CHAPTER II

SOURCES OF AGRICULTURAL FINANCE IN INDIA
The credit requirement of the farmers in India are met by the non-institutional as well as institutional agencies. The former includes agriculturist money-lenders, professional money-lenders, merchants, traders and commercial agencies, land lords, friends, relatives and others. The latter includes Government departments, Commercial banks and cooperative societies.¹

The cultivators depend upon the money-lenders for their requirements of credit. Over the last ten years, the importance of the money-lenders as suppliers of credit to the farmers is declining rapidly. For instance, according to the All India Rural Credit Survey undertaken in 1954, the money-lenders accounted for largely 70% of all rural credit. According to the Reserve Bank Survey for 1961-62 accounted for 49% of rural credit. This fact shows clearly that the money-lender are losing ground for the preponderance of the village money-lenders in rural areas.

There are various mal-practices which are associated with the village money-lenders. They obtain bonds and promisory notes from their debtors in false pretences, and enter in them sums larger than actually lent. They deduct

exorbitant premium. In spite of the legislation in many States the money-lenders have been carrying on their profession almost in the same way as they have done for ages. Attempts to eliminate them or reduce their effectiveness have not fully succeeded. For the farmers were not promised with a comprehensive and adequate finance. The cooperative credit societies and land mortgage banks are becoming significant only in recent years. Secondly the money lenders have intimate knowledge about the farmers and have various holds over them. Thirdly, their methods are simple and elastic and they encourage the simple and ignorant farmers to borrow from them by mortgaging their lands.

According to the All India Rural Credit Survey, 1951-52, the total borrowing of rural cultivators households amounted to ₹750 crores. Of this, the institutional agencies accounted for 7.3% of the borrowing of cultivators. Subsequently, the All India Rural Debt and Investment Survey 1961-62 placed the borrowing of rural cultivator household during July 1961 – June 1962 at ₹1,034 crores, which was about 38% higher than corresponding estimate of All India

1. Ibid., p. 34.
Credit Survey.

In 1961-62, cooperatives have provided 15.5% of the borrowing of cultivator households. In 1967-68, they provided Rs. 358 crores by way of short-term and Rs. 46 crores by way of medium-term loans. It means that the cooperatives met about 30% of the requirements of short-term credit in 1967-68. So far as medium and long-term loans provided by the cooperatives are concerned, they accounted for about 46% and 52% respectively. In the net result, cooperatives provided 33% of the estimated credit requirements of the agricultural sector.

Commercial banks met 5.3% of the total production credit requirements of agriculturists. They met 3.7% of the short-term credit, 13.0% of the medium-term credit and 12.5% of the long-term credit requirements. Thus, 39% of the total credit requirements of agriculture are estimated to have been met by institutional credit agencies. Medium and long-term credit requirements were met to a larger extent than short-term needs.

In the years to come, the credit requirements are bound to be considerably higher than the figures indicated above in the context of High Yielding Varieties Programme.
The All India Rural Credit Review Committee made an exercise in this behalf, taking into account the cash and kind components of credit, and made an estimate of total production credit requirements of agriculturists in 1973-74 at ₹2,000 crores. In addition, they estimated the long-term and medium term credit requirements during the Fourth Five Year Plan (1969-70 - 1973-74) at ₹1,500 crores and ₹500 crores respectively.

Institutional agencies in India have served a great purpose in providing the credit to the farmers. These agencies should overcome the shortcomings of the rural credit system and provide the agricultural credit at low cost. In India, it has been found that private agencies like money-lenders cannot be filled into any scheme of rural credit meant to serve the needs of rural development, therefore, efforts are being made to provide institutional agencies for rural credit.

The Reserve Bank of India is at the apex of the institutional agencies. It was expected that the Reserve Bank of India shall render a great service to the agricultural sector by marketing produce through the agency of the approved money-lenders, by rediscounting at concessional rates for scheduled banks the bills of such
associate drawers for making advances to farmers against the
security of produce on condition that the benefit of the
low rate was passed on to the farmers. While the scheme
was an important landmark in the history of agricultural
finance, it failed due to the fact that farmers borrowed
much for the marketing purposes than for expanding the
agricultural produce.  

