CHAPTER III

CO-OPERATIVE CREDIT STRUCTURE IN INDIA

The Co-operative Credit Sector forms a part of the organised component of the Indian Money Market. Here is attempted to present a picture of the organisational structure of credit institutions meeting the short-term and long-term credit requirements of Indian peasants. For the purpose of pinpointing the place of the District Central Co-operative Banks in the organisational hierarchy of the co-operative structure in India, the whole chapter is divided into three sections. The first section points out the place of co-operatives in the Indian Money Market, the second section, the place of co-operatives in the network of rural financial institutions and the third section, the place of DCCBs in the co-operative credit structure in India.

Section - I

Place of Co-operatives in the Indian Money Market:

The Indian Money Market (IMM) may be divided into two broad sections:

(1) Unorganised Sector, and
(2) Organised Sector.
The unorganised sector we take as that sector which operates outside the provisions of the Indian Banking Companies Act and maintains private accounts which are not audited. The organised market, contrawise, works within the provisions of the Banking Companies Act and maintains accounts which are subjects to audit and regular inspection. The following are the main features that differentiate the unorganised sector from the organised sector of the money market:

(a) blending of money lending with other types of economic activities;
(b) informality in dealings with customers;
(c) personal contact with borrowers;
(d) simple system of maintaining accounts;
(e) flexibility of loan operations; and
(f) secrecy about financial transactions.

The unorganised money market includes (i) Indigenous bankers, (ii) Money lenders (both professional and non-professionals), (iii) Midhis, and (iv) Chit Funds. Money lenders are those whose primary business is not banking but

money lending. The indigenous bankers combine both banking and business; but in their case, banking is the primary business. While indigenous bankers accept deposits and deal in hundis (which are indigenous bills of exchange), money lenders generally do not accept deposits from the public nor deal with hundis but are primarily concerned with the business of money lending. Nidhis are mutual loan associations. Chit funds are loose voluntary associations for mobilising rural savings. Nidhis and chit funds are seen in many parts of South India, particularly in the State of Tamil Nadu. The classification of different agencies which constitute the unorganised sector of the Indian Money Market is presented in Chart III.1:

(vide next page)
The organised or institutional money market consists of commercial banks - both scheduled and non-scheduled, co-operative banks, Land Development Banks, Reserve Bank of India, State Bank of India, Regional Rural Banks, etc. This sector of the money market is regulated and controlled by the custodian of the money market, i.e., the Reserve Bank of India. It is characterised by specialisation in borrowing and lending activities, by formal dealings with customers, by impersonal business-like relations with customers, by comprehensive system of accounts, by loan operations strictly according to rules, and by lack of secretiveness of financial transactions.3

Thus, from the foregoing discussion, it is clear that the co-operative credit institutions constitute one of the important constituents of the organised component of the Indian Money Market. The place of co-operatives in the organisational structure of financial institutions in India is shown in Chart III.2:

(vide next page)

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3 Desai, S.S.M. - Rural Banking in India, HPH, Bombay, 1979, pp. 44-45.
CHART 111-2.

STRUCTURE OF FINANCIAL INSTITUTIONS IN INDIA.

UNORGANISED.

MONEY LENDERS
INDIGENOUS BANKERS
CHIT FUNDS
NIDHIS.

ORGANISED.

MONEY MARKET.

COMMERCIAL BANKS
REGIONAL RURAL BANKS
CO-OPERATIVE CREDIT SOCIETIES

RESERVE BANK OF INDIA/ NATIONAL BANK FOR AGRICULTURE & RURAL DEVELOPMENT

CAPITAL MARKET.

INVESTMENT TRUSTS
LAND DEVELOPMENT BANKS
COMMERCIAL BANKS

POSTAL SAVINGS BANKS

NOTE:— I.F.C.I. STANDS FOR INDUSTRIAL FINANCE CORPORATION OF INDIA.
Section - II

Institutional Rural Credit Structure and the Place of Co-operative Institutions:

It was at the beginning of the present century that the institutional credit system was started with the organisation of co-operative credit societies. The co-operative credit system got further fillip in the mid-fifties in the wake of the recommendations of the AIRCSC Report (1951). After examining all the pros and cons of the problem of agricultural credit and the urgent need for complete institutionalisation of agricultural finance, the AIRCSC came to the conclusion that the long-term solution of the problem could be found in the continuous strengthening and development of the co-operative credit institutions which eventually should meet the entire requirements of both production credit and investment finance. Even while making this recommendation, the Committee was quite conscious of the structural and other deficiencies observed in the functioning of co-operatives. Even then they did not visualise any other alternative institutional agency and desired that the co-operatives should alone be developed, as the sole institutional agency for agricultural finance. It is with this end in view that the Committee recommended the adoption of "Integrated Scheme of Rural Credit". The integrated scheme contemplated the strengthening and
development of co-operative credit institutions at all levels, based on the principles of state partnership (including financial partnership) throughout the federal structure, comprising State co-operative banks at the state level, district co-operative banks at the district level and large-sized primary agricultural credit societies at the village level. The second component of the integrated scheme was a co-ordinated development of agricultural processing, storage, warehousing, marketing, etc. The third ingredient of the scheme was the management and administration of the co-operative movement by qualified, competent and well-trained personnel.

