 to 3081416 in 2011-12. Progress of institutional credit for agriculture and loans outstanding in the post reform period presented in table 3.4

Table 3.4
Progress of Institutional Credit for Agriculture: Loans Outstanding from 2000-01 to 2011-12

<table>
<thead>
<tr>
<th>Year</th>
<th>Co-operative Banks</th>
<th>Regional Rural Banks</th>
<th>Commercial Banks</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000-01</td>
<td>46135</td>
<td>7249</td>
<td>38270</td>
<td>91654</td>
</tr>
<tr>
<td>2001-02</td>
<td>52110</td>
<td>8286</td>
<td>45106</td>
<td>105502</td>
</tr>
<tr>
<td>2002-03</td>
<td>59064</td>
<td>10261</td>
<td>53804</td>
<td>123129</td>
</tr>
<tr>
<td>2003-04</td>
<td>71403</td>
<td>11721</td>
<td>68903</td>
<td>152027</td>
</tr>
<tr>
<td>2004-05</td>
<td>78822</td>
<td>16709</td>
<td>95519</td>
<td>191050</td>
</tr>
<tr>
<td>2005-06</td>
<td>82327</td>
<td>21510</td>
<td>135603</td>
<td>239440</td>
</tr>
<tr>
<td>2006-07</td>
<td>89443</td>
<td>27452</td>
<td>169018</td>
<td>285913</td>
</tr>
<tr>
<td>2007-08</td>
<td>65666</td>
<td>33216</td>
<td>202796</td>
<td>301678</td>
</tr>
<tr>
<td>2008-09</td>
<td>64045</td>
<td>37367</td>
<td>256119</td>
<td>357531</td>
</tr>
<tr>
<td>2009-10</td>
<td>76480</td>
<td>46287</td>
<td>315436</td>
<td>438203</td>
</tr>
<tr>
<td>2010-11</td>
<td>-</td>
<td>55067</td>
<td>357584</td>
<td>412651</td>
</tr>
<tr>
<td>2011-12</td>
<td>-</td>
<td>63823</td>
<td>443298</td>
<td>507121</td>
</tr>
<tr>
<td>Total</td>
<td>685495</td>
<td>338948</td>
<td>2181456</td>
<td>3205899</td>
</tr>
</tbody>
</table>


It is noticed from the table 3.4 that the extent of institutional credit total outstanding increased from Rs 91654 crores in 2000-01 to Rs. 507121 crores in 2011-12 there by recording 5.53 times. The share of loans outstanding percent were 21.38 per cent, 10.57
per cent and 68.05 per cent for Co-operatives, Regional Rural Banks and Commercial Banks. The participation of co-operatives in farm financing increased by 1.65 times, Regional Rural Banks 8.80 times and that of Commercial Banks 5.53 times. The loans outstanding by Co-operatives increased from Rs 46135 crores in 2000-01 to Rs. 76480 crores in 2009-10. The Regional Rural Banks loans outstanding increased from Rs.7249 crores in 2000-01 to Rs. 63823 crores in 2011-12. The agriculture loans outstanding by commercial banks increased from Rs. 38270 in 2000-01 to Rs.443298 crores in 2011-12.

3.2.9 Co-operative Banks:

Co-operative is an economic organization of individuals who get together in participate process for arranging performance of services to meet their felt needs. “The basic objective of the co-operatives is to provide services through self-help and mutual help. The co-operative movement is more than 100 years old. The movement has a rural as well as an urban structure, a credit as well as a non-credit component and within its credit segment, has a short term and long term structure. The International Labor Organization (ILO) considered “Co-operatives to be established and developed as a means of increasing national income, export revenues and employment by a fuller utilization of resources… aimed at bringing fresh areas into productive use and in the development of modern industrial, preferably, scattered processing local raw material”. (Recommendation no.127, 1996).

