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RECONSTRUCTION OF RURAL CREDIT:

Any scheme of rural credit must satisfactorily solve the question of the appropriate agency whether a unified agency can function more efficiently or whether separate agencies are necessary for the different types of rural credit. A co-operative credit system would be the ideal arrangement but the present structure and working of the system reveals serious deficiencies and defects. The deficiencies must be made good and the defects removed in order to render the system more efficient and popular. It would be extremal unwise to brush aside the co-operative agency and try to build altogether a new structure of credit machinery. For that would throw out of gear the entire system and create difficulties for the satisfactory establishment and working of the new credit machinery. It is therefore suggested that a state-cum-co-operative agency must be brought into existence to provide rural finance. The ultimate objective of course is the unification of the system into a co-operative credit system in a co-operative pattern of agrarian economy.

RURAL FINANCE IN INDIA & ITS RISKY CHARACTER:

In India the vast majority of the cultivators own small holdings which cannot always provide an adequate income to the agriculturists. With them agriculture is not so much a profession as a mode of living. They have no substantial assets which can serve as security. In fact agriculture as carried on by this class is not remunerative according to ordinary commercial standards. The financing of the agriculturists who labour for a meagre subsistence is therefore often risky. Uneconomic holdings, inefficient methods of cultivation, the inability of the farmer to utilise modern knowledge of and technique or to use improved seed, manure,
agricultural improvements for proper cultivation, terms of land tenure which offer little inducement for improvement of the soil—all these factors have contributed to make our agriculture a deficit economy, particularly in the areas which are entirely dependent upon the monsoon. "Rural finance, therefore, is fraught with risk and a certain measure of state assistance will be necessary if a satisfactory agency is to be set up or maintained for providing finance in rural areas."*

**EXTENSION OF CREDIT FACILITIES:**

The question of agricultural finance is closely linked up with the improvement of agriculture. The re-organization of agriculture is both urgent and necessary not merely to help the cultivators but of the rut of a miserable standard of living but also to serve the larger interests of the nation. In the reconstituted pattern of agrarian economy, the credit requirements of agriculture could be easily met since the efficiency and therefore the profitableness of the agricultural industry would be greatly increased. The elimination of the weak and inefficient units of cultivation by the welding together of the farms into co-operative joint farms would solve the problem of timely and adequate finance required by all classes of cultivators. The limit to the expansion of the co-operative movement has been set by the credit-worthiness of the cultivator. That credit can be given only to the credit-worthy cultivator is taken as almost axiomatic. But the vast number of cultivators whose credit requirements are in excess of their credit-worthiness remain outside the purview of any organised credit institution and particularly that of the co-operative system based as it is on the principle of unlimited liability. To leave them entirely to the mercy of the money-lender,

who naturally charges unconscionable rates of interest would be no small injustice to this class of agriculturists who would remain perpetually uncreditworthy and would sink into the position of landless labourers. The scheme of reorganization of agriculture seeks to eliminate the distinction between credit-worthy and non-credit-worthy sections by joining them all in co-operative association and enabling all the cultivators to obtain credit from a unified agency.

CO-OPERATIVE CREDIT - THE SOLUTION:

A co-operative rural community whose various activities and efforts will be regulated and organised on the co-operative pattern is the goal to be reached however hard and long the way might be. In the background of the slow and limited growth of the co-operative movement, it will be pertinent to ask whether so much reliance should be placed on the co-operative organization in solving the problems of Indian farming. It has to be said that to generalise on the basis of the slow and limited success of the co-operative movement is to generalise on wrong premises. No concentrated attempt was made to tackle the whole problem of the Indian peasant. The provision of cheap credit was not the solution to the entire problem. There was no concerted effort to improve the efficiency of agriculture or to alter the character of agriculture from a deficit into a surplus economy. There is nothing inherently wrong in the co-operative method itself nor in the people who come into the co-operative movement. The co-operative pattern of agrarian economy will provide the only lasting solution for the many difficult problems which the agriculturist has to face.

THE GADGIL COMMITTEE'S RECOMMENDATIONS:

The Gadgil Committee examined the problem of rural indebtedness and made recommendations for the reorganization of agricultural
finance. The Committee considered that the main aim of this reconstruction in the immediate future should be to provide the solvent agriculturists in all areas with an agency alternative to the private money-lender who is still the most important of the agencies for the provision of agricultural credit in the country. Though on theoretical grounds a single financial agency which covered the entire field of agricultural credit would be the ideal arrangement, the Committee stated that in view of the vast size of the country and the large variety of conditions in the different areas, "the attempt should be made to develop as varied a system of institutional finance as possible for financing agriculture.

Co-operative credit, according to the Committee, cannot be the alternative agency because the present position of the movement does not inspire one with much hope about its success as the sole supplier of agricultural finance in the immediate future. The extension of co-operative credit to meet all the requirements of credit-worthy cultivators all over the country within a short period of time is considered impracticable without a very large degree of state assistance and control which would seriously affect its democratic "co-operative character."*

THE AGRICULTURAL CREDIT CORPORATION:

The Gadgil Committee therefore recommended the establishment of an Agricultural Credit Corporation for each state, except where the Government feel that the co-operative financial agencies are so strong and have such wide scope that they should undertake all the work expected of the Agricultural Credit Corporation. The proposed Agricultural Credit Corporations would be autonomous institutions, half the capital being provided by the State and the rest by joint-stock banks, co-operative banks and marketing organisations, there being no