Along with these proposals, efforts were made to
extend help to the cooperative societies. The Reserve
Bank issued a circular which laid down the conditions for
obtaining accommodation of the state cooperative banks with
the Reserve Bank of India. The banks were also required to
maintain with the Reserve Bank a minimum cash balance
of not less than 2\% of the demand deposits and one per cent
of their time deposits. They should keep the balance sheets
in proper form, submit audit notes and agree to permit the
officers of the Reserve Bank to inspect their books. The
response to the circular was very poor.  

1. Rao, K.S. 'The Role of the Reserve Bank of India in the
   scheme of Agricultural Credit, Reserve Bank of India

approached the Reserve Bank for the assistance till 1942 except for small amount in the way of advances against government securities. Again in 1942, the Bank issued another circular which offered assistance in the form of discount of advances against bills or notes drawn for marketing of crop at concessional rates of one per cent below the bank rate, on condition that the benefit of the low rate was passed on to the farmers, however, the result was in negative as the cooperative bank did not take much response of the second circular.

Some changes were seen after the report of the Rural Banking Enquiry Committee was published in 1951. The Bank observed in 1952 that "In no other spheres perhaps as in that of rural finance, it is of so little use in Indian conditions to run for guidance to the central banking practices evolved in the highly industrialised countries of western Europe. In this matter, as in the extension of banking facilities generally, fresh approaches had to be thought of ..."\(^1\) In view of this, the bank convened an informal conference on rural finance. The conference recommended the following measures: (a) for enabling the

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Reserve Bank of India to work more effectively within the existing framework; (b) for enlarging the framework; and (c) for eventually designing a new and coordinated framework in the light of fact to be ascertained.¹

Accordingly, numerous important procedural alternations were made in order to make accommodation to the state cooperatives. Under this changed procedure, the stipulation previously made, that all loans and advances should be repaid by September 30 of each year was removed. After this, each loan and advance was to be treated as a separate transaction; and the full term of the loan is allowed for repayments. The next set of proposals made by the informal conference involved either the legislation enlargement of the function of the Bank or the reorganisation and development of the cooperative structure of different states. The conference recommended that the Bank be permitted, (a) to include mixed farming and the processing of crop by agricultural producers for which it can grant short-term finance, (b) for the production and marketing activities of the industrial cooperatives; (c) to extend to cooperative banks to a limited extent, medium term agricultural credit for period between 18 months and 5 years.² Legislative proposals were made to the government

based on these recommendations as well as those of earlier committees and the Bank's powers were substantially enlarged.

Some amendments to sections 17 of the Reserve Bank Act were passed in 1951 and in 1953. The two amendments passed in 1951 liberalised the terms of Reserve Bank advances for agricultural purposes. Regarding purchase, sale or rediscount of bill of exchange and promissory notes, arising out of bonafide commercial transactions in accordance with section 17(2)(a) of the Reserve Bank Act, the amendment placed cooperative banks in the same footing as scheduled banks. The second amendment which was related to section 19(2)(a) of the Act, increased the period of accommodation.

The advances of the Reserve Bank of India to the cooperative banks have shown gradual improvement since these amendments were passed. In 1951-52, the amount of advances was of the order of Rs. 11.29 lakhs and the amount outstanding Rs. 7.81 lakhs. In 1959-60 it increased to Rs. 100.65 lakhs and Rs. 74.54 lakhs respectively. In 1962-63 it rose to Rs. 202.28 lakhs and Rs. 124.30 lakhs.¹ In the subsequent years, it continued to increase for seasonal agricultural operations and marketing of crops (at 2 per cent

below the bank rate) rose from Rs. 337.52 crores in 1968-69 to Rs. 370.16 crores in 1969-70. The amount of loan of the state cooperative banks against these limits moved up from Rs. 411.15 crores at the end of 1968-69 to Rs. 425.09 crores at the end of 1969-70, showing a rise of 3\%. The outstanding borrowings under this category which stood at Rs. 214.11 crores at the end of June 1970 were also increased by 17\%.

