CHAPTER I
INTRODUCTION

Agriculture is the major source of income for 80 percent of the rural population in India and it supports 72 percent of her work force.\(^1\) Its percentage share in the net domestic product was 55.36 in 1950-51; 51.42 in 1960-61; 49.2 in 1970-71; 38.6 in 1980-81 and 37.6 in 1983-84.\(^2\) It contributed 41 percent of the total exports in 1950-51; and 38 percent in 1973-74.\(^3\) Diversification of Indian exports has led in recent years to the decline in the shares of agricultural commodities in export. Agriculture has been supplying manpower to industry; landless rural labourers


\(^2\)Based on:


are largely engaged in constructional works, transport, trade and other service activities in urban centres. As Johnston and Southworth observed, in developing countries, "as the largest sector of the economy, at least in the earlier stages of development, agriculture is the source of manpower for industrial expansion, of essential supplies for maintaining a growing industrial population and of exports to be traded for industrial goods, ..."⁴.

In India, the expected growth of labour force by an additional 273 millions by 2000 A.D. would not find additional employment in industrial sector as its "pattern does not promise any significant structural transformation and large scale transfer of population from rural to urban activities".⁵ So, the agricultural sector should play a vital role in creating employment through diversification of economic activities. As the Sixth Plan rightly points out: "Agriculture is an instrument for income and employment generation; when (its) productivity improves, it would be possible to generate more diversified opportunities for employment".⁶


In India, production of raw materials like cotton, jute, leather and leather products, dairying, vegetable oils, tea and coffee, on a large scale would avoid the import of the same for the continuous functioning of agro and agri-based industries. Further, diversification of farm production activities with animal husbandry, fisheries and horticulture would increase the income of the small and marginal farmers and landless agricultural labourers in tune with the objective of "growth with social justice".  

Viewed from the angle of employment, income generation and export promotion, agriculture has a vital role to play in India's economic development. Favourable agricultural base would thus, be the prime cause for the take-off of the Indian economy as it was in the western advanced countries in their economic development.

**GROWTH PATTERN OF INDIAN AGRICULTURE**

There were three distinct phases in the growth of Indian agriculture. The first phase (1900-1947) was a period of near stagnation with an annual growth rate of

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0.3 percent. The second phase (1950-1980) witnessed the process of modernisation. In the third phase since 1980 the emphasis has been on marketing, trade and institutional frameworks to aid small and marginal farmers in reaping maximum benefits from intensive agriculture.\footnote{Sixth Five Year Plan, 1980-1985, op.cit., pp. 97-98.}

The First Five Year Plan (1951-56) had the introduction of the Japanese method of paddy cultivation. The Community Development Programme and National Extension Service Programme further aided agricultural production. Agricultural strategy was to introduce "science and technology" in farming through Intensive Agricultural District Programme (I.A.D.P.) on a pilot basis in 1961, followed by Intensive Agricultural Areas Programme (I.A.A.P.) in 1964-65 and High-yielding Varieties Programme (H.Y.V.P.) in 1966. These schemes were later extended for the country as a whole. To supplement these measures the Government had undertaken the policies of land-reform, procurement of food grains and distribution, and institutional measures for supply of the organised credit to agriculture. Of these, institutional credit arrangements are of vital importance in revitalising Indian agriculture.

**IMPORTANCE OF INSTITUTIONAL CREDIT FOR AGRICULTURE**

Indian experience during the Five Year Plans suggests, that agricultural improvement can be achieved through
intensive and integrated crop-livestock system of farming; preservation and augmentation of resource endowments of the agricultural sector through proper land development measures; increased utilisation of technical inputs like fertilizers and mechanical devices; and enhancement of the technical knowledge of the farming community. This requires use of inputs produced off-farm and consequently huge cash expenses.

With the vicious cycle of low productivity, low income, low saving and low investment in operation, farmers are not able to make investment necessary to adopt new technology. So, they are compelled to borrow. Hence provision of sufficient and timely credit at fair interest rates is an integral part of the Plan. What Nicholson observed as early as in 1895, that "the history of rural economy, alike in Europe, America and India, has no lesson more distinct than this, that agriculturists must and will borrow" is true even today. "This necessity is due to the fact that an agriculturist's capital is locked up in his land and stock, and must be temporarily mobilized; hence credit is not necessarily objectionable, nor is borrowing necessarily a sign of weakness".


