CHAPTER FOUR
Agricultural credit policies of Central Banks of some foreign countries

"The approach of most central banks to agricultural credit and their attitude towards agricultural credit institutes was unsatisfactory. Some of them were almost uninterested in rural credit and failed to provide the financial and technical support so essential for a proper functioning of agricultural credit organisations. In other cases, it was found that the leaders of central banks prepared to finance agriculture, utilized for the purpose, methods and procedures which may be appropriate for financing industry and trade but unsuitable for agriculture." 1

The central banks of most of the countries are not directly charged with the responsibility of providing finance for agriculture. In many cases, the care in this regard is taken by general banking institutions or specialised institutions which in turn may seek help from the Central Bank of the country. In such a situation, the Central Bank's approach is more in the nature of general banking function then a special treatment of the problem. However, this is also not uncommon to find instances where the development of infra-structure and provision of credit for agricultural operations have been envisaged as part of the basic activities of the central banks.

With a view to examine these practices in the context of Indian needs, the systems followed, incentives provided and channels devised, the study of the Central Bank of United States of America and Australia have been attempted in the following paragraphs. The objective analysis on the basis of available information and obvious limitations has been made to see how far these experiences can be utilised in the Indian conditions :

1. Agricultural credit through co-operatives and other institutions - Food and Agriculture organisation of United Nations - Rome 1965 p.8
A) United States of America - Federal Reserve Banks and agricultural credit

(i) Prior to 1933

In America the development of agricultural credit policies on institutional basis had been the culmination of later efforts. Initially the movement developed as farmer's movement and various bodies like farmer's equity, the farmers unions etc. were organised mainly to combat low prices, higher freights, high rates of interests and greater exploitation by middlemen and higher prices for machinery equipments etc.

The Farm Credit System in U.S.A. developed in 1916 when the Federal Farm Loans Act was passed. This Act authorised the establishment of Federal Land Banks and its constituent units. In 1923, with the passage of Agricultural Credit Act a permanent system was established with the organisation of Federal Intermediate Credit Banks for providing operating credit for investment market.

In 1929, the Federal Government enacted the Agricultural Marketing Act and created Federal Farm Boards. The objects were to promote co-operative education and development of co-operative associations. A revolving fund of 500 million dollars was placed at the disposal of the Board to enable it to issue loans to various co-operative associations practically for any purpose. Loans for capital investments as well as current operations were also

References:
A. Reorganisation of agricultural credit by Shri G.D. Agrawal pp. 258-291
B. Observation-cum-study tour of U.S.A., Japan and Phillipines by Shri B.K. Sinha pp. 57 to 73
C. Co-operation in foreign countries by S. Rajagopalan 1954 - pp. 132 to 290
D. Elements of agricultural economics by G.W. Forster and Monroe. Leaser pp. 289 to 314
issued by it.

(ii) After 1933 - Farm Credit Administration (FCA)

In 1933, the functions of the above Board were taken over
by the newly created Farm Credit Administration. The agricultural
credit system is a part of FCA activities. The FCA is under the
department of Agriculture but it has an independent status.
Initially, the capital was provided by the Government but the
same was retired by it in due course. With the retirement of
146,000,000 dollars of the Government owned capital, the farmers
in that country became the sole owners of this 12,000,000,000
dollars credit resource. This ended a significant phase of
partnership between the farmers and their Government in building
this 51 years old system an almost impossible dream come true.
The present net worth of the completely farmer owned system is
over 2,000,000,000 dollars.

The FCA works through 4 separate financial institutions:

(1) Federal Land Banks (FLBs)
(ii) Federal Intermediate Credit Banks (FICBs)
(iii) Production Credit Corporations (PCCs)
(iv) Banks for Co-operatives

For practical purposes, the U.S.A. has been divided into
12 farm credit districts. Each of the above agencies had its
regional unit situated in one common building at such district
headquarters. They have close co-ordination in their activities
and policies for which a credit council consisting of the
elected representatives of the above agencies and Government
nominees has been created.

The details of the working, resources, funds etc. of each
of the above agencies have been discussed in the subsequent paragraphs:

A. Federal Land Banks

The FLBs were established in 1916 under the Federal Farms Act (1916) and provide long term credit to individual farmers. It has 12 regional banks and a large number of subsidiary Associations namely National Farm Loan Associations (NFLA).