The Reserve Bank of India continued to extend financial accommodation to the state cooperative banks for procurement, stocking and distribution of chemical fertilizers at Bank Rate under section 17(4)(c) of the Reserve Bank of India Act, against the guarantee of the state government. The limits sanctioned and draws during the years ending June 1970 and outstandings at the end of the year were Rs. 12.00 crores, Rs. 26.19 crores and Rs. 2735 crores, respectively. The corresponding figures for the year ending June 1969 were Rs. 35.50 crores, Rs. 40.12 crores and Rs. 14.71 crores, respectively.

In the sphere of the medium-term credit, the Reserve Bank of India continued to emphasise the need for rationalising medium term loan policy and procedures so as to ensure that these loans were not utilised as a "ways and means" advance following recommendations of the

Ibid., 1969-60, p. 118.
Standing Advisory Committee on Rural and Cooperative
Medium term loans of the size of Rs. 1,501 to Rs. 3,500 for the
purchase of electric pump-sets, oil engines and for
digging of wells could be issued without insisting on
mortgage of land. The Reserve Bank of India made a further
combination of Rs. 2 crores to the National Agricultural
Credit (Stabilisation Fund during 1969-70 raising the
amount to the credit of the Fund as at the end of June
1970 to Rs. 37 crores.

In the sphere of long-term credits, the Reserve Bank
considerably expanded the scope of its inspections of the
land development banks for keeping a close watch on their
operations which have considerably increased in recent
years. The Reserve Bank made a further contribution of
Rs. 17 crores to the National Agricultural Credit (long-term
operations) Fund in June, 1970, raising the amount to the
credit of the Fund to Rs. 172 crores. During the year loans
were sanctioned to 614 state governments for contribution
to the share capital of cooperative credit institutions which
amounted to Rs. 7.29 crores as against Rs. 4.06 crores sanctioned
to 12 state governments in 1968-69.

The other institutional agencies which provide loans
to the agriculturists are, the State Bank, Commercial
banks, cooperative banks, cooperative societies and land
mortgage banks.
Commercial banks in India have not been much helpful for the farm credit. Their contribution to the total advance to the agriculture reduced from two per cent in 1951 to one per cent in 1961. These banks are normally not in a position to produce large amount of credit to farmers, partly because of the peculiar difficulties of assessing credit-worthiness in agriculture, and especially in small scale agriculture owing to the difficulty of distinguishing between production and consumption loans, partly because of the great difficulties and higher costs of administering farm credit without the fear of substantial losses and largely because most farm credits are needed for periods longer than those common in rural commercial business.

In furtherance of the shift in credit policies of commercial banks towards financing agriculture the banks had begun taking active interest in rural credit since 1968. They had set-up collectively the Agricultural Finance Corporation, stepped up their support to debentures of land mortgage banks, spread agricultural credit cells in their own banks and were evolving loan policies and procedure in the new field of financing.

1. The Agricultural Finance Corporation Ltd., was incorporated in 1968 with an authorised capital of Rs.100 crores and paid up capital of Rs.5 crores. At present, 37 scheduled commercial banks are member of the Corporation. Its two major function are promotion of commercial banks advances for agricultural development and financing of individual institutions and organisations. 
The Agricultural Finance Corporation, during the first 15 months of its operations i.e. upto the end of June 1969 had finalised details regarding financing of 4 schemes with a commitment of Rs.4.20 crores. Out of this amount, Rs.1.50 crores were to be provided by the Corporation and the balance by the member-banks. Total amount disbursed during the period amounted to Rs.0.66 crores by the Corporation and Rs.1.86 crores by the member-banks; the estimated disbursement being made to electricity boards.¹

During the years, the Corporation finalised details regarding financing of 19 schemes its commitment to total outlay being Rs.29.31 crores of which Rs.2.96 crores were to be provided by the Corporation and the balance by the member banks.

Among the promotional activities undertaken by the Corporation, mention may be made of its role in setting up national, state and district level consultation committee for coordination between the cooperative commercial banking sector initiation of Technical Consultancy Service for helping member banks to appraise and finance agricultural projects and organising work shops for formulating various projects and schemes for stepping up agricultural production in scheduled high potential areas in the country.

