CHAPTER VII

NEED OF LONG TERM COOPERATIVE CREDIT

Early History: The past history of long term cooperative credit in this state is well known. It was this state (i.e. undivided Punjab) which had the honour of leading the country in the establishment of Cooperative Land Mortgage Banks. But it is unfortunate that these banks are no longer to be found in Punjab (I) the land of their birth particularly when we see that such banks have been successfully working in States, as Madras, Bombay, and Madhya Pradesh.

The first Cooperative Land Mortgage Bank was started in Jhang (now in West Punjab) in the year 1920 with a view to providing relief to the agriculturists, whose lands were mortgaged with the money-lenders for a small sum, bearing a high rate of interest. This bank sought to advance loans to them against the mortgage of their land at a reasonable rate of interest. The progress in this form of cooperation was slow in the beginning because of the difficulty of financing such banks. So there was only one such bank up to the end of the year 1923 with the total advances of Rs.1 lakh. From the year 1924, due to the changed policy of Government to advance loans liberally to such banks and the consent of the Punjab Cooperative Union to utilise surplus funds of liquidated societies in these banks, their number rose to 3 in 1924 and to 12 in 1929. The advances made also increased rapidly from Rs.1 lakh in 1923 to Rs.2 lakhs in 1924 and Rs.20 lakhs in 1929. The progress and working of these banks from the year 1920 to 1946 can be seen from the following table:-

1. Later on in the year 1926 the Provincial Cooperative Bank Lahore also floated debentures to the value of Rs.5 lakhs having a term of 20 years @ 6% interest.
<table>
<thead>
<tr>
<th>Year</th>
<th>No.</th>
<th>Membership Societies</th>
<th>Individ. Share Capital</th>
<th>Reserves</th>
<th>Deposits</th>
<th>Loans Capital Issued</th>
<th>Working Loans</th>
<th>Loans Received by the end of the year</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
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<td></td>
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<tr>
<td>1920-21</td>
<td>1</td>
<td>-</td>
<td>-</td>
<td>E.</td>
<td>E.</td>
<td>-</td>
<td>E.</td>
<td>E.</td>
</tr>
<tr>
<td>1924-25</td>
<td>4</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>-</td>
<td>E.A.</td>
<td>42</td>
</tr>
<tr>
<td>1928-29</td>
<td>12</td>
<td>196</td>
<td>5,452</td>
<td>1,09</td>
<td>45</td>
<td>6</td>
<td>21,251</td>
<td>42</td>
</tr>
<tr>
<td>1932-33</td>
<td>12</td>
<td>197</td>
<td>5,165</td>
<td>1,16</td>
<td>99</td>
<td>4</td>
<td>18,399</td>
<td>63</td>
</tr>
<tr>
<td>1936-37</td>
<td>12</td>
<td>195</td>
<td>4,920</td>
<td>1,12</td>
<td>1,02</td>
<td>6</td>
<td>14,899</td>
<td>63</td>
</tr>
<tr>
<td>1940-41</td>
<td>10</td>
<td>182</td>
<td>3,761</td>
<td>90</td>
<td>84</td>
<td>13</td>
<td>10,26</td>
<td>63</td>
</tr>
<tr>
<td>1944-45</td>
<td>9</td>
<td>177</td>
<td>3,247</td>
<td>70</td>
<td>67</td>
<td>10</td>
<td>2,05</td>
<td>63</td>
</tr>
<tr>
<td>1945-46</td>
<td>9</td>
<td>176</td>
<td>3,212</td>
<td>68</td>
<td>67</td>
<td>9</td>
<td>1,56</td>
<td>63</td>
</tr>
</tbody>
</table>

