CHAPTER 1

REVIEW OF LITERATURE
AND METHODOLOGY
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REVIEW OF LITERATURE

1.1 Introduction

There is ample literature in the form of books, reports and research papers on agricultural credit at National and International levels. An attempt is made in this chapter to present brief reviews of very important books, reports and papers to bring into limelight the existing literature and the gaps in it and the need for further studies.

1.2 International Perspective

1.2.1 RURAL FINANCIAL MARKETS IN DEVELOPING COUNTRIES; THEIR USE AND ABUSE, BY VON PISCHKE, J. D. et al.,

This book highlights the facets of Rural Financial Markets (RFMs) that have often been neglected in discussions of agricultural credit in developing counties. It moves beyond a narrow concern with the simple provision of credit to a broad consideration of the performance of Rural Financial Markets and of ways to improve the quality and range of financial services for low income farmers. It reflects new thinking on the design, administration, evaluation and policy framework of rural finance and the credit programmes in developing countries.
Many authors in this book, assert that farmers in developing countries are rational in their use of financial markets. This conclusion has important implications for the way RFM interventions are designed. It strongly suggests that supply-led strategies for rural development ought to be de-emphasized. Rather than merely increasing the supply of loanable funds, attention should be directed towards improving the range and quality of rural financial services. Co-operatives have been instruments of government policy rather than business minded organisations serving their members. A common type of co-operative is the single purpose farm credit society, which is often a losing business proposition. Credit unions and multipurpose co-operatives have done much better.

The studies relating to Government policies toward Rural Finance emphasize the noticeably negative effects of such policies in terms of greater inefficiency in resource allocation, penalization of financial savings, credit rationing favouring a few large farmers, and the consequent unequal distribution of income, the encouragement of loan defaults, an impaired viability, financial intermediaries, incentives for capital-intensive production which is not so efficient in developing countries. Excessive governmental regulation has often transformed RFMs into an instrument for introducing political 'patronage' into the allocation of credit.

On the whole it seems to disprove the traditional assumption that the growth in the volume of credit extended at concessionary interest rates is a pre-requisite for the development of agricultural
production and, therefore, for the improvement of the standard of living in rural areas, and emphasizes the need to adopt an integrated approach in both the analysis of RFMs and in the consequent working out of appropriate measures to develop them.

The authors repeatedly underline the importance of exploiting the savings potential of rural areas and emphasize the need for a greater autonomy for and greater competition among financial intermediaries. Government's intervention, on the other hand, should ensure the conditions for a correct and free functioning of RFMs.

The specific measures required to improve the quality of RFMs in different economies will vary. But it appears that most efforts should contribute towards the integration of these markets emphasize voluntary savings mobilisation by formal institutions, and allow interest rates to be determined flexibly by market forces.¹

1.2.2 NATURE OF CREDIT MARKETS IN DEVELOPING COUNTRIES BY - ARVIND VIRMANI

Arvind Virmani in his paper on "The Nature of Credit Markets in Developing Countries", analyses various forms of government intervention in the loan market in terms of their effect on efficiency. This provides the essential basis for evaluating and judging these policies. It also shows where earlier policy prescriptions are correct, incomplete or wrong. One of the implications of the paper is that the credit market differs fundamentally from the market for ordinary goods and services.
Consequently a conventional analysis of the loan markets, based on the theory applicable to product markets, can be misleading even when similar prescriptions are reached. Another important highlight of the paper is the vital role of collateral in the loan market. These two issues are addressed in the introductory discussion on the special nature of credit markets, which forms an important pre-requisite for understanding the subsequent sections of the paper. The paper focuses its attention exclusively on one of the underlying reasons for government intervention, namely, market failure in the credit market. It examines the causes and consequences of market imperfections or failures in the rural credit structure and the effects of different types of intervention and their implications for different policies for correcting market imperfections on the loan side of the market. It assumes the deposit side of the market as given.

The paper provides a unified framework for analysing credit markets and allows apparently desperate observations and facts in the banking and institutional literature to be understood and interpreted. More importantly, it provides a unique framework for determining the effect of government policy on credit market efficiency.

A distinction between empirical testing and practical application needs to be borne in mind in reading the paper. The former was not attempted, given the data limitations and time constraints under which the paper was written. It is presented
more as a practical guide to others wishing to apply the same frame work in the context of similar limitations.