As regards commercial banks' contribution to the debentures of land mortgage development banks, the National Credit Council had indicated the commercial banks should endeavour to increase it by at least 25% as compared to the position in 1967-68. In fact, the banks stepped up their contribution to such debentures from Rs.18.1 crores in 1967-68 to Rs.22.9 crores in 1968-69 and further to Rs.31.8 crores in 1969-70; their percentage share in the total debentures floated, rising from 25.5% in 1967-68 to 28.0% in 1969-70.

Details of commercial banks' advances for agricultural purposes are given in table I at the end of the chapter. The table shows that the total outstanding advances to agriculture increased merely fourfold from Rs.44.58 crores as on June 30, 1968 to Rs.188.42 crores as on June 30, 1969 and the number of borrowing accounts rose from about 1.04 lakhs in 1967-68 to 2.67 lakhs in 1968-69. Out of this, direct credit to farmers rose from Rs.14.30 crores to Rs.53.61 crores while indirect finance showed an increase of Rs.104.53 crores to Rs.134.81 crores. At the end of June 1970 total outstanding credit to Agriculture stood at Rs.341.77 crores which showed an increase of Rs.153.35 crores over June 1969 level. One significant feature of the year was a spurt in the outstanding advance to the farmers. The number of accounts under this head rose
from about 2.57 lakhs at the end of 1968-69 to 8.18 lakhs at the end of 1969-70 and the percentage of outstanding of direct financing to total outstanding from 28.4 per cent to 53.8 per cent.

In pursuance of the National Credit Councils Study Groups' recommendation that in areas where the central cooperative banks were weak, commercial banks as a transaction measure should finance primary agricultural credit societies directly, the Reserve Bank introduced a scheme early in 1970 in 50 districts of the five states, viz. Andhra Pradesh, Haryana, Madhya Pradesh, Mysore and Uttar Pradesh. The aim of this scheme is to fill in to the extent possible, the production and the medium-term instrument credit gaps of these areas with special reference to the credit needs of the small farmers so as to eliminate resource by the farmers to non-institutional credit agencies. Secondly, the scheme aims at revitalising the working of the societies so that they become efficient business organisations operating at village level. In all, 2121 societies in the 50 districts in the above 5 states were selected by 20 commercial banks through 326 of their branches. Besides the State Bank group, 12 public sector banks participated in the scheme.
Due to the failure of the commercial banks to provide farm credit in India and their failure to create an effective coordination, the Rural Credit Survey Committee (1951) recommended the amalgamation of the Imperial Bank of India and the other associates so that such a reconstituted State bank of India would reach the rural areas with a strength and objective necessary for creating agricultural credit. Thus, it was thought that the then Imperial Bank and other state associated banks in an amalgamated form would ideally serve as an agency of the State Bank of India. Following recommendations were made by the Rural Credit Survey Committee: (a) the State Bank should create an 'Integration and Development Fund' to which should be credited the dividend earned by the Government and the Reserve Bank on their shares in the institutions, and the Reserve Bank and the Government should make an important contribution of ₹.50 lakhs towards this Fund; this fund should be used to meet the losses in opening the rural branches, (b) the State Bank should set-up branches in rural areas where cooperative banking has not yet reached. Accordingly, the State Bank of India Act was passed in 1955 which took over the assets and liabilities of the Imperial Bank of India. The Bank has taken a keen interest in the development of the cooperative sector by making credit available to cooperative banks, (a) facilities for remittance of fund through a wide spread network of branches and
sub-urban and rural areas (d) advances against the Government and transite securities; pledge of goods as well as against Government guarantee; (e) financial accommodation to marketing and processing societies; and (f) purchasing and holding debentures of cooperative contract land mortgage banks. In all these spheres the Bank is progressing steadily as is evident from the fact that the credit limits sanctioned by the Bank to cooperative banks other than cooperative central land mortgage banks increased from ₹15.8 crores to ₹22.0 crores during the year ending 1962. The banks holding of debentures of cooperative central land mortgage banks rose to ₹203.5 lakhs in 1962 as compared with ₹113.9 lakhs in 1961.