For modernising agriculture, Indian farmers require credit for the following purposes:

i) for the purchase of operating inputs like seeds, feed, fertilizer and pesticides by the marginal and small farmers operating 73 percent of the agricultural holdings;

ii) for the adoption of modern farm technology with high yielding varieties of crops along with the complementary inputs;

iii) for undertaking permanent farm improvement measures like well digging and deepening, tube well construction and for addition of livestock;

iv) for matching "cash inflows and outflows," and to smooth out the fluctuations in farm income and expenditure;\(^\text{12}\)

v) for avoiding "distress sales" and to continue their farm operations; and

vi) for meeting their past obligations.

Thus, to quote Paul, "Immense number of farmers in developing countries need credit for subsistence during certain seasonal periods; and almost all farmers need credit when they start adopting new methods for which supplies and tools are required."\(^\text{13}\)


The Agricultural credit machinery in India having agriculture as the base industry would have to act as a "catalyst" in the promotion of agriculture through not mere supply of credit but also creation of suitable conditions to induce farmers to absorb and use the credit to augment production and productivity resulting in incremental income, employment and output. Such a sound institutional credit machinery has certain attributes as follows.

Adequacy

Loans given must take care of both production and consumption needs of farmers. As the Rural Credit Survey Committee observed that "while providing adequately for essential items of consumption, its main concern should be with loans for production", 14 The Sivaraman Committee reiterated that "Credit has to be adequate, neither more nor less. In the case of the poorer groups, there has to be a provision for consumption component in the loan to enable them to meet their family needs till the sale of crops/products". 15


Duration

The duration of loan should be related to the purpose of the loan. The repayment period should coincide with the income flow from investment made with the help of the loans. As Louis Tardy pointed out a sound agricultural credit system was one in which credit, "should be granted for a sufficiently long period, commensurate with the length of the operation which it is designated to facilitate".16 Besides, there should be provision to extend the repayment period on genuine grounds such as crop failures (due to floods, droughts and pest menace).

Security

Agricultural credit in the past was linked with the offer of adequate security to avoid any abuse of credit facilities. This denied credit to most of the small farmers. Therefore, the All India Rural Credit Survey Committee stated that the type of security would be such to accommodate a large number of solvent farmers based on expected income.17 So, the credit worthiness of the person should be the basis


17Report of the Committee of Direction, All India Rural Credit Survey, loc.cit.
of credit as recommended by the Sivaraman Committee. This would be a boon to the marginal and small farmers.

Cost

The institutional system of credit would charge reasonable rate of interest falling within the repaying capacity of farmers, leaving enough to add to their equity capital.

Proximity

A close contact between the lending agency and the borrowing farmers is an attribute of a good credit system. As Dubhashi indicated, the change of traditional agriculture into a modern one should require the total involvement of the credit agencies and other institutions of the modern sector. Such a proximity, as Dutt observed, would create a "complete understanding of not only its need for finance but also of its problems and potentialities." It would provide opportunities for the identification of proper

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18 Report of the Committee to Review Arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD), op.cit., p. 25.


beneficiaries, formulation of suitable schemes for different borrowers in different areas, to ascertain the actual credit requirement of borrowers, to arrange for the delivery of credit in suitable form, and in time, to ensure its end-use, and to share thoughts with the borrowers.

In the absence of such a proximity, the Sivaraman committee pointed out that, "...lending may become facile, burdening the borrower with debt, and the institution with overdues." This warrants the location of suitable credit-agencies among the villages and manned by dedicated persons to achieve the national goal of increased productivity and production.

Coordination

The credit system should ensure internal coordination among different institutional agencies providing short, medium, and long term loans and also between credit system and non-credit system for providing marketing and processing facilities to the cultivators.\textsuperscript{22}

\textsuperscript{21} Ibid., p. 28.

