CHAPTER I

DESIGN OF THE STUDY

Introduction

Agriculture is the most important sector in the Indian economy. "Agriculture and allied activities constitute the single largest contributor to the Gross Domestic Product (G.D.P), accounting for almost 33 per cent of the total. They are vital to the national well-being as, besides providing the basic needs of the society and the raw materials for some of the important segments of Indian industry, they provide livelihood for almost two thirds of the work force. The share of the agricultural products in the total export earnings, both in primary and processed form, is very significant."¹

The National Commission on Agriculture (1976) emphasised that the agricultural sector has to grow at a much faster rate than before not only for its own sake, but for the sake of the

economy as a whole. Hence the prosperity of the country entirely hangs on the prosperity of the agricultural sector. If agriculture stagnates, it will act as a break on industrial expansion and halt real growth. But it is obvious that there is hardly any possibility of substantial increase in the area of cultivation. Therefore, intensive cultivation appears to be the only way to boost agriculture. The All India Rural Credit Review Committee (1969) has stated "with arable land in the country forming about 52 per cent of the total geographical area it has generally been recognised that possibilities of the future development of agriculture lay more in increasing yield per unit of land already brought under cultivation. For a breakthrough in agricultural stagnation, it is, therefore, imperative that the farmer is so stipulated and helped that the same land may be used for multiple cropping and for increasing substantially the yield per acre." 

The emergence of green revolution during late sixties

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3 All India Rural Credit Review Committee, Reserve Bank of India, Bombay, 1969, p.55.
and introduction of new agricultural technology in India, has converted the nature of agriculture. Due to these, the farmers tended towards the replacement of traditional methods of farming with scientific and developed methods. For instance, use of High Yield Variety (HYV) of seeds, fertilizers, pesticides, irrigation, machinery and equipment etc. requires huge amount of capital which is beyond the capacity of most of the farmers. Due to this the farmers compulsorily depend upon borrowed funds. This causes the increasing demand for credit. So, in respect of transformation of traditional or subsistence farming into commercial farming, the importance of agricultural credit has increased comparatively more.

The development of institutional credit is, thus, a basic condition for agricultural progress. The history of agricultural development in all advanced countries shows that an integrated system of institutional credit laid the foundation of agricultural prosperity. The objective of the institutional credit is to make a breakthrough in the vicious circle of poverty
and debt, and to stimulate the farmer to boost agricultural productivity.\footnote{Mathur B.S., Land Development Banking in India, National Publishing House, New Delhi, 1974, p.7.}

On the basis of period, credit needs of farmers may be classified as short-term, medium-term and long-term. Short-term loans are given for seasonal agricultural operations directed towards raising crops on land, including reasonable amount for the maintenance needs of the farmer and his family. These loans are given for a period of 9 to 12 months and are repayable after the crops are sold.

The medium-term loans are given for a period ranging from 12 months to 5 years for the purpose of purchasing cattle and farming implements. Long-term credit is given for a period ranging between 5 to 20 years for making permanent improvement in land. The purposes include digging and repairs of well, purchase of motors, agricultural machinery, construction of farm house and for plantations.
Importance of Long-term Credit

In the past, as agriculture was in a primitive stage, the need and necessity of long-term credit was not felt. Agriculture was considered to be a gamble and there was no certainty of assured production on account of various natural calamities. Investment in agriculture was neither adequately rewarding nor the result of investment quickly secured. These factors largely accounted for lack of adequate finance for long-term investments in agriculture.

One of the most encouraging features of the present situation is that the isolation to the agricultural sector is being rapidly broken and, in a sense, agriculture is being industrialised and commercialised. The new innovations in agricultural technology have opened up vast potentialities for development of agriculture. Now long-term credit is viewed essentially as dynamic credit in the sense that it helps the farmer to create assets on land, thereby progressively increasing

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his output and adding to the agricultural production of the country.

The demand for long-term finance has been increasing during the last few years. This is due to the increasing realisation on the part of the farmers that agriculture should be persuaded more as an industry and business, by putting more capital investment on land and increasing the production potential. The most important institutional agency providing long-term credit directly to millions of farmers is the Co-operative Land Mortgage Banks, currently known as the Agricultural and Rural Development Banks.

Agricultural and Rural Development Banks

The Agricultural and Rural Development Banks are the pioneers in long-term credit for agriculture and were established only for this purpose. Still they continue to occupy an important position and cater to the investment credit requirements of farmers. In recent years they have been expanding their activities and diversified lending portfolio not only for the activities based on agriculture, but also for non-farm sectors and
housing in rural India. Thus the scope for these banks is increasing.