1.2.3 UNDERMINING RURAL DEVELOPMENT WITH CHEAP CREDIT BY DALE W. ADAMS et al.

In his work the author outlines that in the past several decades large amounts of money have gone into agricultural credit programmes in low-income countries. The results of these efforts have often been disappointing: persistence of serious loan recovery problems; the rich getting most of the cheap loans; low interest rates discouraging local savings and deposits; and common political intrusions. Hence many financial institutions in low-income countries are floundering. The contributors to this book cite ubiquitous low-interest rate policies and improper use of financial markets as principal reasons for these problems, recommending that higher and more flexible interest rate policies be allowed and that little or no attention be given to targeting loans. They also argue that informal lenders are providing more valuable services than is generally thought and that voluntary savings capacities in rural areas may be substantial. Less emphasis on discouraging the informal lender, more emphasis on voluntary savings mobilization and more access to formal loans by non-farm rural firms are other policy changes recommended in this comprehensive survey. The authors opine that two factors contribute to the failure of Rural Credit Programmes: wrong assumptions about the characteristics of Rural Financial Markets (RFMs) and the consequent rural development strategies adopted by policy makers and development
technicians. With regard to the first point, the authors stress the complete ignorance about the nature of financial processes, the characteristics of financial markets and financial products, the behaviour of the operators that act in the market. To illustrate, credit is viewed as a productive input and policy makers think that it is possible to promote specific agricultural activities by delivering predetermined amounts of loans to farmers. Instead credit is a part of the financial intermediation process. It is a general claim on resources highly fungible and it is costly and its use is difficult to target effectively. The authors demonstrate how the currently accepted assumptions are faulty and how the consequent rural development policies produce undesirable and unanticipated effects. A repressed financial market, it is argued, negatively affects and its contribution of finance to rural development is seriously damaged and limited. Rural credit programmes are often used by policy makers as a tool to grant patronage and to increase one's own political power. The negative effects of projects on income distribution are deliberate. In these cases, the responsibility of industrialised countries and donor institutions become evident. They should refuse any financial support to these credit programmes that repress RFMs and should try to persuade low income countries authorities to adopt the policy changes suggested by the most recent and correct theories about rural credit and finance. 3

1.2.4 EVALUATION OF FINANCIAL POLICY: CREDIT ALLOCATION IN BANGLADESH BY ARVIND VIRMANI:

Arvind Virmani in his working paper analyses the various
credit policies and programmes of Bangladesh. The Bangladesh Government, like the governments of many developing countries, has used a variety of policies to influence the allocation of credit to specific borrower groups like poor farmers, to uses such as housing and to sectors such as agriculture. The policies have also been employed to reduce allocation for certain uses such as inventory holding ('speculative purposes'). The policies employed were interest controls, credit guarantees, refinancing and margin requirements. This paper attempts a systematic analysis of all the policies used by the Bangladesh Government in the light of the explicit or implicit objectives of the Government. The effect of each of these policies used, either alone or in combination, is analysed with a view to evaluating their usefulness and efficiency. The analysis then provides the basis for suggested policy changes in Bangladesh, as well as lessons for financial policy makers in other countries. This paper applies the analytical framework developed earlier by the author in "The Nature of Credit Markets in Developing Countries: A framework for policy analysis."  

1.2.5 WORLD DEVELOPMENT REPORT, 1986 BY WORLD BANK

The World Development Report dealing with the trade and pricing policies in World Agriculture in the context of developing countries, reviews the special programmes for providing credit to farmers generally at low interest rates. Subsidized Credit Programmes usually have harmful side effects on financial institutions, rural financial markets and the wider economy; Cheap loans are therefore unsuccessful in redistributing income among the
rural poor. The value of the subsidy is proportional to the size of the loan and therefore, small farmers tend to receive small loans and thereby small amount of subsidy. Studies in this arena revealed that the typical pattern is for large amounts of low-interest agricultural credit to be concentrated in the hands of a relatively few borrowers who are better off and politically influential. Many rural credit programmes use interest rate subsidies to encourage farmers to use particular inputs or to grow specific crops. But subsidised credit is widely diverted to other uses. Close supervision can limit the diversion, but it is costly and difficult because farmers can reallocate other funds. Credit diversion indicates that farmers own judgments on the best investments do not coincide with the priorities set in credit programmes.\(^5\)

1.2.6 AGRICULTURAL CREDIT IN ECONOMICALLY UNDER-DEVELOPED COUNTRIES BY H. BELSHAW

In almost all developing economies non-institutional agencies of credit play a predominant role and this is a manifestation of the semi-feudal character of their agriculture. Agricultural credit under these conditions has been static in the vast majority of developing countries. The main problem is to convert static into dynamic credit and thus involves a consideration of the requisites of a sound agricultural credit system.