Recently, the State Bank of India and its subsidiaries have made sufficient progress regarding the advance provided for the agriculture. It also started making direct loans available to the agriculturists. So far as the direct finance is concerned, the Bank and its subsidiaries at the end of June 1968, provided an amount equal to ₹3.59 crores and in the years ending June 1969 and 1970 it increased upto ₹40.96 crores and ₹150 crores respectively. Similarly indirect finance have made substantial progress. They have increased from ₹54.60 crores in the years ending June 1968 to ₹206.28 crores and ₹265.20 crores in the year ending June 1969 and June 1970.¹

Cooperative banks have obvious advantages precisely where other institutional agencies have great disadvantages. Cooperatives, like local money lenders can have intimate knowledge of the character and abilities of their members and of local production possibilities. In India, at the end of June 1961, there were in the country more than 3 lakhs credit societies. Of 2.12 lakhs primary agricultural credit societies in the country, 19% were dormant. The population of villages in the jurisdiction of the agricultural credit societies constituted 55% of the rural population. In terms of 100 rural families, only 24 were members of cooperatives and 12 actually borrowed during the year 1960-61.

In the year, the number of primary agricultural credit societies declined from 1.72 lakhs from June 1968 to 1.68 lakhs up to June 1969 mainly due to continued efforts at remitalisation and re-organisation of these societies to form variable units. The membership of these societies however, increased by 4%, from 281 lakhs to 292 lakhs during this period. These societies which covered 94 per cent of villages in the country had in their jurisdiction 90 per cent of rural population. The short and medium term loans advances by them in 1969-70 amounted to ₹456.39 crores
and Rs. 47.48 crores respectively, indicating a rise of 16% and 36% respectively over the previous year.

In the sphere of cooperative marketing, the volume of agricultural produce marketed by cooperatives which was Rs. 525 crores during 1967-68 increased to Rs. 583 crores during 1968-69. The value of foodgrains marketed by the cooperatives increased to Rs. 222 crores during 1968-69.

The cooperatives made considerable progress in the supply of agricultural inputs, particularly fertilizers. During 1968-69 they distributed fertilizers worth Rs. 200 crores as against Rs. 183 crores in 1967-68 for distribution of chemical fertilizers, there were 40,409 retail depots at the end of June 1969.

In the cooperative processing sector, the number of cooperative sugar factories increased by 31 during 1969-70 as against an increase of only 2 during the previous year, thus bringing the total to 110. Other important commodities processed by cooperatives were foodgrains, cotton, oilseeds, fruits and vegetables, plantation crops, jute etc. By the end of 1968-69, 1517 processing societies of various types (other than cooperative sugar factories) were organized assisted by National Cooperative Development Corporation.
The number of cooperative banks coming under the purview of the Banking Regulations Act 1949 (as applicable to Cooperative societies), declined further from 1348 at the end of June 1969 to 1317 at the end of June 1970. The later number comprised 28 state cooperative banks, 366 central cooperative banks and 923 primary cooperative banks.

Licenses to commercial banking business under section 22 of the Banking Regulation Act 1949 (as applicable to cooperative societies) were granted during the year 1969-70 to 2 central cooperative banks and 8 primary cooperative banks raising the total number of banks licensed to 24.¹

The long-term requirement of the farmers were traditionally met by the money-lenders but later by other agencies also, such as the state governments, the cooperative credit banks; but these agencies were found defective for one reason or the other. There was, thus a great need in India for an institution. Secondly designed to cater the long-term credit needs of the agriculturists which would offer long-term funds at moderate rates and recover loans in annual or semi-annual instalments spread over a number of years. Land mortgage banks (land development banks as they are now called) were organised for the purpose of providing long-term credit to farmers.

Land development banks provide credit for a variety of purposes such as redemption of old debt, improvement of land, purchase of costly agricultural equipments, construction of wells and erection of pumps and so on. At one time, the redemption of old debts was the most important and, in a sense, the only purpose for which the farmers approached the land development banks. In recent years, however, the farmers have been borrowing from land development banks mainly for the purpose of land improvement and development. The following table for 1965-66 gives the figures on the subject:

Table 8
Purpose-Wise Distribution of Land Development Bank Credit.