It will be observed that after the year 1929 no new bank was organised and even in the existing banks the future advancement of loans was severely curtailed. The total advances made in 1929 were Rs. 6.31 lakhs, while they were suddenly reduced to Rs. 1.5 lakhs in 1931 and Rs. 0.06 lakhs in 1933. Since then only one or two banks have been advancing further loans while all the rest have been mainly working as collecting agencies for the huge advances made during the earlier period. The chief reason for this was that these banks were organised during the boom period when the prices of agricultural commodities were high. Loans were recklessly advanced and less attention was paid for their recoveries. Though the recoveries from the members were poor from the very beginning but their fall after the year 1930 was spectacular. While the total recoveries during the year 1930 were Rs. 2.72 lakhs, they fell to Rs. 1.77 lakhs in 1931 showing a decrease of Rs. 1 lakh. These continued at this low level till 1942, when there was some improvement. The price rose during the Second World War raising the capacity of the borrowers to pay. This helped the banks in realizing their large amount of old loans. Thus the total amount outstanding which was Rs. 11.5 lakhs in 1938 reached the low figures of Rs. 1.5 lakhs in 1947 when the partition of the country took place. A bank was brought under liquidation as early as in 1927, while three more banks came under compulsory liquidation after 1937, as it was
found that the directors were not assisting these banks in the realisation of their loans. They themselves were defaulters as in case of the other credit societies. It was therefore thought necessary to bring them under compulsory liquidation in the interest of their creditors. Thus at the time of partition there were on the whole 4 banks under liquidation and nine on the register, through these nine were also in the process of voluntary liquidation. None of the nine banks on register was in the area now constituting East Punjab (I). But out of four banks under compulsory liquidation, 3 were in the East Punjab (one at Gurgaon, one at Nariangarh and the third at Sonipat). The total amount due from debtors in these banks on 30th June, 1952 was Rs.17 thousands (Principal Rs.8 thousand and Interest Rs.9 thousand to the date of their cancellation). Out of this, Rs.9,610 was due from Muslim members, about the realisation of which no decision has been arrived at between the two state Governments so far. So it will be observed that after the partition there was no mortgage bank working in the East Punjab thus totally closing the chapter of land mortgage banks in this State, and we will have how to start with a clean slate.

The causes which led to the failure of these banks may be summed up as follows:-

1. Bank started during the boom period: It has been stated above that one of chief causes which led to their failure was the fact of their organisation during the post war boom, when the prices of agricultural commodities were high. This had naturally increased the value of land leaving an ample margin between the value of land provided as security and the loans granted. But with the onset of depression the banks entered upon a difficult period when the income from the land mortgaged was not enough to cover even the interest charges.

2. Hunger of Agriculturists for the Purchase of Land: During the boom period/mood of optimism the borrowers mortgaged their future too heavily. The rising value of the land made the zamindars' hunger for land
all the more intense and this tendency towards the purchase of land forced the prices of land to shoot up. By 1926 the Department realised that the land already stood at an uneconomic price. They therefore decided to refuse loans for the purchase of land. But the borrowers, on rejection of their applications for loans for the purchase of land, resorted to mortgaging their existing landed property in order to buy land and then to apply for its redemption.

3. **No maximum borrowing limit fixed**: The loans were originally limited to fifteen times the net income of land or 30 times the land revenue, but no maximum credit limit was fixed. However, if the loan did not exceed thirty times the incumbrant's income no detailed assessment was generally made of the borrowers' income. It was only in the year 1930 that a maximum limit of Rs. 4,000/- was fixed for the borrower, but even this too was high.

4. **Loans sanctioned without proper scrutiny and directors' dishonesty**. There was no representation of depositors on the directorate and summary enquiry by one of the indebted directors was considered quite sufficient before the sanction of the loan. But directors had nothing to lose by the adoption of a liberal policy. They were rather interested in their friends and relations and never cared to scrutinise the loan applications. Sometimes large sums were borrowed by the directors themselves which were misused by them.

**Frauds**: The objects for which loans were taken, were not correctly given in the applications. Loans for the purchase of land were secured under other pretences. Sometimes borrowers failed to produce the receipts of their creditors within a reasonable time. This raised suspicion that the money was not properly utilised, while in some cases the receipts produced were of some other creditors than those given in the application. The Registrar in his Annual Report for 1928 observed¹ "Not only that I feel that the Mortgage Banks have been grossly misused by the borrowers,

¹ Annual Report 1928, p. 36.
but they have borrowed from the banks for all sorts of purposes, and on all sorts of pretences."