A sound agricultural credit system:

The requisites of a sound system of agricultural credit are:

1. It should generate and mobilise rural savings by devising
appropriate mechanisms;

2. It should ensure a net inflow of funds into agricultural sector;

3. It should deploy credit with utmost efficiency and equity; and

4. It should reduce risks as far as practicable to the borrower, credit institution and lender.

It is well documented in the literature that the non-institutional agencies of agricultural credit such as merchants and moneylenders possess certain advantages for the borrower to the extent that his loans are often unsecured, there is an absence of red tape, funds are readily available under flexible conditions and the transactions are often private. One of the desiderata cited above is fulfilled by non-institutional agencies. The other desiderata, namely, mobilisation of agricultural savings, transfer of capital from the non-agricultural into the agricultural sector and the efficient development of credit are not fulfilled. These agencies charge sky-high rates of interest and divert savings from the agricultural to the non-agricultural sector. They hardly pay any attention to the mobilisation of savings. Thus, on balance the disadvantages inherent in this system more than outweigh the advantages, so that private credit does not conform to the tests of a good agricultural credit system.

1.2.7 AGRICULTURAL CREDIT IN ASIA BY F.A.O.

According to the survey of Rural Indebtedness conducted by the Central Bank in 1969, non-institutional sources provided 84.2
per cent of the total credit requirement in the case of Sri Lanka. Friends, relatives, shop-keepers and moneylenders provide 65 per cent of the total agricultural credit and the remaining was met by institutional agencies in Vietnam during the year 1973.7

1.2.8 THE ASSAULT ON WORLD POVERTY BY THE WORLD BANK

Agricultural development presupposes technological transformation. Credit is often a key element in the modernisation of agriculture. Not only can credit remove a financial constraint, but it may accelerate the adoption of new technologies. Credit facilities are also an integral part of the process of commercialisation of the rural economy. However, no amount of credit, even at the most reasonable rates can guarantee higher productivity or incomes among the rural poor. Success in this respect depends on many factors, including the availability of complementary inputs and services, sound credit policies, well-managed institutions and appropriate delivery channels.

In nine of the thirty nine countries studied by the World Bank, loans from institutions are less than $5 per rural person, while in five countries the amount is in excess of $100 per capita. On a continental basis, in most countries of Africa and Asia, Institutional lending is less than $20 per rural inhabitant, while in a number of Latin American Countries the amounts are in excess of 50 per capita (Appendix I). The percentage of loans made by institutions in Latin America is high, while in Africa and Asia non-institutional lending predominates (Appendix-II)
The percentage of farmers receiving institutional credit varies widely in different parts of the developing world. In certain African countries, around one per cent of the total number of farmers used institutional credit, while in Thailand nearly all farmers have access to it. About 5 per cent of farmers in Africa obtain institutional credit, while the proportion in Latin America and Asia (excluding Thailand) is about 15 per cent (Appendix-III). In the case of small farmers the coverage by institutions is even more limited. Large farmers have been the main beneficiaries of institutional credit. It is common to find 70 to 80 per cent of small farmers in a given country with virtually no access to such credit. In Pakistan, almost 60 per cent of the farmers received 3 per cent of the institutional credit. In Bangladesh, the large farmers received more than 80 per cent of the loans from the Agricultural Development Bank and the Co-operative Banking system. In the Phillipines, 27 per cent of the larger farmers working 61 per cent of the land received 98 per cent of the institutional credit. In Tunisia, 90 per cent of the farmers could not qualify for institutional credit. In Brazil, 3 per cent of the farmers received 34 per cent of the loans. Studies of Thailand, Bolivia, Chile, Colombia, Ethiopia and Honduras indicated that the larger farmers were the main beneficiaries of institutional credit.8

1.3 National Perspective

1.3.1 THE ALL INDIA RURAL CREDIT SURVEY, 1951 BY R.B.I.

The study of the committee was the most comprehensive and
scientific undertaking conducted in the field of rural credit through survey method. Field investigation was conducted in 75 districts covering 1,27,343 families in 600 villages spread all over the country. Seven different types of schedules were used for collecting the data from institutions and cultivators.

The findings of the committee confirmed the dominant position occupied by the non-institutional agencies like moneylenders and traders in the rural credit market. They supplied more than 70 per cent of the total credit requirements and the co-operatives supplied only to the extent of 3.1 per cent. The study also revealed that of the total institutional credit the larger part went to the big farmers while only a minor fraction percolated to the small farmers.

It is observed that agricultural credit fell short of the right type, did not serve the right purpose and often failed to go to the right people. It further observed that although the performance of the co-operatives in the sphere of agricultural credit was deficient in several ways, the co-operative agency still remained, by far the least unsatisfactory channel of credit. Its approach to co-operatives was "Co-operation has failed, but co-operation must succeed."