The intending borrowers join the NFLA and purchase shares to the extent of 5% of their credit needs. The NFLA also invests 5% of its borrowings in the share capital of regional banks. The loans are given on the first mortgage of land for periods ranging upto 65% of the value of mortgage. The purposes for which loans could be made by it are:

(i) Purchase of farms and farm land
(ii) Purchase of live stock, machinery and equipment
(iii) Refinancing of existing mortgages
(iv) Construction and repairs to buildings
(v) Financing of farms and family needs
(vi) Paying other debts

The maximum loan to a farmer could be given to the extent of one lakh dollars. The loan application is processed by NFLA and is finally apprized by the representatives of the regional bank before approval.

The initial capital of the FLBs was provided by the Government which was fully retired by the farmers in 1947. Thus, the FLBs and NFLAs are fully owned by the farmers. The bank raises its resources by floating debentures and bonds on the security of mortgages collected by it from its members. The Federal Farms Mortgage Corporation established in 1934 assisted the FLBs in the sale of bonds etc. The advantage of such
resource mobilisation is that it helps all cultivators equally whether located favourably or not. Shri B.K. Sinha summed up the situation as:

"By pooling mortgages and issuing bonds in this way, the land banks enabled farmers in high risk, high interest rates areas far away from investment market to get long term mortgage loans on a basis similar to those available to farmers located in more favourable areas."

The FLBs are empowered to borrow short term loans from commercial banks and Farm Mortgage Corporations. Thus the FLBs which met the long term requirements are not strictly organised on co-operative basis but are an organisation to provide cheap credit to farmers.

B. Federal Intermediate Credit Banks (FICBs)

The FICB was established with the passage of Agricultural Credit Act 1923. The object of the bank was to gear up the disordered agricultural production. The Bank does not accept deposits and does not transact banking business and also does not lend to the individual farmers. Such banks merely provided discounting facilities and loans to various associations and institutions on securities like live stocks, other collaterals approved by the Governor of the FCA. They provide short term loans to production Credit Associations, farmers co-operatives etc.

Initially, the Secretary of the treasury was empowered to purchase capital stocks but later on Federal Farms Loan Act was amended to empower it to purchase such stocks. The Government provided the initial capital of all the 12 FICBs under the

Agricultural Credit Act. Apart from the 60 million dollars to all the FICBs, an amount of 40 million dollars was also provided as revolving fund which was to be utilised to meet individual credit needs of the eligible borrowers.

The FICBs were also empowered to raise funds by sale of collateral trust debentures with a maturity period of not more than five years to the investing public. Rediscounting with the Federal Reserve Bank, loans from Reconstruction Finance Corporation and loans or rediscounting facilities from other banking institutions were other sources of finance available to it.

The FICBs rediscounted or purchased short term notes of farmers/ranchers which have been given by them to privately capitalised lending institutions including commercial banks, livestock companies, agricultural credit corporations etc. Not only this, it also envisaged that farmers would organise their own organisations to discount such notes with the banks. The FICBs control the discounting organisations from charging rates of interest to the ultimate borrowers in excess of stipulated percentage from time to time.

C) Production Credit Corporations (PCCs)

The PCCs were also created in 1933 under Federal Credit Act. The Corporation also had 12 offices situated at each of the credit district. The cultivators desirous of borrowing, join the Production Credit Associations in their areas by purchasing 'B' class stocks which carried voting rights. Such a share would be required to the extent of 5% of the total credit requirement. When a member does not borrow for two years after the repayment of earlier dues, his stocks are transferred to class 'A' stocks
which are non-voting stocks but carried interest.

Thus, in practice the Production Credit Associations were always controlled by borrowing members. The members can borrow for any agricultural purposes including family expenses. The amount of the loans is restricted to financial soundness of the borrower and also the assessment of the repaying capacity made by the loan committee of the Association.