6. **Land Alienation Act**: One of the serious handicaps was the legal prohibition contained in the Land Alienation Act, which made it impossible for a bank to acquire and sell a defaulter's land. Where the land was taken over for a term of years and leased, people having sympathy with the defaulting members refused to bid or did not bid high realising the position of the bank. On this point Mr. McDougall, one of the experts who came out to India in connection with banking enquiry in 1930-31 wrote as follows:

"In the Punjab the Land Alienation Act makes it impossible to recognize land mortgages as a sound gilt edge investment. Mortgage Banks can only recoup themselves against loss by letting the land to a tenant. This is not sufficient safeguard. It is not for a bank to act as a landlord on a large scale. The cost involved is too great. I do not think it feasible to establish a system of Land Mortgage Banking on ordinary lines in the Punjab without grave risk or severe restrictions unless the Land Alienation Act is amended."

7. **Loans taken for purchase of land**: Loans were generally taken for rather than for its improvement the purchase of land rather than for the improvement or redemption of land, which were difficult to repay when the prices of land fell. The agriculturists being illiterate did not understand the significance of these loans, their idea chiefly being to borrow as much as they could.

**After the Depression**: The general subject of development of land mortgage banking was taken up afresh in 1935. A committee consisting of the Registrar, Financial Adviser to the Cooperative Department and seven non-officials was appointed by the State Government to consider the

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1. Under the Land Alienation Act, the bank could not acquire the land, but possession of the land could be taken temporarily for a maximum period of 20 years.
possibility of any system of long term credit which would afford adequate benefits to the borrowers as compared with the system then existing. According to the recommendations of the committee the immediate necessity was to concentrate on proposals for improving and reorganising the existing system and extending the same instead of starting an entirely new system.

A year later the subject was again thoroughly discussed by Sir Darling (when he was Financial Commissioner Development) Registrar Cooperative Societies, and Financial Adviser to the Cooperative Department and the result of these discussions were embodied in a detailed note dated 28th March, 1936, the salient features of which are:

1. Mortgage Banks will not be able to help the majority of our cultivators, most of whom are one-ploughman and whose margin of income over expenditure is generally too narrow.

2. At first these banks will have to confine themselves to comparatively secure tracts till they pass out of the experimental stage.

3. They require most careful control which means that Land Mortgage Banking cannot be carried out in India without heavy overhead charges, a considerable part of which must, in the early stages, be borne by the Government.

4. Besides the above difficulties in Punjab a further and more serious limitation is imposed by the Land Alienation Act, which makes it impossible for the bank to acquire and sell land of a defaulter if he is an agriculturist.

5. The purpose for taking these loans from the banks is mostly the liquidation of old debts and not the improvement of land, while the loans for the purchase of land are generally undesirable. In Madras loans for liquidation of debts are only given if the total outstanding debt of a borrower can be liquidated; a wise precaution for it is a spur to the borrower to give up all dealings with the money lender and the bank has

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not to enter into competition with him when the recoveries are to be made. It follows that in most cases loans have to be substantial and owing to the very limited repaying capacity of the borrower in this country they have to be spread over a long period which varies generally from 12 to 20 years. If therefore the maximum period for a loan is ordinarily 15 years, business can hardly be extensive. It will not be easy to finance such loans cheaply and for a period during which the value of land may also change.

Concluding their observations, the committee, however, remarked "At the same time we consider that the time has come to test the possibilities of cooperative land mortgage banking in the province by making a systematic attempt on the lines indicated below. The movement is opportune for a fresh experiment and there is no doubt that the economic structure of an agricultural country requires a proper system of land mortgage banking if the country is to develop on modern lines. At present the Land Alienation Act is a serious obstacle and it is alone responsible for the fact that the Madras has now completely outstripped the Punjab in this branch of cooperation." The suggestions made by the Committee for starting new banks are briefly enumerated below:

(1) Maximum amount of loan should be a multiple of 5 to 20 times the land revenue.

(2) No loan should be made for more than 15 years and for 20 years only if the borrowers' sureties mortgage their lands to the same extent as the borrower.

