

AGRICULTURAL CREDIT REVIEW COMMITTEE

**A REVIEW OF
THE AGRICULTURAL CREDIT SYSTEM
IN INDIA**



RESERVE BANK OF INDIA

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List of Abbreviations

AAP	Annual Action Plan
ABD	Agricultural Banking Division
ACB	Agricultural Credit Board
ACD	Agricultural Credit Department
ACR	Agricultural Credit Review
ACSRP	All India Co-ordinated Sugarcane Research Project
AD	Anno Domini
AFC	Agricultural Finance Corporation
AID	Agricultural Input Distribution Sub-System
AIRCRC	All India Rural Credit Review Committee
AIRCSC	All India Rural Credit Survey Committee
AIRDIS	All India Rural Debt and Investment Survey
APC	Agricultural Production Commissioner
APRS	Agricultural Processing Sub-System
APS	Agricultural Production Sub-System
ARC	Agricultural Refinance Corporation
ARDC	Agricultural Refinance & Development Corporation
BCP	Block Credit Plan
BDO	Block Development Officer
BDP	Banking Development Plan/Block Development Plan
BIRD	Bankers' Institute for Rural Development
BR Act	Banking Regulation Act
BSRB	Banking Services Recruitment Board
BTC	Bankers' Training College
CAB	College of Agricultural Banking
CADP	Command Area Development Programme
CAMPCO	Cocoa & Arecanut Marketing & Processing Co-operative Society
CBs	Commercial Banks
CCI	Cotton Corporation of India
CCIS	Comprehensive Crop Insurance Scheme
CCRI	Central Coffee Research Institute
CD	Community Development
CD Ratio	Credit Deposit Ratio
CGCI	Credit Guarantee Corporation of India Ltd.

CMIE	Centre for Monitoring Indian Economy
CRAFICARD	Committee to Review Arrangements for Institutional Credit for Agriculture and Rural Development
CRR	Cash Reserve Ratio
CTC	Co-operative Training College
DBOD	Department of Banking Operations & Development
DCB	Demand, Collection, Balance
DCC	District Consultative Committee
DCCB/CCB	District Central Co-operative Bank
DCP	District Credit Plan
DDO	District Development Officer
DDP	District Development Plan
DIC	Deposit Insurance Corporation
DICGC	Deposit Insurance and Credit Guarantee Corporation
DLCC	District Level Co-ordination/Consultative Committee
DLRRC	District Level Rehabilitation Review Committee
DOM Studies	District Oriented Monitoring Studies
DPAP	Drought Prone Areas Programme
DRDA	District Rural Development Agency
DRI	Differential Rate of Interest
DTC	District Level Technical Committee
DWCRA	Development of Women and Children in Rural Areas
EC	Eligibility Criteria
EEC	European Economic Community
ETP	Entire Transplant
FCI	Food Corporation of India
FSS	Farmers Service Society
GCF	Gross Capital Formation
GDP	Gross Domestic Product
GIC	General Insurance Corporation of India
GOI	Government of India
GOI (MOF)	Government of India (Ministry of Finance)
Ha	Hectare
HADP	Hill Areas Development Programme
HP	Horse Power
HYV	High Yielding Varieties
IADP	Intensive Agricultural District Programme

IBA	Indian Banks' Association
ICA	Institutional Credit Agencies
ICDP	Integrated Co-operative Development Programme
ICOR	Incremental Capital Output Ratio
IDA	International Development Association
IDBI	Industrial Development Bank of India
IFFCO	Indian Farmers' Fertilizers Co-operative
IRD	Integrated Rural Development
IRD P	Integrated Rural Development Programme
ISB	Industry, Service and Business
ISP	Institutional Strengthening Programme
JCI	Jute Corporation of India
JLTC	Junior Level Training Centre
KRIBHCO	Krishak Bharati Co-operative Ltd.
KVIC	Khadi and Village Industries Commission
LAMPS	Large-sized Adivasi Multi-Purpose Society
LB	Lead Bank
LBS	Lead Bank Scheme
LDB	Land Development Bank
LDO	Lead District Officer
LIC	Life Insurance Corporation of India
LT	Long Term
mbp	Maximum borrowing power
MFAL	Marginal Farmers and Agricultural Labourers
MIS	Management Information System
MLA	Member of Legislative Assembly
MLC	Member of Legislative Council
MP	Member of Parliament
MSSC	Management Systems & Standards Committee
MT/mt	Medium term
NABARD	National Bank for Agriculture and Rural Development
NAC (LTO) Fund	National Agricultural Credit (Long-term Operations) Fund
NAFED	National Agricultural Co-operative Marketing Federation of India Ltd.
NAFSOB	National Federation of State Co-operative Banks
NCA	National Commission on Agriculture

NCBI	National Co-operative Bank of India
NCCF	National Co-operative Consumers Federation
NCCT	National Council for Co-operative Training
NCDC	National Co-operative Development Corporation
NCUI	National Co-operative Union of India
NEIBM	North Eastern Institute of Bank Management
NE Region	North-Eastern Region
NFSLDB	National Federation of State Land Development Banks Ltd.
NIBM	National Institute of Bank Management
NIBSTC	Northern India Banks' Staff Training College
NIC	National Information Centre
NNP	Net National Product
NODC	Non-Overdue Cover
NODP	National Oilseeds Development Programme
NRC (LTO) Fund	National Rural Credit (Long-term Operations) Fund
NRC (Stab) Fund	National Rural Credit (Stabilisation) Fund
NREP	National Rural Employment Programme
NSS	National Sample Survey
NSSO	National Sample Survey Organisation
OPTP	Oilseeds Production Thrust Programme
PACS	Primary Agricultural Credit Society
PC	Planning Commission
PCDF	Primary Co-operative Development Fund
PLDB	Primary Land Development Bank
RBI	Reserve Bank of India
RCS	Registrar of Co-operative Societies
RDPC	Rural Development Project Course
R & D Fund	Research and Development Fund
REC	Rural Electrification Corporation
RLEGP	Rural Landless Employment Guarantee Programme
RPCD	Rural Planning & Credit Department
RRB	Regional Rural Bank
RTC	Regional Training Centre
Rs.	Rupees
SAO	Seasonal Agricultural Operations

SAS	Service Area Scheme
SB	Sponsor Bank
SBI	State Bank of India
SCB	State Co-operative Bank
SC/ST	Scheduled Caste/Scheduled Tribes
SCU	State Co-operative Union
SEB	State Electricity Board
SEEUJ	Self Employment Scheme for the Educated Un-employed Youth
SEG	Senior Expert Group
SEPUP	Self Employment Programme for Urban Poor
SFC	State Financial Corporation
SFDA	Small Farmers Development Agency
SFPP	Special Food grains Production Programme
SIBSTC	Southern India Banks' Staff Training College
SIDBI	Small Industries Development Bank of India
SIDC	State Industries Development Corporation
SIDF	Small Industries Development Fund
SKVIB	State Khadi and Village Industries Board
SLCC	State Level Co-ordination Committee
SLDB	State Land Development Bank
SLR	Statutory Liquidity Ratio
SLRRC	State Level Rehabilitation Review Committee
SMI	Small and Medium Industry
SPA	Special Projects Agriculture
SRPP	Special Rice Production Programme
SSI	Small Scale Industries
ST	Short Term
TADP	Tribal Area Development Programme
TAG	Technical Appraisal Group
TCP	Term Credit Projection
TME	Technical Monitoring & Evaluation
TOPIC	Training of Personnel in Co-operation
TOR	Terms of Reference
TRYSEM	Training of Rural Youth for Self Employment
T & V	Training & Visits
USAID	United States Agency for International Development

UTI	Unit Trust of India
UTs	Union Territories
VC	Viability Criterion
VLW	Village Level Workers
VAMNICOM	Vaikunth Mehtra National Institute of Co-operative Management
VVV	Vikas Volunteer Vahini
ZP	Zilla Parishad

INTRODUCTION

A comprehensive study of the problems of rural credit and related issues was undertaken for the first time after Independence in 1951-54 by the All India Rural Credit Survey Committee set up by the Reserve Bank of India. The Study had as its basis a nationwide field survey on an unprecedented scale supplemented by an indepth analysis of the case history of a number of rural institutions and views expressed by officials and non-officials. The enquiry addressed wide-ranging issues relating to rural credit including activities which support the credit systems and the Committee made far reaching recommendations. These, in fact, laid the foundation of the institutional framework for establishing a sound credit delivery system for financing agriculture and allied activities. For developing the institutional framework and strengthening it, the Committee recommended the rebuilding of co-operatives at all levels within each state, viz., the state, district, taluka, and village-level co-operatives. For the first three of these four levels, the Committee also recommended development of both co-operative banking and co-operative marketing institutions, while at the village level, it recommended development of multi-purpose co-operatives of larger size, besides recommending their federating into upper level banking as well as marketing co-operatives. Similarly, it also recommended setting up of commodity specific marketing and processing co-operatives for perishable and easily damageable crops like sugarcane and cotton. The marketing co-operatives at the state, district, and taluka levels and the multi-purpose PACSs at the village level were to undertake both farm inputs and farm produce marketing.

0.02 The Committee's recommendations also resulted in many innovative steps since taken for institution building at all levels in the rural credit hierarchy, including the conversion of the Imperial Bank into the State Bank of India, the setting up of the National Co-operative Development Corporation, the National and State Warehousing Corporations and the creation of a wide network of co-operative training institutions. All these steps were aimed at stimulating the flow of credit to agriculture, ensuring simultaneously also, a suitable institutional framework and necessary credit support for agricultural processing and marketing. Such an integration was necessary, the Committee felt, to enable the agriculturist borrower to secure a fair price for his produce without which prompt repayment of production loan would not be possible.

Within the co-operative credit structure, the Committee's main recommendation was state partnership, so as to strengthen the structure not only financially but managerially as well through the state sharing the risks of business. There was, following this, an all out effort for developing the co-operative credit system as an exclusive agency for purveying agricultural credit. Although the Committee recognised that the system had in the past failed to achieve its objective, it strongly felt that in the context of the social matrix of rural society in India there was no alternative to co-operatives. The years that followed witnessed increasing financial and managerial support to the co-operative credit system from the Government and the Reserve Bank. However, the increased flow of credit and the monopoly of operations by the co-operatives gave rise to many problems which the co-operatives faced in the late sixties and thereafter. Overdues mounted, credit flow got choked and state partnership which was intended to give financial strength to the co-operative system resulted in growing governmental interference in and control of, the system.

0.03 In July 1966, the Reserve Bank set up the All India Rural Credit Review Committee to undertake a comprehensive review of the agricultural credit system so that the bottlenecks which had emerged in the course of the implementation of the recommendations of the Rural Credit Survey Committee may be identified and remedial measures taken. The Committee reviewed the performance of the various institutional credit agencies and made several recommendations for enabling them to play, in this sphere, a larger and more purposeful role than in the past. Among others, the Committee had recommended a dynamic role to the then Agricultural Refinance Corporation and the adoption of various measures for ensuring timely and adequate flow of credit for agriculture through co-operative and commercial banks. A sea change has since taken place in the credit system. Adoption of modern techniques of cultivation, on the one hand, involving greater use of improved seeds and fertilisers which made the green revolution possible and, the widespread and consecutive droughts which in turn led to increased exploitation of groundwater resources through minor irrigation on a massive scale on the other, induced farmers to take to larger investments in agriculture. These changes necessarily led to substantial increase in demand for credit from the institutional agencies. But the co-operatives which until then were, by and large, the sole purveyors of agricultural credit found themselves unable

to meet this increasing spurt in demand partly on account of certain weaknesses in their structure and management and partly because they had not been geared to cope with the new challenge. The Review Committee felt that since agricultural production could not wait till the co-operatives were put back on the rails and adequately equipped for the task, it had become necessary to induct the commercial banks to supplement the efforts of the co-operatives in substantial measure in meeting the increased demand for agricultural credit and the Committee recommended to this end, a multi agency approach as an immediate solution to the problem. The commercial banks thus entered the sphere of agricultural credit and on a massive scale after nationalisation of the 14 major commercial banks in 1969 to be followed by nationalisation of 6 more banks later. Further, with the establishment of the Regional Rural Banks (RRBs) in 1975, one more wing was added to the agricultural credit structure. Although the intention originally as recommended by the Working Group under the chairmanship of Shri M. Narasimham was to establish only five RRBs on a pilot basis, the working group under the chairmanship of Prof. M. L. Dantwala (1978) recommended the extension of the experiment to such of those districts where district central co-operative banks were weak. Furthermore, the RRBs were to be (a) low cost institutions like co-operatives and (b) professionalized in their management like the commercial bank. This was to be accomplished through a capital structure which envisaged participation of the state governments, the sponsoring commercial banks and the Government of India. While the Narasimham Group recommended it to be an institution only for the rural poor, the Dantwala Working Group recommended it to be an institution mainly for the rural poor but did not want the non-poor to be administratively debarred from getting its services. This did not find acceptance of the Government of India. The last of the Working Groups which subsequently reviewed the working of the RRBs, viz., the Kelkar Group in their Report (1986) also rejected the inclusion of non-poor, even to the limited extent recommended by the Dantwala Group. Government of India has accepted this recommendation and RRBs continue to be banks serving exclusively the weaker sections.

0.04 Though it resulted in the increased flow of credit, the multi agency approach gave rise to certain problems. In 1978, the Reserve Bank set up a Committee to Review Arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD), the third in the series of the studies,

the Bank was undertaking in the field of agricultural credit. The major outcome of the CRAFTCARD's recommendations was the separation of the Agricultural Credit Department (ACD) from the Reserve Bank of India (RBI) which handled refinance for the co-operative credit system and its merger with Agricultural Refinance and Development Corporation (ARDC) which had earlier been set up by the Reserve Bank to exclusively handle investment finance for agriculture. As a result, the National Bank for Agriculture and Rural Development (NABARD) came to be set up in July 1982.

0.05 The current review by this Committee is thus the fourth in the series of comprehensive studies undertaken by the Reserve Bank in the field of agricultural credit. The Government's commitment to agricultural and rural development as also poverty alleviation, spelt out in the Seventh Plan document, with the perspective of the year 2000 in view, is expected to spur the future growth of agricultural credit system. Such a growth of the system has necessarily to be combined with improvement both in the quality of lending and its effectiveness with a view to ensuring quality of the total package of services to farmers. Improvements in the fundamentally intricate agricultural credit delivery system called for a carefully thought out action programme which would facilitate reasonable adjustments in the system in a given time frame. This was the major task before us in this review.

0.06 The ARDC of which, alongwith the ACD of RBI, the NABARD is the successor had been obtaining the facility of 'general line of credit' from the World Bank since 1975. Upto the year 1985, ARDC/NABARD availed of 4 such credits involving an amount of US \$ 875 million. In order to maintain the continuing availability of World Bank funds for development lending in India even after 1985, NABARD had in 1983, i.e. during the currency of ARDC IV credit project, proposed the approval of the next general line of credit for US \$ 400 million. Following the request, four World Bank missions visited India and held discussions with the Government of India and the NABARD, on various key issues pertaining to different aspects of the agricultural credit system in the country, on the basis of which the World Bank approved a loan assistance of US \$ 375 million under NABARD I Credit Project. The assistance is by way of participation in NABARD's ongoing refinancing programme for investment in agriculture to increase agricultural production and to strengthen the agricultural credit system.

0.07 While considering the NABARD I Credit Project, the World Bank had observed that although the earlier ARDC Credit Projects had achieved the physical targets, brought about increase in agricultural production and improved agricultural income, adequate care had not been taken of the ability of credit delivery system to handle the growth and had felt that an improvement in credit delivery and control systems would be necessary to save it from the danger of collapse and had, therefore, suggested a general review of the system for improving the quality of lending. Thus arose the need for having another look at the credit agencies for agricultural credit in India. The Government of India agreed to carry out an indepth review of the agricultural credit system in the country as envisaged in the World Bank Staff Appraisal Report on NABARD I Credit Project.

Strategy and Scope

0.08 The objective of this Review among others, is (a) to review the rural financial system in the country and to assess the credit requirements of the agricultural sector during the next decade, (b) in this context, to determine the role of the credit system to support the national plans for agricultural development, (c) to evaluate the major problems and issues currently affecting the agricultural credit system, and (d) to make recommendations for improving the quality of credit and strengthening its efficiency and effectiveness. In view of the complexity and size of the agricultural credit system in India and taking into account the intricate nature and sensitivity of the issues to be addressed, the strategy as agreed to in the Project Agreement between the GOI and World Bank was to split it into five studies with a detailed terms of reference separately for each study and to entrust these to local and foreign consulting agencies selected on the basis of responses received after floating global tenders. Their overall guidance, superintendence and responsibility for the preparation of an intergral report and making appropriate recommendations vested in a Senior Expert Group (SEG). The broad areas covered by the five studies under the review are :

- i) Agricultural Credit in General ;
- ii) Role and Effectiveness of Lending Institutions ;
- iii) Role and Functions of the Apex Level in Agricultural Credit
- iv) Lending Costs and Margins ; and
- v) Organisation and Management of NABARD.

The Senior Expert Group

0.09 Following the Government of India's agreement to undertake such a review, the Reserve Bank of India, in consultation with the Government and the World Bank constituted on 1st August 1986, a Senior Expert Group initially with a Chairman (Indian) and three Indian Members. The three foreign specialists joined the Group in February 1987. The composition of the SEG was as under :

Prof. A. M. Khusro (Former Member, Planning Commission of India)	Chairman
Shri M. M. K. Wali (Former Lt. Governor, New Delhi)	Member
Dr. M. V. Hate (Former Dy. Governor, Reserve Bank of India)	Member
Dr. A. S. Kahlon (Former Chairman, Agricultural Prices Commission, Government of India)	Member
Dr. J. W. Mellor (Director, International Food Policy Research Institute, Washington)	Member
Dr. G. A. A. Van der Linden (Former General Manager, Rabo Bank, Netherlands)	Member
Mr. Basilio Estanislao (Former Chairman, Land Bank of Philippines, Manila and former Chairman, APRACA)	Member

Under the arrangements agreed to during the negotiations between GOI and World Bank, a Secretariat was established for the Agricultural Credit Review (ACR) in the Reserve Bank of India with Shri C. V. Nair as Executive Director to head it. The task before the SEG, which has since been renamed as the Agricultural Credit Review Committee, as set out in the terms of reference required it to evaluate the major problems and issues currently affecting the agricultural credit system and prepare an integrated report setting out their recommendations to strengthen the agricultural credit system together with a time-frame for their implementation. The detailed terms of reference of the SEG are given in Appendix L

0.10 However, in the absence of clearly stated responsibilities in regard

to the tax obligations of the foreign consultants in any of the documents relating to the Project approval, it took time to settle the issue and there was consequently some delay in the consultants taking up their work. This apart, considering the complexity of the issues required to be addressed and the cross country field work and surveys which this involved, the time given to the consultants for the conduct of the studies, as experience has shown, was too short. Further, even the eleven-month period within which the consultants were required to give their final reports in respect of the Studies I to IV was not fully available to them since the consultants were obliged to give both an interim and the draft Report, necessitating the diversion of members of the study teams for this work. So too the thirteen-month period for Consultants V. Moreover, since Consultants I to IV completed their data collection work in December 1987, the latest data available to the Committee from the consultants' reports pertain to year ending 1986. Since the term of the consultants ended as early as June 1988, further data collection or such re-evaluation of the analysis contained in their final reports, as the Committee desired to have, as their work progressed, was also not possible. Overlapping terms of reference as among the five specified areas of study and a certain lack of focus on the perceived objectives were another constraint. These in turn placed very serious limitations on the Committee itself in regulating the studies in a manner they would have liked to, had the studies been undertaken under their own auspices, and some through their own personnel and through their own consultants where necessary in a few highly specialised areas. On the whole, it is our view that the strategy adopted in the conduct of the studies was highly deficient in achieving the purpose intended.