The co-operative banking structure is paramedical in the character. There are primary agricultural credit societies at village level upon which the entire edifice of co-operative finance is based. These societies are federated at district level into “Central Co-operative Banks” and at state level “Apex Bank”. The apex or state co-operative bank in its turn is closely linked with NABARD, which provides considerable financial assistance to
co-operative credit structure. The loan is to advance from state co-operative Banks to Central Co-operative Banks at district level and from them to Primary Agricultural Credit Societies, which ultimately provide credit to the farmers. As by the end of March 2013, there are 31 State Co-operative Banks, 370 District Co-operative Banks and 697 Primary Agricultural Credit Societies in the country. Structure of Co-operative Societies in India is shown in chart 3.1.

**Chart 3.1**

**Structure of Co-operative Credit Institutions in India as by the end of March 2013**

- Credit co-operative (95,156)
  - Rural co-operative (93,156)
    - Short Term (92,833)
      - St CBs (31)
      - DCCBs (370)
      - PACs (92432)
    - Long-Term (717)
      - SCARDBs (20)
      - PCARDBs (697)
  - UCBs (1606)
    - Scheduled (51)
    - Non-Scheduled (1555)

Note: Figures in brackets indicate number of offices.

**Source:** Report on Trend Progress of Banking in India for the Year ended by June 30, 2013, p. 93.

India’s co-operative Banks are increasingly supporting small and marginal farmers. The financial health of co-operatives has become weak, in part because of management and governance problems. Ongoing revitalization of co-operatives through staff training.
Corporate governance improvement, and organizational development is having some positive impact (table 3.5). Deposits held have fallen over the years, but loans outstanding and net profits in 2011-12 were much improved over the previous year. NPA performance has also improved. In the light of these positive changes on the performance of co-operatives as a result of the current reforms and given their expansion outreach in the rural and semi urban areas, co-operatives can be used as an effective means of servicing the small credit needs of the large number of marginal farmers in India. Performance indicators of co-operative banks are shown in table 3.5.

### Table 3.5
Performance Indicators of Co-operative Banks: 2006-2012

<table>
<thead>
<tr>
<th>Years</th>
<th>No. of banks</th>
<th>Deposits</th>
<th>Loans and advances (outstanding)</th>
<th>Net profit</th>
<th>Recovery of loans (%)</th>
<th>NPA to loans outstanding</th>
</tr>
</thead>
<tbody>
<tr>
<td>2006</td>
<td>1,113</td>
<td>135,286</td>
<td>150,480</td>
<td>633</td>
<td>62.4</td>
<td>26.2</td>
</tr>
<tr>
<td>2007</td>
<td>1,116</td>
<td>143,835</td>
<td>167,215</td>
<td>248</td>
<td>63.2</td>
<td>24.6</td>
</tr>
<tr>
<td>2008</td>
<td>1,118</td>
<td>168,602</td>
<td>181,828</td>
<td>475</td>
<td>58.1</td>
<td>27.3</td>
</tr>
<tr>
<td>2009</td>
<td>1,118</td>
<td>200,880</td>
<td>175,354</td>
<td>1,860</td>
<td>61.0</td>
<td>25.6</td>
</tr>
<tr>
<td>2010</td>
<td>1,118</td>
<td>237,730</td>
<td>204,263</td>
<td>1,070</td>
<td>61.5</td>
<td>29.7</td>
</tr>
<tr>
<td>2011</td>
<td>1,118</td>
<td>252,000</td>
<td>228,600.39</td>
<td>892</td>
<td>60.3</td>
<td>23.1</td>
</tr>
<tr>
<td>2012</td>
<td>1,118</td>
<td>262,231</td>
<td>259,714.62</td>
<td>1,993</td>
<td>61.8</td>
<td>22.0</td>
</tr>
</tbody>
</table>


The Co-operative banks should go in for more diversification in lending and other activities, insurance, housing finance, handloom finance and extension of credit to processing industries and production oriented small units will greatly help in earning more. Products and services must be upgraded to compete with commercial banks. Collection of dues and over dues should receive top priority from all personnel of the co-operative credit movement. The huge scope for investment credit to agriculture should be exploited properly.\(^{40}\)
3.2.10 Regional Rural Banks:

The Regional Rural Banks (RRBs) came into being under the 20-point economic programme launched in 1975. Earlier, the Banking Commission, appointed by the Government to study the structure of banking development in India, mooted the idea of setting up RRBs in its report in 1972. The government reviewed the recommendations of the Banking Commission and appointed the Narasimham Study Group on July 1, 1975. It submitted the report in just 30 days and favoured the setting up of RRBs. The government of India promulgated the RRBs ordinance dated September 26th which was subsequently replaced by the Regional Rural Banks Act, 1976. On October 2, 1975, five RRBs were established in four states: 2 in Uttar Pradesh, one at Moradabad by the Syndicate Bank and the other at Gorakhpur by the State Bank of India; one in Rajasthan by the United Commercial Bank; one in Bhiwani (Haryana) by the Punjab National Bank and one in Medla (West Bengal) by the United Bank of India. Regional Rural Banks have been providing credit to small and marginal farmers, agricultural laborers, artisans and small entrepreneurs since 1975. With 17,856 branches in 635 districts as of March 2013, they are integral to India’s rural economy. The performance of RRBs has been modest because of the high cost of lending to the target group, poor recovery of loans, high staff costs, and lack of commercial orientation in management. The government is restructuring RRBs so they can better serve the targeted population without incurring inordinate losses. Restructuring includes training, introducing a common written examination for recruitment of officers, and strengthen the Capital to Risk-weighted Assets Ratios (CRARs) by infusing up to INR 22 billion. Table 3.6 presents recent performance indicators for RRBs.
Table 3.6 reveals recent performance indicators for RRBs. The fall in the number of RRBs is a function of recapitalization. Total deposits declined for two consecutive years (2010-11 to 2011-12) then picked up in 2012-13, indicating improved performance. The same held true for loans, advances, and net profits. In 2013, 64 RRBs made a profit of INR 2383 crores, compared to 82 that made a profit of INR 1857 crores in 2012.

National Bank for Agricultural Rural Development (NABARD)\(^43\) the regulating body for rural banks, has reported that the agricultural credit disbursement by RRBs has been short of the target. The low disbursal of farm credit by RRBs was due to amalgamation and capital adequacy limitations, as these banks had to maintain a capital adequacy ratio of at least nine per cent, which revealed that adding RRBs did not have any source of capital other than paid up capital. Status of RRBs 2013 and 2014 is shown in table 3.7.
Table 3.7
Status of RRBs as on 31<sup>st</sup> March of 2013 and 2014

<table>
<thead>
<tr>
<th>Parameters</th>
<th>March 31&lt;sup&gt;st&lt;/sup&gt; 2013</th>
<th>March 31&lt;sup&gt;st&lt;/sup&gt; 2014</th>
</tr>
</thead>
<tbody>
<tr>
<td>No. of RRBs</td>
<td>64</td>
<td>57</td>
</tr>
<tr>
<td>Share of capital (Rs.cr)</td>
<td>197</td>
<td>197</td>
</tr>
<tr>
<td>Share capital deposit (Rs.cr)</td>
<td>6001</td>
<td>6170</td>
</tr>
<tr>
<td>Reserves (Rs.cr)</td>
<td>13247</td>
<td>15262</td>
</tr>
<tr>
<td>Profit earning RRBs</td>
<td>163</td>
<td>57</td>
</tr>
<tr>
<td>Net profit of RRBs (Rs.cr)</td>
<td>2273</td>
<td>2744</td>
</tr>
<tr>
<td>Accumulated losses (Rs.cr)</td>
<td>1091</td>
<td>949</td>
</tr>
<tr>
<td>Deposits (Rs.cr)</td>
<td>211488</td>
<td>239511</td>
</tr>
<tr>
<td>Loans and advances (Rs.cr)</td>
<td>137078</td>
<td>218110</td>
</tr>
<tr>
<td>Nonperforming loans (%)</td>
<td>6.08</td>
<td>4.35</td>
</tr>
</tbody>
</table>