(3) At least for the first three years the cost of the staff should be borne by the Government as is being done in Madras. Otherwise it will be difficult for the bank to lend at a low rate of interest.

(4) Official control over the banks should be tightened on the lines followed in Madras and Bombay.

(5) Government should supplement the funds raised within the movement from the Provincial Loan Act, until it becomes possible to issue debentures.
(6) A certain proportion of directors which should not be less than one third, be elected by the share-holders who do not borrow.

Need for Land Mortgage Banks: Although the recommendations made by Sir Darling and his colleagues were far reaching and valuable and were endorsed by Mr. Wace in his report, yet no action was taken by the Provincial Government in the matter. Since then, especially after the partition of the state, many important changes have taken place which have further intensified the need for such banks viz.,

1. The deficit of food in the country has made the development of agriculture very important.

2. The rising prices of agricultural commodities during the war and afterwards have given an incentive to the agriculturists to produce more. There has come a great change in the outlook of the agriculturist in certain tracts where they have begun to use modern implements and other equipments on an extensive scale for the improvement of land and for more production, which is the most important object of agricultural long-term finance. At present however they are at a great disadvantage to get loans for the purchase of these implements and other equipments at a reasonable rate of interest.

3. The apprehension that most of the loans are taken for the liquidation of old debts does not seem to be valid now. Most of the old debts have already been liquidated under the Agricultural Debt Legislation of 1934 and subsequent operation of Debt Conciliation Boards. These have been further reduced because of high prices of agricultural commodities which raised the capacity of the borrower to repay. While in the case of those agriculturists who have not been able to repay their loans in spite of high prices, their loans will have to be compulsorily brought down to their repaying capacity if these agriculturists are to be

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1. Mr. Wace in his report endorsed these recommendations and further recommended that (1) Land Alienation Act should be amended (2) powers should be given to the Registrar for the sale of the produce of land mortgaged, in case of default (3) The land mortgaged with the mortgage banks should be exempted from the ordinary procedure of insolvency.
rehabilitated in the real sense. These loans after having been scaled down will have to be taken over by the land mortgage banks and payments made to the money lenders in lump sum.

4. The consolidation of holdings is now proceeding on a very large scale throughout the state under the supervision of a separate department. The scatteredness of holdings which were a serious handicap in digging up wells on small patches of land is thus being removed. Electricity is being provided in the villages which will make the setting up of tube-wells cheaper. During my tour in the villages people expressed their great desire for long term credit on cheap rates for the purpose of setting-up tubewells or for buying agricultural machinery for the improvement of land.

5. It has already stated that the loans to cooperative farming and house building societies have been advanced by the central financing institutions for long periods against their short term deposits, which is not free of great dangers from the banking point of view. It is only the proper function of the land mortgage banks to finance such societies.

6. The land reforms are being introduced under which certain tenants will get security of tenures, while others will have the right to purchase their holdings. Under these conditions they would like to have permanent improvements in their lands for which long term credit will be essential.

7. Lastly, the Land Alienation Act which was a serious handicap in the development of the land mortgage banking has been repealed in 1948. So there is an urgent need for setting up land mortgage banks in the immediate future if the agricultural production is to be raised to a higher level. The need of starting such banks on the lines of Madras State has also been expressed repeatedly by the Registrar in his recent annual reports. In the annual report for 1950, he stated 1 "New ventures in the form of cooperative farming and multipurpose societies requiring

long term finance are much in evidence and their number is increasing... whatever the circumstances, one thing must be clearly realised by those who are anxious to see that cooperative movement play its proper role in the economic regeneration of the State, that unless satisfactory arrangements are made for long term finance, nothing substantial can be achieved in the future." In his next report he again stated "Now that the Land Alienation Act has been repealed it should be considered whether the floating of debentures once again would not be justified, if the cooperative farming and other measures suggested in the First Five Year plan are to be put into effect." For the setting up of these banks on efficient basis a few suggestions may be put forward:

1. In the beginning, the business of land mortgage banks should be confined to the secure tracts, where there is a scope for the use of agricultural machinery, especially tubewells.