Multi-Agency Approach to Rural Credit:

Following recommendations of the AIRCSC, the GOI, the RBI and the State Governments made special efforts to foster the growth of the co-operative movement. However, co-operative credit could not be developed uniformly in all parts of the country. Pari Passu, the credit needs of the agricultural sector, which were the primary concern of co-operative, increased rapidly due to principally the biological and technological developments in crop and animal husbandry. Commercial banks were, therefore, inducted into the field of agricultural credit under the
policy of 'social control' over banks in 1967. After nationalisation of 14 major scheduled commercial banks in July 1969, the process was carried further. As the AIRCRC report put it in 1969:

"At the same time, effort in the sphere of rural credit should not be solely concentrated in the co-operative sector. Co-operatives should be strengthened, but they would be all the better - and the farmer better served if other institutions co-existed with them in healthy competition". (p.411).

This approach which has come to be known as the 'Multi-agency Approach' provides for the commercial banks serving as an additional source of credit to the rural sector. The essence of Multi-agency Approach lies in defining the respective roles of co-operative lending institutions and commercial banking institutional agencies and finding ways of bringing about effective co-ordination in the lending and other related operations of various institutional agencies.

Farmers' Service Societies (FSSs):

For all the agricultural development schemes where

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participation of the small farmers, marginal farmers and agricultural labourers is contemplated, the first essential input factor is credit in the right quantity at the right time for the creditworthy scheme. The second essential factor is supply of inputs of services at reasonable rates at the right time. The third is a fair market where the small men will get a reasonable price for the surplus, and will also be able to buy his requirements at a fair price. The real need of the small and marginal farmers is, thus, not funds alone but timely availability of a package of inputs and services, along with technical advice and supporting services for storage, transportation, processing and marketing, preferably through a single contact point.

It is in the above context that the National Commission on Agriculture (1971) recommended the institution of Farmers' Service Societies, a promising institutional innovation for making specific arrangements at the ground level for the conversion of credit into inputs and services. The Commission felt that the banks and other financial institutions would have to take direct interest in the development of organisations for the supply of inputs and to arrange for custom services, storage, transportation, marketing, etc. The Commission, therefore, proposed that
the farmers' service societies be formed for the purpose of integrating credit function with the supply of inputs and services. The Farmers' Service Society is not merely a modified credit society drawing its funds from the commercial banks rather than from the district central co-operative bank. In fact, either a commercial bank or a district central co-operative bank can launch a Farmers' Service Society. The uniqueness of the concept lies in the stress on integrating the credit function with the function of organising the availability of inputs and services for land development, construction of wells, godowns and roads and hiring of farm equipment.

All the credit requirements of the members will be met by the FSS. The farmers need not go to other agency even for medium-term or long-term needs. Besides the credit function, the FSS will also take up the business of supplying inputs and services at reasonable prices, so that credit gets converted into inputs and repayment is ensured by way of having a direct influence over the use of credit. The FSS may directly enter marketing or may enter into a contract with the principal manufacturers and distribution organisations for all manufactured inputs for farming, including fertilisers, pesticides and equipment for
cultivation and harvesting. It may also undertake certain other services, such as use of tractors on hire, spraying of insecticides, maintenance of pumping sets or field advice regarding the use of fertilisers.

In short, the uniqueness of the FSS, thus, lies in the total responsibility it assumes for the farming operations of all its members, including small and marginal farmers and local artisans. It provides an element of organisation and joint action that enables the small farmers as a group to overcome the handicaps of smallness.

**Large sized Adivasi Multi-Purpose Co-operative Societies (LAMPS):**

In pursuance of the recommendations of the Study (Bawa) Team appointed by the Government of India in December, 1971, LAMPS were organised in tribal areas with the objects of:

1. Providing under a single roof, all types of credit including these for meeting social obligations and consumer requisites;

2. Technical guidance in the intensification and modernisation of agriculture; and
(iii) arranging for the marketing of agricultural and minor forest produce, besides the products of other subsidiary occupations of the tribals.