<table>
<thead>
<tr>
<th>Purpose</th>
<th>Amount in Rs. crores</th>
<th>Percentage of total</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Land improvement (including sinking of well)</td>
<td>31.4</td>
<td>55.7</td>
</tr>
<tr>
<td>2. Purchase of Agricultural Machinery</td>
<td>16.1</td>
<td>28.6</td>
</tr>
<tr>
<td>3. Redemption of prior debt</td>
<td>3.4</td>
<td>5.9</td>
</tr>
<tr>
<td>4. Other purposes</td>
<td>5.5</td>
<td>9.8</td>
</tr>
<tr>
<td>5. All loans</td>
<td>56.4</td>
<td>100.0</td>
</tr>
</tbody>
</table>

The Government has also been a source of rural finance, for short as well as for long term period. Government loans to farmers are known as taccavi loans. These loans are generally given in times of emergency or distress such as famine, flood etc. The rate of interest is low and the mode of payment is very convenient. But these loans, though popular have assumed low significance. We have already seen how only 3.3 per cent of rural finance was from the Government. There are a number of reasons for this unsatisfactory position. The farmers find it difficult to get the taccavi loans, because of the time wasted, the delay involved etc.

To sum up, the traditional source of agricultural finance in India was the money lenders which was extremely unsatisfactory. To save the farmers from the clutches of the money lenders, the government started supplying funds to the farmers directly. But it was found that this source was both inadequate and highly defective, hence the Government started the cooperative finances and land mortgage banks for long-term finance. In 1955, the Government set up the State Bank of India; in 1963 it set up the Agricultural Refinance Corporation, and in July 1969 it had nationalised the leading 14 commercial banks in the country for helping the farmers through institutional credit agencies.
## Table 9

Scheduled Commercial Banks' Advances to Agriculture

<table>
<thead>
<tr>
<th>Period</th>
<th>Direct Finance for distribution of fertilizers and other inputs</th>
<th>Finance Loans to electricity Boards for energising of wells</th>
<th>Agriculture Other types of indirect finance.</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Limit enforce</td>
<td>Balance outstanding</td>
<td>Limits enforce</td>
</tr>
<tr>
<td></td>
<td>No. of Amount account</td>
<td>No. of Amount account</td>
<td>No. of Amount a/c</td>
</tr>
<tr>
<td>June 1968</td>
<td>572</td>
<td>44.76</td>
<td>1,027</td>
</tr>
<tr>
<td>June 1969</td>
<td>2,523</td>
<td>158.73</td>
<td>2,659</td>
</tr>
<tr>
<td>June 1970</td>
<td>5,211</td>
<td>162.17</td>
<td>4,814</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>No. of account</th>
<th>Other types of indirect finance</th>
<th>Direct finance to farmers</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Balance outstanding</td>
<td>Limits enforce</td>
<td>Balance outstanding</td>
</tr>
<tr>
<td></td>
<td>No. of account</td>
<td>amount</td>
<td>No. of account</td>
</tr>
<tr>
<td>11</td>
<td></td>
<td></td>
<td>12</td>
</tr>
<tr>
<td>June 1968</td>
<td>9,081</td>
<td></td>
<td>12.47</td>
</tr>
<tr>
<td>June 1969</td>
<td>6,161</td>
<td></td>
<td>28.18</td>
</tr>
<tr>
<td>June 1970</td>
<td>18,571</td>
<td></td>
<td>37.79</td>
</tr>
</tbody>
</table>
## Table 11

Scheduled Commercial Banks' Advances to Agriculture - Bank-wise

(Rs. in crores)

<table>
<thead>
<tr>
<th></th>
<th></th>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>Direct Finance</td>
<td>Indirect Finance</td>
<td>Direct Finance</td>
</tr>
<tr>
<td>Limits</td>
<td>Outstanding force</td>
<td>Limits</td>
<td>Outstanding force</td>
</tr>
<tr>
<td>1</td>
<td>2.50</td>
<td>10.97</td>
<td>38.51</td>
</tr>
<tr>
<td>State Bank of India and subsidiaries of the State Bank of India.</td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Nationalised Banks.</td>
<td>9.14</td>
<td>4.69</td>
<td>23.26</td>
</tr>
<tr>
<td>Other Banks</td>
<td>9.60</td>
<td>8.52</td>
<td>13.74</td>
</tr>
<tr>
<td>Total</td>
<td>21.24</td>
<td>14.30</td>
<td>75.51</td>
</tr>
</tbody>
</table>