*(Report - P.47).
individual shareholders. The control of the Corporation, after the pattern prevalent in most countries of the world should be in the hands of executive officials and a board with a tenure for a fixed term of years appointed by the State. The corporations would establish branches and agencies all over their regions according to the requirements. The Corporation would supply all types of credit since the usual objection to combining short and long term business by one agency based on the relation between the term for which funds are available, and the term for which they are invested would not apply in this case as a substantial part of the capital and part, perhaps, of the working capital also of the Corporations would be supplied by the State. The Corporation would provide intermediate and short-term finance directly to substantial cultivators. But the intermediate and short-term needs of smaller cultivators based generally on personal security or statutory first charge on the crop would only be provided through co-operative societies or "borrowers" groups. The Corporation, the Committee, felt, would be able to undertake efficiently and expeditiously the work of making available long-term credit on mortgage on a countrywide scale. The Corporation would act as the chief financing agency to co-operative societies where the appropriate higher co-operative organizations do not exist or where the co-operative banking organization is not in a position to give adequate finance.

The rates of interest charged by the Corporations should not exceed 4 percent for mortgage and 6½ percent for other types of credit. The Committee felt that for the bulk of the ordinary business the Corporations would not require any considerable subsidization by the State to maintain the rates of interest recommended by it. But in the less developed areas where the cost of administration and collection of loans as well as the risks connected with them will be large, there would be need for a state subsidy in the form of free funds or the
defraying of the costs of administration and supervision. Also, in those areas where the volume of business is not considerable, the State should provide substantial help.

The Committee, however, did not frame any quantitative estimates relating to the capital or the volume of business of the Corporations for the various regions. For this purpose it said that the States will have to work out the schemes taking into account the effects of legislation relating to adjustment of debts, the development of the co-operative movement, the operation of the private money-lending agencies, the needs of the specially backward areas etc.

CRITICISM OF THE PROPOSAL:

In criticism of the Committee's recommendations, it could be said that while the proposal to set up Corporations in States where the Co-operative banking structure is poorly developed is unexceptionable, the establishment of such Corporations in areas where co-operative banking is highly developed in both ordinary and land mortgage business and where the Corporations would constitute a third system is unnecessary and objectionable. But even where the co-operative movement has not made much headway, attempts could be made to develop it. The co-operators generally disapprove of two alternative credit agencies working in the same field with state support and assistance, and believe that the effect of such competition would be detrimental to the interests of the co-operative organizations. They feel that given the financial resources and assistance contemplated for the Corporations, the Co-operative financing agencies such as the provincial and central banks can equally meet the requirements. The co-operative institutions have the additional advantage that they are already established and have some organisation in the field.
The co-operative banks have been able to attract considerable funds through deposits. The Gadgil Committee did not clarify whether the agricultural credit corporations would accept deposits or perform any other "banking" operations. It is problematical whether the necessary funds could be raised by the corporations in the manner indicated by the Committee.

Moreover, the co-operative movement encourages thrift and small savings which could be mobilised to supply part of the requirements of cultivators. The Corporations have no part to play in the rural savings campaign.

The Gadgil Committee said that the small agriculturists who need finance should be induced to form co-operative societies or borrowers' groups to form a link between the corporation or its local agency and the large number of agriculturist producers. Co-operative credit societies in India have already been dubbed as "groups of borrowers." The organization of separate groups of borrowers therefore would seem to offend the sentiments of the agriculturists in need of borrowed funds. Moreover, the system of "borrowers' groups" has practically failed in Palestine where the co-operative society is now regarded by the Barclays (D.C.O.) Bank as the most hopeful line of approach to the peasant cultivators. The Credit Agricole D'Egypte had a similar experience and has been making special efforts to encourage the formation of co-operative societies by giving them preferential treatment.

The other proposal that the agricultural credit corporations will deal directly with substantial cultivators who can obtain both short-term and long-term finance from them is paradoxical in the extreme. Substantial cultivators form a small percentage of the total number of cultivators in the country and hardly require financial assistance. They have surplus funds which they lend to agriculturist borrowers on the same terms and conditions as the private money-lenders. It has been
pointed out that this better class of cultivators who are really solvent have not joined the co-operative credit societies partly because these societies operate on the principle of unlimited liability and partly because they do not stand in need of financial help. It would be highly detrimental to the social and economic interests of the nation if the substantial cultivators are constituted into a privileged section as this proposal seeks to do. They must be brought into the ambit of the co-operative movement which has been deprived so long of their material help, sympathy and guidance.

Again as the Nanavati Committee pointed out, it is doubtful whether the corporations can immediately come into being and start functioning on the lines suggested by the Gadgil Committee with close links with rural areas and with efficient branches. This must take a long period of years and depend on successful solution of many problems. The Nanavati Committee therefore rejected the proposal for an agricultural credit corporation in Bombay, which, as a rival agency buttressed by a large measure of Government support, will not only arrest further progress of the co-operative movement but may even lead to its disintegration.*

On a consideration of these factors, the Co-operative Planning Committee expressed the opinion that not only in some provinces where the Co-operative movement has attained a high degree of development, but also in other provinces and states, the provincial co-operative bank or other Central Co-operative financing organization can provide the agriculturist with all the facilities which are intended to be given by the Agricultural Credit Corporation. The same measure and type of aids as those recommended to be given to the Agricultural Credit Corporation should be given to the provincial co-operative bank and there would then be no need to start a separate organization for

for this purpose." * The Congress Agrarian Reforms Committee (1949) also felt that the institutional credit facilities short-term, medium-term and long-term, should be organized through the land mortgage bank and the co-operative credit institutions because these bodies have established contacts in course of a period of forty years with the rural population needing such credit advances.