2. Loans should only be given for the improvement of land, and for its redemption only when the cultivator owns less than 10 acres and the land was mortgaged before the starting of these banks. Otherwise there is every likelihood that the loans may be misused. The rate of interest charged on the advances made for the improvement of land should be lesser than for other purposes as is done in the Madras State.

3. There should be strict official control as suggested by Sir Darling, and the borrowers should be severely punished for giving wrong statements in the loan applications. The system prevalent in Madras and Bombay that a certain percentage of directors must be non-borrowers is also commendable.

4. The Government should guarantee debentures in respect of both principal and interest and should contribute to the cost of the staff for the first three years as recommended by Gadgil Committee (1940) and Cooperative Planning Committee (1955).

5. The primary land mortgage banks should not be opened in all the districts, but the work should be entrusted to the District Central Cooperative Banks, which should work as the agents of the Provincial Land Mortgage Bank for distributing long term finance. In this connection the Bombay Agricultural Credit Organisation Committee, 1947, observed: "Many of the primary land mortgage banks in Bombay are starving for want of business and are unable to pay dividend to their share-holders. They also do not possess the same means for keeping closer contact with the cooperative societies and rural cultivators, which the central banks with their inspectorial staff and branches, possess. Besides, this, some loans which were really long term loans were often advanced under the guise of short term loans by the credit societies and the central banks. It should, therefore, be desirable in cases where the primary land mortgage banks are working at a loss, to transfer their work to the central financing agency operating in that area. . . . . It follows, as a corollary of our recommendation that future registration of new land mortgage banks should not be encouraged in the areas where there are no land mortgage banks and this work should be taken up by the District Central Bank." It will also save expenses to a great extent and good reserves can be made easily within a short period.

6. The loans required for the agricultural machinery will be of short duration, say 5 to 10 years, and it would be advisable to raise the bulk of it by means of long term deposits within the movement at not more than 4% rate of interest. This method has been tried by some of the central banks in the State and have proved successful.

7. Under the new reorganisation scheme of rural administrative machinery as contemplated in Chapter XIV there will be no need to appoint separate field staff for evaluation of land etc. and the Cooperative Inspector incharge of that area will be in a position to make local enquiries in this connection.

8. At present the displaced persons have been allotted land on quasi-permanent basis, and they are not in a position to sell or mortgage their lands. So it would be essential to make them allotments on permanent basis for the successful working of the banks.

9. There will be no harm if the work of the Provincial Land Mortgage Bank is taken up by the Provincial Cooperative Bank in the initial stages, to avoid unnecessary overhead charges. When the business sufficiently develops the work may be transferred to a separate Central Land Mortgage Bank.

Conclusion: To sum up we may say that the cooperative land mortgage banks were started in the undivided Punjab, just after the First World War. They stopped further advancement of loans in 1929 and since then they have been working as mere collecting agencies. The main reasons of their failure were, viz., their establishment during the boom period, reckless advancement of loans, advancement of loans for the purchase of land rather than for its improvement and the existence of Land Alienation Act. After the Depression the question of development of land mortgage banks was examined by a Committee in 1935 and a year later by another Committee headed by Sir Darling. The last Committee stated that though mortgage banks will not be able to help the majority of cultivators who were mostly one-ploughman, while Land Alienation Act was a great hindrance, yet they recommended that a fresh experiment in the development of mortgage banking was essential if the country was to develop on modern lines. However no action was taken on these recommendations by the State Government. On the other hand, since then, the need for the establishment of such banks has become all the more important due to changed conditions, such as the deficit of food in the country, incentive of high prices to the agriculturist to bring permanent improvements in their lands, land reforms, consolidation of holding at a greater speed,

1. The Gadgil Committee recommended that the supply of short term and long term credit should be taken up by one agency, i.e. the State Agricultural Credit Corporation.
cheap supply of electricity and lastly the repeal of Land Alienation Act, which was a serious hinderance in the past. So there is an immediate need for setting up new land mortgage banks. However some precautions in their organisation are necessary. The banks should first be started in the secured tracts, loan should as far as possible be given only for the improvement of land, and strict supervision on their actual application should be maintained.