Source: www.allbankingsolution.com

Table 3.7 reveals the status of RRBs in 2013-14. The RRB branches 64 in 2013 decreased to 57 in 2014. There was no noticeable change in the share of capital from 2013 to 2014. The share of capital deposit increased from Rs. 6001 crores in 2013 to Rs. 6170 in 2014. There by recording an increase of RRBs reserves, 1.15 times from 2013 to 2014. During the same period, net profits of RRBs increased from 2273 crores to 2744 crores. The share of accumulated losses declined steeply from Rs. 1091 crores to 949 crores. The deposits showed an increase of 1.13 times. The non-performing loans marginally declined from 6.08 per cent to 4.35 percent during the same period.

Latest progress of Regional Rural Banks 2013-14.

I. After amalgamation, the number of RRBs in the country as on 31<sup>st</sup> March 2014 were 57, with a network of 19,082 branches covering 642 notified districts in 26 states and the UT of Puducherry. (However, as on 20 August 2014, the number of RRBs is only 56).

II. The aggregate deposits of RRBs registered a growth of 13 per cent, borrowings 34 per cent, loans and advances (outstanding) 17 per cent and investments 2 per cent, during the financial year 2013-14.
III. The provisional financial result of RRBs for the year 2013-14, indicates that all 57 RRBs have earned profits aggregating to Rs.2,833 crores.

IV. The proportion of RRBs that are substantially viable viz., earning profits and carrying no accumulated losses has increased from to 86 per cent (49 out of 57) as by 31 March 2014.

V. The aggregate reserve of RRBs increased to Rs.15,736 crores and net worth increased to Rs. 21,199 crores as by 31 March 2014.

VI. There were 8 RRBs with an accumulated loss decreasing to 17 per cent as on 31st March 2014, over the previous year.

VII. The recovery performance of RRBs improved marginally from 812 per cent as on June 2012 to 819 per cent as on 30 June 2013. Nine RRBs had recovery of more than 90 per cent, 19 RRBs had recovery in the range of 60 and 80 per cent and one RRB had recovery of less than 60 per cent. The aggregate gross NPA of all RRBs declined from 6.1 per cent as on 31 March 2013 to 4.4 per cent as on 31 March 2014.

As a strategy towards board’s financial inclusion, RRBs were advised to undertake an aggressive branch expansion programme particularly in hitherto unbanked areas. “RRBs had opened 913 and 947 new branches during 2011-12 and 2013-14, respectively. The RRBs have allocated 22000 villages and at places where opening brick and mortar branch is not considered viable, the banks are allowed to start ultra-small branches (USBs) and thereafter at places where the USBs reached the desired level of business, the same can be upgraded into regular bank branches”. 
3.2.11 Commercial Banks

Commercial banks are the oldest, biggest, and fastest growing financial intermediaries in India. The commercial banks are those financial institutions, which accept deposits from the public repayable on demand and lend them for short periods. They borrow money in the form of deposits at a lower rate of interest and lend it at a higher rate and thereby make a profit. Commercial banking in India is a unique system, the like of which exists nowhere in the world. The truth of this statement becomes clear as one studies the philosophy and approaches that have contributed to the evaluation of the banking policy programmes and operations in India. The banking system in India works under the constraints that go with social control and public ownership. "The public ownership of banks has been achieved in three stages: 1955, July 1969, and April 1980. 14 major commercial banks were nationalized in July 1969 and 6 more were nationalized in April 1980. Efforts are also being made to see that at least 50 per cent of the institutional credit goes to the weaker sections".