0.11 On 19th June 1989, that is to say, a week prior to the meeting of the Committee convened from June 26 to July 6, 1989 to consider the comments of the Government of India, Reserve Bank of India, NABARD and the World Bank on the draft (final) report and in the light thereof to review and finalise the Committee's Report, we lost in the sudden passing away of Dr. Gerrad Van der Linden, one of the three non-Indian members on the Committee. Dr. Linden had participated in all the meetings of the Committee since the induction of the non-Indian members in February 1987, save one held in January 1988, and had contributed significantly to the deliberations of the Committee. His contribution covered all areas of the credit system, but was specially

notable in the area concerning co-operative credit. Particular mention may be made of his contribution in four major areas, viz., organisation and structure from the ground level to the national level, management, training and democratisation of the co-operative credit system. It may be seen from the report that the Committee has made wide ranging recommendations, in all these areas. In making these recommendations, we had the benefit of Dr. Linden's rich experience and erudite knowledge. In fact, the written contribution prepared by him for the meeting held in June-July 1989 which was originally expected to be the last meeting of the Committee to finalise the report, was received by us during the course of the meeting. It could, therefore, be truly said that he participated till the very last meeting at which the report was finalised albeit posthumously in the last meeting. In submitting this report, we place on record Dr. Linden's valuable contribution to the Committee.

Appointment of Consultants

0.12 As mentioned earlier, the review was taken up through five separate studies. These were carried out by five separate consulting groups. While the broad areas to be covered by the studies are indicated in paragraph 0.08, the detailed terms of reference of these studies are given in Appendix II. The consultants selected and studies entrusted to them are as under :

Study	Title of the Study	Consultants Selected
I.	Agricultural Credit in General	Voltas International Limited, Bombay
II.	Role and Effectiveness of Lending Institutions	Agricultural Finance Corporation Ltd., Bombay
III.	Role and Functions of Apex Level in Agricultural Credit	Price Waterhouse Asia Pacific, Hongkong
IV.	Lending Costs and Margins	Administrative Staff College of India, Hyderabad
V.	Organisation and Management of NABARD	Coopers & Lybrand Associates, London, U.K.

Work of the Consultants

0.13 After the selection of the consultants, their teams were briefed by the Review Committee. Studies I, II and IV involved field studies. During the briefing, the consultants' teams were given necessary guidelines by the

Committee about the scope of the field studies and the nature of surveys to be undertaken. The Committee also formed five sub-groups consisting of two/three members, each looking after one study separately for the purpose of intensive monitoring.

0.14 The consultants for Studies I to IV were required to submit an interim report at the close of five months from the date of commencement of the study, a draft report three months thereafter and final report within three months of submission of the draft report. As the findings of these four studies had a bearing on conduct of Study V, this study was required to commence around the time of the submission of the interim reports on Studies I to IV. The Consultants of Study V were required to submit their interim report within five months of commencement of the Study, draft report four months thereafter and the final report within four months after the draft report. While Studies I and II commenced in the last week of June 1987, Studies III and IV commenced around middle of July 1987 and Study V, in the second week of December 1987, i.e. just before the interim reports on the other four studies were available.

0.15 The interim reports on Studies I to IV were submitted by the consultants between the end of November and middle of December 1987. These reports brought out mainly the impressions gathered by the consultants' teams during their field surveys/visits to various institutions/agencies purveying credit or during their discussions with the officials of the state governments/other agencies, etc. The Committee deliberated at length on these reports and thereafter held discussions with team members of the respective consultants so as to bring to the notice of the consultants the shortcomings noticed at that stage, areas on which emphasis needed to be laid etc. and to indicate to them the direction in which they should proceed. The directions given to the consultants of each study were made known to the others for the purpose of co-ordination among the different consultants.

0.16 The draft reports on Studies I to IV were received during March 1988. These draft reports contained an analysis of survey/data/case studies, secondary data available on various aspects of agricultural credit as well as discussions held by them with the representatives of various types of institutions, agencies, Government Departments, etc. The draft reports also contained their draft

recommendations. Besides holding discussions with the respective consultants, a workshop was held in April 1988 at which the teams of all the five consultants including consultant V participated to discuss the issues which had a bearing on the final reports of the consultants. The draft reports on Studies I to IV together with the comments of the Committee were thereafter made available to all the consultants to enable them to take into account the findings of the other consultants and take a second look where necessary, at their own findings in the light of survey data presented in the other reports while finalising their reports. The final reports on the Studies I to IV were submitted by the consultants in the second week of June 1988. The consultants for Study IV later revised their final report and submitted the same in the first week of November 1988. The draft report of the consultants for Study No. V was received in September 1988 and after the Committee considered it, discussions were held with the consultants in November 1988 and certain suggestions made for their consideration and incorporation in the final report. The final report on Study V was received in the second week of January 1989.

Work of the Committee

Meetings

0.17 Inaugurating the first meeting of the Indian members of the committee in Bombay on 22nd August 1986, Mr. R. N. Malhotra, Governor of the Reserve Bank reviewed the developments in the field of agricultural credit in the last three to four decades drawing specific attention to some of the more important issues such as structural viability of institutions, effective financing of borrowers, impact of the general environment on their functioning, a steady erosion of the repayment ethics and the urgent need to correct regional imbalances etc. The Governor met the Committee again on 1st March 1987 after the foreign specialists had joined the Committee and thereafter on 27th July 1988, 24th January 1989 and 16th June 1989. The Committee met altogether on 25 occasions, the last meeting being held from 31st July to 5th August 1989 to approve final report. The report was signed on the last day of the meeting i.e. 5th August 1989. Of the 25 meetings, eleven meetings were attended by the non-Indian members which included the last meeting.

0.18 The first four meetings of the Committee were devoted exclusively

to discussions on providing guidance to the consultants on the frame work of the five studies, the issues to be addressed, the sampling techniques to be adopted and the methodology of field surveys in respect of the Studies I, II and IV and other related issues in connection with the five studies. Specific issues pertaining to the five studies were discussed and resolved at the subsequent meetings.

0.19 Besides the issues thrown up by the consultants' reports and their recommendations, certain issues had been raised by the representatives of various categories of institutions/state governments etc., having a bearing on the performance of the agricultural credit system. The Committee devoted considerable time to discuss these issues with a view to finding remedial measures to these issues.

0.20 After finalising the frame work of the five studies, methodology to be adopted etc. in respect of these studies, the Committee undertook, between November 1986 and May 1988, visits to various states in order to acquaint themselves, first hand, with the working of the various types of institutions purveying agricultural and rural credit, problems faced by them, etc. The Committee visited in all 13 states coming under different agro-climatic zones and representing different stages of agricultural and institutional developments. Besides visits to the institutions at the base level, the Committee in the course of their visits, also held discussions with the representatives of state co-operative banks, commercial banks, regional rural banks and the state government officials. The Committee also met Chief Ministers of these states, where possible, to elicit their views on various issues connected with the agricultural credit and efforts being made by these governments for co-ordination between various agencies functioning in the sphere of agriculture and rural development etc.

Visits to Other Countries

0.21 Splitting in two sub-groups, the Committee undertook short visits to five countries, viz., Netherlands and West Germany in the West and Japan, South Korea and Philippines in the East to acquaint itself with the working of the agricultural and rural banking system, its evolution and growth in the context of agricultural and rural development process in those countries. The visits were rewarding and the experience gained was useful in giving

shape to some of the suggestions in the report.

0.22 The Committee met the representatives of National Federations of State Co-operative Banks and State Land Development Banks to discuss the problems faced by the short-term and long-term wings of the co-operative credit institutions and to elicit their views on issues such as integration of the two wings of the co-operative credit structure, the proposed National Co-operative Bank, crop loan insurance etc. The Committee also met the Indian Banks' Association to elicit their views on certain major issues relating to the commercial banks such as the service area approach, the multi-agency system, profitability of commercial banks vis-a-vis their rural credit responsibilities etc.

0.23 In the course of its work, the Committee also met some distinguished personalities in the field of agriculture and rural credit and sought to benefit from their advice. Among them were Prof. M. L. Dantwala, Shri B. Venkatappiah, Dr. V. Kurien and Dr. C. H. Hanumanth Rao, former Member, Planning Commission. We also had meetings with Dr. Y. K. Alagh, Member (Agriculture), Shri J. L. Bajaj, Secretary, Planning Commission, Shri G. K. Arora, Finance Secretary, Shri V. P. Sawhney, Additional Secretary, Banking Department, Ministry of Finance, Shri C. Srinivasa Sastry, Secretary, Ministry of Agriculture and Shri Vinod Pande, Secretary, Ministry of Rural Development and had the benefit of sharing their views, experience and expertise on the various issues under the consideration of the Committee.

Report of the Committee

0.24 The Report is divided into ten parts with 24 Chapters. The background of the Agricultural Credit Review and the approach of the Committee to this task are spelt out in the Introduction. Chapters I and II in Part I give an overview of the Report and a general view of the emerging agricultural scenario in India during the last decade of the century. The present position of the various streams of credit delivery system, viz., the commercial banks, regional rural banks, short-term and long-term co-operative credit structures is reviewed in Chapters III to VII of Part II while the need for having National Co-operative Bank as the national level apex for the co-operative credit system is discussed separately in Chapter VIII. Chapter IX exclusively deals with NABARD which functions as the national level institution in the sphere

of agricultural and rural credit. Having thus discussed the present position of the credit delivery system, measures necessary to strengthen the credit delivery system, particularly the programme of Institutional Strengthening, to enable the system to meet effectively the demand for credit which will arise in future has been dealt with in Chapter XII in Part III. The various aspects of development of institutions such as credit planning and co-ordination, staff training and manpower development, accounting system, computerisation and management information system alongwith measures for correcting regional imbalances are dealt with in separate chapters in this part. Recovery of agricultural credit has over the years become an intractable problem affecting adversely all the streams of agricultural credit system. Measures for the strengthening of the system will become infructuous unless this problem is tackled satisfactorily. While this major problem is analysed under Chapter XV in Part IV, issues relating to risk in agricultural lending such as natural calamities and crop insurance and guarantee cover in respect of risk prone advances by the credit agencies under Government directions are discussed in Part V in Chapters XVI and XVII. The crucial issue of interest rates, lending costs and margins for the various types of credit institutions and autonomy of the credit institutions have been discussed in Chapters XVIII and XIX in Part VI while the role of the apex level institutions, the Reserve Bank of India and the Government in the sphere of agricultural and rural credit is dealt with in Part VII under Chapter XX. Poverty alleviation programme and their close linkage with Government and credit agencies, on which considerable emphasis is being laid by the Government of India during the last two Five Year Plans and the impact of these programmes on the credit delivery system are discussed in Part VII under Chapter XXI. The Committee's estimates of agricultural credit requirements and supply of resources therefor by the end of year 2000 A.D. along with related issues are discussed in detail under Chapters XXII, XXIII and XXIV. A summary of the Report, action points on the recommendations of the Committee and the various Appendixes are given at the end under Part X.

0.25 The Committee has considered in detail the findings/recommendations made by the consultants in their final reports. In firming up its views on the various terms of reference, the Committee has taken due note of the findings/recommendations of consultants, apart from Committee's own observations made during the field visits/discussions etc. and the voluminous primary data collected

by the Secretariat and the available secondary data. The Reports of the consultants are available in five volumes - Vol. I on 'Agricultural Credit in General', Vol. II on 'Role and Effectiveness of Lending Institutions', Vol. III on 'Role and Functions of Apex Level in Agricultural Credit', Vol. IV on 'Lending Costs and Margins' and Vol. V on 'Organisation and Management of NABARD'. Such of the recommendations of the consultants with which the Committee could not agree, have been specifically commented upon in our Report. Needless to add, where the views expressed by the consultants are at variance with those of the Committee, the Committee's views are final.

0.26 The data and analysis thereof in the consultants reports pertain, by and large, to the year upto 1985-86. The same has been used in the report to ensure uniformity. However, where later data were available and useful in support of any observation or point made in a particular chapter the same have been made use of in appropriate places.

Acknowledgements

0.27 It would be difficult to thank every person and institution from whom we have received much assistance during our work. We would, however, make special mention of some of the individuals and institutions who have greatly assisted us in the onerous task. Our thanks are specially due to the Reserve Bank of India and in particular to the Governor, Shri R. N. Malhotra, for kindly making available to us every assistance and co-operation of all the departments and offices of the Bank towards the successful completion of the assignment. In addition, he gave us considerable time and shared with us his personal and Bank's views on many issues during the various discussions we had with him. We are also thankful to the Deputy Governor, Dr. P. D. Ojha for the valuable assistance rendered and advice given to us at various stages of our work. We are grateful to the Chairman and Managing Director of NABARD for the co-operation extended to the Committee in all stages of its work through their central and regional offices.

0.28 We are grateful to the Government of India in the Ministry of Finance, Department of Economic Affairs and Department of Banking as well as in

the Ministry of Agriculture and Rural Development for the valuable assistance provided to us in many ways. We are also grateful to various state governments and their officials, state co-operative banks and land development banks and commercial banks for furnishing us with information required by us and giving us the benefit of their experience and knowledge during the discussions held with them. particular mention may be made in this behalf of the Presidents of the Federations of State Co-operative Banks and State Land Development Banks, as also the Chairman of Indian Banks' Association.

0.29 Finally we would like to place on record our high appreciation of the contribution of Shri C.V. Nair, Executive Director, as the Secretary of the Committee. We thank him for his sincere and hard work and the cheerfulness with which he devoted himself to the strenuous task of the Committee. We are also thankful to all the officers of the Secretariat who helped us with background notes and draft chapters for preparation of the report. We would particularly mention the names of Shri V.P. Nargolkar, Chief Officer and Sarvashri S. John, A. B. Unde, K. P. Padmanabhan and G. B. Bhooshanan (during his association with the Secretariat from May 1988 to May 1989), all Joint Chief Officers and Shri M. P. Sukumaran and Shri H. N. Bhoobe, Deputy Chief Officers. Shri Bhoobe, deserves our thanks also for the arrangements made for the Committee's numerous visits and meetings at various places during the last three years. Mention needs to be made of Shri R. Sundaravaradan, Chief General Manager, NABARD, who worked for the Secretariat as a Consultant from January to March 1989. The other Officers and staff of the Secretariat played an equally creditable supporting role. The names of all Secretariat staff appear in Appendix III.

PART I
GENERAL

I THE REPORT : AN OVERVIEW

II EMERGING SCENARIO IN AGRICULTURAL ECONOMY

CHAPTER I

THE REPORT : AN OVERVIEW

The main purpose of this Chapter is to present an overview of this Report of the Agricultural Credit Review Committee (ACRC). In doing so we

- A) make explicit our approach to the problems of agricultural and rural credit and highlight the main building blocks of that approach,
- B) take stock of the structural and operational deficiencies, constraints, quantitative gaps and qualitative weaknesses of the three rural banking systems - the Commercial Banks (CBs), the Regional Rural Banks (RRBs) and the Co-operative Credit Institutions - and the National Bank for Agriculture and Rural Development (NABARD) which is the intermediate apex of the three systems below the Reserve Bank of India (RBI), and
- C) express our main concerns about the systems and highlight the key messages of our Report for major systemic improvements.

1.02 We have approximately a 15-year time horizon beginning with the year 1990 - though it is conceded that horizons become increasingly blurred as the eye traverses farther and farther into the time-distance.

1.03 Judging by the trends already visible and the policies and programmes already launched in the agricultural sector and projecting the possible impact of a large number of our own recommendations, we foresee the following developments in the forthcoming future and these developments in turn become the basis for our analysis and recommendations on agricultural/rural banking.

- (i) In the coming years, the cereal economy would still have to expand vigorously and at a higher growth rate to meet the unsatiated demand for human and animal feed, to meet the export potential, to build up a safe level of stocks and indeed to promote faster general economic growth. Much resources would have to be deployed still in the cereal sub-sector.
- (ii) However, the newly emerging high-demand sub-sectors, chiefly horti-

culture, livestock and dairying, fisheries, poultry and forestry would expand rapidly and would require very considerable resources too.

- (iii) Much greater emphasis would have to be placed on the financing of inputs - irrigation, seeds, fertilisers, tools and farm machinery and on processing, storage, marketing and transportation and the integration of these processes.
- (iv) The new agricultural technologies which have remained confined to the North-West and to some extent to the South, will spread to Central and Eastern India while the technology plateau can lift up further in areas of progress through R & D in agricultural universities and other developments.
- (v) Another development that is occurring fast is a decline in the share of agriculture in total output, now standing at 32 per cent. But the share of agricultural workforce in total workforce is not declining *pari passu*, owing to a low absorptive capacity for labour in industry. The situation is fraught with rising unemployment and downward pressures on productivity per man in agriculture.
- (vi) A declining farm size resulting from a sub-division and fragmentation of land and a proliferation of concealed tenancies will continue to put downward pressures on the productivity of land as well. Both these tendencies must be countered in many ways - through efforts to raise agricultural growth and productivity with infrastructural and agricultural employment generation under the development plans, through efficient anti-poverty programmes and through the promotion of additional non-farm as well as off-farm activity. It follows that banking institutions must prepare for these situations and must begin to give larger farm credits, larger non-farm credit to farmers as well as credit to the non-farmers for enhanced activity in the rural sector.

1.04 We have accordingly made projections of demand for agricultural credit and of the possible supply of resources from the banking systems on what we thought to be the most feasible assumptions. In our

estimate as may be seen from Chapter XXIII, direct demand for agricultural credit will gradually rise from Rs.27,551 crores in 1989-90, to Rs.57,316 crores in 1994-95 and further to Rs.110,873 crores in 1999-2000. As against this, the resources available in the banking system would be of an order of Rs.28,694, Rs.51,829 and Rs.89,447 crores respectively in these years. The resulting deficits of Rs.5,487 and Rs.21,426 crores in 1994-95 and 1999-2000 could be met by the banking system by further aggressive deposit mobilisation for which we have made several suggestions and through refinance facilities of NABARD.

1.05 As we observe the infrastructural, technological, managerial, and attitudinal changes and the new policy frames increasingly taking shape in India's rural economy and project these in the future to foresee agricultural growth, especially in the newly emerging sub-sectors, we get a vision of the future agricultural and rural economy which is very different from the past. In many parts of the country the dynamism of the farmer, together with supportive policies and technological changes has ushered in the green revolution phenomenon which has radically altered the agricultural economy. But on the other hand, there is also the stark fact that in extensive areas there exists a weak and emaciated form of agriculture with a peasantry still struggling with subsistence farming under unstable rainfed conditions with few techniques of dry farming, little access to new technologies and none too healthy institutions for credit support. Farmers in many parts of the country are still operating under unsecure and unrecorded tenancy arrangements burdened with high rents. But the agricultural scenario at and immediately after the turn of the century, we believe, would be of a different kind of agriculture - an efficient and modernised agriculture in which education and awareness is extensive, infrastructures and technologies are widening and deepening, research and extension services are effective and widespread, yields and efficiencies are high, and increasing farm incomes and profits are the order of the day. It is in this environment that we envisage the evolution of vibrant and efficient banking institutions, and it is these institutions that will in turn provide a critical impact in making the environment as robust as we envisage it.

1.06 We are clear in our mind that the economy and the institutions act and react upon each other and either reinforce each other's strength or mutually

weaken each other. In the Report we are concerned with the strength of the agricultural/rural credit institutions as much as we are with the economy of the area and of the people on whom credit institutions impinge. We have, therefore, worked towards a comprehensive set of measures which impel efficiently performing banking systems to influence and impact the agricultural/rural economy and lead such an improving economy in turn to influence and impact the banking institutions.

A. The Committee's Approach to Credit - Basic Building Blocks

(1) A Market-based and not an over-administered Banking System

1.07 Our concept of banking of tomorrow is not an over-administered banking system perpetually subject to directives and guidelines from the Government and the banking authorities in almost all crucial areas of their operation. We are quite certain that moving out of the stage of administrative paternalism, with rigid rules and stipulations, a plethora of interest rates for lending and borrowing and sprawling subsidies and other fixations, the banking-system in the next 10 to 15 years must come to be operated on much freer commercial and developmental lines. It has to pay a great deal of attention to the market conditions of supply and demand, with little pampering or spoon-feeding, no populist subsidies, concessional interest rates, writes-off of interest and loan amounts and overdues etc. and must become an autonomous, self-reliant, robust and cost-effective system which does not work on crutches and concessions nor on tactics to please the populace temporarily. Thus our first building block is a far less administered and a far more market-based banking system which takes full cognisance of the forces of supply and demand. This of course does not mean that we do not recognize the need and the ability of monetary and fiscal authorities to influence supply and demand especially when some markets are oligopolistic and income distribution is inequitable.

