Chapter No. II

Theoretical Background
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Concept and Principles of Co-operation

2.1 Introduction:

The term co-operation, in the literary sense means ‘working together’ but in technical sense it means working together for some economic pursuit, on the basis of certain basic principles, which differentiate it from other forms of organization. The co-operative planning committee (1946) defined co-operation “as a form of organization in which persons voluntarily associate together on the basis of equality for the promotion of their economic interests”. The committee further stated that, those who come together have a common economic aim which they cannot achieve by individual isolated action, because of the weakness of the economic position of a large majority of them. This element of individual weakness is overcome by the pooling of their resources, by making self help effective through mutual aid, and by strengthening the bonds of moral solidarity between them.

According to International Co-operative Alliance, “a co-operative is an autonomous association of persons united voluntarily to meet their common economic, social and cultural needs and aspirations through a jointly owned and democratically controlled enterprise”.

Phillips stated that the “co-operative Association is an association of firms or households for business purposes, and economic institution through which economic activity is conducted in the economic objectives.”

From the above definitions, we can conclude that, co-operatives by nature are neither capitalistic nor socialistic but are neutral between the two and its main aim is to further social, economic and cultural interests of its members. It can serve various aims and serve the needs of politically, socially and religiously divergent people at the same time.

2.2 Need of co-operation.

The concept of money, property and their ownership gave rise to inequalities in the distribution of income and wealth among the people. In a capitalistic system
profit motive of private enterprises leads to exploitation of workers and consumers. The human values are not honoured and workers’ personality is reduced to very low level. The concentration of wealth in a few hands gives them social strength and political power. The alternative economic system suggested by economists includes communism and various forms of socialism. However even in communism of state socialism where there is socialization of property, there is concentration of power in few hands and the liberty of individual is highly restricted. Co-operation is a special type of economic combination of men of moderate means to save themselves forms the exploitation of rich by pooling their resources on the basis of equality within capitalist or semi socialist system. Among capitalism and communism co-operatives act as a balancing factor. It combines in itself the good points of capitalistic and socialistic forms of organizations.  

According to Calvert H (1933) co-operation is “a form of organization, where in persons voluntarily associate together as human being on the basis of equality for the promotion of the economic interests of themselves”.

Fay C.R. (1908) defined co-operation as “A co-operative society is an association for the purpose of joint trading originating among the weak and conducted always in an unselfish spirit, on such terms that all who are prepared to assume the duties of membership may share in its rewards in proportion to the degree in which they make use of their associations”.

The Maclagan committee (1915) has stated that “The theory of co-operation is very briefly, that an isolated and powerless individual can by association with others and by moral development and mutual support obtain in his degree, the material advantages available to wealthy or powerful persons and thereby develop himself to the fullest extent of his natural abilities. By the union of forces material advancement is secured, and by united action of self reliance is fostered and it is from the interaction of these influences that it is hoped to attain the effective realization of the higher and more prosperous standard of life which has been characterized as better business better farming and belter living.”

Herrik MT (1933) defined Co-operation as “the act of persons voluntarily united for utilizing. Reciprocally their own forces resources on both, under their mutual management to their common profit or loss”.

The co-operative planning committee (1946) defined Co-operation as “a form of organization in which persons voluntarily associate together on the basis of
equality for the promotion of their economic interests. Thus those who come together have a common economic aim which they cannot achieve by individual isolated action because of the weakness of the economic position of a large majority of them. The element of weakness of individual is overcome by the pooling of their resources by making self help effective through mutual aid and by strengthening the bonds of moral solidarity between them.

2.3 Co-operative Vs Non Co-operative Enterprises.

In order to know the true character of Co-operative, a comparison is made between Co-operative and non co-operative enterprises. There are three main categories of enterprises namely private enterprises, public enterprises and co-operative enterprises. The private enterprise is based on the philosophy of capitalism, the public enterprise is based on the philosophy of socialism and co-operative enterprise is based on philosophy of co-operation. Following are the similarities and differences between these three systems.