Priority Sector Advances by Commercial Banks

Priority sector lending includes lending to those sectors that impact large sections and the sectors, which are employment intensive such as agriculture and tiny and small enterprises. The categories under priority sector include agriculture, micro small enterprises, education, housing, export creditor, and others. Priority sectors have been an integral part of bank credit delivery in India. Priority sector lending includes lending to those sectors that impact large sections of the population, the weaker sections and the sectors which are employment intensive such as agriculture, and tiny and small enterprises. The categories under priority sector include agriculture, micro small enterprises, education, housing, export credit, and others. The commercial banks play a significant role among the
institutional sources of credit for priority sector in India. The significance of bank credit in the priority sector can be observed against the backdrop of increasing quantum of such credit to this sector. The following table 3.8 presents commercial bank advances to priority sector in India during 2000-2013.

### Table 3.8

Advances to Priority Sector of Scheduled Commercial Banks in India: 2000-2013

<table>
<thead>
<tr>
<th>Year</th>
<th>Priority sector advances</th>
<th>Trend%</th>
<th>Share of PSA in total advances</th>
<th>Trend%</th>
</tr>
</thead>
<tbody>
<tr>
<td>2000</td>
<td>1557.79</td>
<td>100</td>
<td>35.4</td>
<td>100</td>
</tr>
<tr>
<td>2001</td>
<td>1822.55</td>
<td>117</td>
<td>31.0</td>
<td>88</td>
</tr>
<tr>
<td>2002</td>
<td>2056.06</td>
<td>132</td>
<td>34.8</td>
<td>98</td>
</tr>
<tr>
<td>2003</td>
<td>2546.48</td>
<td>163</td>
<td>35.1</td>
<td>99</td>
</tr>
<tr>
<td>2004</td>
<td>2638.34</td>
<td>169</td>
<td>34.5</td>
<td>97</td>
</tr>
<tr>
<td>2005</td>
<td>3814.76</td>
<td>245</td>
<td>36.7</td>
<td>104</td>
</tr>
<tr>
<td>2006</td>
<td>5101.75</td>
<td>327</td>
<td>35.3</td>
<td>100</td>
</tr>
<tr>
<td>2007</td>
<td>6553.17</td>
<td>421</td>
<td>33.1</td>
<td>94</td>
</tr>
<tr>
<td>2008</td>
<td>7814.76</td>
<td>502</td>
<td>31.6</td>
<td>89</td>
</tr>
<tr>
<td>2009</td>
<td>9089.29</td>
<td>583</td>
<td>30.3</td>
<td>86</td>
</tr>
<tr>
<td>2010</td>
<td>10915.10</td>
<td>701</td>
<td>31.2</td>
<td>88</td>
</tr>
<tr>
<td>2011</td>
<td>13158.59</td>
<td>845</td>
<td>30.6</td>
<td>86</td>
</tr>
<tr>
<td>2012</td>
<td>14710.50</td>
<td>944</td>
<td>29.5</td>
<td>83</td>
</tr>
<tr>
<td>2013</td>
<td>16411.00</td>
<td>1053</td>
<td>28.8</td>
<td>81</td>
</tr>
<tr>
<td>Average</td>
<td>7013.58</td>
<td>450</td>
<td>32.71</td>
<td>92</td>
</tr>
</tbody>
</table>


The priority sector advances have raised from Rs.1557.79 billion in the year 2000 to Rs.16411 billion in the year 2013 but the share of the same decreased from 35.4 per cent in 2000 to 28.8 per cent in the year 2013. The trend analysis shows a growth rate of 953 per cent with an average growth rate of 450 per cent and the same has a declining rate of degree of relationship of priority sector. Advances over the years are calculated as a high
positive correlation of 0.97 and the same is negative (-0.74) for the share of priority sector advances in total advances.