The basis of the future policy laid down by the Survey Committee was the positive and deliberate creation of conditions in which co-operative credit would have a reasonable chance of success. For this purpose, it made several recommendations collectively
known as the Integrated Scheme of Rural Credit. The main features of the scheme were:

1. State partnership through contribution to the share capital of co-operative credit institutions;

2. Full co-ordination between credit and other economic activities, especially marketing and processing; and

3. Administration through adequately trained and efficient personnel responsive to the needs of the rural population.

Production-oriented loan policy, known as the crop loan system was to form the basis for short-term co-operative credit.9

1.3.2 UTILISATION OF CO-OPERATIVE LOANS, 1965 BY GOVERNMENT OF INDIA

The study was conducted by the programme evaluation organisation of the Planning Commission. A sample of 25 central banks in 15 States was taken up for this study. Again from each of the selected banks, a sample of 5 PACs and from each of the selected society a maximum of 12 member borrowers were selected. The study noted the physical growth of the co-operative credit societies, but at the same time found that the growth of overdues also was alarming, particularly in Assam, Bihar, H.P. (Himachala Pradesh), Rajasthan and U.P. The supervisory staff was overburdened with the procedural and administrative work and, therefore, they had no time to supervise the utilisation of the loans.10
1.3.3 ALL INDIA RURAL CREDIT REVIEW COMMITTEE, 1969 BY R.B.I.

In 1966, the RBI set up the All India Rural Credit Review Committee in order to re-assess the developments that had taken place in the field of rural credit since 1954. The committee submitted its report in July 1969. The Committee emphasised that while re-organisation of co-operative credit should be pursued and the integrated scheme implemented vigorously, efforts should not be concentrated solely in the co-operative sector and that considering the magnitude of the problem of agricultural credit, the Commercial Banks, especially the nationalised banks, should embark on wide and intensive efforts for provision of agricultural credit. The adoption of a number of progressive measures by both the co-operative and the commercial banks was suggested for ensuring the timely and adequate flow of credit. The review Committee also recommended the establishment of two new organisations, viz., the Rural Electrification Corporation for financing rural electrification schemes through the State Electricity Board and the rural electric Co-operatives and the Small Farmers Development Agency (SFDA) designed to identify the problems of small but potentially viable farmers and to ensure that agricultural inputs, services and credit were made available to them. The Committee recommended the enlargement of the Reserve Bank's role in regard to the Co-operative movement. While it endorsed the policy till then pursued by the Bank in the provision of rural credit through the co-operative agency, it suggested liberalisation in some respects and
also among others, the introduction of certain measures to correct
the tendency on the part of the co-operative banks to borrow
more from the Reserve Bank, by linking the rate of refinance with
the co-operative bank's own effort to mobilise deposits.\textsuperscript{11}

1.3.4 REPORT OF THE COMMITTEE ON INTEGRATION OF
CO-OPERATIVE CREDIT INSTITUTIONS, 1976, BY
A.R.D.C.

R. Hazari Committee after discussions with Chief Ministers
and Ministers for co-operation, officials and non-officials in 13
states and by conducting studies on integration of the two wings,
short and long term co-operative credit recommended the
integration of the two wings of the co-operative credit structure
at all levels, i.e., the primary, the intermediate (district), and the
apex (State). However, one of the members of the Committee
Mr.B. Viswanathan, in his capacity as Chairman of the National
Co-operative Land Development Banks Federation in his minutes of
dissent found that the disadvantages for outweighed the advantage
of integration and pleaded that the long term credit structure
should not be disturbed. It may be noted herewith interest that the
Madhava’s Committee also recommended integration of co-operative
credit institutions in the north eastern States.\textsuperscript{12}

1.3.5 RURAL MONEY MARKET IN INDIA, 1976 BY SUBRATA
GHATAK

He made a pioneering study of the Indian Rural Money
Market. His study was directed to answer the following issues:
a) To study the nature, composition and working of the organised and unorganised money markets in the Indian Rural Economy;

b) To examine the factors affecting the demand side of agricultural credit.

c) To discuss the working of the major organised agencies; and

d) To specify the existing links between the rural money markets and to derive and policy implications which may emerge from the study.