(ii) The Need for a market credit allocation

1.08 But clear as we are on the need for the credit system to be market-based, commercially orientated, cost-minimising and reasonably profitable, we are equally clear about the need in this country for the credit system to assist vigorously in lifting the backward or less developed sectors like agriculture as also lifting the poor from the poverty zone to above-poverty levels - and to do so speedily and effectively. We are broadly in agreement with the

developmental policies and the anti-poverty programmes of the country. We believe that the credit system has an important role to play in effectively backing up the anti-poverty programmes, though credit alone is not enough. We are sure that without the directives and the policy mandate from the Government the banking sector would not have moved so rapidly and vigorously into the agricultural/rural sector, normally shunned by commercial banks. Similarly, without the mandatory allocation of 16 per cent of credit to agriculture, the banks would not have lent such a proportion on their own volition.

1.09 In respect of the economically weaker sections of the community, and only in respect of them, we appreciate the role of concessionary finance, of low interest rates, of limited, well-focussed subsidies to specified target groups among the poor and of promotional measures to bring up the economies of low-income farmers, and weaker sections of rural people, mostly first generation entrants into the fold of credit. We believe that bringing them into credit system will itself benefit them by inculcating discipline and offering productive opportunity and that they need special help in entering that system. And we are also clear that this special help to the weaker sections of society is not just a welfare-promoting measure but will, if administered judiciously, graduate these weaker sections into productive and profit making functionaries.

1.10 Thus, this committee has a two-category view of the credit system, the larger category functioning with a developmental logic, cost-effectiveness, efficiency, rising productivity, surplus generation and market orientation, while the relatively smaller category of well-specified, low-income segments and socially weaker sections of the community, - and they alone - qualify for an anti-poverty treatment, and only until they graduate away from the poverty zone to the realm of non-poverty. In fact it is the surplus generated in the economy as well as in the credit systems from the efficient operation of the larger category that should go to meet some of the costs and, if and to the extent necessary, some specific subsidies for the low-income category.

1.11 That is to say, that barring these two categories - clearly defined at a time but changing over time - there should be no other intermediate, vaguely described, categories which sometimes do and at other times do not qualify for concessionary treatment and which tag themselves on to the

concessionary category for the sake of obtaining undeserved concessions. We are thus keen to see the legitimate concessionary category, such as the beneficiaries of the anti-poverty programmes or the marginal and small farmers and artisans, as a narrow and well-defined band, and we do not wish the other non-deserving elements to enter this band. In other words, we should like to see great clarity in the credit system as well as in Government policy in defining who is who and who does or does not qualify for a priority or a promotional treatment.

(iii) A Two-category Solution

1.12 Once it is recognised that India's banking system should as a rule be a market oriented system working on commercial lines except for the important area of poverty removal where some administrative fiat will be necessary, it becomes obvious that the over-administered structure of interest rates must be corrected, and that the determination of interest rates must be left substantially to the forces of demand and supply, in a freely competitive environment. If the markets are distorted owing to a serious maldistribution of income or the existence of monopoly - oligopoly, correctives should be applied. It follows that in such an environment banking institutions themselves should be left relatively free to follow the market rates of interest, costs and prices and that only in the case of mandatory programmes and policies focussed on the weaker sections and low income groups in society, administered and concessional interest rates and prices should be permitted.

(iv) Avoidance of Populism

1.13 But while mandatory and concessionary programmes and interest rates are valid, we are clear that these should not be administered with populist motives. In fact, we believe that time has come for political, social and institutional leadership, including the leadership of the credit systems, to signal and to tell the people and the recipients of credit etc. that the future lies not in demanding a further benefit, a further subsidy, a further reduction in concessionary lending rates and a further write-off of interest and loan amounts, that is to say, yet another set of crutches, but in productive endeavour, discipline, and risk-taking, leading to self-reliance, higher incomes and better life. The credit system and indeed many other systems in the country now need to be free from concessionality as well as conditionalities.

(v) **Freer Structure of Interest Rates**

1.14 The Indian credit economy, especially in the rural/agricultural sector, has lived too long with administered rates of interest both in lending and in borrowing. Different lending rates are officially specified for different categories of borrowers and these categories are sought to be spelled out in at least two different ways. In one categorization, the size of farm is worked out in a complicated manner through a conversion of a certain level of income into acreages held by different farmers. When categorised in this manner, the borrowers are defined as marginal farmers (often 0-1 hectare), small farmers (generally 1-2 hectares), middle farmers and large farmers. In an alternative reckoning the categorization is by the size of loan e.g. less than Rs.7,500, between Rs.7,500 and less than Rs.15,000, between Rs.15,000 and less than Rs.25,000 and more than Rs.25,000 etc. Such administrative dual reckoning, especially when imposed as a strait-jacket, is fraught with several hazards. For instance, a large farmer with, say 5 hectares may borrow only Rs.7,500 and qualify for a low interest rate. On the whole in an administered system there is no guarantee that lending officials and institutions can correctly ordain the lending and borrowing rates appropriate to particular cases.

1.15 That is why in the generality of circumstances, these matters are best settled if the market is left relatively free and competitive. We have, therefore, recommended that the Indian set-up must now move in the direction of doing away with the over-administered interest rates and leave a great deal of interest determination to the banks and institutions in line with the market forces of supply and demand. This new arrangement may have some inequities especially when markets are oligopolistic and not fully competitive, but are certainly less prone to error than the arbitrary decision-making according to an administrative rule of thumb. Banks must, therefore, be left free to make haste albeit slowly towards market oriented rates for lending and borrowing for the generality of farmers and rural people. In this context we appreciate the recent policies of the RBI which spell a degree of liberalisation and freedom to the commercial banks in the non-agricultural sector in determining the rates of interest charged above a certain limit. This movement can be allowed cautiously to go further and envelope agricultural lending as well. This freedom will also enable the commercial banks to secure interest earnings consistent with viability which the present system of administered rates does not ensure.

1.16 A safeguard is, however, necessary as the banks with their newly won freedoms, could become over-zealous and charge inordinately high rates, say 20 per cent p.a., to some customers. To prevent such excessively high rates and to avoid high cost of production we suggest continuance of the present ceiling rate of 15.5 per cent for agricultural lending in the immediate future.

(vi) Administered Rate for Specified Categories of Borrowers

1.17 However, there is a compelling need in the present context of the rural economy to have, for the weaker sections of the rural community e.g. small and marginal farmers, artisans etc., a concessional interest rate. We have recommended that this rate should not be less than 1.5 percentage points above the highest commercial banks deposit rate. This means that the level of concessional interest rate would not be less than 11.5 per cent (from which level, it was brought down to 10 per cent in 1987 in the context of the severe drought).

1.18 This said, our other important assertions must be repeated to state that lower rates such as 11.5 per cent and other concessionalities in the terms and conditions of lending must be practised only in lending to the weaker sections such as the marginal and small farmers, rural artisans and professionals. So long as the overall credit economy is generating surpluses, concessional rates focussed on the poor cannot do institutional harm but may do a great deal of social and economic good.

(vii) Government to bear the Cost of Infrastructures and Mandatory Programmes

1.19 We have stated that the economic environment and the banking system mutually act and react on each other. The improvement of economic environment in a developing economy requires infrastructures as well as development programmes. These infrastructures and programmes, be they for the poor or the not-so-poor, would have to come nearly wholly from the governments and we do not see the banking system as the provider of infrastructures. Similarly in the provision of other necessary mechanism like extension services we believe that this too is an appropriate function of the government. In any case, the banking system cannot bear these costs. However, we see that when a banking system moves in a real sense to development banking, it will be called upon to bear some of the costs of mobilisation, canvassing, propagating, field work and developmental work, besides the normal costs

of its commercial operations - that is to say, the costs of all the tasks that developmental banking is required to perform and no more. We believe that on the whole the costs of developmental programmes, especially the mandatory anti-poverty programmes, should fall largely on the governments. The banking system should not be called upon to bear the cost burden of items which are normally in the area of responsibility of the government. We note that in any case the present day RRBs and co-operatives are in no position to bear the costs of developmental banking while the commercial banks have already been burdened to such an extent that their annual profits have come to be only about Rs.260 crores in 1987 which constitutes only 0.21 per cent of their working funds.

B. Critical Stock-taking of the Rural Credit System

Quantitative Expansion

1.20 The acceptance and implementation of the many recommendations of the Rural Credit Survey Report (1954) gave a new impetus to the co-operative institutions and spelled a massive expansion of both the short-term and the long-term co-operative credit systems in partnership with the governments. Then came the nationalisation of commercial banks in 1969 and the consequent massive extension of commercial banking in hitherto unbanked and less banked agricultural and rural areas. Since 1975, yet another set of banking institutions - the Regional Rural Banks (RRBs) - has emerged on the rural horizon with the intention of supplying inexpensive credit to the poor and has managed to proliferate extensively.

1.21. The years since 1961 have witnessed a colossal expansion of numbers in all credit systems (See Annexure). Between 1969 and 1986 the number of commercial bank branches has increased from 8,262 to 41,395 of which rural branches have spiralled from 1,832 to 18,286 in 17 years so much so that rural branches now constitute 44.2 percent of the total branches, though credit disbursed through them is still only 15 per cent of the total commercial bank credit. During 1961-1986 period, deposits have increased from Rs.1,745 crores to Rs. 1,03,309 crores with an annual growth rate ranging from 11 to 28 per cent in different quinquennia. Even in the 10 years 1976-86, short-term loans and advances of commercial banks to the agricultural sector have gone up from Rs. 212 crores to Rs. 1,252 crores (about five fold) while term loans have increased from Rs. 192 crores to Rs.1,476 crores (about seven fold).

1.22 The RRBs too have multiplied from 6 in 1975 to 194 in 1986 and their branches have grown from 17 in the earlier year to 12,838 in the latter. Their deposits have moved from a meagre Rs.7 crores in 1976 to Rs.336 crores in 1981 and to Rs.1,714 crores in 1986. Starting with negligible figures, their short-term and long-term loans issued during 1986 have reached a figure of Rs.672 crores.

1.23 As for the co-operative sector, for the period from 1961 to 1986, though the number of Primary Agricultural Credit Societies (PACs) declined, as a result of reorganisation from 2,12,129 to 92,408, taking the PACs together with the District Central Co-operative Banks (DCCBs) and the State Co-operative Banks (SCBs), their total deposits have moved on from Rs.199 crores in 1961 to Rs.8,889 crores in 1986 - the annual percentage growth ranging between 13 and 19 in different quinquennia. The short-term and the long-term loans issued by PACs increased from Rs.203 crores in 1961 to Rs.3,140 crores in 1986, a point to point rise of 14.0 per cent in 25 years.

1.24 And finally in the long-term co-operative system i.e. the State Land Development Banks (SLDBs) the loans issued by the system grew from Rs.56 crores to Rs.533 crores - a 9 fold increase in 20 years between 1966 and 1986.

1.25 In consequence of all this, institutional credit has been extended quantitatively to a very large number of borrowers. Millions of first-generation depositors and borrowers have been introduced to the banking system and have shifted their loyalties from the non-institutional money-lenders and pawn-brokers to banking institutions and co-operatives. These latter have competed away the exorbitant interest rates and usurious terms and conditions imposed by the money-lenders and have considerably lowered the whole structure of rural interest rates-their own by their exertion and the money lenders' by their example. The 'dual economy' has melted substantially but the money-lender has not gone away. The non-institutional sources still remain, purveying their credit at high interest rates which, however, are now lower than before. Some of the basic needs like consumption credit are in the main met by these sources.

1.26 These remarkable expansions, obtaining universally in all the rural credit structures of the country in the past quarter of a century, which under-

lining the important phenomena of larger access to credit and to a substitution of institutional for non-institutional credit, also reflect real growth even when adjusted for the rate of inflation which has generally ruled around 10 per cent and sometimes even more, in the last quarter century. A 10 per cent growth in a mere monetary quantity like deposits or advances is roughly equal to no growth in real terms. We notice, however, that even after correcting for inflation, the real terms growth in the deposits as well as the loans of nearly all of the credit systems has been positive and in the case of commercial banks quite impressive.

Structural Defects and Operational Deficiencies in the Credit Systems

1.27 But this growth of deposits and advances, far from exploiting the potential fully, has not made much dent in the rural economy as evidenced by the fact that only about 30 per cent of the rural families have demanded or have obtained access to the institutional credit system. It is true that the small and the marginal farmers, with land holdings of less than 2 hectares and operating about 25 per cent of the sown acreage, have received about 42 per cent of the total institutional credit. This, in all probability, is due to specific policies and concessionary conditions of credit offered by the banks and the government. At the other extreme, the larger farmers with holdings of more than 4 hectares and commanding 52.6 per cent of the cropped area also seem to have access to credit in a proportion larger than their acreage warrants. This is presumably owing to their influence, bigger asset holding and greater dependance on hired labour. But it is the middle level farmers with holding between 2 to 4 hectares and commanding a large percentage of sown area, who seem to have lesser access to credit than warranted by their large hectarage. All in all, in the aggregate as well as for the middle farmers, the credit system has a long way to go before it can be said to be extensively used or begin to change the weak structures of the agricultural economy and of the rural credit institutions. Except for the commercial banks, we are not satisfied with the quantitative real-terms growth in rural banking nor with the quality of performance in any of the institutional credit systems and hence we have focussed in the Report on the widening as well as deepening of this system.

1.28 Through the work of our consultants as well as our own nationwide observation and analysis, we have identified a large number of weaknesses,

limitations, inadequacies and flaws, as well as basic structural defects, some pertaining to the credit systems as a whole and some relating specifically to one or the other of the credit institutions. We propose first to deal with the weaknesses of the credit system as a whole and then with an analysis of the weaknesses of specific credit institutions.

(i) Weak Recycling of Credit

1.29 Running like a thread in all the institutional credit systems - the CBs, the RRBs and the Co-operatives - is a failure to recycle credit effectively in order to perpetuate and enlarge this credit cycle. The credit cycle has three major segments; the first is to mop up resources from the society through deposit mobilisation and other means; the second is to lend the funds so mobilised to worthwhile borrowers who have viable agricultural/rural projects to run; and the third is to recover fully and promptly whatever has been lent, so that the recovered amounts can be put back into the credit cycle together with any further resources mobilised meanwhile alongside some refinancing from higher institutions, to the extent possible. We have made a thorough analysis of all the three credit systems and have highlighted the common as well as the specific weaknesses of these systems in generating, sustaining and augmenting the credit cycle.

(ii) Poor Deposit Mobilisation

1.30 With the possible exception of the commercial banks, we notice that neither the RRBs nor the co-operatives have really developed a culture of deposit mobilisation and resource generation. While the European co-operatives of the Raiffeisen or the Schulze Delitzsch variety, and the co-operatives in Japan and South Korea in somewhat comparable periods of economic development, never relaxed on deposit collection, the Indian co-operatives did not make it their business to mobilise deposits from the poor and, arguing that the poor had no savings, softpedalled resources mobilisation. They thus came to depend heavily on refinancing and other funds coming down vertically from the higher tier institutions and shunned self-reliance on own funds. This being the case, the members, that is the share holders of the PACSs in many cases never came to treat the PACSs funds as their own funds, never exercised the needed vigilance on their managements and allowed the system to perform

weakly and fall into numerous inefficiencies ranging from low-paid and unskilled secretaries to low-powered management, shabby physical structures and slapdash and unprofitable performance.

1.31 As for the RRBs, though there was no bar on raising deposits from any category of the local population, the bar on lending to the non-poor and economically resilient sections demotivated the non-poor categories from depositing their savings and earning in the RRBs system; for depositors would generally deposit in institutions which also offer to them other services like loans and advances. The bar on lending to the non-poor was a well-meaning constraint; but it did have the unintended result of acting as a constraint on the further deposit mobilisation.

1.32 All in all, we notice that deposit mobilisation which is the crucial starting point of the credit cycle is a weak aspect of the co-operative and to a lesser degree of the RRB system and such growth rate of deposits as is in evidence, does not amount to very much when corrected for inflation and observed in real terms. The starting point is almost fading away. The commercial banks, even in their rural garb, seem to be doing better on deposits but even here, when corrected for inflation, the rates of deposit growth are not particularly impressive.

(iii) **Ineffective Lending**

1.33 Coming to the second segment of recycling, namely effective lending, we find that all the three systems are a scene of considerable deficiencies. The co-operatives lend only to their members and the way things are, there are many impediments in the enlargement of borrowing membership to anything like an extensive, leave alone a universal, scale. It is of course right and fair that co-operatives should lend primarily to their members. But we are going to find other methods for a much enlarged co-operative lending possibility.

1.34 Even the commercial banks cannot be totally absolved from a lack of serious effort in lending to the agricultural/rural population despite

the existence of a unique cross-subsidisation possibility. This hesitancy of the commercial banks' staff, barring some dedicated and selfless people, is predicated on the fact that they have not yet been able to convert commercial banking into development banking successfully. Owing to traditional, institutional and attitudinal factors, many of the commercial bank staff do not stir themselves often enough from the bank parlours into the field to canvass deposits on the one side and prepare suitable projects, tie up the loose ends and canvass potential borrowers to avail themselves of the lending facilities on the other. As a matter of fact, many of the CB staff are not oriented towards staying and performing willingly and wholeheartedly in rural areas - often, of course, for good reasons such as lack of facilities and amenities in rural areas, besides their urban moorings. In effect the CB staff work in rural areas on sufferance and are generally looking forward to the time when they will be transferred to an urban branch. This is an intricate subject which demands very serious attention and we have made some recommendations in this regard. Meanwhile the problem remains that none of the three systems has broken the back of the problem of enlarged and effective lending and hence this second segment of the credit cycle too remains weak and faltering.

(iv) Poor Loan Recovery

1.35 The third and final segment which completes the credit cycle requires that what is lent should be recovered and that the recovered resources should be put back into the system in the next round of the cycle, along with further resources mobilised afresh or obtained through refinance from higher institutions or the system's surpluses, if any. But we notice that the third segment of loan recoveries is faltering even more seriously in all the rural credit systems. In 1986 the percentage of overdues in relation to demand was 41 in the co-operatives, 51 in the RRBs and 43 in the commercial banks. Here, there is nothing to choose between tweedledum and tweedledee. Neither the co-operatives with their membership loyalties, nor the RRBs as banks for the rural poor, nor the commercial banks with all the efficiencies attributed to them and their better trained staff have been able to yield results in terms of rural loan recoveries.

1.36 The credit cycle then is in a battered shape on all the three counts - deposit mobilisation, lending and recovery - in all the three systems - the CBs,

the RRBs and the Co-operatives - except that deposit mobilisation is better in the CB system. We have suggested a series of structural, operational and other measures impinging on all the three segments of the credit cycle in all the systems. But before taking care of these general weaknesses, common to all systems, we must highlight the spheres of major weaknesses which are specific to each system.

Systemic Deficiencies

The Limitations of the Present Day Co-operatives

1.37 We have shown that the co-operatives have been subject to undue governmental interferences and the elected boards have been superseded frequently. They have thus been prevented from developing steadily as a self-reliant and resilient credit system. Moreover, not only are the PACSs and even DCCBs and the SCBs, faltering on all the three counts of resource mobilisation, effective lending and full recovery but have infrastructure weaknesses and functional flaws of their own. Most PACSs do not look like banks in the first place and have failed to inspire the confidence of the potential (or even the present) members, depositors and borrowers. The secretary of the PACS barring exceptions, is a badly chosen, ill-equipped, non-professional and low-paid functionary with little motivation. He is generally not equipped to undertake such demanding responsibilities as canvassing deposits, seeking out good borrowers, preparing, evaluating and monitoring the loan projects and having an acclaimed authority in that area to watch and promote recoveries. Nor is he well-versed in the non-credit business which the co-operatives do and should undertake. As a rule he has a very low salary, out of line with the minimum needs and inflation rates and has no incentive system built into his earnings. He is selected generally by a cadre system in many states and is responsible to the cadre authority rather than to the society. Similarly, the management of the society also has some serious failings comprising as it does unmotivated and untrained members of the Managing Committee with no worthwhile leadership and little guidance coming from the higher rungs of the co-operative structure - the DCCBs and the SCB. All in all, the present day co-operative structure must change structurally and operationally.