The loans could be made with the help of FICBs by pledging members notes as security for funds. The PCCs perform 4 specific purposes:

a) Help in organisation of production Credit Associations in their areas or districts
b) Furnish share capital to the Associations
c) Provide general supervision and advice
d) Represent the Associations in dealing with FICBs

The initial capital was provided by the Government which was partially invested in A class shares and partly in the interest earning securities. Loans for crops, live stocks, dairying, poultry and other general purposes like repairs and equipment etc. could be borrowed from the Associations. The farmers offer first lien on crops and live stocks as security. The rate of interest does not exceed 3% over the Discount Rate of FICBs. The earnings of the Associations are utilised for the following purposes:

a) Recoup losses in excess of reserves for bad debts
b) To remove impairments on capital
c) To create and maintain bad debts reserve
d) To maintain a guarantee fund amounting to atleast 25% of the paid-up capital
e) To pay dividend with the approval of PCCs
f) To retire the stocks owned by PCCs

D) Banks for Co-operatives

One Central Bank for Co-operatives and 12 regional banks
for co-operatives were established in 1933. The objects of these banks were to provide loans to the co-operatives and not individuals. The initial share capital for these banks have been provided by the Government through FCA. The borrower has to invest 5% of his borrowing needs in it for operating loans. In case of commodities or facilities type of loans, the ratio of share holding was 1:100. The holding of shares gave voting rights. Normally no single loan exceeded 10% of the bank's total resources. In case of large loans, they are drawn on Central Bank for Co-operatives at Washington D.C.

The eligible institutions are Associations of farmers working in joint processing, purchasing and grading, extension of farm business services etc. Three types of facilities are available from these banks:

a) Operating loans

They are borrowed at the peak periods and may be secured or unsecured depending upon the financial position of the borrowers. Mostly they are for short periods and are liquidated by the end of marketing seasons.

b) Commodity loans

They are for short periods and secured by commodities like farm produce etc. and are liquidated out of the sale proceeds of the commodity.

c) Facilities loans

Such loans are given to enable the purchase of land, building and fixed equipments. The security is generally the property acquired. The period is usually upto 10 years but can be extended to 20 years.
(iii) Farmers Home Administration (FHA)

In order to assist those farmers who are otherwise not eligible for finance due to inadequate security etc., the FHA provides loans through 40 state offices and scores of county offices. The FHA was established in 1946. Its main objectives were to strengthen family farms, develop rural communities, and reduce rural poverty etc. Combination of supervision and the credit is the most distinctive feature of the Administration.

The supervisor of FHA calls for an informal meeting with the intending borrower, analyses his farm business, identifies his needs and problems, plans for future, prepares a repayment schedule, maintains records books etc. Thus, apart from credit, FHA extends technical guidance and assistance. The loan is adequately supervised. It is said that 95% of the supervision under the supervised credit takes place before a loan is made to a new member.

(iv) Research Department - FCA

The FCA is maintaining a Research and Advisory department under its co-operative division, which is concerned with all aspects of agriculture, co-operatives, processing and statistics. It also provides advice on all matters affecting farmers.

(v) Educational Programme

Another point of interest in the working of FCA is the education programme conducted by the FICBs. They organise a variety of educational and staff manager and director development programmes. While for the newly recruited staff or elected directors, more intensive programmes are designed, those for
experienced staff, managers and directors one or two days seminars at various levels are held either separately or jointly for different categories of personnel.

(vi) Co-ordination between FCA and FHA

FCA and FHA are thus, two agencies which take care of all types of credit needs and requirements and extend support to all types of farmer borrowers. The relationship between FCA and FHA are, therefore, expected to be harmonious and cordial. While generally FCA is treated as conservative in its approach, FHA is treated as liberal in its policies. FCA does not have its own supervision and extension machinery and has to work through FHA machinery. In theory, FCA and FHA are expected to go hand in glove with each other.

Besides these two institutions, there are other units also in the field of agricultural credit. Such units include Rural Electrification Administration which was established in 1935. The Administration achieved significant success in the provision of electricity to farms and homes.

B. Australia - Reserve Bank of Australia

The Common Wealth Bank of Australia worked as the Central Bank for Australia prior to 1960. This bank was established by an Act of Parliament in 1911. It had two departments dealing with agricultural credit:

(A) Rural Credit Department (RCD)
(B) Mortgage Bank Department (MBD)

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The RCD was created in terms of section 67 of part VIII of the Common Wealth Bank Act and was established in 1925. The department was later on retained by Reserve Bank of Australia which assumed the central banking functions of the Common Wealth Bank of Australia in 1960.