He examined the foregoing issues on the basis of the available secondary data using quantitative techniques and statistical tools. He considered the working of PACS on the supply side of institutional credit and came to the conclusion that they generally failed to satisfy the different criteria of financial viability so far as the composition of the financial structure and loan operations were concerned. Increasingly greater dependence on borrowing, failure to mobilise deposits appreciably as well as mounting overdues became their chief problems. The hypotheses about positive correlation between income and repayments and negative correlation between the rate of interest and income and repayments were empirically justified.¹³

1.3.6 REPORT OF THE NATIONAL COMMISSION ON AGRICULTURE BY GOVERNMENT OF INDIA, 1976

Efforts should be made to develop a total system of credit support to all activities facilitating modernisation of agriculture and
rural development. The system should facilitate suitable linkages between finance and services for current inputs and capital investment in land development, major irrigation and farm equipment. The institutional and public resources used for capital investment in, and working capital of, actually or potentially viable agricultural activities must generate, over a period, adequate income for repayment of loans. Where necessary, organisational support should be provided to generate financial viability. 14

1.3.7 REPORT OF THE WORKING GROUP ON MULTI-AGENCY APPROACH IN AGRICULTURAL FINANCE, 1978 BY R.B.I.

The present system of agricultural credit in India consists of two sectors, viz., the institutional and the non-institutional. The non-institutional sector consists mainly of professional and agricultural moneylenders, traders, commission agents, relatives and friends. The institutional sector comprises Co-operatives, Commercial Banks, Regional Rural Banks and the Central and State Government Agencies. Inspite of the significant expansion of the institutional sector, non-institutional agencies still continue to play a dominant role in the provision of credit for production and consumption purposes. Their lending procedures being simple, money lenders are known for quick service but they charge high rates of interest and follow unethical practices. These make the moneylenders' credit costly. However, the share of the non-institutional sector in the total borrowings of farmers has recorded a decline from more than 95 per cent in 1952 to 85 per cent in 1961-62, 75 per cent in 1971-72 and to about 65 per cent in 1978. 15
1.3.8 REPORT OF THE COMMITTEE TO REVIEW ARRANGEMENTS FOR INSTITUTIONAL CREDIT FOR AGRICULTURE AND RURAL DEVELOPMENT (GRAFICARD), 1981 BY R.B.I.

As smooth flow of funds at reasonable rates of interest is a crucial input for development, it was considered necessary on the eve of launching the Sixth Five Year Plan to review the existing institutional arrangements and to bring about necessary improvements. The R.B.I., therefore, appointed a Committee under the Chairmanship of B. Sivaraman in March 1979. The terms of reference of the committee were:

1. To review the structure and operations of the Agricultural Refinance and Development Corporation;

2. To examine the need for and the feasibility of integrating short and medium-term credit structures with long term credit structure;

3. To consider the relative merits of three-tier and two-tier structures for co-operative financing institutions; and

4. To review the role of R.B.I. in the field of rural credit, having due regard to its central banking functions, etc.,

Field of Enquiry

The committee visited 14 states for the field level discussions and issued checklist of points for discussions at the block, district and State levels. This was followed by separate questionnaires, one on the national level institutions and the second
one on the field level credit delivery system i.e., Scheduled Commercial Banks, State Co-operative Banks, State Co-operative Land Development Banks.

Findings

1. After a careful review of the views expressed by the earlier committees, the committee felt that there was a need for a new organization and recommended the establishment of NABARD.

2. The Committee preferred to have more than one organisation for different purposes and arrangement for co-ordination of those organisations instead of integration of different credit structures.

3. The committee opined that a two-tier structure may be conducted in smaller states and union territories, whereas the three-tier structure could remain as the general pattern for bigger states.

4. The role of the R.M.I. in the provision of rural credit has to be assessed not merely in quantitative terms but also with reference to its qualitative aspects such as strengthening of the institutional framework, improvement of lending policies, resource mobilisation, designing of special schemes and regulatory functions to promote co-operative banking on sound lines. Given the enormity of the task and the constraints, the progress made by the rural credit system so
far, is in no small measure, due to the active part played by the Reserve Bank. This has been possible because of the position the Bank occupies as the ultimate source of finance and as the monetary authority of the country and all along the R.B.I. management has taken the view that a central bank of a developing country has to act as a development bank. This is the reason why the R.B.I. sponsored the ARDC and has taken various promotional measures under the Multi-agency approach. 16

1.3.9 REPAYMENT OF INSTITUTIONAL CREDIT, 1989, BY NABARD

NABARD launched field studies in nine States to gain perception into the problems of delinquency in loan repayment from the demand side. The demand side studies covering two states* with good recoveries and seven states** with poor recoveries, were undertaken with varying number of defaulters/non-defaulters and the following findings were arrived at:

The level of overdues was higher for investment credit (term loans) than for crop loans (short-term credit). A considerable proportion (30 percent - 45 per cent) of the default in respect of investment credit extended by PLDBs was over five years old, whereas in the case of short-term crop loans borrowed from PACS it was typically less than 2 years old. One wonders, therefore, whether the greater and prolonged default in respect of investment credit is associated with the less frequent need for its borrowing,
Large farmers defaulted more than the small farmers. Members who made partial payment and those who defaulted on the entire amount, constituted 25 per cent and 35 per cent respectively of the total borrowers. The supply side studies conducted in five states examined the impact of faulty lending and recovery procedures followed by Land Development Banks.