Like the FSS, these societies are expected to cover larger areas of operation than the PACS.6

Agricultural Refinance and Development Corporation (ARDC):

The Corporation was set up by an Act of the Indian Parliament and started functioning from 1st July, 1963. The Corporation has been conceived of as an agency (now NABARD from July 12, 1982):

(i) to supplement the resources of institutional agencies for provision of medium and long-term loans for agricultural investments in the country;

(ii) to reorient the policies and procedures for term-lending for agricultural investments for making them responsive to growth-oriented lending; and

(iii) to refine projects with large outlays which cannot be financed by the existing institutional set-up.

The Corporation had been functioning as a Development Bank for agriculture in the country. In order to emphasize the promotional and developmental role, it had been renamed as the "Agricultural Refinance and Development Corporation" with effect from November, 1975.

The ARDC provided refinance assistance to a wide range of activities for the development of agriculture and other matters connected therewith or incidental thereto. The major single purpose of investment refinanced related to minor irrigation covering both ground water and surface water exploitation, such as construction of wells, tube wells, installation of pumpsets, lift irrigation units, etc. Besides, land development, soil conservation and water management schemes were also eligible for refinance. Under diversified lending, the emphasis was on animal husbandry schemes like dairy development, poultry farming, sheep breeding and piggery which serve as important subsidiary occupations to small and marginal farmers.

Commercial Banks and Rural Finance:

The first effort to involve a commercial bank in rural credit began with the conversion of the Imperial Bank of India into the State Bank of India in accordance with
the recommendation of the Rural Credit Survey Committee Report (1954) which proposed that "the new institution should draw up, in collaboration with the Reserve Bank, and undertake a much larger programme of branch extension to rural areas". It was only after the Government's policy of social control over commercial banks in 1967 and the bank nationalisation in 1969, commercial banks as a class began to enter into the rural sector in a big way. The Indian Banks' Association (IBA) promoted the Agricultural Finance Corporation Ltd., with a view to speeding up project lending by commercial banks in the agricultural sector in 1967. Further, commercial banks endeavoured to increase their direct involvement in rural credit firstly, by rapid expansion of branches in the rural and semi-urban areas, and secondly, through a number of operational renovations such as establishing specialised branches exclusively or mainly oriented to farm lending, intensifying their efforts in specific areas under the village adoption scheme, linking up their lending to schematic programmes under Five Year Plans with the assistance of the ARDC, taking over PACSs and organising FSSs. The banks have made serious efforts to move nearer to their clientele in the rural sector and to serve them better. In this, they have been additionally assisted by the Lead Bank Scheme (LBS) and setting up of RRBs in
In 1975, Government of India appointed a Working Group under the chairmanship of Shri M. Narasimhan to review the flow of institutional credit, especially to the weaker sections of the rural community. The Group identified certain deficiencies in the role of the two major agencies in the field, the co-operative credit institutions and the commercial banks. It also came to the conclusion that the regional and functional gaps in the rural credit cannot be met within a reasonable period by reorganising or restructuring the two systems. At the same time, it recognised certain commendable features in both the systems which could be combined in a new type of institution.

The Working Group, therefore, recommended the setting up of State-sponsored, regionally-based and rural-oriented banks called Regional Rural Banks (RRBs). They were meant to combine the local feel and familiarity with several problems which the co-operatives possess and the degree of business organisation, ability to mobilise deposits, access to central money market and a modernised outlook which the commercial banks have. Accepting this recommendation, the GOI promulgated the RRBs Ordinance on 26 September 1976 and

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the first five RRBs were established on 2 October 1975. 

RRBs, thus, came to form the third component of the multi-agency credit system for agricultural and rural development.

RRBs are sponsored by scheduled banks, usually a public sector commercial bank. The Steering Committee on RRBs (now in the NABARD) identifies the districts requiring RRBs and later the GOI in consultation with the State governments and the sponsor banks proceeds to set up RRBs. RRBs are visualised as the rural arm of the commercial banks.

The major objective of the RRBs is to develop the rural economy by providing credit and other facilities for agriculture, trade, industry and other productive activities in the rural areas, particularly to the small and marginal farmers, agricultural labourers, artisans and small entrepreneurs.

The NABARD — as an Apex Refinancing Institution of Rural Finance:

The Committee to Review Arrangement for Institutional Credit for Agriculture and Rural Development (CRAFCARD) set up by the RBI in consultation with the GOI in 1979 under the chairmanship of Shri B. Shivaram felt that there was a need for a new organisational device for providing undivided attention, forceful direction and pointed focus to the
rural credit problems arising out of integrated rural development. The Committee, therefore, suggested a new bank, viz., the National Bank for Agriculture and Development (NABARD) to operate as an apex institution within the complex of the RBI.