**REORGANISATION OF CO-OPERATIVE CREDIT STRUCTURE:**

In view of recent developments in the field of co-operation, it appears that there is a general preference for the reorganisation of existing co-operative banks, where necessary and their expansion and development, than for the establishment of new agricultural credit corporations. The Nanavati Committee opined that the co-operative financing institutions in the Bombay State would be able to undertake the tasks envisaged by the Gadgil Committee for meeting the requirements of all creditworthy cultivators.

The Gadgil Committee too expressed itself in favour of the co-operative organization. The Committee said, "We are in general agreement with the view that the spread of co-operation would provide the best and the most lasting solution for the problem of agricultural credit in particular and of those of the rural economy in general".

The defects of the Co-operative movement, which the Committee pointed out, can indeed be moved easily and the efficiency of co-operative finance improved greatly. The Committee averred, "the Co-operative Credit movement can, however, be made to play a greatly increasing part in agricultural finance if it is reorganized and run on sound lines," and recommended "that systematic and intensive development of the co-operative movement should form an integral part of the plan of reconstruction."

@ Report - P.99.
% Report - P.47.
ORGANIZATION OF MULTI-PURPOSE SOCIETIES

The problems of co-operative credit have, therefore, to be understood and tackled in a manner which would improve the working of the system. The Rural Banking Enquiry Committee suggested that the weakness of the co-operative structure seems to lie mainly in the primary institutions where it comes directly into contact with the rural people rather than in the superstructure. The trend of opinion has now definitely shifted in favour of the multi-purpose society. In the place of one society dealing with only one aspect of the economic life of the cultivator as has been the case so far, efforts should be made to bring all the aspects of the life of the cultivator within the compass of the same society. A multi-purpose society will tackle credit, better farming, marketing of agricultural produce, cattle welfare, organization of suitable agro-industries and supply of consumers' goods. The compass of activities of a multi-purpose society would be so large that the whole village population could be included in its membership for one or other benefit arising from it.

The Indian farmer is happy when all needs can be satisfied by the same agency, and is used to the money-lender who supplies all his wants. He approaches the money-lender for credit, both short and long-term, gets the consumers' goods and disposes of his marketable surplus through him. The multipurpose society would replace the money-lender and would naturally fit into the psychology and economic background of the peasant.

The Nanavati Committee said "As regards the future, we think that looking to the economic and social conditions in rural areas, the normal policy should be to organise multipurpose societies only and to convert the existing village primaries into multipurpose societies preferably on the same liability. Such societies should satisfy the
normal cultivation needs of their members as well as supply credit for agricultural needs. They should also serve as agencies for supply and sale and as they develop their capacity, in course of time should also act as consumers' societies."

**LIMITED LIABILITY - THE BASIS.**

The principle of unlimited liability on the basis of which the agricultural credit societies are founded is essentially co-operative principle in that it creates among members a sense of collective responsibility and mutual watchfulness. Apart from considerations of co-operative principle and of moral gain, the Gadgil Committee felt that in most parts of India a co-operative society will not be able to raise adequate finance and make it available to the bulk of the agriculturists on any other basis. However, it is frequently asserted that in many areas the rule of unlimited liability prevents substantial cultivators from joining these societies and imparting strength to the movement. In most provinces the trend of thought is in favour of limited liability. The Co-operative Planning Committee therefore recommended "that except where unlimited liability has produced good results, the liability of the reformed and reorganized primary society should be limited." The liability in such cases may be limited to the value of shares held by a member or to a multiple thereof provided that a substantial part of the funds required by the society can be raised through share capital.

**AREA OF OPERATIONS:**

The area of operations of such a society would not be confined to a single village but would extend over a group of contiguous villages. With the adoption of the policy of extending the area of

@ Report - P.24.
operations, the membership of such societies will increase. There should therefore be no limit to the maximum number of members in a society. The Nanavati Committee devised the arrangement of nominal membership for individuals who keep out of the credit societies because they are based on unlimited liability. But that arrangement would vitiate the atmosphere and must therefore be considered unsatisfactory. In our scheme all the members of the village society - farmer, trader, money-lender, artisan, will be drawn into the multipurpose society and will reap the benefits flowing from it. Nor should separate credit associations of bigger cultivators be encouraged since that would defeat our objective of imparting strength to the movement. The combined resources of small, medium and big landowners must necessarily be drawn into a common pool out of which the funds for investment in agricultural enterprise and production would be provided. If co-operative joint farming is to be established all over the country within a measurable distance of time, it seems inevitable that even a certain measure of compulsion must be adopted.

As regards the credit needs of the members, the basis of the repaying capacity of the members is also more appropriate in a programme of reconstruction and development. For with such a basis the credit of a member will depend on the extent to which he takes loans for productive purposes and brings about an increase in income and repaying capacity. With the formation of co-operative farms, the credit-worthiness of individual members will cease to be the criterion and the credit needs of all co-operatively joined together in the business of farming will be adequately met. The efficiency of farming operations will be greatly enhanced and agriculture will become a surplus economy that it is not today.
short and intermediate-term credit:

The supply of credit will be one of the functions of the multipurpose co-operative society. Credit is required for production as well as marketing. Loans for current agricultural needs such as the purchase of seed or manure generally called short-term credit and loans for productive purposes such as the purchase of bullocks or implements called intermediate or medium-term credit will be disbursed by the society. The period of intermediate loans should ordinarily be three years which might in exceptional cases be extended to five years by a society in a strong financial position.* So long as individual cultivation prevails, it will be necessary to take into account the personal credit of the borrower. But once joint cultivation on a co-operative basis is introduced, the principle of collective security will prevail. If co-operative finance is to be made a vital factor in agricultural reconstruction and development, co-operative finance must be rendered efficient and popular.