2.3.1 Capitalism Vs Co-operation:

Capitalism is a system of economic organization in which industrial and business organizations are organized and carried out for profit motive by private enterprises with minimum government intervention. The main features of capitalism are -

i) Primary motive is personal gain and individualism

ii) The means of production are owned by private sector.

iii) Private property and Laws of inheritance are in operation.

iv) It is the free market mechanism which regulates prices and business activities.

v) There is freedom of contract and free enterprise.

vi) Class conflict between labour and capital exists

vii) Absence of state intervention.

According to some thinkers, co-operation is only a specialized part of the private enterprise and private capitalism. They believe that there is no inconsistency between co-operation and capitalism; hence both these systems can co-exist. According to Jerry Voorhis “A Co-operative is a better kind of private business”.

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2.3.2 **Similarities between Co-operation and capitalism.**

i) Like capitalism co-operatives also accept the right of private property, the right of contract, inheritance and the right of private enterprise.

ii) The Co-operatives also use capital to carry on the activities and pay interest on its use.

iii) Co-operatives also depend upon business efficiency for their success just like capitalist enterprises.

iv) Co-operatives also lay emphasis on profits.

v) Co-operatives like capitalists tend to oppose the government intervention in business activities.

2.3.3 **Difference between Co-operation and Capitalism.**

1) Co-operative movement has its roots in the injustices and economic ills created by capitalist system so co-operation is itself a protest against capitalism. According to Laidlaw co-operative capitalism is a contradiction. The Co-operative movement has a unique, hopeful and thrilling message to tell the world and all mankind. Its message may be much garbled and much misunderstood if it is tied to the philosophy of economic capitalism\(^\text{10}\).

Co-operation differs from its rival capitalism in that, it promotes peace and not strife, unselfishness and not self-seeking capitalism attempts to crush down poor people. Co-operation gives them enough strength to fight out for their existence. Capitalists believe in the theory of “Survival of Fittest” and hence promote competition which develops a spirit of rivalry and results into clashes of interests in the society. As against this, Co-operatives work on the principle of self help through mutual help and adopt peaceful means in a spirit of service to its members. Capitalism is based on exploitation and exists for profit and the capitalists do not hesitate to destroy a portion of their produce if they fear a reduction in price. The structure of capitalism is built up with money while that of co-operation with men under capitalistic organization money rules men, but in co-operative organization human beings meet on the basis of equality. Capitalism lacks in morality so it is regarded as anarchic and inhuman in nature. A capitalist economy based on competition and monetary system is unstable in nature and undemocratic in nature because of domination of by a few members. On the contrary co-operative economy is stable because it does not allow accumulation of unconsumed stocks and is democratic as it is based on one man one vote.
2.4 Socialism Vs Co-operation

Socialism especially state, socialism is a socio economic system in which material means of production are owned and controlled by public authority or the community and operates not for profit but for the service of the society/community. Under socialism the state owns, operates and distributes all the productive resources of a community. The main features of a socialist economy are -

i. All the means of production and distribution are owned and controlled by the state.

ii. It aims at attaining and maintaining full employment.

iii. Central planning is the main instrument for achieving proper production and just distribution.

iv. All the social services such as education, medical and other welfare services are given top priority and become the responsibility of the state.

v. Each individual gets fixed wages on the basis of his needs and profits of industry go to the state

The socialist movement and co-operative movement are conceived as revolt against the rise of capitalist system. Some of the principles of co-operation and socialism are the same. Both the systems emphasize human and social welfare and at abolishing profit economy. Both the systems emphasize social service and avoid satisfaction of individual greed. “The fundamental theory of both rests on an economic theory of collective action as opposed to the individualism of capitalist system.

Although there are various similarities between socialism and co-operation both the systems are not identical and there are differences in their objectives, aims and methods. Socialists aim at complete reduction of capitalist class and elimination of private property. Marx argued that the society could only be reformed by the destruction of private property.

In co-operative society private property and capital occupy important position as individuals are encouraged to own some property for themselves. Thus co-operation is not against capital and private property. It only aims at evil doing power of capital. If socialism is a proposed political remedy for economic ills, co-operation is a non political remedy for economic maladjustment. Under socialism there is no freedom and voluntarism as it believes in the methods of closed shops, compulsory
bargaining and compulsory arbitration. But co-operative system believes in freedom and voluntarism. Under socialism the state is the supreme authority and the rights of the state get priority over trace of individual. Hence it is said that, in a socialist state individuals exist for the state and not the state for the individuals but in co-operative system the individuals are assigned higher status. Co-operation insists on self help through mutual help and not any outside aid, even including state aid. Even if it accepts state aid, co-operation does not accept interference of state in its internal management. However co-operation in developing countries like India has been still in the process of development to be fulfledged independent entity as it has to depend on state aid and to create state interference.