1.3.10 REPORT OF THE COMMITTEE TO REVIEW WORKING OF THE MONETARY SYSTEM, 1985 by R.B.I.

The committee to review the Working of the Monetary System with Sukhamoy Chakravartty as Chairman was asked to review critically the structure and operation of the monetary system in the context of the basic objectives of planned development, and to evaluate the various instruments of monetary and credit policy in terms of their impact on the credit system and on the economy. In this context links among the banking sector, the non-banking financial institutions and unorganised sector could be assessed.

The committee envisaged a strong supportive role for interest rate policy in monetary regulation based on monetary targeting. It also pointed out an important role for interest rate policy in regard to promoting the effective use of credit and in short-term monetary management. The committee emphasized that the credit budgeting, to achieve the desired sectoral credit

* Punjab and Kerala
** Bihar, Gujarat, Karnataka, Madhya Pradesh, Maharashtra, Tamilnadu and West Bengal.
*** Bihar, Gujarat, Karnataka, Madhya Pradesh, and West Bengal.
allocations in line with plan priorities, should continue. It recommended that no more than two concessional interest rates should apply to Bank Credit made available to specified priority sector borrowers, one of which should be equivalent to the basic (minimum) lending rate and the other somewhat lower than the basic lending rate. The committee also emphasized that interest rates on bank credit prescribed for target groups under the priority sector should reflect societal concerns which need to be respected and accordingly these aspects should be taken into account while rationalising the array of concessional interest rates. It also suggested that the Regional Rural Banks (RRBs) that are extensively involved in lending to the priority sector at concessional interest rates should receive special assistance from the State Governments and the Central Government. The Committee noted with concern the high level of overdues in the priority sector lending programme. It suggested that a detailed review of overdues by area and by activity should be undertaken to facilitate remedial action by the concerned development agencies and banks.

It is of the view that in the Indian context non-banking intermediaries have traditionally been meeting some of the credit needs of the informal sector and their operations are governed by long standing conventions and practices. These aspects should be taken into account in any assessment of their role as an adjunct to the formal banking system. A system of licensing should be introduced to protect the interest of depositors, of non-banking financial intermediaries and a suitable cut-off point may be laid
down in regard to their level of business beyond which they will be under a legal obligation to obtain a licence.

While determining the interest rate structure, the need for bringing into the fold of organised financial system the left out rural sections and the unorganised sector should not be kept out of sight. Firstly, the level of interest rate on bank deposits and small savings schemes should not be kept unduly low. Even in a period of near-zero inflation rate it would not be practical to assume that rural savers would be happy with nominal rates of interest on their deposits. The 'Money illusion' is of considerable practical importance to the rural as well as some parts of the unorganised sectors of the economy, and for these sectors the levels of interest rates would not be conducive enough for bringing them into the organised financial system.

The Chakravarthy Committee's report is undoubtedly a landmark in the literature on the subject. There is a danger however, that, because of its rather uncritical market orientation, it may prove a disastrous landslide. 18

1.3.11 REPORT OF THE AGRICULTURAL CREDIT REVIEW COMMITTEE, 1989, BY R.B.I.

Brief extracts from the summary of this report are presented here. (The paragraph numbers in brackets refer to the paragraph numbers in the original report).

The emerging agricultural technologies and the secular shifts
in the agricultural sub-sectors in favour of commercially orientated agriculture are expected to create in the coming decades, a robust agricultural economy in India. It is to these changes and the associated problems that the rural credit system will have to effectively respond and gear itself (Paras 1.03 to 1.06).

Earlier reviews on rural credit in India had emphasised institutionalisation of rural credit to wean away the poor peasantry from the money lenders. There is no need for a major structural reorganisation as the basic foundations of the credit systems have been found sound and well suited to Indian conditions. The only two structural changes visualised are the merger of the Regional Rural Banks (RRBs) with their subsidiary banks (SBs) and the creation of a national apex Co-operative Bank of India. A comprehensive crop insurance scheme and and a separate corporation to administer this as well as Agricultural and Rural Development Corporations in certain States with a view to correcting the regional imbalances have also been recommended. These are meant to reinforce the existing two systems of credit delivery. (Paras 1.42 to 1.45, 1.61 to 1.68 of the R.B.L., Review Committee Report).