utilisation of credit:

The Indian farmer makes but little productive use of credit to increase his income-earning capacity. It is, therefore, suggested that it is necessary to ensure the proper application of the loan advanced by the society. Cash loans should give place to loans in kind for that will ensure the proper application of the loans. The multipurpose society, therefore, should undertake to supply the requirements of farmers in kind, i.e. seed, manure, implements, etc. and debit it to the account of the members. The Gadgil Committee said that the proper application of loans could be ensured (1) by supplying as far as possible the requirements of the members (in kind) through direct agreement with purchasing unions and consumers’ stores.

which would supply the goods to the members by debit to the society's account. In the absence of such organisations, the society itself might supply the goods but it should work strictly on indent system and should not undertake any trading risks; and (2) by a constant and careful supervision of the operations of societies and their members through an efficient supervisory staff whose cost of maintenance should be met by the state." Such an arrangement would be greatly advantageous to the members too for the prices of the materials and goods supplied to them would be almost at cost and the loans therefore could be put to the maximum use. The requirements of the members can be assessed at the beginning of each agricultural year and met in the manner indicated above.

**CONTROLLED CREDIT:**

The recovery of loans would then be an easy affair. The society which has made loans in kind will have a statutory charge on the crop which could not be hypothecated to any private agency by one who has taken co-operative credit. The effectiveness of this charge would be increased if the sale of agricultural produce is done through the society. This has already been attempted in certain areas in Madras under what is known as the scheme of "Controlled Credit". The members who obtain credit should execute an agreement to sell the produce through the society or the sale society to which the village co-operative society is affiliated. The dues of the member to the Society or the land mortgage bank should be deducted from the sale proceeds of the produce and the balance credited to the member's account in the society's books. Thus not only the proper application of the loans but also the recovery of the loans could be easily ensured.

**CREDIT LINKED TO MARKETING:**

The proper planning of co-operative finance, therefore, involves the disbursement of loans in kind and the clearance of the
loans due from members to societies out of the sale proceeds. This arrangement would remove the difficulties of agricultural marketing and enable the agriculturists to obtain better prices for their products. The Co-operative Planning Committee recommended that for the proper development of Indian agricultural economy, credit should be linked with marketing. The condition for the grant of loans by the co-operative society should be that each member will sell all the marketable surplus of agricultural produce through the Society. The co-operative society should assemble the produce of its members and arrange for its transportation. Where processing and grading are necessary before the produce could be marketed, the co-operative society would be in a much better position to undertake those activities. As the Co-operative Planning Committee aid, ordinarily the society should not hold over produce in the hope of a rise in prices. The society may give an advance to the member after keeping an adequate margin at the time the produce is delivered to it. The produce will be stored in the godown or warehouse and the society will be in a position to secure finance from the Central financing agency.

GODOWN FACILITIES:

Co-operative marketing can hardly make headway without adequate storage or godown facilities. The Madras Government have encouraged co-operative sale societies and rural credit societies to construct their own godowns by offering loans and free grants, the loans being for a period of 30 years. By 1945, 28 sale societies owned 37 godowns and 49 credit societies had built 52 godowns. The progress is far from satisfactory. In 1949-50 the Government sanctioned a scheme for the grant of subsidies to the extent of 50 percent of the cost of construction of godowns built by co-operative societies. Even in Bombay where co-operative marketing has reached a fairly high stage of development, the construction of godowns has not been
undertaken on the required scale. The Government is giving loans at a low rate of 3½ percent and subsidies to the extent of 25 to 50 percent for building of godowns by co-operative organizations but much use has not been made of these facilities. That liberal state assistance for the construction of godowns is necessary has been emphasised by more than one committee. The Rural Banking Enquiry Committee aptly remarked that "without greater initiative and assistance from the state much progress in this direction is not likely to be achieved." The Committee recommended the establishment of a Warehousing Development Board for providing financial assistance to commercial banks and co-operative institutions in the form of free grant up to 25 percent and long term loan at a low rate of interest up to another 25 percent of the cost of godowns. The Committee also suggested that banks should be permitted to form subsidiaries for constructing and running warehouses provided that not more than five percent of their owned funds are utilised for the purpose and that as an experimental measure certificates issued by such subsidiaries might be recognised as valid warehouse receipts by the Reserve Bank for the purpose of Section 17 (4) of the Reserve Bank of India Act. The construction of a chain of warehouses in the country is unlikely to attract immediately sufficient private capital and it might also not be desirable to leave the running of the warehousing system in private hands. The co-operative societies should be provided with all the funds required for the construction of godowns by the Government or the Reserve Bank. The Rural Banking Enquiry Committee estimated that on the basis of the assumption of the cost of a small godown at Rs.20,000/- two thousand godowns could be constructed in the next five years at a cost of Rs.4 crores. The Government should incur this total outlay instead of forcing the co-operative societies to share 50 percent of the cost.
The construction of these licensed warehouses would solve the problem of marketing finance. The receipts issued by such warehouses in the country would constitute a first-class security against which even the commercial banks will lend. Under section 17 (4) (d) promissory notes of any scheduled bank or state co-operative banks supported by such receipts will be discountable with the Reserve Bank. Thus the establishment of warehouses in India will open an important avenue for the Reserve Bank to provide finance to agriculture. The system of licensed warehouses apart from contributing to smooth and orderly marketing of agricultural produce, will not only increase the volume of finance available to agriculturists but will also cheapen credit. The system of loans in kind and recoveries through sales of produce by the Society will put an end to the defaults which are so common at present. Defaults occur not because the members wilfully resort to a breach of the contract but because circumstances compel them to do so. With the adoption of co-operative farming and price stabilisation measures, the repaying capacity of the members would greatly improve and the repayments would be automatic and certain. Extension of the time limit may be allowed in cases where the members are in temporary difficulties. For wilful defaults there should be no hesitation in resorting to coercive measures. To minimise delay, the Co-operative Department should be vested with powers to adopt coercive measure where necessary.