Co-operation and socialism differ in their methods used to attain their objectives. Under socialism the use of force, strikes, violence, etc are common methods used for achieving goals, while these methods are not favored in the co-operative economy. The co-operative economy insists on using methods of education and propaganda for achieving its goals. Under socialism, control is exercised by state officials and bosses of political party whereas in cooperatives it is done by the members on democratic lines. Under socialism politics is given top position but under co-operation, political neutrality is the highly valued objective.

2.5 Co-operation – The middle way.

Socialism and capitalism have their own advantages and disadvantages, as the extreme systems. The system of free enterprise under capitalism leads to exploitation, oppression and concentration of wealth in few hands. Under socialism there is loss of individual freedom curtailment of initiative. Under such conditions co-operation can be said to be middle way between the two systems. But it cannot be said that co-operation is most useful and the best system which can replace capitalism and socialism. There are some sectors of the economy where public enterprises are most effective, while there is other sector where private enterprises are useful. However much depends upon the character of the people. For example, the same public enterprises which had worked profitably in some countries still in other countries they have worked on losses. In India many public undertakings are running in losses due to inexperienced officials who are unable to manage them efficiently. In case of small scale industries private ownership has been observed to be successful. So it is common in most of the countries in the world.
As co-operative form of organizations possesses certain advantages which neither capitalism nor socialism can possess. Co-operative organization offers a means of achieving results valuable to the community by drawing upon incentives which are social and also individual.

According to Huxley the political road to a better society is the road of decentralization and responsible self government.\textsuperscript{12} “Capitalism tends to produce a single centralized totalitarian dictatorship widening absolute authority over all its subjects through a hierarchy of bureaucratic agents.”\textsuperscript{13} The co-operative movement is method of approach which would bring about a kind of social pattern in which it would be possible to have synthesis between individual freedom and state control.

Thus in an ideal society, there is a need to have all the three types of systems to work side by side, suited to different sectors of the economy. As Bernard Russell has pointed out, “A healthy society requires both central control and individual and growth initiative without control there is anarchy and without initiative there is stagnation.”\textsuperscript{14}

According to the Indian planning commission “In a regime of planned development, co-operation is an instrument which while retaining some of the advantages of decentralization and local initiative can yet serve willingly and readily the overall purpose and directive of the plan. The cooperative form of organization can no longer be treated as only a species within the private sector. It is an indispensable instrument of planned economic development in a democracy.”\textsuperscript{15}

\textbf{2.6 Principles of Co-operation.}

Principles of co-operation are the guidelines and ground rules for co-operative enterprise. They are code of conduct for co-operative organizations, the practice of which may change according to local conditions. These principles are as follows.

\textbf{1) Voluntary Association or open Membership.}

Membership of a Co-operative Society should be voluntary and available without artificial restriction or any social, political, racial or religious discrimination, to all persons who can make use of its services and are willing to accept the responsibilities of membership.\textsuperscript{5}
2) Democratic Control.

Co-operative Societies are democratic organizations. Their affairs should be administered by persons elected or appointed in a manner agreed by the members and accountable to them. The members should enjoy equal rights of voting (one member one vote) and participation in decisions affecting their societies.

3) Limited Interest on capital.

As co-operatives are user’s organizations for mutual service, any capital owned or employed by them only a means of production. Share capital used in the business of a co-operative would be entitled to its appropriate rate of interest.

4) Distribution of Surplus –

Surplus or saving, if any, arising out of the operations of a society belong to the members of that society and should be distributed, in such a manner as would avoid one member gaining at the expense of others.

5) Co-operative Education.

All co-operative societies should make provision for the education of their members, officers and employees and of the general public, in the principles and technologies of co-operation, both economic and democratic.

6) Mutuality or co-operation among co-operatives –

All co-operative organizations, in order to best serve the interests of their members and their communities should actively co-operate in every practical way with other co-operatives at local, national and international levels.