The rural credit problem in the Indian context could be summed up on "Credit well delivered will be well accepted - Credit can be well delivered only by well conceived institutions."

It can be said that Indian agriculture will experience a longer growth by the turn of the century. It can also be expected
to be a scene of a relative sub-sectoral shift. This will need agricultural development programmes in different States being strongly supported by financial institutions to make agricultural and rural economies more viable, productive, progressive and profitable (Para 2.117).

Interest Rates, Costs and Margins

An administered interest rate structure came to be evolved in India in view of the distortions in the money and capital markets so as to ensure flow of adequate credit to the preferred sectors and the target groups at certain concessional rates of interest while working towards maximising the returns to the savers on their deposits. The Sukhamoy Chakravarty Committee which had examined the interest rate structure obtaining in the financial systems in the country had brought out the deficiencies of the administered interest rates. They are summarised as follows:

1. It failed to promote the effective use of credit and the concessional rates of interest appeared to have allowed projects of doubtful viability to be undertaken; and

2. It has resulted in poor customer service and low profitability of the banking systems (Para 18.01).'

However, in the present stage of development of the Interest Money and Capital Market, determination of interest rates cannot be entirely left to market forces and a fair degree of regulation of interest rates is necessary so as to provide for an
orderly mobilisation of financial savings for the purposes of planned economic development and in the interest of the viability of operations of banks of widely varying sizes in terms of deposits and advances and differing greatly with regard to the quality of their human resources (Para 18.02).

METHODOLOGY

1.4 Introduction

Agricultural development is important because it provides economic sustenance and builds up a strong base. Capital formation and the level of economic activity depend upon the agricultural production. Thus the development of agriculture is an 'accelerator' of the overall economic progress of the country. Gunnar Myrdal said, "It is in the agricultural sector that the battle for long term economic development in South Asia will be won or lost." So, it is an imperative need to stabilise and strengthen the agricultural sector.

The main occupation of the rural masses is agriculture. As is well known three-fourths of the cultivated area depends on monsoon rains. This means agriculture is seasonal and employment in agriculture is mostly seasonal too. Further the agricultural sector is the major sector of the rural economy in which unemployment and underemployment prevail. Poverty is essentially a rural problem linked with the backwardness of agriculture which
implies low productivity of land, low purchasing power of farmers and low capacity to employ more workers gainfully. Improving the social as well as the economic life of agriculturists depends very much upon the several inputs, but the one input that can help the farmer to apply the other inputs is the capital, namely, "Credit".

1.4.1 FARM CREDIT REFORM AND GROWTH IN FORMAL CREDIT

The role and contribution of capital in the farm sector is rapidly increasing. Indian farmers with their meagre financial resources are not in a position to meet the increasing demand for capital input in the farm sector. Especially after the introduction of new-farm technology the credit requirement of farmers is increasing. This is recognised by the Indian Government and has emphasized the need for increased flow of institutional credit to agricultural and rural development. The policy of the State today is to provide institutional credit to the entire farm sector. Necessary steps are taken to change the farm credit structure. Multi-Agency approach was accepted as an appropriate strategy. At present co-operatives, commercial banks, regional rural banks, apart from many rural development agencies sponsored by State and Central Governments are actively financing the farm sector. But still non-institutional agencies are dominating the rural credit scene in some areas. The share of institutions in the total farm credit is about 60 per cent in the country. The performance of institutions is not uniform in all the regions. There are inter-regional variations and the role of rural credit institutions is favourable for
the development of developed regions. There is a felt need to correct the regional imbalances in the flow of institutional credit to agriculture. The study of the farm credit structure in different agro climatic regions is essential to take steps in this direction. The present study is a modest attempt relating to the Agricultural Credit in Nellore District of Andhra Pradesh.

1.4.2 NEED FOR THE PRESENT STUDY

The credit needs of the farmers in Nellore district for agriculture can be examined in two different angles, namely, on the basis of time such as short term, medium term and long term and on the basis of purpose such as productive, unproductive and consumption needs. Taking into consideration the various trends and developments in the sphere of agricultural credit in Nellore district, the need for conducting an indepth study over the supply of credit by the credit agencies to different farm-size groups and demand for credit by different farm size for the progress and development of agricultural credit in Nellore district, this research study has been undertaken.