**RATES OF INTEREST:**

According to the Gadgil Committee the Indian agriculturist has to pay for his financial requirements from the Co-operative Societies at a very high rate of interest. The Committee recommended that the maximum interest charged for development loans should be
4 percent and for current finance 6½ percent. In India where agriculture is inefficient and therefore low-income yielding, a rate of 6½ percent in the present circumstances is the maximum that the agriculturist could pay for current finance. Even when the efficiency is improved by co-operative farming methods, the rates of interest on loans for agricultural purposes should be kept down to the minimum. The basic reasons for the high rates of interest, as pointed out by the Nanavati Committee are, apart from the small size of primary units (a) the high rates charged by the Central banks, (b) high cost of running the societies and (c) failure to raise local deposits adequate for their needs. If the rate of interest charged to members is to be reduced the societies must obtain funds from central banks at rates lower than at present, spend less on staff, maintenance etc., and attract large local deposits. With the reorganisation of the village society and the increase in membership and the altered character of its working, it is expected that the societies will come into possession of larger resources which will enable them to operate on an economical basis. The provision of funds at lower cost by central financing agencies will help the societies to reduce their lending rates. Also as the Nanavati Committee pointed out, the Societies should be in a position to work within a margin of 2½ percent and bring down the rates of interest to the target fixed by adopting the following measures. (a) by increasing their size with a view to enable them to run as economic units; (b) by collecting local deposits where feasible, at low rates of interest; (c) by undertaking multifarious activities with a view to supplementing their profits; (d) by cutting down all overhead expenditure."* Apart from these measures, state aid to co-operative societies should be increased greatly. This aid would be in the form of a liberal subsidy to multipurpose societies initially for a period of five years to cover the entire cost of management.

The Nanavati Committee pointed out that one unsatisfactory feature of the rural movement is the high percentage of the cost of management to the working capital of the primary societies, which in Bombay works out at 4.4 percent. This, it is said, was partly due to the expanded activities of the rural credit societies in recent years. The establishment of multi-purpose societies for a group of villages would initially increase the cost of management though in later years the enlargement of the unit and the greater resources which it would control, would tend to bring down the cost. Hence the state should help the societies by a liberal subsidy in the first few years of expansion.

The Rural Banking Enquiry Committee, however, has expressed the opinion that "the principle of subsidising co-operative institution to a limited extent in the initial years, in view of the risky character of rural finance, the low rates of interest they are attempting to establish and the need to provide the necessary secretarial and supervisory staff appears to be unobjectionable although we do feel that the proposals sometimes put forward that the state should find subsidies for all sorts of purposes to the extent of crores of rupees do not seem to be based on sufficient appreciation of the implications, financial and otherwise."*

The dawn of a new era in co-operation is heralded by the multipurpose society. The multipurpose society is an effort to cater to the various needs and requirements of the agriculturists through a single agency. It could be said that the peasantry will take to the multipurpose co-operative easily because the peasant is used to deal with one institution for all purposes viz. the village money-lender.

* Report P.49.
Success in the organization of multipurpose co-operative societies will depend largely on local leadership and official guidance and supervision. The affairs of the society must be supervised by a directorate composed of men of ability and integrity who command the confidence of the people. Again the expansion of the activities of the village society will necessitate the employment of an efficient staff. The manager must be a person who is familiar with all aspects of village life and has been trained in the methods of co-operation. In the early stages, progress, particularly in areas where local leaders of high calibre are not available, will depend on the manager's initiative and his influence with the people. The dependence on the honorary staff for the successful working of these societies will not carry us far. The manager and his assistants must be paid well to invoke the necessary zeal and enthusiasm. The society would find it difficult in the early years of its existence to meet the cost of a well-paid manager and other staff and the government should subsidise the societies to the full extent of the cost during an initial period of five years.

Self-help is the foundation of the co-operative movement and the members of the primary societies must recognize that responsibility for the working of the institutions rests primarily upon them. But until the principles of co-operation are more fully understood, it is essential that official guidance and control must be maintained.

The Central Financing Agencies:

The financing agency is not one but consists of the banking unions, central banks and the apex bank joined together in a loosely federal type. The development of banking unions, one for each taluka,
seems to be unnecessary since a central bank or a branch of the Provincial bank operating over a district secures funds at reasonable rates of interest, offers cheaper services to its constituent societies, exercises adequate control over credit policy, ensures economy of overhead charges and provides a large field for selection of men of management. It is contended that if societies are reorganized on a multipurpose basis banking unions would possibly earn greater profits than the central banks and would be able to maintain an efficient staff. The Madras Committee on co-operation said that "multipurpose societies are yet to come and that we must not count the rupees that the multipurpose chicken are going to earn for us even before the eggs are hatched."* A central bank operating over a wide area can make a greater profit on a large turnover with narrow margins than a banking union can expect to do. The district central banks have greatly developed in Bombay and Madras and are a valuable feature of the co-operative movement. The proposal for the conversion of the district central banks into branches of the Provincial Co-operative bank has been made from time to time. The arguments in favour of the proposal are as follows: First, it is stated that central banks are more or less intermediaries in the co-operative banking structure and that they can be eliminated with advantage to the ultimate borrower who could then be provided with cheaper credit. Secondly it is argued that the conversion of central banks into branches of the Provincial Bank will concentrate funds and banking experience in one place and effect a saving in expenses of management. Thirdly it is said that the constitution of branches of the Provincial Bank in place of central banks might ensure uniformity of financial control and co-ordinated action. The Madras Committee pointed out several objections to this proposal, the chief among them being that central

banks have served well during the period of their existence, that
the existence of intermediary bodies serves to distribute any
sudden shock to the financial structure over the whole movement and
that they have developed an intimate contact with their affiliated
societies which is so essential for the success of the movement.