7) Self- Help through mutual co-operation –

A co-operative association is generally an organization of financially weak individuals. At the individual level their resources are so weaker that they cannot derive any benefit and improve their conditions. Hence, in order to convert their weakness into strength, they pool their resources and they work together for mutual benefits.  

8) Principle of Thrift –

A co-operative organization should inculcate the habit of savings among members. Thrift is considered to be the first step in self help. Thrift implies not only
frugality and savings, but also economical management by avoiding wasteful expenditure.

9) Principle of Service –

A co-operative enterprise is motivated by the spirit of service. Its main objective is to provide services most economically; co-operative is one way in which public-spirited citizens can devote their time and energy to the service of their fellows.

10) Principle of Publicity –

Principle of publicity implies doing everything in public. All business is transacted with the maximum of publicity within the society. Publicity protects public against suppression of material facts.

11) Honest Dealings –

The co-operatives should always sell pure and unadulterated commodities giving true weight and measure and be willing to accept complete responsibility. The members should be honest in their dealings with the co-operatives. The amount borrowed from the society is promptly paid.

12) Principle of Social Ownership.

A co-operative represents joint social ownership. Every member can become co-owner of the co-operative and take full advantage of its services.

Thus because of its inherent qualities e.g. equity, equality, democratic administration, social ownership and high moral values (spirit of service and honesty) it has been regarded as a panacea of many problem of the industrial age where capitalism and authoritarian tend to create a number of social and economic problems, for which co-operation is an ideal remedy.

2.7 Origin and Growth of Co-operative Banks

Cooperative Banks are a part of vast superstructure of cooperative institution. These institutions are engaged in multiple activities such as production, processing, marketing, distribution selling and banking in India, the origin of cooperative banking
can be traced back to 1904. When government initiated to create a new type of institution based on the principle of cooperative organization and management, which were considered to be suitable for solving the problems related to the availability of credit in rural areas of India. In rural areas, for agricultural and rural activities, the supply of credit especially institution credit was not available as required, hence unorganized money market agencies, such as local money lenders were providing credit by way of charging exploitative interest rates. Under such conditions cooperative banks were received as substitute for such agencies, who can provide adequate short term and long term institutional credit at reasonable rate of interest, and also to integrate the unorganized and organized segments of Indian money market.

After independence, on the every economic planning in India, cooperative banks were made an integral part of the institutional framework of community development are National Extension Services, and these institutions were assigned the important role of delivering the fruits of economic planning at the grassroots levels. As a result, they become a part of the arrangements for decentralized plan formulation and implementation for the purpose of rural development in general and agricultural development in particular.

At present cooperative banks are important parts of a set of institutions which are engaged in financing rural and agricultural development. This set up of institutions include the RBI, NABARD, commercial banks, regional rural banks and cooperative banks. It is interesting to note that relative importance of cooperative banks in financing agricultural and rural development has been characterized by certain changes over the years. Till 1969 they increasingly substituted the informal second lenders. But after nationalization of banks and the creation of regional rural bank and NABARD, their relative share started declining. All the institutional sources together contributed about 4 percent of the total rural credit till 1954 and this share increased to about 62 percent by the end of 1990. The share of cooperative banks in this institutional lending has steadily declined from 80 percent in 1964 to about 42 percent in 2001. The percentage of rural population covered by the agricultural credit societies was 7.8 percent in 1951, which increased to 36 percent in 1961 and 65 percentage in 2001.
Features of cooperative Banks

Some distinguishing features of the cooperative banks are stated below:

1) The cooperative banks are organized and managed on the basis of principles of cooperation, self help, and mutual help. They function with the rule of “one member, one vote”

2) They function on the basis of “No profit, No loss”. Even for commercial banks, now profitability is no longer the main objective because this change was the result of social or public policy, while cooperative banks, by nature, do not focus the goal of profit maximization.

3) Co-operative banks perform all the main functions of banking especially deposit mobilization, supply of credit and providing remittance facilities. However it has been observed that the range of services offered by cooperative banks has been narrower and the degree of product differentiation in each main type of service is also much limited as compared to the commercial banks, thus the cooperative banks were characterized by functional specialization. But now many changes are taking place in the system of cooperative banks, for example, co-operative banks one now ready to provide nursing loans. The state cooperative Banks, central cooperative Banks and urban cooperative Banks are extending nursing loans up to Rs. One Lakh to an individual. The scheduled UCBs can lend up to Rs. 3 lakh for nursing purposes. The UCBs also provide advances against shares and debentures.