\textsuperscript{22} Report of the Committee of Direction, All India Rural Credit Survey Committee, loc.cit.
Supervision

Since the majority of the rural people in India are illiterate, they lack technical knowledge of modern farming. The mere supply of credit to them without adequate technical guidance would prove to be futile. As Johnson and Johnson, opined, "in under-developed countries, the improvement of farming to increase the productivity and standards of living of rural people can be fostered by a programme of supervised credit." 23

Continuity

Changes in the farmers' attitude towards modern farming methods would be a long run process paving way for agricultural development. This long drawn process needs continuous flow of credit—short, medium and long-supported by adequate technical guidance. Therefore, the credit institutions should have suitable arrangements for raising funds and develop in-built financial capacity to have continuous credit flow even in the event of non-repayment of loans due to vagaries of nature or price fluctuations.

In India, the development of institutional system of rural credit began with the then Government lending to

the farmers through the Land Improvement Loans Act of 1883 and Agriculturists Loans Act of 1884. However, a more formal, and permanent institutional system of agricultural credit came into being in India with the enactment of the Cooperative Credit Societies Act of 1904. As the Royal Commission on Agriculture (1926) observed, "the salvation of the rural masses from their crushing burden of debt rests in the growth and spread of a healthy and well-organized cooperative movement...Cooperative credit provides the only satisfactory means of financing agriculture on sound lines." This was also highlighted by the All-India Rural Credit Survey Committee (1951-52) when it recommended the cooperative society as the suitable credit agency for villages. This marked the beginning of institutional credit to farmers.

The present three-tier system of cooperative institutional structure for short and medium term loans and a separate cooperative institutional set up for long term loan come to be permanently established in the late thirties. But the cooperatives could not meet even one-tenth of the credit needed by the farmers in 1951-52 as estimated by All India Rural Credit Survey Committee (1951-52). This led to the

intensification of the cooperatives' credit activities during the First Three Five Year Plans. Despite intensive efforts, the institutional sources met only 18.70 percent (cooperatives 15.5 percent) of credit needs of farmers in 1961-62.  

In 1969 the Government made a significant shift away from a single agency approach to the multi-agency approach involving commercial banks on a large scale in the provision of institutional agricultural credit. Commercial banks, which were following urban-centred lending policy, were to involve in the process of rural development through their lending to the priority sector. A mandate to this effect was given by the Nationalization of 14 major commercial banks in July, 1969 and another six banks in April, 1980. Subsequently, the regional rural banks were established in 1975 to focus special attention on the marginal and small farmers, agricultural labourers and rural artisans.

Thus, today in India, there are three institutional agencies namely cooperatives, commercial banks and regional rural banks, extending agricultural credit to

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RURAL FINANCE - INSTITUTIONAL SET-UP

I National Level
- Reserve Bank of India
- Government of India
- Industrial Development Bank of India
- National Cooperative Development Corporation
- Commercial Banks
- Sponsoring Bank
- State Cooperative Banks
- State Government
- Local/Regional Offices
- Regional Rural Banks
- Regional Banks
- Central Cooperative Banks
- Primary Agricultural Credit Societies
- Primary Land Development Banks

II State Level
- Borrowing beneficiaries - Farmers, Agricultural Labourers and others

III District Level
- Commercial Bank Branches
- Regional Rural Bank Branches
- Short, medium and long-term credit

IV Primary Level

N.B.: This diagram is based on the Committee's Report on the Arrangements for Institutional Credit for Agriculture and Rural Development (CCFICARD), Reserve Bank of India, Rural Planning and Credit Cell, 1964, p. 32.

1) Sources:
- 1 and 2 Re-financing of short, medium and long-term loans to the Cooperatives and the Regional Rural Banks.
- 3 The above re-financing for special purposes.
the farmers for various farming and allied activities. Credit is now being provided based on the credit-worthiness of the purpose and expected generation of income replacing the security-oriented non-institutional system of lending.

The chart flow diagram depicts the current structural pattern of the farm credit lending institutional agencies in India (Diagram I).

**STATEMENT OF THE PROBLEM**

As agriculture and allied activities constitute the major sector of the rural economy, development of the Community Development blocks depends upon the support they can extend to agriculture. Nationalization of 20 major commercial banks since 1969, the subsequent introduction of Lead Bank Scheme, starting of the regional rural banks in 1975, and the setting up of the National Bank for Agriculture and Rural Development (NABARD) in 1982 as the linking and coordinating agency of all lending institutions to agriculture have facilitated the provision of financial support to the rural development schemes on a priority basis. There has been thus, an impressive growth in the number of agencies and the volume of credit serving agriculture. Time has come now to make an objective assessment of progress and prospects of institutional
credit to farm sector. More specifically, "the major issues for examination are the quantitative and qualitative expansion in credit supply resulting from the increase in the different types of credit agencies operating in the rural areas." Against this background, the present study entitled, "A Study on the Extent of Flow of Institutional Credit and its Impact on Agricultural Development in Annur Block of Coimbatore District" is undertaken.