**Mortgage Bank Department (MBD)**

The MBD was established in 1943 under section 80 of the Common Wealth Act. This department was created with a view to provide advances to persons engaged in farming, agriculture, horticulture, pastoral and grazing operations etc. Section 82/85 of the Act provided for the percentage of valuation, amount of loan, period and repayment arrangements while section 80 provided the security acceptable for such advances.

After the formation of the Reserve Bank of Australia the MBD was not taken over by the new bank. It was handed over to a still newly created Common Wealth Banking Corporation in a strong and efficient condition.

The position of the long term mortgage loans facilities extended by it during 1956-57 to 1958-59 i.e. before transfer to Common Wealth Banking Corporation are given below:

<table>
<thead>
<tr>
<th>Co-operative Year</th>
<th>Number of Loans</th>
<th>Amount Approved</th>
<th>Loans Outstanding</th>
</tr>
</thead>
<tbody>
<tr>
<td>1956-57</td>
<td>260</td>
<td>0.92</td>
<td>N.A.</td>
</tr>
<tr>
<td>1957-58</td>
<td>369</td>
<td>1.26</td>
<td>5.8</td>
</tr>
<tr>
<td>1958-59</td>
<td>329</td>
<td>1.00</td>
<td>6.1</td>
</tr>
</tbody>
</table>


1. Reserve Bank of Australia: Staff paper: Flow of Funds 1959-60 to 1961-62 pp. 25
The MBD provided a better part of resources for the projects designed to foster increased operating efficiency and development of productive capacity. Among others, loans for timber treatment, pasture improvement, irrigation and development of other water facilities were provided by it.

It also provided assistance towards establishment of settlers who acquired properties by Government ballot. The extent of such assistance was £1.78 lakhs, 2.57 lakhs and 1.67 lakhs during 1956-57 to 1958-59 respectively.

Rural Credit Department

The RCD operates under part VI of Reserve Bank of Australia Act 1959. Its function is to provide finance to statutory marketing boards, similar authorities and to co-operative associations of primary producers. Advances are mostly used by the borrowers for making payments to growers for their produce pending its sale and to finance its marketing expenses which may include processing and manufacturing of commodities. Section 57 (ii) of the Reserve Bank of Australia Act 1959 provides:

"advances by the department to co-operative association of persons engaged in farming, agriculture, horticulture, pastoral and grazing or fishing operation."

Thus, the department was to extend and support for all types of activities relating to agriculture. The capital between 1925 to 1933 was built up by receipt of 25% of the net profits of the note issue department while from 1951 to 1956 the capital was increased by equal contribution from profits arising out of central banking business and note issue department. In terms of Reserve Bank of Australia Act 1959 the capital was increased to £4,714,000 on 14 January 1960 by allocation from the reserves.
of the Bank. Under the Reserve Bank of Australia Act 1959, 1/4 of the department's profits were to be placed with the Rural Credit Development Fund and another 1/4 to the department's Reserve Fund.

The Reserve Bank of Australia is empowered to make direct loans to the Rural Credit Department. Further the Act also provided that the treasurers of the Commonwealth can make loans to Reserve Bank of Australia for Rural Credit Department. The Department itself is empowered to make loans and extend discounting facilities to the eligible borrowers. The nature of securities acceptable to the department is at the discretion of the Bank and may often take any of the following forms:

a) Charge over commodities
b) Floating charge over entire assets or book debts by means of bills of sale
c) Specific charge over land and building
d) Guarantee of the Commonwealth or appropriate State Government

The Reserve Bank of Australia Act prohibits the department to make advances for periods exceeding one year so that orderly marketing of commodities may be encouraged. As such normally, the department is not expected to provide finance for capital expenses except in special circumstances. The details of advances made by the Rural Credit Department indicates wide fluctuations mainly due to market trends, supply and demand factors and variation in prices etc.
Table No.6