The Disabilities of the Regional Rural Banks

1.38 We have seen that the well-intentioned prohibition put on the RRBs,

preventing them from lending to anyone, but the weaker sections tended to make them non-viable. The intended service to the poor became poor service. Though an earlier Committee (Narasimham Committee) had recommended such a restriction on their lending, a subsequent Committee (under Professor M.L. Dantwala) had recommended relatively greater latitude. But this did not find acceptance and the constraint remained. The staff in the RRBs, though recruited from local areas, often did not have the training and exposure to effective methods of development banking. The net result has been that out of 194 RRBs only about 46 are working with some profits, while 148 are running in losses. The commercial bank branches in rural areas, despite their own weaknesses, are lending to the poor as well as mobilising deposits from them in a much bigger way compared to the RRBs. (Even in lending to poor beneficiaries under the Integrated Rural Development Programme, the share of the RRBs is only 18 per cent). The RRBs have thus become anaemic and debilitated structures with very little possibility of rehabilitation and resurgence. Also they have no capacity for cross-subsidisation, unlike the commercial banks. If their loan portfolio were to be opened up for all categories of borrowers, then this will take away their main distinction and make them no different from the rural branches of commercial banks.

The Deficiencies in Rural Commercial Banking

1.39 The rural branches of commercial banks doubtlessly have all the advantages of a resilient banking system including trained staff, fair salaries, cross-subsidisation possibilities and a great banking tradition. Yet certain aspects of their performance leave a great deal to be desired. Nor does the profitability of the rural branches of the CBs turn out to be positive as the operational costs of the CBs are quite high. All these factors require some structured solutions, some managerial ones, and some prescriptions for attitudinal changes, but above all a basic shift from merely commercial to development banking. Luckily the emerging ideas on the linkages between credit planning and development planning in rural areas and the Service Area Scheme recently launched by the RBI promise some breakthroughs in rethinking and implementation and in motivating not only the CBs but the other systems as well. We have some major recommendations to make for all the credit systems in this regard, but especially for the commercial banking system, as we believe that our recommendations will give force, substance and meaning to the concepts of

development planning, credit planning, the service area scheme (which, in an improved form, we call the development area scheme), as well as the IRDP.

NABARD

1.40 Visualised as a centre-piece for the entire rural credit structure at the national level, the NABARD has by now completed seven years during which it has made significant progress in giving refinance to client banks. But, it has yet to emerge as the central driving force of the rural credit system. Of the three main functions, refinancing, inspection and institutional development, the NABARD's thrust has so far been essentially in the areas of refinancing and inspection. Though, of late some steps have been taken, institutional development has not received due place on the agenda of NABARD's principal activities. It is, therefore, necessary that NABARD should from now onwards take fresh initiatives in this direction. It has to take upon itself the responsibility for the promotion of viable co-operatives without which the refinance will have failed to achieve the desired objectives of increasing agricultural production and raising the level of the rural economy. It should also simultaneously take steps to improve the functional capabilities of the client banks in project identification, preparation, appraisal and monitoring by forging a better linkage between its inspection and development functions.

1.41 We recognize the several constraints within which NABARD operates, to name a few, the administered rates of interest, its limited clout over its client institutions, deficient organisational structure inherited from the parent bodies and the emerging resource constraints to meet the lending programmes. We have elsewhere, in this report, made recommendations covering several of these aspects of the rural credit system which will facilitate NABARD's own smooth functioning. Simultaneously, NABARD should concentrate more in the building up of the co-operatives and promotion of finance for the non-farm sector. NABARD and client banks need to improve their project monitoring activities and ensure proper use of credit and recovery of loans to enable the ultimate borrowers to realise full potential from the sanctioned projects. We have suggested that NABARD should increasingly use the leverage of refinance to build up its clout with its client banks. NABARD has to graduate, in course of time, to be a strong development bank with its own stature and image to enforce the required discipline among its client banks. We are confident, that basically a financially strong institution like NABARD should

be able to cover considerable ground in the next decade or so with the active support of the Reserve Bank and the assistance of the newly proposed National Co-operative Bank.

C. Restructuring and Reforming the Agricultural Credit System

1.42 On the question of restructuring and reform of agricultural and rural banking we first deal with those issues which affect the credit system as a whole - such as the elimination of over-administration, inculcation of higher efficiency, lower costs and improved margins and the provision of development planning and credit planning mechanism at the district, block and village levels and then move on to the restructuring of and the operational changes in each one of the three systems. While approaching the solution we remind our readers of one of the basic tenets of our thinking - the two category solution - that credit policy and also developmental policy in general must now become commercially oriented, market oriented and development oriented as a rule, barring policies designed for the weaker and the low income sections of the population which still need a priority treatment in concessional terms. There, in the priority areas, and there alone, should policy deviate from market orientation and undertake special measures, including special credit measures like lower rates of interest and well focussed subsidies for the sake of uplifting the poor.

Improvement in Margins for Banking Institutions

1.43 Studies and observations, whether by our consultants or by ourselves, confirm the fact that the gross margin, the difference between the lending rates received on the one side and deposit and borrowing rates paid on the other - though positive are very low in all the credit systems. It is also clear that the administrative and other non-interest costs of all the systems are quite high per unit of operation, without even taking into account the cost of risks, overdues and bad debts. The small scale of operation makes the overhead costs per unit of operation excessively high. By the time these high unit costs of operations are deducted from the thin, though positive, gross margins, the net margins become either extremely low or negative, barring some segments of one or two systems. This is an untenable situation. The banking institutions can survive and grow only with the earnings of reasonable margins.

1.44 The effect of freer interest rates as recommended by us will obviously be, in a capital shortage economy, to enhance the average level of interest rate in the rural sector, barring the poor. The gross margins will definitely increase and, other things being equal, bank profitability and the credit cycle will get enhanced.

1.45 Simultaneously with the increase of gross margins the banking system has to make a serious effort to enlarge the net margins which finally generate bank profitability and enhance the resources for further expansion of the banking system. Enlarged net margins also permit, if required, a cross-subsidisation of the socially necessary but economically less rewarding segments. Little has been done in the Indian system for cost reductions, as the focus has not been on the improvement of quality and efficiency but on the expansion of volume. We have several suggestions to make for cost reduction such as improving productivity per worker through better recruitment and training, better understanding of development banking norms by the staff and manager, more active field workers both for the canvassing of deposits and better lending by bringing in worthwhile project-oriented borrowers into the banking system, enhanced loan recoveries and risk reduction, computerisation and the consequent efficiency improvement and so on. To the extent these things happen, efficiency improves on the one hand and volume of business on the other; and to the extent business volume increases, the costs per unit of operation will come down and net margins will get enhanced. As the banks and credit institutions earn and live by the net margins and business volume, we believe, our suggestions in this regard are crucially important and make all the difference between a loss making and profitable banking system.

Development Planning, Credit Planning and the Development (Service) Area Scheme

1.46 We have referred earlier to the linkage between the state of the economy and the efficacy of the banking system. This underlines the need to link credit planning with development planning at the district, block and the village level as far as possible. In the formulation of the district plan, aside from the government functionaries at the district level and the representatives of the people, the participation of the representatives of the banking and credit institutions including the co-operatives, is absolutely essential. Until such time as information and data at the block and the village levels

emerge, development plans should be made, with rigorous methodologies, at the district level and be split subsequently into block and village plans. Later on, as data emerge, planning can come down to the grass root level of the block and the village.

1.47 The credit plan at the district level, prepared essentially by the banking institutions in the district should emerge from the development plan and should not be unrelated to it, as has been the case in the past.

1.48 But our next crucial and important recommendation is that neither the district credit plan nor, for that matter, the derived block and village credit plan should become merely a preserve of the commercial banks. A full-fledged participation by the representative of the co-operative systems-long and short - both in the making and implementing of the credit plan and in the operation of the service area scheme is absolutely essential. The service area scheme should be a combined effort of the commercial banks, the RRBs (which will merge with the commercial banks and begin to operate as their rural branches) and the co-operatives. No doubt the District Lead Bank Officer will be the key co-ordinator in the credit planning system and may well be the Chairman of many of the crucial Committees, but the role of the co-operatives cannot be soft pedalled. We say this emphatically because we have an irksome feeling that the co-operatives tend to get sidelined and neglected in several models of district planning and block planning both in developmental and credit terms.

1.49 In our chapter on Development Planning & Credit Planning, we bring out a set of major recommendations on this crucial subject of district, block and village development and credit planning and link up all this with the Development Area Scheme for a grass-root credit reorganisation. We suggest the evolving of a methodology for a district development plan which will then generate a district credit plan.

- i) One part of this methodology will be for the provision by the State of infrastructures like minor irrigation, roads, power generation facilities, extension services, health clinics, hospitals, vocational and technical schools, training centres, animal breeding centres,

market structures, public storages etc. The other part will be a plan for private production and asset construction embodying various schemes and projects for land utilisation, private irrigation, electrification, rural industrialisation and technology improvements, bunding, drainage, well-sinking and provision of tools, designs and transport etc. equipment. This plan will be evolved from past trends and future potentials and endowments.

- ii) The next step will be to generate the district credit plan from the district development plan. The two will be inextricably linked with each other. While the State's infrastructures at the district level will be built from budgetary resources, the private assets and output will come out of private savings and institutional finance. The institutionally financed part will be the district credit plan.
- iii) The next thing to do is to develop strong linkages.
 - a) a vertical linkage between the district, block and village development plans,
 - b) a lateral linkage between development plans and credit plans at the district, block and village level, and
 - c) a horizontal linkage between PACSs, PLDBs, CBs and RRBs (new rural branches of the CBs) in the service area scheme, to be redesignated in its improved form as the Development Area Strategy (DAS)
- iv) Thereafter, the district development plan and the district credit plan will be split into their block and village counterparts, the block credit plan being dovetailed with the block development plan and the village credit plan with the village development plan.
- v) At each of the three levels - the district, the block and the village the respective credit plans will be made, allocated and operated by credit institutions.
- vi) At the grass-root level of the village, the major credit agencies - the CBs, the erstwhile RRBs (new rural branches of the CBs), the PACSs and the PLDBs - will co-ordinate their credit activity horizontally.

Some Important Features of the Development Area Approach

1.50 We are in broad agreement with the service area scheme recently

evolved by the RBI, its essential feature being the allotment of every village in the country, to one commercial bank or another for effective banking service. We, however, wish to deepen the effectiveness of the scheme through what we call a Development Area Scheme. This scheme embodies a re-ordering and a rationalisation of the branch network of the CBs in order to avoid wastage of resources and effort, generate scale economies and reduce costs. It also embodies the inclusion of the co-operative banking system as a partner in credit planning and implementation. Moreover, it requires a shift from mere commercial banking to a development banking strategy in which emphasis shifts, on the one hand, to effective savings mobilisation through new techniques of financial intermediation and, on the other, to effective lending, with the banker going out of his parlour to canvass new schemes and projects, tying up credits with inputs, inputs with outputs, outputs with repayments and repayments with new lending. The banker thus enlarges the credit cycle continuously by becoming a friend, philosopher and guide of the client at every stage.

1.51 We recommend that even as each village is allotted to a commercial bank branch, a block should be allotted to one commercial bank instead of many. This would presumably be the bank which already has the largest presence in that block - an area with about 100 villages. We have shown that such an arrangement does not compromise the main tenet of the multi-agency system namely the freedom of access on the part of a borrower or depositor to more than one banking institution that is, a co-operative or a commercial bank branch, or another branch of the same commercial bank within the block, or another commercial bank just outside the block or at the district centre, or indeed any commercial bank branch anywhere.

1.52 Such a homogenisation of blocks with the presence primarily of branches of one commercial bank, as we have shown in the relevant chapter, eliminates wastage, reduces banking costs, makes guidance and monitoring by supervisory staff possible on regular and continuing basis rather than for a few days in a year and builds into the system many economies of scale.

The Co-operative System

1.53 To reform the co-operative system and to put it back on the rails, our recommendations are nothing short of major structural as well as operational

and managerial changes. We believe that the co-operative movement has never been allowed to function effectively and has been vitiated by too much officialdom, although it has great potentialities for specialised service as well as credit disbursement.

1.54 To make the co-operative system what it should be, governments must forthwith withdraw their intervention and interference. Nominated functionaries presiding over the SCBs and other co-operative institutions should be withdrawn and the elections of the office bearers and the managing committees should be held promptly. In fact, changes need to be introduced in the co-operative law which will make it impossible for protracted supersession and take over of the co-operatives to take place. We recommend that such changes in the co-operative law be brought about soon. Similarly, changes in co-operative practice would have to be made to ensure that under no circumstances role of the Co-operative Registrar is an overpowering one. A good deal of decision making has to be transferred back to the co-operative institutions and even some of the overseeing has to come from the higher level co-operative institutions such as the DCCBs, the SCBs and the SLDBs. We have made various recommendations in this regard at appropriate places.

1.55 Aside from the undue supersessions and interventions, the most serious difficulty in the co-operative system, as we have shown, is at the level of selection, training, accountability, range of responsibilities and performance of the secretaries of the PACSs and the managers of the PLDBs. We have made strong recommendations to the effect that the secretaries of PACSs and the managers of the PLDBs should be persons of higher qualification. They should be chosen by the managing committees of the primary units rather than be selected under a cadre system. This, we believe to be a crucial requirement in order to establish accountability of the functionaries and the self-reliance of the movement.

1.56 As for the salary of the primary level secretaries and managers we have recommended that they should have a two-part salary structure, that is, of a clean and respectable living and increasing sensibly enough to cover inflation. But our most important recommendation here is that in addition to a reasonable basic salary, they should get an incentive payment linked with

their performance in specific identified areas of work such as (a) deposit mobilization (b) loaning (c) recoveries (d) commodity sales and (e) profits.

1.57 We have also recommended a series of measures for the training and re-training of PACSs' secretaries and co-operative managers at various other levels and indeed for the training of the members of the managing committees. On the whole we believe that a well selected, well trained, well paid and incentive oriented functionary like the secretary, responsible to the society itself, would doubtless improve its performance and profitability especially when the other measures we have recommended are also adopted simultaneously.

1.58 We are quite clear that the co-operative base level institutions which do not look like banks in the first place, should have a major face-lift and essential facilities such as a proper building, banking counters etc., so as to inspire confidence among the present and the potential members of the co-operatives.

1.59 We would like to point out that in order to bring about such a nation-wide face-lift and a nation-wide training of co-operative functionaries, the own funds and profits from within the co-operative system would certainly not suffice. Here is a legitimate need where a major long-term arrangement or a subsidy to the co-operative movement, continuing over a period of years and tapering off later, would be absolutely necessary. And this, in our view, would have to come from the government and the national level institutions like NABARD and the co-operative institutions - SCBs, SLDBs and DCCBs.

1.60 We have shown in the Report that a basic built-in weakness of the Indian Co-operative Credit System has been its inability to mobilize adequately deposits and small savings horizontally and hence its dependence vertically on funds from higher institutions. This led to non-self reliance on the one hand and a lack of proper vigilance on the part of co-operative membership on the other. One of our key recommendations, therefore, is that the co-operative banking system at all levels must make it as an article of faith to mobilize deposits and other resources in much larger volumes in order both to reduce its external dependence and to improve the process of credit recycling.

The National Co-operative Bank of India

1.61 The leadership of the co-operative credit movement at the national level is currently going by default, and to provide such a leadership backed with its resource, we have strongly recommended the establishment of a national co-operative apex institution to be called the National Co-operative Bank of India (NCBI).

1.62 We notice in the first place that there are as many co-operative apexes as there are state co-operative credit organisations - perhaps 50 in number and there are no inter connections between them. There are no organic arrangements for the transfer of the surplus funds of one co-operative apex to another. All in all, there is no possibility at present of balancing within the system, of funds between surplus and deficit co-operative systems.

1.63 The National Co-operative Bank of India (NCBI) which we envisage will function essentially as a balancing centre. It will retain the co-operative business which is currently going away to the other banking sectors and will be a receptacle and lender of funds for national federations and other co-operative structures such as the IFFCO, KRIBHCO, etc. It will also be a receptacle of funds from international institutions such as funds from the World Bank, IDA, etc. The bank will assist through funding and the building up of new co-operative businesses like exports and housing as is happening in the resilient co-operative credit movements of countries such as Holland, the Federal Republic of Germany, the Republic of Korea and Japan.

1.64 The agricultural rural economy is now a nationally integrated economy but there is no national co-operative credit apex to represent the movement. Providing such a national representation to the co-operative movement in decision making at such levels as the Bankers' forums and other national and regional decision-making authorities appears to be an absolute necessity.

1.65 The NCBI, though beginning with a modest but viable size, will grow with its own momentum and the momentum of the movement in course of time. We have also clearly stipulated that the NCBI will not act as a channel of NABARD/RBI funds and will not add another tier to the refinancing chain.

The National Co-operative Bank, therefore, is not cast as a counter to or a competitor with NABARD. The NABARD is not the apex of the co-operatives nor is it a co-operative bank. It is the higher apex of the co-operative as well as the commercial and the regional rural banks, performing the re-financing function and other functions which do not compete with those allotted to the new Co-operative Apex Bank. Elsewhere in this Report we have made many suggestions for the strengthening of the NABARD itself and for its more effective functioning with better leadership qualities for the rural banking system as a whole than it now has. The NCBI will indeed be an ally to NABARD in the total process of development.

A Fully Rounded Co-operative Sector

1.66 We thus provide from many directions measures for the strengthening and more resilient and profitable functioning of the co-operative movement, profitable to itself and to the economy. Our recommendations about the co-operatives thus amount to :

- i) the elimination of supersessions and interferences, a very early conduct of elections, legislative prohibitions for future supersessions and interferences and the establishment of an autonomous co-operative movement;
- ii) a strengthening of the base of the co-operative movement by various structural and operational measures recommended by us in the Report and by suggesting better selection, higher qualification, improved training, enhanced scales of pay and incentive earning linked with performance; for PACSs secretaries ;
- iii) the provision of a National Co-operative Bank of India to balance surpluses and deficits, to assist in retaining and securing co-operative business in profitable field and to provide national representation to the co-operative movement and ;
- iv) a clear shift of emphasis towards the mobilising of deposits and small savings so that the co-operative system not only reduces its excessive vertical dependence on extraneous finance and improves its horizontal self reliance but also subserves the national objective of savings, enhancement, balanced sectoral investment and resilient economic growth.

Regional Rural Banks

1.67 We have in this Report analysed the working of Regional Rural Banks (RRBs) in great detail. Though the RRBs have proliferated to be 194 in number with 12,838 branches, they have, as might have been expected, become a scene of severe economic losses and have brought upon themselves what appear to be permanent disabilities. As we have already stated, only 48 out of the 194 RRBs are making some semblance of profit but the remaining 146 are in the loss making category. Their intended low-cost structure has ceased to be low-cost with progressive increases in the scales of pay of their staff, now in many states on par with Central Government scales. Studies have shown that they will continue to be non-viable even if they are allowed to lend to an extent to the non-poor category of borrowers also.

1.68 While we fully share the concern of the governmental policies and programmes to uplift the poor, we realize that none of the factors which are affecting the viability of the RRBs, can change favourably with the present structure of the RRBs. Thus, these institutions seem to be subject to permanent disabilities, so much so, that the aim of serving the poor has ended up in giving poor service. It is owing to these permanent disabilities that after much search for alternative arrangement, we have reached the conclusion that there is no choice except to put the RRBs under the umbrella of the sponsoring commercial banks, in a major overhaul of the present structural arrangements. It should be noted that in terms of our recommendations, the RRBs would stand abolished as legal entities and would merge with the commercial banks which originally sponsored them. Their branches may continue as rural branches of commercial banks. However, we stress that it should be incumbent on the commercial banks to maintain after merger in the new rural branches, at least the same proportion of lending to the poor as prevailed before the merger. We have also recommended that the current target of lending to weaker sections by the commercial banks at 10 per cent of net bank credit be raised to 15 per cent to take care of such increased lendings to poor in the post-merger period. We believe that such a merger will have the advantage of larger resources for the merged RRBs through cross-subsidisation possibilities. As the erstwhile RRBs, that is to say the new rural branches, will lend to anybody, though especially to the poor, they will, by raising larger deposits from the small as well as the large depositors, be able to serve the needs of the area better.