4) Although cooperative banks do banking business mainly in the agricultural and rural sectors, still certain types of banks such as UCBs, SCBs, CCBs, operative in urban, semi-urban and metropolitan areas also. Hence the urban and non- agricultural business of these banks has grown in recent years. Thus the co-operative banks demonstrate a shift from urban to rural areas.

5) Co-operative banks can be said to be the first government sponsored, government supported and government subsidized financial agency in India. These banks get financial and other type of help from the RBI, NABARD Central Government and State Governments. They constitute the “most favored” banking sectors without any risk by nationalization. For commercial banks the RBI is the lender of the first resort which provides financial resources in the form of contribution to the initial capital. Through State Governments, working capital and refinance. The promotional role of the RBI
is dominant in respect of co-operative banks which supersedes the regulatory role in case of cooperative bank. As co-operative banks get a lot of help from the government, it results into increasing interference of the government in the working of the co-operative banks, the co-operative banks are subject primarily to the control, audit, supervision and predict inspection to the Co-operative Department of the State Government under the Cooperative Societies Act, but relatively less rigorously by the RBI under the Banking Regulation Act. The RBI and the State government lay down rules for investment of surplus resources, reserves and the loan policy of co-operative banks consequently, compared to commercial banks, cooperative banks have less freedom and flexibility in conducting their operations.

6) Co-operative banks belong to the money market as well as the capital market. Primary agricultural credit societies provide short term and medium term loans. Land Development Banks (LDBs) provide long term loans, and UCBs meet working capital and fixed capital needs of customers. SCBs and CCBs also provide short term loans. They accept short term and long term deposits and some of them mobilize resources through the issue of debentures.

7) Co-operative banks are financial intermediaries but only partially. The main sources of their funds are:

a) Central and Stat government (b) the RBI and NABARD (c) other cooperative institution, (d) ownership funds e) deposits or debenture issues, in case of cooperative banking intra-sectored flows are much greater than in case of commercial banks. Intra bank deposits, borrowings and credit form a significant part of assets and liabilities of cooperative banks. Thus intra sectored competition is absent and intra-sector integration is very high in case of cooperative banks. In practice, cooperative banks have to face stiff competition from commercial banks and other financial intermediaries. This competition has increased after nationalization. Before nationalization certain areas of operations were reserved for cooperative banks but now the competitions from LIC, UTI and small savings organizations has become very keen, hence the cooperative banks are in a disadvantageous position in the area of intersectoral competition.
8) Cooperative banks have a federal structure of three tier linkages. Their operation is also of mixed banking type Primary credit Societies are unit banks. Similarly many LICBs are also unit banks, but SCBs, DCBs, (CCBs) and SLDBs, PLDBs and many LICBs have several branches. Thus, it can be said that each cooperative institution, in each tier is a separate entity with definite jurisdiction and has an independent board of management.

9) Some cooperative banks are scheduled banks. The SCBs and some UCBs are scheduled banks. At present 28 SCBs and 11 UCBs with Demand and Time Liabilities over Rs 50 crs each are included in the Second Schedule of the RBI Act.

10) Cooperative banks accept current, saving and fixed on time deposits from individuals and institutions including banks. Some UCBs are allowed to open and maintain NRI accounts in rupees but not on foreign currency Deposit is mobilized by them in a given area are used for financial activities in that locality.

Some cooperative banks like Land Development Banks issue debentures to raise resources for performance their operation. These are secured debentures by mortgaging lands belonging to borrowers from LDBs and one often guaranteed by the state governments. They once regarded as trustee securities and are treated on plan with government securities for making advances. These debentures are of three types, namely ordinary, rural and special. These debentures are entirely subscribed by institutional investors like LIC and the government.