<table>
<thead>
<tr>
<th>Year</th>
<th>Peak advances made during the year</th>
<th>Outstanding balance</th>
<th>Reasons for variations in peak advances</th>
</tr>
</thead>
<tbody>
<tr>
<td>1955-57</td>
<td>74</td>
<td>49</td>
<td>Fall in wheat stocks and poor harvest.</td>
</tr>
<tr>
<td>1956-57</td>
<td>50</td>
<td>35</td>
<td>Higher production of wheat &amp; Barley</td>
</tr>
<tr>
<td>1958-59</td>
<td>100</td>
<td>72</td>
<td>Increased exports of wheat &amp; Barley</td>
</tr>
<tr>
<td>1959-60</td>
<td>97</td>
<td>75</td>
<td>Lower crop of wheat and Barley</td>
</tr>
<tr>
<td>1960-61</td>
<td>122</td>
<td>82</td>
<td>Record wheat crop</td>
</tr>
<tr>
<td>1961-62</td>
<td>113</td>
<td>59</td>
<td>Increase in wheat shipments and early receipts of export proceeds</td>
</tr>
<tr>
<td>1962-63</td>
<td>136</td>
<td>105</td>
<td>- - N.A. - -</td>
</tr>
<tr>
<td>1963-64</td>
<td>127</td>
<td>65</td>
<td>Increased demand for sugar, fruits, eggs but fall in wheat production</td>
</tr>
<tr>
<td>1964-65</td>
<td>322</td>
<td>243</td>
<td>Demand for wheat, dairy products, sugar, fruits, barley and number of oil seeds</td>
</tr>
<tr>
<td>1965-66</td>
<td>291</td>
<td>175</td>
<td></td>
</tr>
<tr>
<td>1966-67</td>
<td>437</td>
<td>361</td>
<td></td>
</tr>
</tbody>
</table>


The above reasons also revealed that production and its disposal or marketing raised the main problem before the farmers. The exports and the realisation of remittances played an important role. The observations made in ICA (International Co-operative Alliance) bulletin for July 1972 as quoted in the Co-operative News Digest for January 1973 in this connection may have some significance:

"The size of holding and lack of irrigation makes cultivation most expensive........the benefits of large scale operations although common, are not universal..... The agriculturists in Australia depend on export for their livelihood and any change in international market situation can have serious consequences on their economy........The Co-operatives in Australia are very individualistic. They have no incentive to pool their resources........ The safeguarding of their trading interest is the only thing that will tempt them to rally round the Federation. The commodity boards and such other agencies are already doing this job and hence very little is left for the Federation."

1 Co-operative News Digest - January 1973 - p.5
The above observation also reveals how important it is for RCD to provide finance to marketing, processing and manufacturing of the primary produce in Australia.

Rural Credit Development Fund

Another important activity of the RCD is the creation of the above fund in 1926 along with the department itself. The object of this fund was to provide grants for research and extension work for the promotion of primary production. The supported projects included:

(A) Basic research
(B) Applied research and
(C) Extension and education work

The organisations included Universities, Junior farmer movements, Research institutes and Committees. The subjects included projects supporting soil fertility, beef cattle, physiology of sheep under tropical conditions, fruit growing, market problems, pasture improvement, farm management, agricultural engineering and economics. It also supports the postgraduate training of the scientists.

The resources of the fund were half of the profits of the Department. As the profits of RCD fluctuate, it was not possible to approve grants against incomes yet to accrue. For this reason the bank originally tended to support the projects for a year at a time. Since 1960 the bank has endeavoured, when practicable, to provide finance for the full prospective period required to bring the project to a defined stage or to completion.

The details of the grants made by the RCD are given below.
Table No. 7

(Amounts in million £)