Overdues in the Banking System

1.69 Running like a thread throughout the agricultural/rural credit system is the problem of high overdues. It will be seen that the loans overdue in the commercial banking system ranged between 43 per cent and 48 per cent of demand during the decade 1976-1986. The overdues in relation to demand were somewhat higher among the RRBs and hovered between 48 per cent and 52 per cent. In the short-term co-operative system (PACSS), the comparable percentage of overdues ranged between 34 and 43, though in 1981-82 the percentage rose to 50. In the co-operative long-term credit system (LDBs) the overdues varied between 34 per cent and 46 per cent of demand. It would thus appear that irrespective of the system, the overdues are a hardened constant. In our report we have analysed the overdues from various angles, that is to say according to the type of credit institutions, by regions, by states, according to the purpose of borrowing in different credit institutions, by type of areas such as irrigated or otherwise and dry or hilly and tribal, by different class of borrowers such as large, small and marginal farmers and landless labourers and indeed by the age of loan.

1.70 From our own analysis and those of our consultants it is clear that variations apart, whatever category is analysed, the percentage of overdues to demand works out to be an alarmingly large figure. These overdues impair, on the one hand, the eligibility of the borrower for fresh loans and his access to resources for raising the next crop and, on the other, place a serious constraint on the lending capacity, liquidity, profitability and, in the ultimate analysis, the solvency of the institutions. For the system as a whole these overdues give a body-blow to the credit recycling process inasmuch as that which cannot be recovered, cannot be re-lent and put back into the cycle. We note that the famous banking theorem that deposits create advances and advances create deposits is true only when the amounts advanced are also recovered. But this truth is not being realised in any of the Indian rural banking systems.

1.71 We have come upon numerous causes of the inordinately high percentage of overdues to demand and have presented in our chapter on overdues, the relative importance of these factors or causes as observed by the institutions

and indeed by the borrowers themselves. It appears that overdues mount owing to factors internal to the lending institutions as well as extraneous to them. Overdues also mount owing to causes within the control of the borrowers e.g. wilful defaults through cynicism, defiance, etc., and those external to and beyond the control of the borrowers e.g. droughts and poor crop seasons, absence of backward and forward linkages in the farm economies such as input availabilities, extension services, marketing arrangements, transport systems, storage facilities, insurance covers, etc. The overdues could also emerge for any of the other numerous reasons such as insufficiency of the loan amount and scale of finance for a given purpose, too early a date fixed for repayment, absence of a cash credit system and the insistence by the institutions on the repayment of the last rupee of loan before the next loan could be given. The overdues situation could and does worsen owing to insufficient staff for monitoring and recovering the loans, inadequate penal provisions and teeth in the law and its execution in dealing with wilful defaulters, the creation of an atmosphere of defiance and non-repayment - and several other factors.

1.72 As bad debts, wilful defaults and extra-ordinarily high overdues constitute a basic malaise of the prevailing rural credit set-up, we have examined the underlying issues and causes thoroughly and have made a series of major and minor recommendations to improve the atmosphere and make it conducive to repayment and recovery. Among the extraneous factors, we argue strongly for a depoliticization of loans, for a total elimination of loan melas and other populist measures and for an identification and strict treatment of wilful defaulters. Simultaneously, in order to tone up the external economy surrounding the borrowers whose weakness is itself a major cause of overdues, we advocate a whole range of improvements to be brought about by the Government such as balanced infrastructural developments, roads, minor irrigation, dry farming methods, spread of new and relevant technologies, better input availability through extension services, multiplication of market structures, transport systems, storage facilities etc. Internal to the credit institutions we advocate a revision of loan recovery dates, rephrasing of loans in suitable cases and a case by case treatment of overdues when these arise owing to flaws within the credit institutions. We also advocate emphatically the establishment of cash credit system in irrigated areas with multiple cropping.

1.73 We emphasise in particular the fact that unlike a previous era when farmers did not have holding capacity and sold their produce almost invariably in the post-harvest season, a very large number of the present day farmers have developed holding capacity and storage and wish to sell the crop well after the harvest when the prices are high. We have accordingly recommended that when a farmer is willing to lodge his produce with the PACSs and agrees to let the institution sell it later on his instructions the institutions should cease to treat the loan amount as overdue. The loan amount and the interest due would be adjusted against the sale proceeds. We have also recommended separately the shifting of the due date of repayment of Rabi loans till the end of August instead of June end.

1.74 We observe that the Crop Insurance Scheme which is being implemented by the General Insurance Corporation since 1985 suffers from several weaknesses. Firstly, the scheme covers only a few crops. Secondly, the state governments have often opted for insurance cover only in respect of crops/areas most vulnerable to damages to the exclusion of others. Thirdly, under the 'area approach' which characterises the scheme, the basic unit for determining the threshold yield and for assessment of crop damages is as large as the district in some cases and talukas/blocks in others. This has resulted in indemnifying farmers generally in specific areas irrespective of the genuineness of losses incurred individually. Further, the insurance premia which are presently fixed on an ad hoc basis under the scheme are as low as 1 to 2 per cent. This has made the scheme non-viable and losses have been mounting year after year.

1.75 We have accordingly recommended that the scheme should cover all cultivated areas as well as the major crops grown and that there should be automatic cover for all borrowing farmers raising those crops in a state. While crop insurance on an 'individual basis' would be ideal, since the administrative difficulties are far too many, we have accepted that there is at present no alternative to an 'area approach'. In regard to the premia rates, we have recommended that these be fixed on an actuarial basis and shared between the insured farmers, the lending agencies and Government, the share of the insured farmers and lending agencies being kept to the minimum. Further with a view to ensuring adequate relief to the farmers, it has been suggested that the sum insured covers the cost of production, interest on crop loans and imputed

cost of family labour of the farmers. We have also emphasised the need for a separate Corporation to be established under an Act of Parliament for implementing the crop insurance scheme.

1.76 We have thus buttressed our recommendations with a crop insurance scheme and a series of other measures as well as a programme of action for an expeditious recovery of overdues. In the programme of action we have proposed a higher recovery rate for current demand than for the old overdues. We believe that a change in the whole package of practices both internal and extraneous to the institutions and to the farm economy will lead to a major improvement in the recovery of loans. But we believe that depoliticization of banks' lending and recovery activities is an important pre-condition for successful recoveries.

Financing of Integrated Rural Development Programme (IRDP)

1.77 In some developing countries economic growth itself is seen to be a poverty alleviating factor as it trickles down into the poverty zone and uplifts the poor. In India owing to the phenomenal mass of people below the poverty line and the relative slowness of economic growth, ranging between 3.5 and 4.5 per cent per year, the trickle down effect was seen to be very limited. Hence major anti-poverty programmes were run in the hope that if growth does not penetrate poverty, the programmes will. One of the most remarkable among Indian anti-poverty programmes and the one which is currently operating in full force is the Integrated Rural Development Programme (IRDP). There are other programmes too for poverty alleviation but the IRDP is substantially a credit-linked programme, unlike others. The basic idea in IRDP was to :

- (i) select several million families - about 15 million in the 6th and about 20 million families in the 7th plan - below the poverty line (defined in recent years as annual income upto Rs.6,400 per family),
- (ii) select viable economic activity in the region ,
- (iii) marry the activity with the selected beneficiaries,
- (iv) provide a capital asset for an activity in the primary, secondary or

tertiary sectors - with a subsidy and a bank loan; in the hope that if the additional output is adequate the family will cross the poverty line.

The programme has been well conceived but several flaws have emerged in its implementation. Drawing upon various evaluations of the IRDP including concurrent evaluations by the Ministry of Rural Development in conjunction with various academic and non-academic institutions, and adding our own observations and analysis made in different parts of the country by us and our consultants, we have provided an appreciation as well as a critique of this important programme and have made recommendations for its toning up and a much better implementation.

1.78 We notice on the financial side that at present the banks are involved neither in the selection of beneficiaries, nor in the identification of viable activities, nor in the matching of activities with the beneficiaries, nor indeed in helping the beneficiaries to prepare feasible projects. The net result is that the banks do not regard the IRDP as their programme and are only involved in it in a mechanical manner. This affects the quality of credit, the goodness of the project, its operations and the recovery.

1.79 We observe that while the average loan recovery rate in direct agricultural advances by the public sector commercial banks was 56.5 per cent and 57.4 per cent in the years 1985-86 and 1986-87, the recovery rate in IRDP for these years and for these banks was 42.8 per cent and 45.3 per cent respectively. We also note that despite colossal expenditures under the programme, amounting to Rs.4,763 crores during the 6th and about Rs.6,702 crores during the 7th plan, only about 12 per cent of the families have crossed the poverty line nation-wide. But even this result was achieved without deducting the loan repayment and interest from the gross income of the beneficiaries which means that the percentage of beneficiaries graduating into non-poverty was even less than 12 per cent.

1.80 IRDP has been reduced essentially to a set of targets to be fulfilled in terms of persons, subsidies and credit given. Substantial increases in IRDP finance have diluted the concept of schematic lending by the banks and most banks have come to accept sponsored applications or some walk-in business to complete their targets.

1.81 In order to involve the commercial banks and the co-operatives more readily in the programme and to motivate them, we advocate that the DRDA and official functionaries should send to the local financial institutions a list of families below the poverty line without naming the beneficiaries and without linking them with a list of economic activities. A suitable list of bankable activities should be separately drawn up by the banks in conjunction with the DRDA. The banks and the co-operatives should prepare feasible projects in line with the potential of the area, pick out the families with reference to their skills, place them in particular activities and project and then give the bank finance. This will make for a responsible involvement of the banking functionaries in consonance with banking principles and practices.

1.82 As the abuse and the wastage of subsidy has acquired alarming dimensions and as the grant of a capital subsidy at the very beginning is the major cause of that abuse, it is one of our strong recommendations that instead of adjusting the subsidy to the unit cost at the beginning, the same should be retained as a fixed deposit at the normal rate of interest with the bank in favour of the beneficiary and adjusted towards the last one or two instalments of loan repayment. That is to say, the bank will have to extend the full unit cost as loan at the beginning and recover the last instalment(s) from the subsidy-deposit. In this manner, we are sure, the abuses will be substantially reduced, the assets will in fact be created and the beneficiaries will overcome the poverty barrier in much larger numbers.

1.83 As the IRDP often flounders on the shortage of assets like milch cattle, sewing machines and other equipments, we advocate the financing of back-up programmes to generate such assets and make them available in larger numbers. We also advocate a technical toning-up of the IRDP through a modernisation of production processes, provision of new technologies, designs, storage and marketing arrangements through co-operatives, non-government organisations and private efforts. We also advocate a decentralization of the public programmes and a variation in the magnitudes and guidelines in order to match the diversity of conditions in a very large country.

1.84 And finally, it must be observed that entrepreneurship is not a common quality and it is not realistic to expect that the country will produce 20 million entrepreneurs - even of small magnitude - in a period of 5 years. It is, of

course, true that entrepreneurship and managerial ability for self employment emerges from unsuspected quarters and millions of people who have never had a chance to run a small business can actually emerge to do so when given the opportunity. It is nevertheless true that millions of others selected in the programme will not be able to make the grade as small entrepreneurs and their businesses will not succeed. We suggest several measures to make a success of those who have managerial potential but we nevertheless make the point that several million people who are or will be selected in the future under IRDP would not make good and had better be given an opportunity for employment in other programmes rather than be pushed into self employment. We strongly recommend the enlargement of the dimension of wage employment programmes such as the Jawahar Rozgar Yojana and a relative containment of the targets of the self employment programmes such as IRDP.

Autonomy of Banking Institutions

1.85 Aside from extraneous factors like an unwholesome economic milieu and some internal weaknesses like inability to recover the overdues fully, the banking systems have come under great pressure from governments both in terms of interference with financially sound decision-making and supersessions of elected boards of management on the one side and being overloaded with (mandatory) lending (and catering) to serve populist objectives on the other. All this amounts to a serious abridgement of the autonomy of financial institutions and this has nearly brought these institutions to the brink of disaster. All this, we assert, must now be put right in terms of a re-establishment of autonomy and responsibility of the banking system.

1.86 To spell out this important matter somewhat we observe that the Rural Credit Survey (1954) strongly recommended a partnership between the co-operative system and the government. That was done with the pious intention of strengthening the financial and the supervisory aspects of the system. But as the recommendations were accepted and implemented, the so-called partnership of the governments became a synonym for paternalism at best and interference at worst. The compelling negativity and one-sidedness of the partnership throttled the system which virtually lost its meaning as a co-operative movement. Self-reliance vanished and tutelage and even captivity to the state administration became the order of the day. Control and regulation in day to day

matters become all too stifling. All too often the boards of co-operatives were superseded, their democratic functioning stopped and the government officers, who had no stake in the independence and self-reliant functioning of the system, took over. The result of this, along with other factors, was that the co-operative "movement" became a static and decaying phenomenon and did not develop the required professionalism. In the process the inherent capabilities of the co-operative movement in terms of educating and training local people in democratic self-management became a casualty. Co-operative funds came to be regarded as government funds and the clock was put back by decades. Our effort in this report is to find solutions for rectifying this situation.

1.87 On the side of commercial banking, there has been a massive expansion in the loan business of the commercial banks since their nationalisation in 1969. The expansion has not, however, been without the concomittant systemic stresses and strains. Among these, the most disconcerting has been the progressive decline in the quality of their loans and advances portfolio. The mounting overdues of agricultural loans and sticky advances locked up in sick units in the industrial sector are a witness to the inevitable strain to which the system has been subjected. One of the reasons for this phenomenon is the increasing involvement of the banking system in providing 'mandatory credit' entailing very rigid 'target setting' pursuant to policy directives by Government. It must, however, be stated at once that it is not our case that the credit systems should or can distance themselves from development programmes. We believe on the contrary, that banks must actively involve themselves in supporting such development programmes as the Government might evolve in the furtherance of its social objectives. Our concern in fact is the irrational manner of extension in the coverage of 'mandatory credit' programmes and over-stretching the 'target setting' in such a way that it goes far beyond what the banking system could contend with or its overall profitability can tolerate. A second concern we have is the interference of the Government and its functionaries with the commercial judgement of the banker and marginalising his role in the appraisal and sanction of projects after defining the limits of 'mandatory credit' and the 'target setting'. In other words what we are against is the short-circuiting of the appraisal procedures and flouting of the established credit norms to suit populist goals since in our view this would be destructive of the credit delivery system itself and in the process, self-defeating in achieving the goals set for the development programmes themselves. The inroads

into the autonomy of the commercial banking system has permeated both the functional and operational areas of the commercial banks.

1.88 It is these areas of inroads into functional and operational autonomy of the credit systems, whether they be commercial banks or co-operatives that we have addressed ourselves in the chapter on the 'Autonomy of Credit Institutions' and several others viz, 'Co-operative Banking Systems -An Overview', 'Short-term Co-operative Credit Structure' and 'The Overdues Syndrome'. We do hope that the recent assurance given by the Union Finance Minister in the Parliament on non-interference by the Central and state governments in the working of the banking and co-operative systems, would provide the basis of future policy in Government's relationship with the credit institutions.

Annexure

Table 1

Deposits, Loans and Overdues - Commercial Banks

Particulars	(Year ended March) (Rs. crores)					
	1960-61	1965-66	1970-71	1975-76	1980-81	1985-86
I. (a) Deposits	1,745	2,950	6,216	11,476	40,549	1,03,309
(b) Percentage growth (Annual)	-	11	16	13	28	20
II. Direct Loans and Advances to Agriculture						
(a) Short-term			236	212	517	1,252
(b) Term Loans				192	746	1,476
III. Overdues in Agricultural Loans						
(a) Amount	-	-	-	200	727	1,878
(b) Percentage of overdues to demand	-	-	-	48	47	43

* Amount outstanding

Table 2

Deposits, Loans and Overdues - Regional Rural Banks

Particulars	(Year ended December) (Rs. crores)		
	1976	1981	1986
I. a) Deposits	7	336	1,714
b) Percentage Growth (Annual)	-	113	38
II. Loans issued	1	406	672
		(Outstanding on 31.12.1981)	
a) Short-term	NA	NA	169 (Short-term crop loans)
b) Term Loans	NA	NA	503 (Others)
III. a) Overdues	NA	54	412
b) Percentage of overdues to demand	NA	48	51

Table - 3

Deposits, Loans and Overdues - Co-operative Banks

(Rs. crores) (Year ended June)

<u>Particulars</u>	<u>1960-61</u>	<u>1965-66</u>	<u>1970-71</u>	<u>1975-76</u>	<u>1980-81</u>	<u>1985-86</u>
I. <u>a. Deposits</u>						
Primary Agricultural Credit Societies	15	34	69	113	291	572
Central Co-operative Banks	112	237	439	985	2423	4932
State Co-operative Banks	72	147	279	724	1674	3385
Total	199	418	787	1822	4388	8889
b) Percentage growth (Annual)		16	13	18	19	15
II. <u>Loans Issued</u>						
Short term (PACs)	183	305	519	917	1513	2746
Term Loans (-do-)	20	37	58	105	243	394
III. <u>Overdues</u>						
Amount	44	125	322	561	1086	1807
Percentage of overdues to demand (PACs)	20	29	39	39	41	41

Table 4

Deposits, Borrowings, Loans and Overdues - State Land Development Banks(Rs. crores)
(Year ended June)

<u>Particulars</u>	<u>1960-61</u>	<u>1965-66</u>	<u>1970-71</u>	<u>1975-76</u>	<u>1980-81</u>	<u>1985-86</u>
I. a) Deposits and other borrowings	42	189	749	1422	2056	2882
b) Percentage growth (Annual)	-	35	32	14	8	7
II. Loans issued	12	56	168	205	363	533
III. a) Overdues	-	3	14	64	243	323
b) Percentage of overdues to demand	NA	2	23	38	53	45

Table 5

Gross and Net Margins
(per Rs.100)

Institution	Income	Financial Cost	Gross Margin	Transaction Cost	Net Margin
(1)	(2)	(3)	(4)	(5)	(6)
PACS	12.09	9.90	2.19	5.40	(-) 3.21
DCCB	11.56	7.47	4.09	3.18	(+) 0.91
SCB	9.59	7.56	2.03	1.51	(+) 0.52
PLDB	10.17	7.78	2.39	3.39	(-) 1.00
SLDB (Federal System)	7.88	6.44	1.44	1.35	(+) 0.09
SLDB (Unitary System)	9.88	6.51	3.37	4.04	(-) 0.67
RRB	11.00	7.80	3.20	6.90	(-) 3.70
CB	11.62	7.48	4.14	6.00	(-) 1.86

Table 6

Overdues of the Various Credit Institutions
As percentage of Demand

Agency	1975-76	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
A. Commercial Banks (CBs)	48	47	48	47	48	46	43
B. RRBs	-	48	50	48	50	52	51
C. Co-operatives							
1. PACSs	34	43	50	40	43	42	41
2. LDBs	34	46	40	44	36	40	39

CHAPTER II

EMERGING SCENARIO IN AGRICULTURAL ECONOMY

Recent Developments

The main purpose of this Chapter is to develop a futuristic view of agriculture towards and a little beyond the year 2000 AD. Starting with a rapid survey of the development of agriculture since independence and taking into account the current situation and the evolving trends we proceed to reflect on how the agricultural scene might improve itself in the next 15 to 20 years.

2.002 Agriculture still remains the foundation of the Indian economy. In good agricultural years food is adequate in relation to effective demand, prices remain stable, agro-business and industries look up, employment improves and rural poverty recedes somewhat. In fact, the total economy becomes buoyant.