The sources of agricultural credit in the district are divided into two, namely, Institutional Credit by Co-operatives, Commercial Banks and Regional Rural Banks and Non-institutional Credit by landlords, agricultural moneylenders, professional moneylenders, traders, relatives/friends and others.
1.4.3 OBJECTIVES

The main objectives of the study are as follows:

1. To describe the nature and character of agricultural credit structure in two sample villages -- Somarajupalli in the delta area and Budamagunta in the non-delta area;

2. To examine the relative role of institutional and non-institutional credit agencies in the farm sector;

3. To study intra and inter village variations in the agricultural credit delivery systems by formal and informal agencies; and

4. To measure the cost of the credit agency-wise.

1.4.4 HYPOTHESES

The following hypotheses are specified:

1. Credit taking pattern between delta and non-delta villages is the same.

2. Credit taking pattern between farmers is the same.

3. Credit distribution pattern between institutional and non-institutional agencies is the same.

4. Intra village credit variations are not significant among various credit agencies.

5. Inter village credit variations are not significant.
6. Credit pattern in delta and non-delta regions is independent among the marginal farmers.

7. Credit pattern in delta and non-delta regions is independent among the small farmers.

8. Credit pattern in delta and non-delta regions is independent among the medium farmers.

9. Credit pattern in delta and non-delta regions is independent among the large farmers.

10. Category of farmers and type of credit are independent in non-delta village (Budamagunta).

11. Category of farmer and type of credit are independent in delta village (Somarajupalli).

12. Incidental charges are equal for both institutional credit and non-institutional credit.

13. Incidental charges borne by the various farmer groups are the same; and

14. Incidental charges borne by the delta and non-delta farmers are one and the same.

1.4.5 SAMPLE DESIGN

The agricultural economy of Nellore district like that of the country is characterised by regional disparity. The delta segment of the district is supposed to be highly prosperous and advanced. The
non-delta segment is backward, though there are a few prosperous villages. Therefore, with a view to presenting a realistic picture of the agricultural sector, a village from the delta -- Somarajupalli and another village from the non-delta -- Budamagunta, have been purposively chosen on the basis of irrigation. The district itself is purposively selected because of considerations of familiarity and convenience. An intensive travel across the villages of the district was undertaken before the villages were purposively selected. Stratiﬁed random sampling technique was considered to be more efﬁcient and ﬂexible in the selection of ﬁnal statistical units. The sample is to be restricted to ten from each strata of the farmers. The number so arrived through this process is eighty for both the villages. All the farm households in the villages have been classiﬁed into the following categories based on the size of operational holding.

1. Large farmers (10 acres of wet land or above or 20 acres of dry land or above).

2. Medium farmers (5 to 10 acres of wet land or 10 to 20 acres of dry land).

3. Small farmers (2.5 to 5 acres of wet land or 5 to 10 acres of dry land).

4. Marginal farmers (up to 2.5 acres of wet land or up to 5 acres of dry land).
A structured questionnaire was canvassed personally among the sample households.

1.4.6 Data Base

Two types of data have been collected for the present study -- Primary and Secondary.

(a) PRIMARY DATA

To analyse the credit operations of different size groups, size of holding, cropping pattern, cost of cultivation, asset structure, credit structure and cost of credit were collected from the sample farmers for the agricultural year 1988-89, through the questionnaire.

(b) SECONDARY DATA

The secondary data are collected from the published reports of the Centre and State Governments, Zilla Parishad and the Syndicate Bank which is the lead bank in the district. Information has also been collected from the District and Mandal level offices such as District Planning Office, District Rural Development Agency, District Co-operative Central Bank, Office of the Director of Bureau of Economics and Statistics, Hyderabad, Integrated Rural Development Programme, Drought Prone Area Programme Agency and from the reports of Reserve Bank of India.

1.4.7 TOOLS OF ANALYSIS

The data drawn from the various sources were subjected to
statistical treatment. Simple averages, percentages, ratios, correlation, Analysis of Variance and Chi-square test are employed at appropriate places in the study. Maps, Diagrams, Tables and Graphs are presented to illuminate the facts and figures.

1.4.8 LIMITATIONS

The period taken for the study is the Agricultural Year 1988-89. The study covers all the categories of Farm households. This study is a representative study and confined to only Nellore District. The main focus of the study is on agricultural credit. The conclusions drawn are relevant only in such areas and villages.

1.4.9 CHAPTER SCHEME

The study is presented in six chapters. The first chapter deals with the review of literature and methodology. The Agricultural Credit System in India is dealt with in the second chapter. The third chapter covers the farm credit structure in Nellore District. The supply of credit by different agencies to different size groups is presented in the fourth chapter. The demand for credit by farm size is discussed in the fifth chapter. The last chapter is devoted to present a brief summary of major findings and conclusions of the study.

To indicate the scope and nature of literature used in this study, a brief bibliography of books, reports, articles, and journals is given at the end of the study.
REFERENCES


17. NABARD: Seminar on Repayment of Institutional Credit, Vignan Bhavan, New Delhi, Feb.6, 1984.