OBJECTIVES OF THE STUDY

The specific objectives of the study are:

i) to assess the supply of farm credit in terms of size, composition, source of supply and adequacy vis-à-vis the requirements of the farmers;

ii) to assess the extent of overdues and causes there of;

iii) to assess the impact of credit in terms of returns per rupee, per hectare, repayment capacity, risk-bearing ability and productivity gains; and

iv) to identify the strategies for the expansion of supply of institutional credit to farm sector to serve as an instrument of agricultural development.

HYPOTHESES OF THE STUDY

The above mentioned objectives would suggest the following hypotheses:

1) Credit is *sine-qua-non* for farm production;

2) Expansion of institutional credit substituting non-institutional credit results in more efficient use of credit by farmers;

3) There is scope for improving gains from supply of credit to farmers through changes in pattern and procedure for lending; and

4) Efficient use of credit depends also upon the availability and use of complementary inputs like technical advice, irrigation, and policy support for input supply and marketing of products.

SCOPE OF THE STUDY

The study focuses attention on the supply of and demand for institutional credit and its impact on agricultural development at the block level (macro level). It throws light on the farm assets, farm income, credit requirements and other complementary aspects at the farmers' level (micro level). These macro and micro aspects of the study would bring to lime-light the targets and achievements of credit plan by Lead Bank Scheme at the block level, credit requirements of different groups of farmers for permanent farm improvements in future, productivity gains, returns, repaying capacity, risk-bearing ability, and overdues. Hence the findings of
the study would be useful to the Lead Bank in general, especially in Coimbatore district to plan for credit on more realistic basis. Besides, it would be useful in policy-framing with regard to distribution of credit among different groups of farmers and villages for various agricultural purposes by different institutional agencies and the Government.

LIMITATIONS

The study had covered both micro and macro aspects of institutional credit for agriculture but only at block level i.e., Annur block. All credit institutions (located inside and outside the block) extending credit to Annur block were covered. The collection of secondary data were subject to the following limitations: (i) for accounting purposes, different institutions followed different year systems such as the cooperative year in cooperatives, calendar year in commercial banks, and financial year in Government departments. For the purpose of analysis in this study, the cooperative years namely 1978-79; 1979-80; 1980-81; 1981-82 and 1982-83 and the financial years namely 1978-79, 1979-80, 1980-81, 1981-82 and 1982-83 had been treated as 1979, 1980, 1981, 1982 and 1983 respectively; (ii) purposewise details of defaulters and overdues were not available in cooperatives and Government departments; (iii) beneficiary groupwise details of agricultural jewel
loans were not attempted in the study; and (iv) outstandings of the agricultural credit at the year end for Annur block were not available from the Avanashi Primary Land Development Bank and the commercial banks. Primary data were collected from 220 sample farmers for the agricultural year, 1982-83 only. They provided the data by recalling from their memories with all its limitations. It was a location oriented study as it was confined to Annur development block with its specific agro-climatic conditions. Therefore, the conclusions of this study should be generalized, with care and attention to the basic conditions.

PLAN OF THESIS

The thesis is arranged into five chapters as follows:

Chapter I - This chapter presents the place of agriculture in the Indian economy, growth pattern of Indian agriculture, importance of institutional credit for agriculture, statement of the problem, objectives, hypotheses, scope and limitations of the study.

Chapter II - This chapter has three sections namely (i) concepts; (ii) history of rural credit in India; and (iii) past empirical studies.
Chapter III - This chapter describes the methodology followed in the present study.

Chapter IV - Results of the study are presented and discussed in three sections: (i) descriptive account of the study area; (ii) analysis of the secondary data; and (iii) analysis of the primary data.

Chapter V - Summary of the results and conclusions of the study are presented, and policy and research implications are listed.