2.003 What is important to note is that a sustained high growth rate in agricultural output is not only a strong anti-inflationary force but also makes a favourable impact on industrial growth. According to the World Bank Report, 1980, a one per cent increase in agricultural growth in India is correlated with an increase in internal growth of 0.5 per cent and national income of around 0.7 per cent.

2.004 It is estimated that with the growth of the economy, the share of agriculture in the net domestic product will decline to 32.17 per cent in 1990-91 and further slide down to 25.32 per cent by 2000-2001 as happens normally in the process of economic growth. But the proportion of the population dependent on agriculture has declined only slowly from 70 per cent in 1950-51 to 65.5 per cent in 1984-85 which means that about two-third of India's population still remains dependent on agriculture and allied occupations. This is further evident from the fact that whereas nearly 7 million people come to the employment market every year, the number of new jobs in the organised industry is reported to be not exceeding 500 thousand a year so that most

of the population either gets absorbed fully or partially in the unorganized sector or remains bottled up in the agricultural sector.

2.005 More specifically, agriculture's share in national work force or consumption pattern would decline much more slowly than its share in national income, particularly when Indian agriculture is characterised by small farmers and high population density, which require land and labour technological change to reduce the constraint of primary foods/non foods and consequent constraint of goods and raw materials. Such land and labour augmenting technological change would also facilitate diversification of agriculture and development of food processing industries which would in turn demand strong support of institutional credit and public and private investments.

Land Reforms

2.006 Recognising that absentee ownership and insecure tenancy were the major causes of lack of incentives, low investments and low productivity in agriculture, Indian agricultural policy was deeply concerned with basic structural changes in the land ownership rights, tenurial security and land distribution in favour of the landless and small farmers. Although this experiment met with some success in some parts of the country and millions of tenants obtained ownership rights and millions of absentee owners began to cultivate their lands themselves, the problem of share-croppers bataidars or bargadars continues. These are actual tenant owner farmers who supply not only their and their families' labour to their farm but also provide inputs like bullocks, ploughs, fertilizers, manure etc., but are not recognized as tenants and pass on as mere farm-hands or wage-recipients. In fact, they cultivate themselves and give a share of the crop, say 35 to 50 percent, as rent to the land-owner. Their names are not recorded in the Record of Rights or other village papers and they do not get any other rights under tenancy reforms. Nor has the land distribution strategy under land reform and ceiling legislation succeeded in releasing much land for transfers to the poor farmers or the landless and numerous benami transfers and subtle or open violations of law taken place. Hence the need to identify the true tenants through village committees and other methods and the need to give them their rights under land reforms continues with the growth of population and prevalence of here-

ditary rights at death, the sub-division and fragmentation of landholdings continues unabated. This is affecting and bound to affect not only productivity of agriculture adversely but also the capacity of the agricultural credit institutions to manage vast number of small accounts. To break this bottleneck, consolidation of holdings should get a top priority in the development programmes of the nation. Also, institutional factors such as effective implementation of the existing legislation on land reforms and incentives to the tenants for the application of available technology are extremely important for creating the necessary environment for breakthrough in agriculture.

Production Performance

2.007 Agricultural production has shown reasonably good growth in the Five Year Plans from 1950-51 to 1985-86, more particularly since 1967-68 to the post-Green Revolution period. The increase in production of different crops between the triennia ending 1969-70 and 1985-86 are presented in table 1.

Table 1
Increase in All India Production of Principal Crops
between Triennia ending 1969-70 & 1985-86

Crop	(Million tonnes/bales)			
	Production Triennia ending		Increase in Production	
	1969-70	1985-86	Absolute increase	Percentage increase
Rice	39.27	60.86	21.59	55
Wheat	18.43	45.48	27.05	147
Coarse Cereals	27.09	30.51	3.42	13
Pulses	11.40	12.61	1.21	11
Total Foodgrains	96.19	149.46	53.27	55
Groundnut	5.16	6.36	1.20	23
Rapeseed & Mustard	1.49	2.77	1.28	86
Soyabean	0.02*	0.85	0.83	-
Total Oilseeds	7.63	12.26	4.63	61

(Million tonnes/bales)

	Production Triennia ending		Increase in Production	
	1969-70	1985-86	Absolute increase	Percentage increase
Cotton**	5.60	7.84	2.24	40
Jute and Mesta**	6.07	9.41	3.34	55
Sugarcane	118.40	172.03	53.63	45
Potato	4.29	11.81	7.52	175
All Crop Index	100.00	156.00	56.00	56

* For the triennium ending 1972-73

** Million bales

2.008 As will be seen from table 1, the index of agricultural production rose by 50 per cent during the period 1969-70 to 1985-86 and the foodgrains production experienced a similar growth.

2.009 Agricultural development in the 70's was spearheaded by foodgrains production partly by high yielding varieties of wheat and rice in combination with such complementary inputs as high levels of fertilizers, expanded irrigation facilities and farm equipment and machinery. As a result, a qualitative change has come about in the form of relative shift in area and production in favour of cereals with superior technology, especially wheat and rice.

2.010 A new resilience has been imparted to agricultural production which is showing larger spurts to higher peaks in favourable years and smaller dips in the unfavourable years. The peaks and troughs in foodgrain production are shown in table 2 for the period 1970-71 to 1988-89.

2.011 It will be seen from table 2 that the shortfalls in foodgrains production during unfavourable years compared to preceding peak years have been of smaller magnitude in the eighties compared to the position during the seventies.

2.012 More recently, the performance of foodgrains sector during the 1987-88 drought, which is rated to be even more severe than that of 1979-80,

Table 2
Peaks and Troughs in Foodgrains Production

(Million tonnes)

Year	Peak	Trough	Shortfall of trough from previous peak	
			Quantity	Percentage
1970-71	108.4			
1972-73		97.0	11.4	10.5
1975-76	121.0			
1976-77		111.2	9.8	8.1
1978-79	131.9			
1979-80		109.7	22.2	16.8
1981-82	133.3			
1982-83		129.5	3.8	2.9
1983-84	152.4			
1987-88		138.4	14.0	9.2
1988-89	* 168.6			

* Provisional

also reflects the emergence of greater resilience. A sharp decline in the output of kharif foodgrains in 1987-88 was made up by an increase of 2.4 per cent in the output of rabi foodgrains as compared with the drought of 1979-80, when kharif foodgrains output declined by as much as 19 per cent and the rabi foodgrains output declined by 13.7 per cent.

2.013 The impressive record of achievements in the past notwithstanding, Indian agriculture has still not moved away from the cyclical pattern of peaks and troughs. Growth has not only to be stimulated to new heights on a continuing basis but also sustained and stabilised. In this context, the need for the development of a drought proof technology to insulate farming against adverse weather conditions cannot be over emphasised.

2.014 As will be seen from table 2, foodgrains production in India is characterised by a step-wise movement. After touching the level of 152.37 million tonnes in 1983-84, the output of foodgrains dropped to 145.5 million tonnes in 1984-85 and recovered to a level of 150.4 million tonnes in 1985-86. The

production again dropped to 144 million tonnes in 1986-87 and further to 138 million tonnes during severe drought year of 1987-88. Keeping in view the fact that total rainfall during 1988 south-west monsoon was as high as 116 per cent of the normal, the latest estimates are that 92.5 million tonnes kharif foodgrains production target would be realised during 1988-89 and the rabi foodgrains targets have been revised to 76.7 million tonnes from the 73.7 million tonnes fixed earlier which reflects the narrowing of the spread between kharif and rabi output achieved over the recent years. Thus the 1988-89 foodgrains production is likely to be the highest food production peak achieved so far.

2.015 Whereas foodgrains production has increased in spurts, the domestic demand in cereals generally grows over a gradual secular trend path. In such a situation, supplies may exceed the demand when production rises from one plateau to another, while demand may exceed supplies in the opposite case.

2.016 Considering such a production pattern, we do not want to draw the conclusion that the foodgrain production problem is solved. In fact, we are sobered by the realisation that while foodgrain production has taken a big upward jump from 138 million tonnes in 1987-88 to an estimated 168.6 million tonnes in 1988-89, this peak of 168.6 million tonnes has occurred after a gap of five years, since the 1983-84 peak of 152 million tonnes. If one observes the peak to peak growth as one should, as an indication of full capacity production, then, neither the growth over these five years, nor the average annual percentage growth can be rated as spectacular. While the average growth in agricultural production for the first four years of the Seventh Plan worked out to a shade higher than the plan target of four percent, the period has been characterised by considerable instability. We further note that with the new thrust of public policy coming on such intensive employment schemes as Jawahar Rozgar Yojna, the effective demand for foodgrains in the country will improve with improvement in the levels of income of the poor sections of the population. Considering the syndrome of high population pressure, poverty, food security and high income elasticity of demand for such foods as edible oil, sugar, milk and horticultural products etc., the production of foodgrains and other

foods has to be increased on a sustained basis. Increased production of foodgrains would lead to an increase in rural income which would lead to expenditure patterns that help in the diversifications of agriculture and relax the demand constraint that agriculture in general and agro-industries in particular often face in countries with high population density and widespread poverty.

2.017 Again, in view of the fact that greater vacillations in the output of coarse grains have contributed to widening the fluctuations in foodgrains production from year to year, public investments and price support and procurement policies of the government need to be geared to raising production and income of the coarse grains producers. It is, however, quite apparent that over a stretch of time, consumer preference for fine grains will increase and high value crops will be substituted for low value crops. At that stage it would become economical to use coarse grains for feeding livestock and particularly milch cattle.

2.018 Availability of agricultural land which stood at 0.48 hectare per capita in 1951 may decline to 0.14 hectare by 2000 A.D. Indian population will be in the periphery of 1000 million and will require roughly 228 million tonnes of foodgrains. Considering the rising marginal costs of incremental production after reaching high levels of productivity and production in foodgrains in Punjab, Haryana and Western U.P. the less developed regions have to play a predominant role in achieving augmented national foodgrain targets towards the year 2000 A.D.

2.019 The Planning Commission has worked out demand projection of foodgrains for the 8th Plan (1990-91 to 1994-95) and the 9th Plan (1995-96 to 1999-2000), taking into account important parameters such as population projections, growth rate of per capita consumption and expenditure elasticity of demand. According to these projections, the total demand for foodgrains will be of the order of 197.2 million tonnes by the end of the 8th Plan and 228.3 million tonnes by the end of the 9th Plan. To achieve these higher levels of foodgrains output, much higher levels of public and private investments would be necessary, so that the additional supplies of primary food commodities reduce the raw

material input constraint that food processing industries would be facing in the future.

Lessons learnt from the Green Revolution

2.020 Before discussing some disquieting trends that have developed in the agricultural economy in the wake of the green revolution during the recent years, it would be pertinent to observe that green revolution has been one of the great landmarks in the history of agricultural development in India and that some very useful lessons can be learnt from this development. It is true that the green revolution remained confined to some areas of India and the strategy of the green revolution turned out to be more successful in some regions/countries than in others. It succeeded in areas in which new high yielding technologies and management systems were adaptable; where the profitability of such technology was realizable through adequate public and private investments; where it was properly backed by adequate rural infrastructure and institutions such as feeder roads, inputs supply services, integrated nutrients supply system, integrated pest management and farm credit facilities etc. and where it was supported by price support policy and reliable procurement system. In summary, the experience has shown that whereas technological developments are a necessary condition, technology is not a substitute for effective institutional structure and effective public policies. Unless all these components of the system are present, economic development cannot be accelerated.

2.021 Accelerated developments always pose some problems and the green revolution has its own share. The processes of modernisation and commercialisation of agriculture through such developments as the green revolution result in larger and larger shares of purchased inputs utilised in agricultural production. The share of farm inputs in the total value of Indian agriculture increased from 25 per cent in 1970-71 at constant prices to 31.8 per cent in 1980-81 and further to 32.2 per cent in 1981-82. The new technology certainly needed more investments in farm equipment and more and more expenditure on production inputs which could not be met from farmers' owned savings and had to be increasingly supported by financial institutions.

2.022 Starting around the mid 60's, incremental yields and outputs were initially obtained at low unit costs in the green revolution areas. But as the major inputs in real terms in the aggregate increased at a rate of 5.2 per cent per annum between the triennia ended 1972-73 and 1986-87, and the real output increased at the rate of 2.3 per cent per annum during this period, the index of productivity of inputs declined sharply from 110 in 1970-71 to 62 by 1986-87. Such a change implies that cost per unit of output at higher levels of output did not decline.

2.023 Again, the capital formation in agriculture sector has become very costly. In the three plan periods, in the post green revolution era, private investment in agriculture was higher than in the public sector and in the 6th plan period, a short fall in the public sector was made good by an increase in the private sector investment. But from the point of view of capital formation, it is important to note that, while the implicit index of prices at which the GDP in agriculture increased was 76 per cent between 1973-74 and 1984-85, the implicit price index of gross capital formation in agriculture rose by 169 per cent during the same period. The bulk of the rise in the latter price index came between 1973-74 and 1980-81, when it rose by 89 per cent while the GDP's price index rose by only 34 per cent. The sharp increase in the cost of investment in agriculture since 1973-74 implies that in order to create additional assets of a given quantity, a relatively large sum was needed compared to the value of output it could produce than was the case in the first phase of the green revolution.

Constraints on Expanding Production

Declining Farm Size

2.024 Looking to the future, a rapidly declining farm size is likely to hamper agricultural growth perhaps more than any other factor. The increase in cultivated area has not been commensurate with increase in population. As against 66 per cent increase in the rural households between 1953-54 and 1971-72, the cultivated area increased by only 20 per cent which led to a reduction in the average size of farm holding from 2.5 hectares to a little more than 1.5 hectares. Marginal holdings of less than 1 hectare increased from 15.4

million to 35.6 million and the average size of these holdings fell from 0.20 acres to 0.14 acres during the same period .

2.025 During the years 1970-71 to 1980-81, the number of operational holdings increased from 70.49 million to 89.30 million mainly due to a continuous process of sub-division of holdings, while the area operated increased by a mere 0.67 million hectares. The number of marginal holdings increased by nearly 15 million and that of small holdings (1-2 hectares) by 2.5 million. Consequently, the proportion of marginal holdings (below one hectare) rose from 50.6 per cent of the total in 1970-71 to 56.5 per cent in 1980-81 and is likely to reach 60 per cent in 1990. This process of marginalisation of agriculture will certainly pose formidable problems.

2.026 We do not suggest that small and marginal farmers, artisans and landless labourers be left to their lot in the matter of institutional financial support. Many small farmers have the capacity of adaptive management required in the farming system in response to new opportunities but a larger proportion of non-viable small and marginal farmers should find a place in the rapidly growing secondary and tertiary sectors of the economy.

Irrigation Constraint

2.027 Over exploitation of water in the green revolution area, particularly where wheat and paddy rotation followed year after year is another problem of deep concern that should engage the attention of the policy makers and farmers of these areas. When paddy was transplanted in July, the rainfall received during this month replenished water recharge by about the same amount as is used up by the paddy crop. About 75 per cent of water used for paddy would go down deeper to form a part of the recharge. Now that paddy transplanting has been advanced to May and June, water requirements of paddy during these two hot months would add up to about 50 per cent of water requirement of the whole season.

2.028. Again, with the establishment of more sugar mills, sugarcane area is fast expanding. It is observed that acre-inch water requirements of sugarcane

in April, May and June are higher than for the remaining 9 months. Consequently, withdrawals of water in the green revolution areas would far exceed the ground water recharge which in turn results in the water level falling faster than before. Unless ground water development is restricted to yearly replenishable recharge on an area specific basis, water level will fall too deep to operate centrifugal pumps commonly used for private wells. But for heavy floods in Punjab and in some other areas, which while causing serious damage to crops and livestock, have nevertheless effected some improvement in ground water recharge, the drop in the water level would have become more alarming by this time. In any case, the improvement in recharge resulting from the 1988 floods will not last for long. The solution perhaps lies in increasing the real price of water to the beneficiaries, which means that the flat rate policy of costing water has to be given up.

2.029 According to the Economic Survey 1986-87, a cumulative irrigation potential of about 69.8 million hectares (gross) was created by the end of 1985. The gap between the irrigation potential created and utilised has increased from 6.9 million hectares in 1984-85 to 7.5 million hectares in 1985-86 and the targets for 1986-87 indicate that the gap may increase to over 8 million hectares in that year. To bridge this gap, the imperatives of the situation demand that irrigation projects are regarded as complete only when all physical activities for the delivery system at the farm gate are completed and water courses, field channels, field drainage, land levelling and land shaping form part of the irrigation project.

2.030 What is yet to be recognised is that water is becoming increasingly scarce and a severe limiting constraint to the growth of agriculture and of rural incomes. Even if the full potential were to be realised, a significant proportion of land would remain without irrigation. Improved efficiency in the use of water through better water management, therefore, assumes critical importance, particularly when the cost of creating fresh irrigation potential has increased from Rs.1200 per hectare in the 1st Plan to Rs.27,000 per hectare in the 7th Plan.

2.031 One promising and productive change that needs to be made in order to improve the efficiency of water distribution is to reduce the size of the area served by each outlet by having the government to construct a higher proportion of the distribution system, leaving less to be managed by the farmers. Maharashtra's experience shows that irrigation requirements per hectare declines with smaller outlets, and by lining a higher proportion of the system.

2.032 Conjunctive use of water with surface irrigation replenishing aquifer and ground water developments, simultaneously supplementing surface supplies and reducing water-logging and the drainage development can provide high combined profits. An all-out effort should, therefore, be made to achieve this goal.

2.033 Finally, the role of irrigation in releasing the land constraint through an increase in irrigation and cropping intensity should remain a critical part of the development strategy for Indian agriculture. The shortfalls in actual expenditure as compared to plan expenditure or outlays in the Seventh Plan seem to be very significant for agriculture, particularly irrigation. It should be possible to have a time bound programme for the exploitation of groundwater for the small farmer, particularly for the Eastern Gangetic belt in the country.

Energy Constraint

2.034 In spite of a very large share of public investment going into the energy sector in the five year plans, energy constraint persists as a critical factor to the rapid growth of the economy. Perhaps, the greatest failure in the Indian economy which has a major effect both on employment growth and on agricultural growth is the failure of the country to do as well as many other developing countries did at a comparable stage of development to expand electric power generation. A growing intensity of capital employed in energy production and external constraints on increases in energy supply capacity such as environmental factors and transport bottlenecks have limited power generation growth to no more than 10 per cent when at least 15 per cent reliable growth in power was needed to meet the new needs of the economy. Again for several years now, most countries in the world have pursued an end use orientation which

permits planners and policy makers to evaluate fuel switching operations within an economical framework both in the short and the long runs . Planning process in India needs to be moved in this direction to balance the supply and demand for electric power generation.

2.035 Finally, a critical analysis of the development of different regions of the country shows that the constraints discussed above have operated much more severely in underdeveloped regions than in the better developed regions of the country. We will address the rectification of these imbalances in the forthcoming sections.

Price Policy and Terms of Trade

2.036 The rising input-output ratios, high cost capital formation and low absorption capacity of capital in the under-developed areas are not the only constraints to rapid growth of agriculture. The profitability at the farm level is a function of prices of both inputs and outputs of individual items in relative terms to each other. These prices have to be traced backward in the case of inputs to their original sources of manufacture within the economy vis-a-vis border prices in the case of traded inputs. A good proportion of farm fertiliser subsidy, for example, can be traced back to the inefficiency of the domestic fertiliser manufacturing sector, resulting from the retention price policy designed by the Government for this sector. In fact, in the case of fertilisers, not only is the industry guaranteed a fixed rate of return, based on certain capacity utilisation but such feed stocks as naptha and fuel oil are also subsidised.

2.037 In spite of the support price policy, terms of trade during the recent years have become unfavourable to the agricultural sector. The Commission for Agricultural Costs and Prices (CACP) in its latest report on the Price Policy for kharif crops for 1987-88 has observed that the terms of trade in 1983-84 and 1984-85 were still adverse at 86.3 and 86.0 respectively. In the following two years, the terms of trade further deteriorated to 82.3 in 1985-86 and 81.9 in 1986-87. The Commission has also emphasised that between 1983-84

and 1986-87, the prices paid for commodities purchased for capital formation increased by over 19 per cent as against an increase of about 13 per cent in the prices received by the farm sector, which means that the capital formation in the agricultural sector has become more costly at a time when the capacity of the farmers to invest in productive capital assets has gone down.