The Agricultural and Rural Development Banks in Kerala have a two-tier-structure, viz., Primary Agricultural and Rural Development Banks at the primary level and State Agricultural and Rural Development Bank at the apex level. They are organised on a co-operative basis. These banks play a significant role in the long-term agricultural finance. Currently, of the total requirements of long-term agricultural credit in Kerala about 40 per cent is met by these banks. They have to provide sufficient capital to farmers at reasonable cost and at the same time, as an organisation they have to maintain a minimum level of profit. It is true that profit alone is not the main or sole motive of co-operatives. But the objective of any organisation is to increase volume, reduce cost and overheads to obtain a surplus for its strength, stability and growth.

The primary banks in Kerala are passing through a critical stage in their growth. A good number of them is running at loss and their overdues are increasing over the years (Table 1.1). The operational aspect of these banks is also not
<table>
<thead>
<tr>
<th>Year</th>
<th>Percentage of primary banks in loss</th>
<th>Percentage of overdues to demand</th>
</tr>
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<tbody>
<tr>
<td>1983-84</td>
<td>18.78</td>
<td>18.06</td>
</tr>
<tr>
<td>1984-85</td>
<td>8.82</td>
<td>19.89</td>
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<tr>
<td>1985-86</td>
<td>17.14</td>
<td>27.22</td>
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<tr>
<td>1986-87</td>
<td>19.44</td>
<td>30.60</td>
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<td>1987-88</td>
<td>18.92</td>
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<td>1988-89</td>
<td>32.50</td>
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<td>33.33</td>
<td>46.80</td>
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<td>1990-91</td>
<td>47.62</td>
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<td>1991-92</td>
<td>51.16</td>
<td>37.43</td>
</tr>
<tr>
<td>1992-93</td>
<td>48.84</td>
<td>40.04</td>
</tr>
</tbody>
</table>

Source: Government of Kerala, Hand Book on co-operative Movement, Various Issues, Department of Statistics, Thiruvananthapuram.
satisfactory and hence there is the need for a detailed study of the factors affecting the operational efficiency and profitability of the Primary Agricultural and Rural Development Banks in Kerala.

Statement of the Problem

In recent years, the profit earning capacity and funds management of the Primary Agricultural and Rural Development Banks in Kerala are under severe strain. Fifty per cent of the primary banks are running at loss. Apriory two basic reasons can be attributed for this state of affairs. One reason is the constantly increasing overdues and the second is the inefficiency in the funds management of these banks which is the result of multiple factors. Because of these problems nowadays majority of the primary banks are forced to follow the policy of restricted lending. If this situation continues it may even question the very existence of these banks. Hence the study was conducted with the following objectives.

Objectives

The objectives of the study are:-

1. To examine the funds management practices of the Primary Agricultural and Rural Development Banks in Kerala.
2. To evaluate the operational efficiency of these primary banks.

3. To study the factors affecting profitability and to examine its relation with the overdues.

4. To analyse the structure of overdues in these primary banks.

5. To identify the determinants influencing overdues.

6. To identify the operational and managerial problems of the Primary Agricultural and Rural Development Banks.

The major hypotheses of the study are the following:

1. There is an inverse relationship between profitability and cost of management of the Primary Agricultural and Rural Development Banks.

2. Quantum of overdues and the rates of profit are inversely related.

3. Wilful default of the beneficiaries is the major reason responsible for mounting overdues.

4. Cost of management continuously increases due to the constant increase in the establishment charges.
Scope of the Study

The scope of the study is limited to the selected Primary Agricultural and Rural Development Banks in Kerala and it mainly concentrates on three important aspects:

1. The efficiency and effectiveness of the funds managed
2. The structure of overdues
3. The reasons and factors affecting overdues and its impact on profitability.

Methodology

The Primary Agricultural and Rural Development Banks and their defaulters constitute the universe of the study. On 31st March 1991 there were 42 primary banks in the State. Of these, 10 banks started functioning only after 1983, i.e., during the study period. The Perinthalmanna Bank was working with an overdue of 80 per cent and was in loss for all the years because of special lending to Adivasi Project of the State Government. Hence these banks were left out while selecting the sample banks.
The National Bank for Agriculture and Rural Development (NABARD) divides the primary banks into different categories on the basis of the percentage of overdues. But the norm followed by the NABARD is inconsistent due to frequent revisions (Appendix I). So for the present study the primary banks were grouped into three, as those banks which have overdues less than 20 per cent, those between 20 per cent to 40 per cent and those between 40 per cent to 60 per cent. The number of banks in group I is nine, in group II twelve and in group III ten (Appendix II). From these three groups two banks each were selected. While selecting these banks due consideration was given to have representation to different districts and banks with different volume of funds. The selected primary banks in group I are Irinjalakuda and Tirur, in group II Thodupuzha and Ernakulam and in group III Kozhikode and Thiruvananthapuram.