Distribution of commercial bank branches in India is presented in Table 3.9. Table 3.9 presents the number of nationalized commercial banks increased from 66190 in 2002 to 105753 in 2013. During the year 2002 the share of branches in Rural, Semi urban, Urban, Metropolitan were 48.92 per cent, 22.28 per cent, 15.83 per cent and 12.97 per cent respectively. The share of rural branches in the total increased from 48.92 per cent in 2002 to 37.20 per cent in 2013. The relative share of semi urban, urban, and metropolitan branches gradually increased from 22.28 per cent, 15.83 per cent, 12.97 per cent to 26.12 per cent, 19.25 per cent, 17.69 per cent respectively. The rural and semi urban branches were 62178 amounting to 63.07 per cent of total branches. Only 36.94 per cent of the new branches were opened in the urban and metropolitan centers during the period. Today, the commercial banks in India are penetrating every corner of the country and are extending a helping hand in the growth process of the rural sector in the country. The flow credit to farmers has not been adequate, forcing the farmers, especially the small farmers, to take loans from moneylenders at exorbitant rate of interest. Though those many number of branches are working in the rural area to provide credit for farm sector, still farmers are taking loans from moneylenders. Because, there is more demand for rural credit, but the supply of credit is inadequate to meet the demand of farmers.
### Table 3.9

*Population Group-wise Number of Bank Branches of Scheduled Commercial Banks: 2002-2013*

<table>
<thead>
<tr>
<th>Year</th>
<th>Rural Branches</th>
<th>Rural Branches%</th>
<th>Semi Urban Branches</th>
<th>Semi Urban Branches%</th>
<th>Urban Branches</th>
<th>Urban branches%</th>
<th>Metropolitan branches</th>
<th>Metropolitan branches%</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>2002</td>
<td>32380</td>
<td>48.92</td>
<td>14747</td>
<td>22.28</td>
<td>10477</td>
<td>15.83</td>
<td>8586</td>
<td>12.97</td>
<td>66190</td>
</tr>
<tr>
<td>2003</td>
<td>32303</td>
<td>48.55</td>
<td>14859</td>
<td>22.33</td>
<td>10693</td>
<td>16.07</td>
<td>8680</td>
<td>13.05</td>
<td>66535</td>
</tr>
<tr>
<td>2004</td>
<td>32121</td>
<td>47.81</td>
<td>15091</td>
<td>22.46</td>
<td>11000</td>
<td>16.37</td>
<td>8976</td>
<td>13.36</td>
<td>67188</td>
</tr>
<tr>
<td>2005</td>
<td>32082</td>
<td>46.93</td>
<td>15403</td>
<td>22.53</td>
<td>11500</td>
<td>16.82</td>
<td>9370</td>
<td>13.71</td>
<td>68355</td>
</tr>
<tr>
<td>2006</td>
<td>30106</td>
<td>43.09</td>
<td>15760</td>
<td>22.56</td>
<td>12200</td>
<td>17.46</td>
<td>11800</td>
<td>16.89</td>
<td>69866</td>
</tr>
<tr>
<td>2007</td>
<td>30248</td>
<td>41.86</td>
<td>16522</td>
<td>22.86</td>
<td>13070</td>
<td>18.09</td>
<td>12421</td>
<td>17.19</td>
<td>72261</td>
</tr>
<tr>
<td>2008</td>
<td>30772</td>
<td>40.35</td>
<td>17768</td>
<td>23.30</td>
<td>14333</td>
<td>18.80</td>
<td>13383</td>
<td>17.55</td>
<td>76256</td>
</tr>
<tr>
<td>2009</td>
<td>31453</td>
<td>39.21</td>
<td>19058</td>
<td>23.76</td>
<td>15374</td>
<td>19.17</td>
<td>14332</td>
<td>17.87</td>
<td>80217</td>
</tr>
<tr>
<td>2010</td>
<td>32473</td>
<td>37.97</td>
<td>20778</td>
<td>24.30</td>
<td>16810</td>
<td>19.66</td>
<td>15457</td>
<td>18.07</td>
<td>85518</td>
</tr>
<tr>
<td>2011</td>
<td>33909</td>
<td>37.20</td>
<td>23053</td>
<td>25.29</td>
<td>17749</td>
<td>19.47</td>
<td>16445</td>
<td>18.04</td>
<td>91156</td>
</tr>
<tr>
<td>2012</td>
<td>36428</td>
<td>36.95</td>
<td>25750</td>
<td>26.12</td>
<td>18980</td>
<td>19.25</td>
<td>17439</td>
<td>17.69</td>
<td>98597</td>
</tr>
<tr>
<td>2013</td>
<td>39336</td>
<td>37.20</td>
<td>28264</td>
<td>26.73</td>
<td>19941</td>
<td>18.86</td>
<td>18212</td>
<td>17.22</td>
<td>105753</td>
</tr>
</tbody>
</table>