The bank has been conceived as an exercise in decentralisation of RBI's functions in the sphere of rural credit. It has been envisaged not only as a sole refinancing agency but also as the leader of the entire rural credit system in the country. Not only the ARDC is assimilated in NABARD but most of the functions of the agricultural credit department and rural planning and control cell of the RBI have also been transferred to it, leaving the matters relating to credit and monetary policy with the RBI.

NABARD shall be responsible for the development, policy planning, operational matters, co-ordination, monitoring, research, training and consultancy, etc., relating to rural credit. It shall provide refinance to the cooperatives and the RRBs for short, medium and long-term requirements not only for credit but also for marketing and distribution arrangements and to the commercial banks against term-lendings. It will also take care of the
refinancing and other facilities for the rural industries, handicrafts and artisans, etc. It will also undertake inspection of the co-operative banks and RRBs and advise the state governments and Federation of Co-operatives, etc., regarding co-operative movement in the country.

It would have organic links with the RBI by virtue of the latter's holding 50 per cent of its share capital at any time, the other 50 per cent being held by the GOI.

The place of co-operatives in the network of rural financial institutions is shown in Chart III.3:

(vide next page)

Agricultural Credit Delivery System.

Short-Term & Medium-Term Agricultural Credit System

National Bank for Agricultural & Rural Development

Commercial Banks

State Cooperative Banks

Regional Rural Banks

Central Cooperative Banks

Primary Agricultural Credit Societies, Farmers Service Societies, Large-Sized Advasi Multi-Purpose Societies

Agriculturists

Long-Term Agricultural Credit System

National Bank for Agriculture & Rural Development

Commercial Banks

State Cooperative Banks

State Land Development Banks

Central Cooperative Banks

Regional Rural Banks

Primary Land Development Banks

Primary Agricultural Credit Societies, Farmers Service Societies, Large-Sized Advasi Multi-Purpose Societies

Agriculturists
Section - III
Co-operative Credit Structure in India and the Place of District Central Co-operative Banks

The co-operative credit societies in India consist mainly of:

(a) Short-term and medium-term agricultural credit societies;
(b) Long-term agricultural credit societies; and
(c) Non-agricultural credit societies.

The organisational structure of Co-operative credit institutions and the place of the DCCBs can be seen in Chart 2.4: (vide next page).

As regards the short-term and medium-term agricultural credit societies, they consist broadly of three categories:

(i) Primary agricultural co-operative credit societies at the village level (PACSs);
(ii) Central co-operative credit societies at the district level (DCCBs); and
(iii) State Co-operative Banks (or Apex Banks) at the State level (SCBs).
(a) **Short-term and Medium-term Co-operative Credit Structure:**

The primary co-operative credit societies at the village level are federated at the district level into a central society called the District Central Co-operative Bank. At the state level, the District Central Co-operative Banks are federated into an Apex Bank. The Apex or State co-operative bank, in its turn, is closely linked with the RBI (now the NABARD), which provides considerable financial assistance to the co-operative credit structure.

(i) **Primary Agricultural Credit Societies (PACS):**

The PACSs form the base of the co-operative credit structure, and on their working depends, to a large extent, the soundness of the whole co-operative credit structure. The PACS is intended to promote the economic interests of its members in accordance with the co-operative principles, and this aim is achieved by activities in different directions such as promoting savings among members, providing loans to them, supplying them with agricultural requisites and arranging for the marketing of their agricultural produce.

Working funds of PACSs consist of share capital, membership fees, reserve funds, deposits of members and non-members, loans from DCCBs and the government donations, grants and subsidies.
(ii) **District Central Co-operative Banks**:

District Central Co-operative Banks (DCCBs) are the intermediary agency between the PACSs at the village level run by the agriculturists having no touch with the money market and the State co-operative banks run mainly from the metropolitan cities; having little direct association with the countryside. The DCCB is closer to the primary societies than the Apex Bank and, therefore, it affords opportunities to them for influencing policies to suit their requirements and enables them to train themselves in sound banking principles and practices. The DCCB's functions are:

1. to finance the affiliated PACSs;
2. to act as a balancing centre for the resources of PACSs;
3. to attract local deposits;
4. to supervise the working and management of the affiliated PACSs;
5. to train the members of PACSs in the principles of co-operation;
6. to provide a safe place for investing the reserve of the PACSs; and

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(vii) to help the development of the co-operative movement on sound lines in the area of its operation.