2.038 Conscious policy decisions are required to improve the terms of trade for the agriculture sector and help farmers secure more remunerative prices for their produce by strengthening on farm storage facilities. Now that the Indian agriculture has become demand constrained, public policy should also integrate demand for agricultural product in the 8th & 9th Five Year Plans of the country. Otherwise the Government would find itself spending large sums of money for agricultural price support.

2.039 There is some historical evidence to show that in the process of development, some highly developed countries had transferred resources from the agricultural sector for rapid development of the secondary and tertiary sectors. This philosophy does not hold good in the present situation of the developing countries. The transfer of resources from agriculture should come about naturally through growth in agricultural productivity. In fact, the farm and non-farm sectors are so much intertwined and interdependent that macro economic policies have a strong bearing on agricultural growth, rural income and rural development. Hence the need for evolving a sound economic policy which would promote the development of both farm and non-farm sectors cannot be over-emphasized.

Outlook for the Future

2.040 The ecological system in India is currently under great pressure owing to growing pressure of human and livestock population. Resource conservation for sustained agricultural development, therefore, assumes critical importance. Keeping this objective in view, more attention has to be paid to resource conservation research - soil and water conservation, better water management, conservation of flora and fauna and conservation of post-harvest food losses both in quantitative and qualitative terms. More specifically, the environmental

impact studies need to be woven into the economic review and appraisal of the projects. Once this kind of project appraisal becomes a part of the system, the conflict between the environment and development would be reduced to manageable proportion.

2.041 Another major issue in Indian agriculture that has come to assume topical significance relates to the redressal of fundamental structural problems of crop-regional imbalances in growth. At one extreme, some regions have witnessed a sharp growth but limited to a few crops, and at the other, some other regions have shown a rigid inability to show any comparable signs of development. Clearly, when such a situation arises, it is indicative of the inability of the policy makers to design a programme that would allow orderly adjustment of the agricultural sector production programmes and development through farmers' response stimuli following farm management approach. The sharpening of focus on the measures to secure greater diffusion of growth across regions is, therefore, necessary in the future development plans of the country.

2.042 specifically, now that the food situation has become easier, the emphasis in Indian agriculture has shifted to diversification of agriculture, correcting regional imbalances in agricultural productivity and development, improving dry farming/rainfed farming systems, stimulating development in the Eastern and North Eastern regions of the country and increasing the production of oilseeds. Imparting stability to agricultural output, bringing the benefits of the green revolution to the weaker sections of farmers and shaping the agricultural credit policy to stimulate balanced growth, are some other related problem areas that have also assumed topical significance.

New Approach to Cropping Systems

2.043 Instead of increasing grain production of individual cereal crops, the new cropping systems would call for a systems approach to study not only the impact of preceding and succeeding crops on soil's ecology and environment in the totality, but would focus on crops and plantation-based cropping system. Pulses and oilseeds are known to be intercropped with HYV based cereal

crops, but research studies have shown that even sugarcane based cropping system can be intercropped with mustard crop. In this system, not only sugarcane yields remain stable but the oilseed crop yield increases because of the benefit it gets from irrigation provided to the sugarcane crop.

2.044 Modifications of planting geometry (Paired row planting) for intercropping has shown high promise. The plant density of the base crop is generally maintained at the recommended optimum level, besides pushing in additional plant density of intercrop without affecting the productivity of the base crop adversely. In the process, crop intensification in time and space stabilises the desired plateau in crop production and increases not only the production of cereals but also of pulses and oilseeds etc.

Diversification of Agriculture

2.045 Indian agriculture has come to a stage of development when its farming business should get more and more commercialized with the farmers extending their activities/operations to expand dairy, poultry, fisheries, horticulture and forestry enterprises to improve their farm incomes rather than limiting themselves to crop husbandry. The foodgrains strategy of growth relentlessly pursued in the 1970s has certainly made the food situation easier, but it did not bring about much poverty alleviation as it lacked the desired intensive approach embracing a wide range of crops, livestock, fishery and forestry components of agriculture.

2.046 Diversification of agriculture has become all the more necessary in these regions of the country where two crops wheat-paddy rotation repeated year after year on an extensive scale has made the agro-systems of some states extremely fragile in the context of pests and crop diseases, soil health and overall living environments. The process of agricultural diversification will, however, not get going in these areas unless consciously designed public policies and intensive research programmes are developed to promote such farming systems which can successfully compete with returns from paddy-wheat rotation to the farmers.

2.047 Again, considering the fact that labour absorption capacity of the crop husbandry sector is limited, such technological development which are even more labour intensive, are to be consciously promoted to diversify agricultural development. Integrated agricultural development can be best fostered by strengthening complementary relationships between crop husbandry, livestock and dairy development, intensification of horticulture, social forestry and fisheries.

Farming Systems

2.048 The conclusion drawn from empirical studies is to stress intensification of agricultural development not only by producing more cereals per hectare, but by maximising the value per unit of land through scientific farming systems. Crop-livestock system, crop-fish system and crop-livestock-fish production system offer considerable potentials for generating additional income and employment as well as efficient energy conversion. Agro-forestry, sylvi-pastoral, sylvi-horticultural and other combined land use systems are extremely important for meeting food, feed and fuel requirements, but these systems are yet to receive detailed scientific and extension attention they merit.

Livestock and Dairy Development

2.049 Again, it is often argued that in the absence of strong technological developments in livestock farming, fisheries, farm forestry and horticulture, etc., these enterprises will not make much headway. Some technological developments in these sectors are also underway. But what will particularly help the growth of these sub-sectors is the high income elasticity of demand for their products. It has been noticed that genetic studies in crossbred cattle, for example for evolving new high yielding breeds and for improving productivity of indigenous draught and dual purpose breeds through selection and generating superior germplasm have been the major research effort in cattle. The genetic potential for milk of Holstein 1/2 breeds and Holstein - Jersey 3/4 breeds under concentrate feeding has exceeded 4000 litres per lactation.

2.050 Again, through bio-technological innovations, the development of genetically engineered foot and mouth disease vaccine is in progress. Bio-technical

innovations, especially multiple ovulation embryo technology for enhancing genetic improvement and genetic conservation hold out a great promise, but they will take time to get perfected and their major impact on productivity may be felt around 2000 A.D. but not in the immediate future. The process can however, be speeded up if dairy development strategy improves production by improving the genetic stock of the national herd without increasing its size.

2.051 Technological developments in any enterprise are, no doubt, highly important but technology is no substitute for institutions and public policies. Green revolution was a greater success in some parts because technological developments in these areas were strongly supported by such infrastructural facilities as adequate and timely supply of inputs, support services, effective marketing structure and an assured national market through public price support policies. It is these areas that need to be strengthened to stimulate the growth of dairy, poultry, fisheries, farm forestry and horticultural enterprises where technological developments are coming up through intensification of farming systems research.

2.052 To quote one example, dairy development did not succeed in those areas where dairy technology was erroneously considered as a substitute for such public policies as establishment of multiproduct dairy plants in optimal locations, milk distribution routes and economical routing of milk vans. It is not enough to provide a farmer with a cross bred cow or any other high yield milch cattle. Adequate fodders, forages, health cover, efficient management and technical services associated with such technologies should be present to fully exploit the production potential of such technologies. Given the almost stagnant production of green fodder, the lack of good grazing land and the expense of animal feeds, the expansion of the organised dairy sector, at the extensive margin, is not sustainable. Again, the market for milk and milk products has to be assured to provide an incentive to dairy farmers to make the necessary investments for raising the productivity and production of their dairy enterprise. Nyholm et al. observed that dairy co-operative societies in the Bangalore milk-shed area did not achieve higher levels of production

despite substantial demand and attributed this in part to the absence of organised markets.

2.053 It cannot be over emphasised that marketing and processing of agricultural produce have become more serious constraints on raising the production of foodgrains and particularly on stimulating production and farm incomes in these areas. Rural financial institutions can promote greater access to marketing and processing services by expanding their agricultural produce, marketing and processing sub-systems.

Farm Forestry

2.054 The present canvas reveals an ever increasing rise in the demand for farm products of a developing and growing society on the one hand and sharply declining forestry resources on the other. The need for tree farming on all available waste and marginal lands, unsuitable for profitable agriculture, is necessary not only for meeting the basic requirements of fuel, fodder and small timber but also for maintaining ecological balance.

2.055 Consistent with the farm management approach, the tree species proposed to be grown have to be selected, keeping in view the agro-climatic conditions, and should be sufficiently quick growing and capable of yielding higher economic returns, particularly when the gestation period is longer. Eucalyptus and poplar plantations meet this test readily.

2.056 Bulk plantation of eucalyptus would pay more on marginal lands where common field crops are not remunerative. The success of this enterprise will greatly depend on the adoption of farm management approach where the right density of plant population and inter-cropping systems are adopted, market is assured and harvesting and transportation costs are kept under control*.

2.057 In the case of poplar plantations, poplars combined very well with

* In the case of border plantation, such cultural practices as North-South direction plantation would cause a minimum strain on the main crops.

the regular cropping pattern. Inter-cropping is possible right through the 8 years period due to the growth characteristics of this tree. As such, there is no significant diminution in regular yields and no diversion of land to monoculture plantation.

2.058 A proper follow up of inter-cultural practices will make this enterprise a greater success. A four metre distance from plant to plant and five metres from row to row promotes inter cultivation of young plants and facilitates inter-cropping with potatoes, alfalfa, winter maize, legumes, fodders and guinea grass. Fodders can be fed to integrate livestock and particularly milk production enterprise with farm forestry. FYM produced by animals goes as a manure to the fields and produces complementary relationship with other inputs. Inter-cropping necessitates irrigation and in turn fosters rapid growth and early maturity of the poplar plants. As the plants grow, their shade reduces evaporation losses.

2.059 Industry linked farm forestry has a greater chance to succeed. WIMCO has taken a lead in this direction and has undertaken to provide the entire transplant (ETPs) and other inputs such as fertilizer and extension services to farmers who choose to avail the services from them. The Company has guaranteed and assured buy-back arrangements based on minimum floor price. It is this integrated process of production and assured marketing, following the farm management approach that can make farm forestry a competitive enterprise. The scheme of tree pattas would also help overcome the inhibitions which some of the state governments have in making available suitable tracts of land for farm forestry to small and marginal farmers.

Social Forestry and Wasteland Development

2.060 The Government of India have set a target of bringing 5 million hectares of land every year under tree cover. The programme calls for a massive institutional credit support. In the estimation of the National Wastelands Development Board, even with only marginal inputs, the afforestation cost would be a minimum of Rs.5000 per ha. At this rate, to achieve the target of 5 million hectares, would require an annual investment of Rs.25,000 crores. At present, overall achievement is around 1.79 million hectares arising from organisational and resource constraints.

2.061 In view of the decision of the Government of India not to permit leasing of various lands for development through user industries, the development of such lands would have to be tackled by the various Development Corporations. There has been a spurt in the afforestation programmes formulated by the Forest Development Corporations. The massive programme for afforestation of 89,000 hectares of degraded lands by the Development Corporation of Maharashtra with financial outlay of Rs.1,908 crores is an indication of the high financial requirements for such enterprises.

2.062 Wasteland development has also to cover private wastelands. The project for reclaiming wastelands of individual beneficiaries and also those schemes where tree pattas are issued in favour of the rural poor either as captive plantation schemes or farm forestry schemes should receive high priority. NABARD has decided to provide 100 per cent refinance assistance to banks in respect of schemes formulated by them for afforestation of wastelands by individual farmers/entrepreneurs and/or groups of farmers, either on their own lands or on the lands obtained on lease from the state governments, Panchyats etc.

Fish Farming

2.063 Recognising that no significant increase in fish production can come from capture fisheries, a major step towards shift from capture fisheries to culture fisheries was taken with the sanction in 1979 of the World Bank assisted Indian Fisheries Project.

2.064 Inadequacy of credit for fish pond improvements and fish seed and low use of such inputs as fertiliser and seed are a serious constraint on the development of fish farming in India. With good management and adequate supplies of high quality seed and complementary inputs, it appears that high levels of yields can be achieved for both the existing fish ponds and the new ponds to be brought under fish culture.

2.065 Induced breeding of carp species to extend the spawning period has made a major contribution to fish culture development and has provided the

technological basis for further fish development in the country.

2.066 A major problem in regard to brackish water prawn farming is the policy relating to leasing on a long term basis of brackish water areas owned by the Government so that brackish water fallows could be converted into prawn farming.

2.067 More recently, some steps have been taken to integrate aqua-culture with agriculture and animal husbandry and NABARD has extended refinance for such integrated fisheries projects as duck-cum-fish culture and paddy-cum-fish culture. But this is not enough and is only a beginning made.

Oilseeds and Edible Oil Policy Perspectives

2.068 In the absence of a real breakthrough in the production technology of oilseeds crops, the area under oilseeds almost stagnated and only increased from the earlier peak of 17.7 million hectares in 1978-79 to 18.9 million hectares in 1981-82; about the same level has been maintained in the years since then.

2.069 As compared to Rs.14.2 crores in 1975-76, Indian imports of edible oil stood at a colossal figure of Rs.832.2 crores in 1984-85. The present policy of imports and distribution of edible oils has further aggravated the problem of imbalance in the demand for and supply of edible oils. Despite per capita domestic production being lower in 1985-86 than that in 1970-71, the prices of edible oils in real terms have been lower than that in 1970-71. As a result, the apparent per capita consumption of edible oils escalated from 3.5 kg in 1975-76 to 6 kg in 1984-85. In the absence of larger per capita domestic production of oilseeds/edible oils, demand will continue to outstrip domestic supplies, making it still more difficult to achieve self sufficiency in edible oils. Self sufficiency in oilseeds and edible oils production has, therefore, rightly become the primary objective of governmental policy. Faced with a situation of heavy imports of edible oils, research activity on development of oilseeds technology has been intensified. As a result, GSL variety of Gobhi Sarson (Brassica Napus) which has shown a yield potential of 23 quintals/ha

when 60 days old seedlings were transplanted during the third week of November, could be cultivated in large areas of Punjab and Haryana, following the kharif rice and cotton crops. Such developments hold out good promise but the achievement of high production targets in oilseeds would ultimately depend upon the relative profitability of oilseeds crops with the competing crops in each region and location specific situation.

2.070 The pertinent problem in raising oilseeds production is a high degree of instability characterising the oilseeds economy, as almost 84 per cent of oilseeds are cultivated under rainfed conditions. Also, oilseed farmers hesitate to use modern inputs because of the high risks involved in yield and production, inadequate availability of certified seeds, susceptibility of oilseeds crops to pests and diseases and inadequate use of improved agricultural implements for proper placement of seeds and fertilisers.

Strategy for improving oilseeds production

2.071 Faced with an annual average Rs.800 crores of edible oil imports, a Technology Mission of Oilseeds has drawn up action plans for 180 districts to promote and co-ordinate research in extending quality seed production and supply and other allied activities that have the overall effect of accelerating the growth rate of oilseeds production in the country. The latest developments in biotechnology offer new opportunities in genetic mutations to evolve such strains in major oilseeds crops as would give much higher yields on the one hand and make the plant more resistant to pest and adverse climatic conditions on the other. But the gene revolution will take time to develop. Even oilpalm, the richest source of vegetable oil among cultivated crops is yet to take off as a commercially viable crop.

2.072 In the mean time, farm management economics approach can be profitably employed to exploit the existing production potential through field level improvement in dry farming techniques. This could be done by delineating compact areas which are more suitable for oilseeds production and enjoy comparative economic advantage with competing crops, particularly in Gujarat, Rajasthan, Madhya Pradesh, Orissa, Andhra Pradesh, U.P. and Haryana. Within

these states, there are types of farming areas where the oilseeds production has an edge over the competing crops in terms of providing higher net returns to the farmer. Production of rapeseed and mustard for example has been substituted in those areas of Madhya Pradesh where unirrigated marginal lands under wheat paid much less than rapeseed cultivation. An all-out development effort has to be made to expand oilseeds production through such techniques as inter-cropping, sequence cropping and relay cropping. Certainly, oilseed crops grown in rotation have a better chance to succeed in certain areas than the individual oilseed crop. Thus the lesson learned is that oilseeds production must become an integral part of a HYV based cropping system, rather than an individual crop and duly supported by public policies and institutions to produce a greater impact on the income of oilseed growers.

Oilseeds Processing Units

2.073 There is some evidence to show that certain oilseeds production areas do not have adequate oilseeds processing facilities. In order to provide stability to production and prices, and to ensure easy market clearance, it is important that some high technology oilseeds processing units are established to match the targetted production of 18 and 26 million tonnes by 1990 and 2000 A.D. respectively.

2.974 Finally, with a view to providing an incentive for large scale production of edible oils from rice bran, oil cakes, cotton seeds and tree oilseeds, certain concessions have been provided in the excise duty rates for the use of these oils in the manufacture of vanaspati and soaps. Mustard oil could be used for vanaspati to stabilize the price of mustard oil which would otherwise experience wide price fluctuations.

2.075 The real breakthrough in the extraction of edible grade oil from rice bran will come through stabilization of rice bran at the level of modern rice mills. Research to stabilize rice bran should be intensified so that the solvent extraction plants can use stabilised rice bran for effective and efficient extraction of edible oils.

Price Support Policy for Oilseeds

2.076 So long as market demand for a commodity outstrips its production/supplies, market prices would tend to increase and this is what has happened during the last decade. For this obvious reason, recent market and administered prices of oilseeds and pulses have generally ruled much higher than those of cereals. A careful analysis of the relative price structure of oilseeds and major cereals shows that, over the years, price policy changed in favour of oilseeds and pulses and yet their production increased only marginally between 1969-70 and 1979-80. Between the triennia ending 1969-70 and 1979-80, whereas the price index of cereals increased by only 62.6 per cent, the index number of wholesale prices of oilseeds increased by 117 per cent. In the case of a major oilseed such as groundnut, its price in terms of paddy was only 1.5 times in 1970-71 but rose to 2.42 times in 1982-83 and to 2.46 times in 1986-87. In the case of pulses, gram price was 0.8 times of wheat in 1970-71 but escalated to 1.60 times in 1984-85. Again, the wholesale price index of wheat, deflated by all commodities, declined sharply from 94.7 in 1971-72 to 68.7 in 1983-84. It seems certain that faster growth in wheat production in Punjab, Haryana and Western U.P. has come from the adoption of technological package of HYVs and the associated inputs supported by an assured market and better implementation of the price policy than from higher support price relative to the prices of the competing commodities. Thus the real problem in the case of oilseeds is more technological than that of unremunerative market or price support policy.

2.077 The real weakness of government price policy lies not in fixing unremunerative prices for oilseeds, but in its implementation. A careful analysis of the implementation of price support policies does uphold the thesis that the implementation of wheat and paddy/rice support policy has been a greater success than the adhoc arrangements made with NAFED for the procurement of oilseeds, when their market prices fall below the support price. This limited support price policy did not provide a real incentive to oilseed farmers to expand their investments in oilseeds production. It is only since 1984-85 that standing arrangements have been made according to which NAFED and state federations enter the market and undertake price support market intervention

operations as soon as market prices of such commodities fall below the support level. During 1984-85, NAFED and state corporations and marketing federations procured soyabean, mustard and rapeseed at support prices in sizeable quantities. If an assured market is provided to the oilseed growers on a continuing basis, it will be a positive step to expand oilseeds production. We understand that National Dairy Development Board has taken charge of domestically produced oilseeds to build up the stock of edible oils for market intervention. This pragmatic approach will certainly go a long way to help oilseed farmers raise their production and the country to reduce its heavy edible oil imports, and become self-reliant over time.

Dry Farming/Rainfed Farming System

2.078 Dry land farming constitutes 70 per cent of land area under cultivation but contributes only 42 per cent to agricultural production because of low productivity which has contributed to regional imbalance in agricultural production within the country.

2.079 The Seventh Five Year Plan emphasises that high priority will be given to dry land farming with a view to raising productivity and reducing poverty, unemployment and regional disparities.