11) The cooperative banks are subject to CRR and liquidity requirements like other banks. However they are required to maintain the CRR and SLR only at the level of three present and 25 percent respectively. The UCBs are advised to lend 60 percent of their total advances to the priority sectors. Thus the target of priority sector lending has been fixed at a higher level for UCB than for commercial banks. Since January 1989 UCBs have to get approval for granting advances to a single party exceeding certain credit limits which varies from bank depending on their size.
12) Since 1966, the lending and deposit rates of commercial banks have been directly regulated by the RBI. Although the RBI had powers to regulate the rates of cooperative banks also, these powers were not exercised much till 1979, in respect of their lending rate, because SCBs and CCBs were expected to provide finance for agricultural and allied activities to the ultimate borrowers at reasonable rates i.e. at concessional rates as they were entitled to concessional refinance from the RBI. In case of their non agricultural advances for the propose of production and marketing activities of cottage and small scale industries, the RBI imposed certain conditions about rates to be charged by these banks for such propose. Regarding their non-agricultural advances, they were free to change any rates at their discretion. As the RBI did not regulate at all the lending rates of UCBs, there was little uniformity in the rates charged by different UCBs. The SCBs were also exempted from the levy of interest tax.

In 1979 the RBI decide to maintain parity among the rates of interest on all agricultural advances irrespective of credit agency. Hence the rate of interest changed to the ultimate borrowers by co-operative banks was also brought in line with those charged by the commercial banks. The RBI advised all the SCBs in 1980 to change ceiling rates on agricultural advance. While ceiling rates were presented for short term agricultural advances, the lending rates for medium term agricultural credit were kept as fixed rates. Similarly lending rates of co-operative banks including UCBs for non agricultural advance also become subject to the directives issued by the RBI with effect from 1981. As a result of the measures adopted by the RBI 1980 and 1981, some uniformity was brought about in respect of the lending rates charged by the co-operative banks in different states and between commercial banks and co-operatives banks. Since 1974 the deposit rates of co-operative banks have been regulated by the RBI. Initially the RBI policy was to specify that the rates prescribed for commercial banks should be considered as the minimum to be offered by the cooperative banks, but the directives of commercial banks for which fixed rates have been stimulated for different types of deposits. These current accounts were excluded from the preview of the directive, while commercial banks were prohibited from paying interest on current accounts. This led to relatively higher rates being paid by co-operative banks on their
deposits, which adversely affected the deposit mobilization of commercial banks. Hence the RBI changed the policy in 1974 and began to direct co-operative banks not to pay interest at rates in excess of certain percentages over the minimum rates percentages over the minimum rates prescribed by the RBI for commercial banks. The ceilings laid down over the minimum rate were 0.25, 0.5, and 1.0 percent with regard to SCBs, CCBs, and Primary Agricultural Credit Societies (PACSs) respectively, on term and saving deposits. They have been prohibited since 1975 from paying interest at a rate exceed 0.5 percent per annum an current accounts, deposits up to 14 days and those subject to withdraw or repayment after a notice of 14 days or less. The latter facility has been withdrawn from March 1989 in respect of UCBs. Structure of co-operative banks is quite complex. The rates charged by them depend on the type of bank, the type of loans and vary from state to state.

13) Although the main aim of the co-operative banks is to provide cheaper credit to their members and not to maximize profits, they may access the money market to improve. Their income for their survival and growth. Their need to access money market arises on account of various reasons. Firstly CCBs are mainly in the field of financing seasonal agricultural operations, which create cycles of flows of funds of funds. Secondly, the short term agricultural loans are given at concessional rates of interest where as interest rates paid on deposits by cooperative banks are higher than those paid by the commercial banks, as they get concessional refinance form the NABARD, but its availability depends upon fulfilling conditions such as minimum involvement, non overdue cover etc. There is a need for co-operative banks to access money market to deploy their short term funds profitably and cross subsidies their lending operations.

**Conclusion**

Co-operative Banks in India have played key role in development of short term and long term rural credit structure over the years. The co-operative credit system covers more than 74 percent of rural credit outlets and has a market share of about 46 percent of total rural credit in the country. The co-operative banks have
contributed significantly towards widening institutional agricultural credit because their retail outlets are so widespread and far flung that no other type of agency can reach all corners of the country as cooperative banks have done. On account of too much intervention by the state in day to day management has resulted in the lack of involvement and ownership of people in their functionality. There is an urgent need that the co-operative banks have to become member driven banks. There is also a need of removing dual control over co-operative banks by the RBI and the state government. They need big support in respect of infrastructure, resource base, professional management etc.
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