The important constituents of the composition of the working capital of the DCCBs are:

(i) share capital,
(ii) undistributed profits,
(iii) membership fees from PACSs,
(iv) deposits from the public, and
(v) loans from the SCB and in some cases, joint banks.

It should be noted that the Apex Bank, (i.e., SCB) is a very important source of funds for the DCCBs. When the Government or the RBI (now the NABARD) decides to provide finance to the agricultural sector, the RBI (now NABARD) passes on the funds to the SCB which in turn passes on the amount to the DCCBs which in turn lend amounts to PACSs. 9

It is, thus, crystal clear from the above description that the DCCBs, which form the middle tier in the three-tier co-operative credit structure, are the connecting links between the Apex Bank, (i.e., SCB) in a State on the one hand and the various PACSs on the other.

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(iii) State Co-operative Banks:

The constitution of a co-operative banking institution at the apex level was considered essential as early as in 1915. The Maclagan Committee (1914) emphasized the need for having an apex bank in each major province to co-ordinate and regulate the working of DCCBs. The apex bank at the State level operates as a balancing centre for the resources of the movement in the entire State. At the top of the federal structure, it derives its strength from its affiliated PACSs and gives, in return, the strength earned, as a result of its contacts with the monetary structure of the country. The apex bank provides the link between the RBI (now the NABARD) and the money market on the one hand, and the entire co-operative credit structure, on the other. It acts as the custodian of the surplus resources and the reserves of the DCCBs and supplements them by attracting sizeable deposits and by obtaining loans from the RBI (now the NABARD) and the State Government. The State Co-operative Bank, therefore, occupies a key position in the entire structure of short-term as well as medium-term co-operative credit.

The financial resources of the SCB consist of:

(i) Share capital, (ii) Deposits, (iii) Retained profits, (iv) Surplus funds of affiliated DCCBs, and (v) Loans and advances from the NABARD, the SBI, and other commercial banks.
(b) **Long-term Co-operative Credit Structure:**

The organisational structure of long-term co-operative agricultural credit, unlike the short-term and medium-term structure, is not of a uniform pattern all over the country. A majority of the states have the federal set up with the State Land Development (also called Central Land Development Bank) at the State Level and affiliated primary land development banks (PLDBs) at the district or taluka levels. In some states, the structure is of unitary type, the operational units below the State Land Development Bank (SLDB) being its branches. Credit is provided to the peasants on the security of land mortgaged to the bank. The SLDBs raise the funds required by them by issuing ordinary debentures and rural debentures. PLDBs obtain funds mainly from the SLDBs.

(c) **Non-agricultural Credit Societies:**

The non-agricultural credit societies need mainly the financial requirements of artisans and small industrialists. Though these institutions are found functioning in rural areas, they are, however, more popular in urban areas.

The position of the co-operative credit structure as on 30th June, 1980, is shown in Table 3.1 (vide next page):
Table III.1: Co-operative Credit Structure in India (end June 1980).

<table>
<thead>
<tr>
<th>Credit Institutions</th>
<th>Total Number</th>
<th>Total Membership (in 000s)</th>
<th>Deposits (Rs. in crores)</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>I. SHORT TERM AND MEDIUM TERM CREDIT:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>a) State Co-operative Banks</td>
<td>27</td>
<td>23</td>
<td>1,424</td>
</tr>
<tr>
<td>b) Central Co-operative Banks</td>
<td>337</td>
<td>264</td>
<td>1,978</td>
</tr>
<tr>
<td>c) Industrial Co-op. Banks</td>
<td>9</td>
<td>60</td>
<td>29</td>
</tr>
<tr>
<td>d) Primary Agricultural Credit Societies</td>
<td>94,592</td>
<td>54,836</td>
<td>250</td>
</tr>
<tr>
<td>e) Grain Banks</td>
<td>4,998</td>
<td>495</td>
<td>2</td>
</tr>
<tr>
<td>f) Primary Non-agricultural credit societies*</td>
<td>21,546</td>
<td>14,257</td>
<td>1,287</td>
</tr>
<tr>
<td><strong>II. LONG TERM CREDIT:</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State Land Development Banks</td>
<td>19</td>
<td>2,374**</td>
<td>25</td>
</tr>
<tr>
<td>Primary Land Development Banks</td>
<td>896</td>
<td>6,205**</td>
<td>7</td>
</tr>
</tbody>
</table>


**NOTE:** * Includes primary co-operative banks coming under the purview of the Banking Regulation Act, 1949 (as applicable to co-operative societies).

** includes nominal membership.