<table>
<thead>
<tr>
<th>Year</th>
<th>Grants made during the year</th>
<th>Total grants made since the inception of the fund i.e. 1925</th>
</tr>
</thead>
<tbody>
<tr>
<td>1957-58</td>
<td>0.1</td>
<td>1.1</td>
</tr>
<tr>
<td>1958-59</td>
<td>0.1</td>
<td>1.2</td>
</tr>
<tr>
<td>1959-60</td>
<td>0.1</td>
<td>1.3</td>
</tr>
<tr>
<td>1960-61</td>
<td>0.2</td>
<td>1.5</td>
</tr>
<tr>
<td>1961-62</td>
<td>0.2</td>
<td>1.7</td>
</tr>
<tr>
<td>1962-63</td>
<td>0.2</td>
<td>1.9</td>
</tr>
<tr>
<td>1963-64</td>
<td>0.2</td>
<td>2.1</td>
</tr>
<tr>
<td>1964-65</td>
<td>- - - Not available</td>
<td>-</td>
</tr>
<tr>
<td>1965-66</td>
<td>0.5</td>
<td>5.2</td>
</tr>
<tr>
<td>1966-67</td>
<td>0.6</td>
<td>5.9</td>
</tr>
</tbody>
</table>

Source: Annual reports of Commonwealth Bank and Reserve Bank of Australia 1957-58 to 1966-67

Thus, the Reserve Bank of Australia provided huge funds for long term research work which may not have a direct bearing on the activities of its constituents but have a long term influence on the pattern of production. The bank has spent about £6 million during 40 years. During the last few years the pace of contribution for research has gone up substantially.

Lessons for India

The above details, obviously, indicate that the role of the central banks of U.S.A. and Australia respectively had been different in their own way in the financing of agriculture and allied activities. State partnership, subscription to debentures, issue of debentures for resources, separate agencies for short and medium term requirements and long term requirements etc. have been the salient features of the agricultural policies in U.S.A. Most of these concepts or features have been already introduced by us in our country either in the same form or in modified forms. There are still some other features which can be fruitfully introduced in India to overcome certain shortcomings. It
is, therefore, desirable to introduce following features keeping
in view the agrarian conditions of the country:

a) Development of a separate system like FHA to provide
finance for farmers not eligible for finance in traditional
manner. Although Small Farmers' Development Agencies and Marginal
Farmers and Agricultural Labourers Agencies have been created in
the country but the scope of their working and the objects are
different than that of FHA. The scope of S.F.D.A./M.F.A.L
agencies may, therefore, be extended to cover large number of
activities on permanent basis. Further more resources may be kept
at the disposal of these agencies to enable them to formulate
viable schemes for farmers. They may have their own machinery to
implement their policies. In India SFDA/MFAL have to implement
their policies through the institutions which are implementing
normal policies. This would help psychologically inasmuch as the
attitude of the institution dealing with weaker section should be
differently oriented.

b) Provision of revolving fund/credit to the apex bank by the
State Government to meet their financial problems and encourage
the developmental activities.

c) Provision of the non-voting class of special stocks from
non-borrowing members at the societies level but carrying
interest on attractive terms.

d) Creation of a co-ordination machinery at the regional
level between various agencies. This can be done in the form of a
Standing Committee of all concerned on statutory basis or on
informal basis.

e) Training of directors and members of the co-operative
organisations.

Similarly certain special features were observed in the Australian system also. The Reserve Bank of Australia has special responsibilities. It has a department like India under the provisions of the statute, but there are no tiers in the structure. Further, RCD deals directly with the co-operative marketing Boards and associations. Here again there are separate institutions for short and long term requirements. The department gets funds out of the profits of the bank and the department itself. A part of the profits are transferred to a special fund for supporting research and extension work.

As there may not be many things common in the Indian and Australian agricultural and financial policies, there are few lessons which can be fruitfully introduced in India. However, the role of RCD in allocating funds for extension and research work for the development of agriculture and allied activities has a special significance for us. Although we have also created special funds out of profits but these funds are utilised for extending financial facilities to the lending institutions. In addition to these funds, assistance is being extended for training in co-operation but the research activities in the field of agriculture have not been supported by it. Since in all domains of science, progress depends primarily on assiduous and systematic research, it is unrealistic to expect that rapid progress could take place in the fields of agricultural credit, banking and co-operatives in developing countries, as long as little or no research work is undertaken. It is, therefore, suggested that the Reserve Bank of India may create a special fund from out of
its profits and encourage research work and extension work in the field of agriculture which becomes still more necessary in view of diversities in the needs, soil, climate, customs etc., in Indian countryside and agriculture. The beneficiaries may include Universities and research institutes so that independent work may be undertaken by them and more constructive and effective suggestions to improve the policies may be made.