A uniform co-operative banking structure in all the states
may be desirable but not feasible in the immediate future. In areas
where central banks have not developed it is recommended that the
state co-operative bank should set up branches of its own. Even in
the co-operatively developed state of Bombay the central banks do not
cover all areas in the state, for about ten districts are served
directly by the branches of the state co-operative bank. If it should
be considered necessary for the apex bank to subscribe to the share
capital of central banks, the former may well prefer to set up its
own branches. In those states where the co-operative movement has
not gained momentum, the central financing agency may be the state
co-operative bank which could operate through its branches.

CONSTITUTION OF CENTRAL BANKS:

The present constitution of the central banks provides for
membership of both co-operative societies and individuals. Though
individual shareholders were necessary in the early stages of the
movement it is for consideration whether the time has not now come
for the elimination of the outside element. In Bombay the number of
Central Banks in 1949-50 was 43 with a membership of 31,999 individuals
and 7,231 societies. Compared with Madras the rise in individual
membership in Bombay has been spectacular. It has been noticed that
the business which these banks are doing with the individual borrowers
very often trades - is almost as extensive as with co-operative societi
Individual finance was allowed, as the central banks had large surplus funds and this business has enabled them to earn large profits. Some of these banks are beginning to look upon their business with co-operative societies, for which they were organized as risky and unpleasant. The Nanavati Committee said that this unhealthy tendency has to be firmly curbed if the central banks are not to become useless for the purpose for which they were organized. As the Committee observe, "certainly business with individuals should not absorb the attention of any central bank to such an extent as to make it apathetic to its normal functions of financing rural societies or to render it incapable of carrying out these functions efficiently on account of its funds being locked up in finance to individuals."* For the healthy working of the central banks it is necessary to eliminate individual shareholders so as to make them pure type banking unions composed only of affiliated societies.

**LENDING AND BORROWING RATES:**

The central banks maintain very wide margins between their lending and borrowing rates (2.7 per cent to 4.4 per cent). This is obviously an unsatisfactory state of affairs. It will not be possible for the rural societies to make funds available to the ultimate borrower at 6.25 per cent unless they get funds from the central banks etc. at 4 per cent or less and do not have to keep a margin of more than 2.25 per cent.

The borrowing rates of the central banks have to be kept low. It is hoped that the central banks will come into possession of larger funds by pooling together the increased resources of the societies. The central banks have also to practise economy in their working.

LIMITATION OF DIVIDENDS:

The banks pay dividends at rates varying from 4 to 10 per cent in the different parts of the country. These institutions therefore have become dividend-hunting concerns. The limitation on dividends is necessary. The central banks seek government help to enable them to maintain low interest rates and the government therefore should exercise the right to place an upper limit on dividends.

STATE (PROVINCIAL) CO-OPERATIVE BANKS:

The State (Provincial) Co-operative bank is the apex institution which coordinates and centralises the work done by the central banks and the primary societies. As the apex credit institution, it acts as the balancing centre for the finances of the movement and is the main source of contact with the Reserve Bank.

Except in the state of Bombay, where the apex bank has established 56 branches in ten districts to deal directly with societies and individuals, the state co-operative banks do not have branches but deal mainly with their members, namely, the affiliated central banks and other co-operative institutions. The funds of these banks mainly consist of share capital, deposits from members and the public, and also amounts received from government either in the form of contributions to share capital, deposits from members and the public, and also amounts received from government either in the form of contributions to share capital or by way of loans for special purposes.

In recent years many of the banks engage in commercial banking business and accept current deposits from the public, almost in competition with central banks. While there should be no objection to raising deposits from the public, the commercial business of these banks which is on an extended scale is to be deprecated. These banks
by engaging in commercial business are frittering away their resources an exposing themselves to risks which they are not in a position to bear. The banks, as apex institutions, should try to develop and strengthen the co-operative movement in the states. The extension of the sphere of co-operation and the increase in membership will mean a corresponding increase in the demand for loans and advances and the central financing agencies may then be confronted with a dearth of funds. The dependence of central banks for financial accommodation on the apex banks and the Reserve Bank may therefore tend to increase. The apex banks have to seek ways of increasing their owned funds to finance the movement in the different states. The apex bank in Bombay has been recently reorganized and strengthened to enable it to extend its activities and to finance all credit worthy cultivators through its branches or through the central banks.

The state co-operative bank should be extended all the aids recommended to be given to the agricultural credit corporations which the Gadgil Committee proposed. The state should not only provide a portion of the share capital but should also contribute to the cost of administration including the cost of supervision, audit and inspection subject to certain conditions such as the limitation of dividends.