For the purpose of the study altogether 300 defaulters were selected from these six banks. The sample was taken by categorising the defaulters into three: small farmers with land area less than 1.50 acres, medium farmers with 1.51 to 2.50 acres...
and large farmers having more than 2.50 acres. Landholding in Kerala is comparatively low in relation to other states in India and larger number of lending is to those farmers below 1.50 acres. So the number of defaulters selected from small farmers was 150, medium 90 and large 60. Thus from each bank a sample of 50 defaulters were selected maintaining the same proportion of different farm size of defaulters. For the selection of the sample, a list of defaulters dividing them into small, medium and large were taken from the selected banks as on 30th June 1992. While drawing the sample due care was given to select the defaulters who have taken loan under different schemes through stratified random sampling. The defaulters in the schemes of non-farm and rural housing were not included in the survey as they were introduced recently and not directly related to agricultural activities.

Period of the Study

The study is restricted to 10 years, i.e., from 1983-84 to 1992-93. This is due to the following reasons:

1. The National Bank for Agriculture and Rural Development
(NABARD) was formed only on 12th July 1982.

2. The data prior to this period is rarely available and data of a minimum period of 10 years is advisable for statistical analysis and statistical significance.

Data and Procedure of Collection

The study was conducted with the help of primary and secondary data. The data for analysing the fund management practices and operational efficiency were collected from the Annual Reports of these selected banks for the period 1983-84 to 1992-93. For analysing the structure of overdues an age-wise and purpose-wise classification of overdues were taken from the records of these banks. To analyse the factors affecting overdues the primary data were collected from 300 defaulters through a pre-tested structured schedule. The primary level survey was conducted during the year 1992-93. A detailed interview and discussion with the presidents and other top officials of the selected banks were also conducted to identify the managerial and operational problems.
Tools for Analysis

To examine the fund management practices and to evaluate the operational efficiency, ratio analysis has been used. The ratios were calculated by grouping them into three:

1. Ratios in relation to mobilisation and deployment of funds.

2. Ratios in connection with expense and overall efficiency.

3. Ratios in relation to spread and burden.

The computed ratios were compared with the standards developed.

Average Annual Growth (AAG) rate was used for the comparison of growth rates of different financial variables like income, expenses, borrowings, credit, overdues, profit etc.

Regression analysis was attempted to identify the factors affecting the profitability of the banks. The independent variables selected were overdues, non-interest income, interest income, non-interest expense (cost of management) and interest
expense. ANOVA (RBD type) was used for examining the intra bank and inter bank variations.

The structure of overdues was analysed with the help of percentages. To know the impact of the socio-economic variables on the nature of default chi-square test was used. The determinants influencing the overdues was examined with the help of step-wise regression. The independent variables selected were the amount of loan, agricultural income, total income and family consumption expenditure. Graphs were also used to indicate the trend of essential variables.

Limitations

The structure of Agricultural and Rural Development Banks in Kerala consists of a two-tier system — primary banks at the base and the apex bank at the state level. The scope of this study is restricted to the selected primary banks and the sample defaulters.

The period of the study is limited to 10 years from 1983-84 to 1992-93. However, in the year 1989 the Co-operative
Act was amended making the co-operative year from 1st April to 31st March in order to bring a uniform pattern in tune with the financial year of other organisations. In order to bring these changes the absolute figures for the year 1988-89 was appropriately adjusted.

Scheme of the Study

The study consists of eight chapters. The introductory chapter starts with a discussion on the importance of Agricultural and Rural Development Banks in investment credit. This is followed by the statement of the problem, objectives, hypotheses, methodology, scope and limitations of the study.

The second chapter traces the evolution of the Agricultural and Rural Development Banks and reviews their growth. A brief description of the selected primary banks is also given.

A review of fund management is given in chapter three. The conclusions and recommendations are given in the final chapter.
The efficiency in mobilisation and deployment of funds is explained in chapter four. The ability to control expenses and to increase the overall efficiency is also examined.

The factors affecting the profitability and its relation with overdues are studied in chapter five. An intra bank and inter bank comparison is also attempted.

The sixth chapter analyses the structure of overdues. This is done by taking scheme-wise and age-wise classification of overdues.

The impact of socio-economic factors on the nature of default and the reasons for overdues are analysed in chapter seven. The determinants influencing the overdues are also analysed.

The conclusions and recommendations are given in the final chapter.