3.2.12 Government Loans

Government assistance by way of direct finance to agriculturists is a very old practice in India. Loans were used to be granted under Deccan Agricultural Relief Act (1979), Land Improvement Loan Act (1983) and Agriculturist Loan Act (1884). The last two sources of credit in force were generally known as the Taccavi loans, the former being a source of long-term loans and the latter short-term loans. The grant of these loans was at the time of famines, floods or other calamities. The Venkatappaiah Committee, having suggested certain measures for the improvement of taccavi loan system in the country, ultimately advocated the discontinuance of the system. Hence, it was no longer regarded as an important source of agricultural credit in the country. Based on the learned opinion that government is not the right agency for advancing loans to agriculturists, various committees that examined the problem of rural credit suggested channeling government funds through co-operatives. The advantages of taccavi loans lie in their long-term duration and low rates of interest. But the total amount lent under both acts is extremely insignificant and accounts to a mere drop in the ocean. Except in special cases, government funds should be distributed through co-operatives rather than directly by the government. The rate of interest on these loans is low at about 6 per cent and the mode of repayment is very significant. The government and other formal credit was only 7.3 per cent in 1971. It rose to 7.8 per cent in 2011. It is obvious that government credit, though important, is not a major source of agricultural finance. Farmers find it difficult to get ‘taccavi’ loans because of many procedural rigidities, waste of time and the delay involved. The repayment of these loans is rather very strict. Hence, the taccavi loans have not played a significant role.
The government of India has initiated several policy measures to improve the accessibility of farmers to the institutional sources of credit. The emphasis of these policies has been on progressive institutionalization for providing timely and adequate credit support to all farmers with particular focus on small and marginal farmers and weaker sections of society to enable them to adopt modern technology and improved agricultural practices for increasing agricultural production and productivity. The policy lays emphasis on augmenting credit flow at the ground level through credit planning, adoption of region-specific strategies and rationalization of lending policies and procedures. These policy measures have resulted in the increase in the share of institutional credit of the rural households. The government is implementing a package for revival of short-term rural co-operative credit structure in the country. The revival package is aimed at strengthening the short-term rural co-operative credit structure and make it a well-managed and vibrant medium to serve the credit needs of rural India, especially the small and marginal farmers. The standing guidelines of Reserve Bank of India (RBI) provide for rescheduling of short term crop loans upon declaration of a natural calamity including drought. Such rescheduling of crop loans converts them into term loans for which normal rate of interest are applicable. Due to deficient rainfall in the drought affected areas reduction of interest rates has been under the consideration of the government. In order to provide relief to drought affected farmers, it has been decided that in case where such loans are restructured due to drought, the interest subvention of 2% which is already available for short term crop loans to public sector banks, co-operative banks and regional rural banks will continue to be available for the current financial year on the full restructure amount. The debt waiver exercise was
completed by 30th June 2008, whereas the debt relief exercise was closed in June 2010 after granting a few extensions. The government of India has so far sanctioned Rs.52,516.86 crores in 5 installments as reimbursement to the banks under the scheme. Out of this Rs.29,275.81 crores was passed on to NABARD for reimbursement to RRBs and co-operative banks and an amount of Rs. 23,159.76 crores has been reimbursed to scheduled commercial banks, local area and urban co-operative banks.