"INTEGRATED AGRICULTURAL CREDIT" IN BOMBAY:

The scheme of "integrated credit" in operation in Bombay illustrates ways in which state assistance is rendered to the co-operative credit movement. According to the scheme of extension of co-operative credit, instructions were issued to primaries to reorganise their structure to (a) ensure admission of as many new members as may be consistent with safety; (b) provide current agricultural credit to all credit worthy borrowers at 6½ per cent; and (c) develop non-credit activities by being multi-purpose. To enable primary societies to
advance loans at 6\% per cent the Government is providing assistance to multi purpose societies on a graded scale for the first five years and subsidy to agricultural societies for secretarial expense subject to certain conditions up to the maximum of 2.5 per cent of their working capital and 4 percent in case of societies operating in undeveloped areas provided that the societies do not increase their lending rates beyond 6\% per cent.

The state government has amended the constitution of the Bombay Provincial Co-operative Bank providing for subscription to the share capital by the government and representation on its board by three nominees of the government. In order that the Provincial Bank, the central banks and banking unions should function as an integrated credit system, the Provincial Bank has been enabled to subscribe to the share capital of central banks subject to a maximum of Rs.25 lakhs with a limit of Rs.5 lakhs for a single institution.

The government has agreed to contribute to the Provincial Bank a sum equal to the contribution of the Bank to the share capital of central banks. To encourage the Provincial Bank or the central banks to open branches at all places necessary to provide credit facilities to all credit worthy borrowers and adjusted debtors, the government has agreed to subsidise for an initial period of three years, "uneconomic branches" to the extent of the actual deficit subject to a maximum varying from Rs.2,500 to Rs.5000 per annum, the actual limit being dependent on the total volume of agricultural loan business transacted by the branch during the year. The government have also agreed to guarantee the losses of banks and societies to the extent of 5 per cent of the total crop finance advanced by them.

Though increased state aid is sought and given and must be pronounced as indispensable for giving the necessary fillip to the movement, it is wise to recognise that the credit machinery should
raise adequate funds by way of share capital and deposits or debentures from the public. For as the Rural Banking Enquiry Committee points out, the assumption generally made that the state would be able to raise from somewhere vast amounts of capital to be put at the disposal of such machinery is unrealistic.

**LONG-TERM CREDIT:** Long-term credit is supplied by land mortgage banks - the primary land mortgage banks and the Provincial co-operative land mortgage bank. The primary banks are ordinarily not autonomous and act in the main as agencies for the Provincial Land Mortgage Banks. The constitution and working of both the Provincial and District Land Mortgage banks further show much fewer traces of the specific co-operative element.*

Land mortgage banking is inadequately developed in the country. Of the total number of primary land mortgage banks which stood at 283 in 1949, 126 were in Madras. Bombay, the other state where the co-operative movement has made great progress had only 19 primary banks. As has been pointed out before, the business of these banks is small and the total amount of the loans advanced by them covers only a small percentage of the total requirements of long-term credit.

According to our scheme, debt adjustment must necessarily be undertaken before a sound system of rural finance is built up. The adjustment of old debts will throw the entire burden of providing the required finance on the land mortgage banks. Their constitution and working have therefore to be devised properly in order that they may fulfil the role assigned to them and ensure the sound working of the system.

The Gadgil Committee recommended that long term credit on the mortgage of land, should be supplied through land mortgage banks where they are established; where they are not, it should be supplied by the agricultural credit corporations to be established which would

deal with borrowers through their branches, since the provision of all types of credit by a single agency would lead to better co-ordination of credit. The Nanavati Committee did not agree with the suggestion that the same agency should disburse both short-term and long-term credit. The Committee said that no useful purpose would be served "if the Provincial Land Mortgage Bank is merged with the Provincial Co-operative Bank." The 15th Registrars' Conference also discountenanced the proposal for the merging of institutions providing short and intermediate credit with those providing long-term credit.

**LAND MORTGAGE CORPORATIONS:**

In the field of long-term credit, the present position is discouraging. More primary land mortgage banks have to be organised; more funds have to be made available for development of agriculture. A vigorous drive therefore has to be started for the establishment of such institutions which will be of a co-operative character, in all the States. A central Land Mortgage Bank will be the pivot of the structure of long-term finance to the agriculturists in the states.

The impetus to the organisation of primary land mortgage banks should be provided by the stage governments. The establishment of a land mortgage corporation in each state should be undertaken by the government. The government should provide 50 per cent of the capital the remainder to be subscribed by the Reserve Bank and Co-operative banks. The control of the corporation according to the pattern prevalent in most countries will be in the hands of executive officials appointed by the government. The policy will be framed by a Board consisting of nominees of the government and the Reserve Bank and representatives of the co-operative banks.

The share capital of the land mortgage corporation may consist of 100,000 shares of Rs.100 each but it may well differ from state to state. The stock owned by the government will not earn a dividend
at least in the initial period, say, five years. The maximum rate of dividend to be paid in respect of shares held by others may be limited to 3 per cent.

The Corporation should be authorised to issue debentures for raising funds for its business. These debentures should rank as Trustee securities which could be subscribed to by the Reserve Bank. They should carry a guarantee by the government in respect of principal and interest. The issue of debentures may be restricted, as under the Madras Co-operative Land Mortgage Banks' Act of 1934, so that the total amount due and outstanding on the debentures issued cannot exceed at any time the total amount due on the mortgages. It is usual to set a limit to the amount of the debentures issued so as not to exceed 20 or 25 times the paid-up capital stock. But in view of the fact that the corporation will have to provide the finance to pay off the adjusted debts to the creditors, the volume of such business will necessarily be large and cannot be determined before such adjustment takes place. The rate of interest on debentures may be limited to 3 per cent. Where the rate must be higher in order to attract the necessary funds, the government will have to make good the loss which the corporation will incur by maintaining a low rate on advances made by the corporation.