3.2.13 NABARD

In December 1971, the National Commission on Agriculture (in its interim report on credit services for small and marginal farmers and agricultural laborers) expressed the view that it might be ultimately necessary to set up an Agricultural Development Bank of India on the lines of the Industrial Development Bank of India. The Committee to Review Arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD) headed by B.Sivaraman favored the setting up of an all India institution, though there is a view that such an institution will only add to the cost of credit and the red-tapism associated with procedure. The National Bank for Agricultural and Rural Development (NABARD) is an apex institution of national importance for providing short-term, medium and long-term credit for financing agricultural and allied activities including processing, storage etc. It started functioning from July 12, 1982.51

NABARD has over 25 regional offices in the country and a paid up capital of Rs.100 crores, contributed by the government of India and the Reserve Bank of India. This was raised to Rs.500 crores later and at present it has increased to Rs.2000 crores. NABARD has created special funds namely, tribal development fund, integrated
development of back ward blocks, research and development fund, farm innovations fund, micro financed development and equity fund for sustainable development interventions. NABARD has provided rural employment through cluster development, rural haats, rural entrepreneurship, rural industrialization and skills up gradation of handloom weavers. NABARD should achieve success in ensuring not only flow of more funds into the rural sector, particularly agricultural sector, but also optimum utilization of available resources in tune with planned priorities. The table 3.10 provides the clear details of NABARD’s financial assistance for agriculture and allied activities from 2004 to 2013.

Table 3.10

<table>
<thead>
<tr>
<th>years</th>
<th>No. of schemes sanctioned</th>
<th>Total financial assistance sanctioned</th>
<th>Disbursements</th>
</tr>
</thead>
<tbody>
<tr>
<td>2004</td>
<td>7626</td>
<td>83.49</td>
<td>76.05</td>
</tr>
<tr>
<td>2005</td>
<td>161</td>
<td>92.77</td>
<td>85.77</td>
</tr>
<tr>
<td>2006</td>
<td>132</td>
<td>88.66</td>
<td>86.22</td>
</tr>
<tr>
<td>2007</td>
<td>69</td>
<td>96.31</td>
<td>87.95</td>
</tr>
<tr>
<td>2008</td>
<td>21</td>
<td>97.04</td>
<td>90.46</td>
</tr>
<tr>
<td>2009</td>
<td>28</td>
<td>116.21</td>
<td>105.35</td>
</tr>
<tr>
<td>2010</td>
<td>3</td>
<td>123.08</td>
<td>120.09</td>
</tr>
<tr>
<td>2011</td>
<td>3</td>
<td>147.38</td>
<td>134.86</td>
</tr>
<tr>
<td>2012</td>
<td>2</td>
<td>157.58</td>
<td>154.22</td>
</tr>
<tr>
<td>2013</td>
<td>1</td>
<td>180.62</td>
<td>176.74</td>
</tr>
</tbody>
</table>


Table 3.10 reveals the financial assistance of National Bank for Agriculture and Rural Development (NABARD) from 2004 to 2013. NABARD’s total disbursement is tremendous and increased from Rs.76.05 crores in 2004 to 176.74 crores in 2013, increased by 2.43 times. Total financial assistance sanctioned has taken place from
Rs.83.49 crores in 2004 to 180.62 crores in 2013, increased by only 2.16 times. Number of schemes sanctioned are marginally declined from 7626 in 2004 to 1 in 2013.

NABARD has taken several measures, both at policy and operational levels, for improving the quality of lending by ensuring adherence to technical and financial parameters and by supporting national policies for increasing agricultural production and rural employment through efficient use of national resources. NABARD aims at increasing the financing absorption capacity of the credit delivery system by improving the health of the credit agencies involved in credit dispersion. NABARD has been performing a variety of role functions in tune with its mandate.53
References


15. Reserve Bank of India (1966): “Report of the All India Rural Credit Review
Committee”, Mumbai, p.999.


43. www.All Banking Solution.Com
49. Jha .D: “Agencies for supplying agricultural credit’ in Rural Banking in India”, oxford publishing co., Ltd; New Delhi, 1975, pp.36-37.
50. agricoop.nic.in/agriculture-credit.
52. Pramon S. Bhatnagar: “Liberalizing Rural Lending”, Yojana, July 13-16,1988, p.31

*****