The Corporation should advance funds to the primary land mortgage banks or where they do not exist at present to the central banks which should undertake this lending business.

The Land mortgage Corporation should charge a rate not exceeding 3 per cent on its advances so that the ultimate borrower gets finance as recommended by the Gadgil Committee at 4 per cent.

The land mortgage corporation should draw up a scheme for the provision of loans for land development.
At the same time, steps should be taken to organise primarily land mortgage banks in all states cooperatively less developed. Even in the state of Bombay there are only 19 primary banks. These banks should be at the district level for it would be uneconomical to set up one for each taluka. Besides the share capital, the primary banks may collect deposits from the borrowers for adjustment against their loans or for the purchase of debentures of the land mortgage corporation.

The primary banks should advance two types of loans: (1) loans against mortgage of land for periods not exceeding 20 or 30 years; (2) improvement loans for periods not exceeding 10 years. The amount of the loan may be 50 per cent of the appraised value of land on the first mortgage and may be up to 75 per cent on the second mortgage.

The loans for land improvement may be at a slightly lower rate than the rate charged on loans for debt redemption. The schemes of development will have to be worked out and approved by the Agricultural Department. It has been pointed out elsewhere that the primary banks should be given full freedom and authority in the matter of sanctioning of loans. Whether it is a taluka or a district, the primary banks have established an intimate contact with the cultivator in the area and are in a position to assess their creditworthiness and distribute loans on a correct appraisal of the value of the landed or other assets. This will ensure the proper distribution of the loans and regular repayments.

The problem of valuation is of fundamental importance in mortgage credit and the land mortgage corporation should help the primary banks by supplying them with the requisite expert staff for valuation purposes.
The primary land mortgage banks should work in close co-operation with the primary credit societies. The primary society should be consulted and its opinion obtained in the case of a loan application received from a member of the society. The primary societies may also assist the primary land mortgage banks in recovering their loans.

Until the establishment of primary land mortgage banks in their areas, the district central banks should transact business of this kind and obtain all the funds required from the land mortgage corporation. Where district central banks do not exist and the work is done by branches of the state co-operative bank as in Bombay, they should transact the business with funds provided by the land mortgage corporation. There should be close coordination between the primary banks and the central organisation. As the primary banks will be mainly depending upon the land mortgage corporation for their finance, it will be desirable to have on their Board of Management, a representative of that institution.

In a large number of countries, successful mortgage banking systems have been built up by government and it is generally admitted that the cost of an official or a quasi-official system and its efficiency compare favourably with the activities of private finance. Even in the more advanced countries, co-operative finance departs to a substantial extent from the strictly co-operative pattern. Co-operative mortgage banking is inadequately developed in India and stands in need of state backing. In our scheme, as has been indicated previously, the finance of all whose debts have been adjusted must be necessarily taken up by the land mortgage institutions. Thus there is a little doubt that for making available mortgage finance on a country-wide scale, it would be best to resort to a state agency which alone could raise the necessary funds.

**ROLE OF THE RESERVE BANK:**

The role of the Reserve Bank in the scheme of agricultural
credit is indeed very important. The Reserve Bank has been providing increasing financial accommodation to the apex institutions which in turn pass on the funds for distribution to the cultivators. The Reserve Bank itself has pointed out and perhaps rightly that the functions of the Bank are more to create monetary conditions under which commercial banks, co-operative institutions and private agencies would operate on sound and economic lines rather than supply credit itself. The Bank is expected only to be a lender of the last resort both with regard to commercial and with regard to agricultural finance. While predominantly interesting itself in maintaining satisfactory monetary credit conditions and creating a sound system of rural finance through advice, direction, technical assistance and co-ordination, the Reserve Bank has come forward to provide normal finance required by co-operative banks for financing seasonal agricultural operations and marketing." But even the Reserve Bank has limitations and cannot assume the responsibility of providing all the financial requirements of the agricultural industry in this limited field of seasonal production and marketing finance of the whole country.

The financial assistance rendered by the Reserve Bank depends as we have noted, on the financial strength and soundness of the co-operative institutions. The Reserve Bank certainly cannot pump into them funds on a scale consistent with the needs of the agricultural industry.

The recent amendment to the Reserve Bank Act has enabled the Reserve Bank to make medium term advances up to a limit of Rs.5 crores to the co-operative movement.

The Reserve Bank should subscribe to the share capital of the land mortgage corporations in the states and should take up debentures of the land mortgage corporations up to the value of 25%. The Reserve Bank may also undertake to float the debentures of the
land mortgage corporations on their behalf. It should study the conditions in the money market and advise the land mortgage corporation as to the most suitable time for floating the debentures at the lowest possible rates of interest.

With the development of the co-operative movement in all states the Reserve Bank as the pivotal organisation is destined to play a much bigger part in the provision of rural finance.

The conclusion may be briefly stated. Co-operative endeavour in all forms is the best and the most lasting solution for the problems including the provision of rural finance. But the co-operative movement has made limited progress in the country. However, the gains must be consolidated and fresh efforts must be made to forge ahead. In order to accelerate the pace of development, increased governmental aid is necessary. A state-cum-co-operative system of rural finance therefore seems to be the best arrangement.

The Planning Commission has indeed emphasised the part played by the co-operatives and has recommended that for achieving the targets in the plan "it is necessary that a detailed plan of agricultural finance and co-operative development should be worked out by every state in consultation with the leaders of the movement, the Reserve Bank and the Central Government."