2.080 The dry farming regions suffer serious constraints of risk and uncertainty. Total rainfall fluctuates widely not only from year to year, but between seasons and there are great variations in the onset and withdrawals of monsoons and dry spells within the monsoons, which necessitate contingency planning, seeds stocking and adjustments in cropping patterns that have their own costs. Precipitation often occurs at a high rate of intensity which does little good to soil moisture retention, but does aggravate the danger of soil erosion and inadequate drainage.

2.081 Soil conservation has been the main treatment to raise productivity in the dry farming areas. These programmes are, however, overplayed at the cost of dry land farming (although the two are inseparable) with over-emphasis on soil conservation. These did not, therefore, make a dent in raising

productivity, particularly when their maintenance remained very poor.

2.082 The fact remains that risk and uncertainty are some of the critical factors that cannot be ignored while expanding credit flows in dry farming areas. Many farmers in dry farming areas hesitate to accept credit because of the instability in yield levels and farm production obtained in these areas and credit does not reduce the risks associated with variable yield technology. Watershed development approach can go some way to remedy this problem but what is really important is not only the role of credit agencies which is limited to intermediation but it must cover some effective mechanism for risk management.

Watershed Development Strategy

2.083 Recognising the risk and uncertainty elements inherent in agriculture and limitations of the soil conservation programmes, the focus has now shifted to infiltration of rain water in situ conservation of moisture and prevention of run off erosion. With this orientation, the watershed has come to be recognised as the natural entity for planning and implementation of rainfed areas, following farm management approach to increasing productivity and production of complementary enterprises. The integrated watershed development strategy should not be limited to better crop management, as on the demand side, low value status of coarse cereals such as sorghum and pearl millet restricts their absorption capacity for yield enhancing inputs such as chemical fertilizers and pesticides. A remedy lies in building up strong complementary relationships between crop husbandry, animal husbandry, horticulture, agricultural forestry and fisheries to reduce risk of putting all eggs in one basket and optimize production and farm income in the watershed areas. Such an integration has its own costs and complexities and one has, therefore, to be very selective in the formulation of watershed project. It is for this reason that the financial institutions should better initially concentrate on financing those watersheds where average annual mean rainfall is 750mm and above, so that the risk of the failure of the crops and other enterprises is minimized and banks can take on more and more financing of such projects.

Land use classification

2.084 The amount and distribution of rainfall, soil type and depth and slope characteristics are the main parameters that determine the success of different systems of farming and particularly the cropping pattern in dry farming regions. It is of primary importance that land use classification is built for the widely varying conditions of rainfall, soil type and soil depths in these areas. In the absence of this classification, limited land and other resources are liable to be misutilized. Alfisols for example are deficient in soil moisture and moisture retention is often limited due to their shallowness and yet during the recent decades more and more alfisols, which are at best only marginally suitable for crop farming, have been brought under cultivation. In the case of vertisols (black soils) which have a much higher moisture holding capacity than the alfisols in the areas of good rainfall, workability of the soil remains poor during the kharif season, making it difficult to raise a good kharif crop. The problem gets aggravated by the fact that crop response to irrigation is small, particularly in good monsoon years, which discourages the farmer from making investment in wells and other irrigation structures. Consequently, most farmers do not prepare the land for irrigation which makes protective irrigation more difficult and much more costlier. Such typical situations of the rainfed farming system demand not only high yield but high stability technology if small and marginal farmers of these areas are to be helped to take to such technology.

2.085 Again, there is no real breakthrough in technology for the development of rainfed areas. Such innovations as the broad bed furrow system, run off harvesting techniques and tropiculture etc. are not yet readily accepted by farmers because of the wide variability of the environmental conditions. Contour surveys are yet to be completed and it is observed that land is ploughed and sown with little regard to direction of slope, resulting in furrow erosion, particularly when these furrows are up and down the slope.

2.086 Farmers are even more reluctant to adopt the package of practices recommended by the research organisations for the integration of crop-live-stock, fishery and social forestry systems and the cultural practices associated

with them, as these are much more capital intensive and have long gestation periods. Unless development plans are made more responsive to local problems and a closer interaction with the local population is achieved through a community management approach, complex problems of land use would not be easily resolved. As a first step, the whole focus of the Farm Extension Service must change from an individual farm approach to a group approach. Social, economic, household and farm crop surveys to identify constraints and potentials of different components of the projects would help in the proper identification of the farmers' problems in these areas and their reactions to different development programmes to be planned for these areas.

2.087 A good beginning could be made by correlating the cropping pattern with delayed onset of monsoon and their normal, delayed and early withdrawal patterns, based on a long-term analysis of the rainfall data. This is a difficult task for the planner and even more difficult for the farmers, as such adjustments in cropping patterns demand not only a high level of management but incorporation of costly farm implements and machinery to ensure timely planting of crops which turn out to be uneconomic for small size holding. Wheeled seed-cum-fertilizer drill and wheeled-tool carrier are, for example, important for timely sowing and other farm operations; but very few farmers can utilize such costly farm machinery on an economic basis, unless it is made available on a custom service basis by the state government or the lease companies.

2.088 Research efforts have to be further intensified to develop viable inter-cropping systems and improve the intensity of cropping. It is, however, important that all possible improvements are first made in raising the productivity of the major crops and then the limited available resources are diverted to raising the cropping intensity, which would, in turn, improve employment opportunities for the rural population.

2.089 Once the productivity levels of the major crops are raised substantially higher than the present levels, the stage is set for a rapid improvement of livestock and dairy developments. Fodder production in these areas is too small to cope with traditional overstocking of livestock. The search for fodder

and fuel has led to further degeneration of vegetative coverage and erosion. Resistance to controlled grazing from owners of livestock is quite common. Exchange of high-yielding milch cattle seems to be necessary but such high yielding cross breeds have to be stall fed. Hence forage production, grass cutting and forest conservations are the pre-requisites for raising successful dairy enterprise which still remains untested.

2.090 Recognising the complementarity between these enterprises, National Bank for Agriculture and Rural Development, through a strong support of its refinancing programme, is promoting an integrated watershed strategy which is not only limited to crop husbandry, but focuses on the complementarity between crop husbandry, animal husbandry, horticulture, forestry and fisheries to optimise production and farm incomes in the watershed areas.

2.091 Finally, owing to a small size of the holdings on the one hand and ecological limitations of dry land agriculture on the other, the latter, even with strong support of new technologies may not provide a total answer to the problems of low incomes of those who depend on dryland farming. The need for developing strong and viable programmes of non-farm activities as a part of rural development programme cannot, therefore, be overstated.

Credit Flows in Semi-Arid Tropics

2.092 There is research evidence to show that degree of agricultural progress was positively related to the share of agricultural inputs sub-system credit (AIS). Again, the share of current production/income growth (CPGS) credit in total credit was highly positively associated. This was also true of the share of kind credit in CPGS loans from co-operatives.

2.093 These three types of credit would well ensure backward and forward linkages between agricultural production system and agricultural inputs sub-system. Such a strategy has the potential of not only improving factor productivities, loan repayments at the farm level, growth rates in agricultural production and value added, but also viability of rural financial institutions, particularly in the semi-arid tropics of the country. This strategy is recommended for

such crops as jowar, bajra, ragi, such pulses as tur, gram, moong, urd and oil-seeds like groundnut, rapeseed and mustard, castor or soyabean. Adequate supplies of such inputs as quality seeds and such scientific implements as seed-cum-fertiliser drill, wheeled tool carrier, would be required to support the transfer of this technology at the field level.

2.094 The NABARD and the rural financial institutions in general do require to take priority action on developing agricultural inputs marketing credit and evolving comprehensive service system for accelerating agricultural production system and agricultural inputs.

Financing Micro Watershed Areas

2.095 We have to bear in mind that the watershed strategy of development is basically an area development approach which makes it difficult to identify the individual farmer or the group of farmer beneficiaries who will be willing to repay the loans raised from the banks. More specifically, the high cost soil conservation and run off harvesting technique do not concern individual farmers which makes it difficult to recover the cost of such loans and advances unless the state government bears such costs.

2.096 Finally, composite credit should come as a package. It is not enough that technology should change, farmers should change and the administrative culture should change. The banking culture should also change so that the one window concept provides the farmer both production credit and investment credit to facilitate such organisational and operational changes in the farm organisations which raise farm production and income to a level high enough to help the farmers pay back their institutional loans.

Export Potential

2.097 A diversified export structure should help reduce India's risk against changes in international markets. Growing prospects in world trade are better for high income elasticity horticultural products than for traditional agricultural commodities. As per capita income rises, a larger proportion of total food expenditure will be spent on horticultural products. Currently, the developed

countries account for more than 80 per cent of total world imports of horticultural products. World exports of horticultural products in recent years amounted to about 25 billion dollars, or about 11 to 12 per cent of total world agricultural exports. India should get a much greater share of this world market through intensive development of the regions which are specially suited for this activity.

2.098 As horticultural products are increasingly produced for the national market rather than for a regional market, they will undergo higher stages of processing, storage and marketing. As the wage costs go up, such developing countries as India would have a comparative advantage and would capture a large share of the market over the time. Developing countries need to focus on these products with high growth prospects in which they have a comparative advantage either because of their ecological characteristics or lower labour costs.

Cereal Exports

2.099 Of the 14 broad sectors which have been chosen by the Ministry of Commerce, Government of India, for making a special thrust in markets abroad, cereals (in particular wheat), processed food, marine products, and tea form important components.

2.100 An erroneous impression often persists that India is an inefficient producer of wheat. The cost of production data of wheat in India and the U.S. in Table 3 shows that the Indian farmer produces wheat at a cost lower than that of the U.S. farmer. Recognising that India enjoys freight advantage vis-a-vis other exporting countries in some markets, it should be possible for the country to export atleast some quantities of wheat on a sustained basis. The freight advantage enjoyed by India, is no doubt, more than counter balanced by the extra cost of handling, but those costs could be cut down considerably by creating bulk handling facilities at ports and at a few selected markets. The successful implementation of wheat export programmes would, however, depend on wheat surplus producing states/farmers getting full encouragement for cultivating such varieties of wheat which have potential export markets.

Table 3

**Cost of production of wheat in India and
United States (Rs per quintal)**

Year	Cost of production			
	India	United States	U K	France
1	2	3	4	5
1979	99.32	107.58		
1980	108.12	121.33		
1981	122.88	138.75		
1982	128.53	145.07	134	129
1983	128.82	146.43		163
1984	137.44	170.86	137	

Notes :

1. For cost estimates in India, the source is comprehensive scheme for studying cost of cultivation of principal crops in India, Directorate of Economics and Statistics, Ministry of Agriculture.
2. The cost estimates for India are the weighted average of the cost of production estimates for all the states for which the estimates are available for a given year, production of wheat in the specified year being the weights.
3. The cost estimates in United States are the economic cost in dollars per bushel converted into rupees per quintal using following conversion factors :

(i) one bushel : 27.215 (kgs)

(ii) The conversion rates from US dollars to Rs. for different years are as under :

1979	1	US	\$:	Rs.	8.18
1980	1	US	\$:	Rs.	7.88
1981	1	US	\$:	Rs.	8.70
1982	1	US	\$:	Rs.	9.79
1983	1	US	\$:	Rs.	10.14
1984	1	US	\$:	Rs.	11.37

4. Cost of production estimates in United States are based on "Economic Indicators of Farm Sector: Cost of Production 1984, National Economic Division, Economic Research Service" USDA, United States of America.

Cotton

2.101 A significant increase in the production of cotton through development of hybrids during the eighties holds out a good promise for exporting cotton and cotton yarn. The production of cotton during the triennium ending 1986-1987, on an average was higher at 11.3 million bales compared with 8.1 million bales for the triennium ending 1983-84.

2.102 An analysis of export quota for cotton released by the Ministry of Textiles shows that such decisions, in many cases were taken when peak production marketing season was over. In this context, the need for improving the reliability of domestic production of cotton cannot be over emphasised. The CACP in its price policy report for kharif crops of 1988-89 has observed that if the official statistics relating to cotton output were to be relied upon, the country should have imported over 10 million bales of cotton during the last 10 years to keep the supply and demand in balance, yet the net exports of cotton from India was of the order of 45 lakh bales during this period.

Strengthening Agricultural Research

2.103 The technological changes and developments that are necessary to accelerate the growth of the different sectors of the agricultural economy have been outlined in this chapter. Such biotechnological and genetic engineering innovations do not come easy and even when some are imported, they would take more resources and time to be adapted to the Indian conditions on small and fragmented holdings, particularly when they are not scale neutral, which was not the case with the adoption of high yielding varieties of wheat and rice.

2.104 To meet the new challenge of producing accelerated cost effective growth, agricultural research has to be considerably strengthened to cut down the time lags involved in the development of sophisticated technological advances

envisaged for a time horizon of 2000 A.D. and beyond. Technology may not be a substitute for institutional improvements and public policy, but in the ultimate analysis there are no two opinions that it is a powerful engine of growth which no scientific public policy can afford to neglect. To achieve this objective, it is not enough to establish a small Department of Biotechnology, which is yet to take off the ground. What is even more important is to attract some top scientists to provide professional leadership in these areas and ensure adequate research funds and facilities that would help achieve the goal of economic development of a progressive, productive and profitable Indian agriculture that would spearhead rapid growth of the Indian economy.

2.105 The gap between technological potential for crop yields and actual yields is fairly high in most parts of the country. To bridge this gap it is necessary to strengthen adaptive research in different agro-climatic regions of the country.

2.106 Apart from intensification of agricultural research, two related areas which are no less important are education in agriculture and the whole gamut of extension work that would promote adoption of new technologies in different sub-sectors of the agricultural economy. All these areas need to be developed in symbiotic relationship, each deriving strength from the other, so that agricultural economy of the country becomes technologically sound and more cost effective and viable.

Overview

2.107 We are aware that, viewed as a whole, the canvas of the Indian agriculture, as it would emerge by the turn of the century, can be painted only by using a broad brush. The directions in which various sub-sectors of the agricultural economy are moving are set out in this chapter. It would, however, be somewhat difficult to quantify the growth rates that would be realised in these sub-sectors by the year 2000 A.D. However, considering the technological developments that are in the pipeline and the new thrust of the public policy on expanding food processing, productivity and production of livestock and dairy products, horticultural products, oilseeds and edible oils etc. for

which the income elasticity of demand is high, growth rates in these sectors would improve substantially.

2.108 More specifically, the rising levels of cereal production will improve incomes of farm families which would result in diversifying their expenditure pattern, thereby lifting the demand not only for industrial goods but also for dairy products, horticultural products and edible oils etc. increasingly produced not only for the domestic market but also for the international market.

Dry Farming/Rainfed Farming

2.109 Keeping in view that dry land farming constitutes 70 per cent of the area under cultivation, but contributes only 42 per cent to agricultural production, public policies have in recent years accorded high priority to dry land farming with a view to raising productivity and reducing unemployment and regional disparities.

2.110 Integrated watershed development strategy has been developed with a central thrust on building up complementary relationship between crop husbandry, animal husbandry, horticulture, farm forestry and fisheries to optimise production and farm incomes in watershed areas. Implementation of this development strategy is, however, confronted with high technology risk and uncertainty problems as the risk aversion of most people in these areas runs very deep.

2.111 In the black soils of these areas, workability of the soils remains poor during the kharif season, making it difficult to raise a kharif crop. Crop response to irrigation is small, particularly in good monsoon years, which discourages the farmer from making investments in wells and other irrigation structures. Farmers are even more reluctant to adopt the package of practices recommended by the research organizations for integrating crop, livestock, fisheries and farm forestry systems, as these are not only more capital intensive but have a long gestation period.

2.112 Again, the high cost soil conservation and run off harvesting techniques

do not concern individual farmers which makes it difficult to recover the cost of such loans and advances unless the state government bears such costs.

Coarse Cereals

2.113 Public policy is moving in the direction of stabilizing coarse cereals production through improvements in their market structure and more effective procurement programmes. Sorghum and pearl millet seed-based technology has produced some good results but they will remain low-value crops with low absorption capacity of inputs which would tend to be substituted by high value commodities for which the income elasticity is greater than unity. As the production of superior grains rises, consumer demand for coarse cereals would fall, but expanded production of coarse grains could be used as concentrate feeds for high yielding cross-breds.

2.114 Genetic studies in cross-bred cattle for evolving new high yielding breeds and for improving productivity of indigenous draught and dual purpose breeds through selection and generation of superior germplasm have been the major research effort in cattle. If adequate fodders, forages, health cover, efficient managements, technical services associated with such technologies and such infrastructural facilities and multi product dairy plants, milk distribution routes and economical routing of milk vans could be assured to dairy farmers to make the necessary investments for raising productivity and production of the dairy enterprise, the white revolution would find its real roots at least in those regions of the country, where the demand for milk and dairy products is expanding and market infrastructure is fully developed.

2.115 Oilseeds and pulses will get more and more intercropped with HYV (high yielding variety) based crops to produce a greater impact on incomes of oilseeds growers. Since the prices of imported edible oils are close to the prices of oilseeds in India, it would take time to phase-out imports of edible oils, which might stand in the way of raising oilseeds production to the targetted level of 28 million tonnes by the turn of the century. The import bills of edible oils etc. could, however, be met by exporting the agricultural surpluses which emerge from such commodities and products which have high supply

elasticity. Among the cereals, wheat is a good candidate for raising its productivity in less developed regions and exporting the surplus to world markets. Processed food and marine products also have promising export potential. Now that the Government of India have organized a special Ministry to promote the rapid growth of the processing industry, horticultural products would raise productivity and farm incomes without producing ill-effects on the environment in the long run. This development will also result in increased gainful employment in the rural sector which is not only the crying need of the hour today but will remain so even by the turn of the century.

2.116 Finally, knowing too well, that technological change does not occur automatically, conscious policy decisions have to be taken to strengthen agricultural research and extension education institutions with an added thrust on evolving and adapting new cost effective technological knowledge and associated inputs.

2.117 In sum, it can be said that Indian agriculture will experience not only larger growth in absolute terms by the turn of the century and beyond, but it will also certainly be a scene of relative sub-sectoral shift, provided agricultural development programmes in different states are strongly supported by financial programmes of the financial institutions so that the two can develop in symbiotic relationship and make agricultural and rural economics much more viable, productive, progressive and highly profitable.

PART II

AGRICULTURAL CREDIT SYSTEM : A REVIEW

- III COMMERCIAL BANKS AND RURAL CREDIT
 - IV REGIONAL RURAL BANKS
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CHAPTER III

COMMERCIAL BANKS AND RURAL CREDIT

Induction of Commercial Banks to Rural Finance

Commercial banking which had its beginnings in India in the middle of the 18th century, took roots mainly in the urban and metropolitan centres. Its object primarily was the financing of trade and commerce. However, with the diversification and growth of Indian industry particularly during the war-time conditions of the forties, commercial banks started financing industry on an increasing scale.

3.02 Banks with a few exceptions considered the financing of agricultural sector as hazardous and unprofitable and hence did not enter this area. It was only after the All India Rural Credit Survey Committee (1954) which for the first time envisaged a role for the commercial banking system in rural credit albeit a supplementary one that the system made its debut in this area. But in the context of the rural credit policy then being pursued, the Committee believed that the role as envisaged could be fulfilled effectively only if there was a state partnered commercial bank which would have an obligation laid on it to discharge the new responsibility. The Committee accordingly recommended the conversion of the Imperial Bank of India into the State Bank of India (SBI) as a subsidiary of Reserve Bank of India. The preamble to the Act setting up the SBI stipulated as one of the main objectives of the bank "the extension of banking function on a large scale, more particularly in the rural and semi-urban areas". The SBI Act provided that the bank should open not less than 400 branches within the first five years of its working. Its focus, however, was on the financing of marketing of agricultural produce and to an extent on processing and other related agricultural business.

3.03 The main task of meeting the credit requirements in the rural areas, therefore, still remained the primary concern of the co-operative banking structure. By mid sixties there was, however, a growing realisation that in view of the larger and increasing credit needs of Indian agriculture in the wake of modern technological innovations, the efforts of the co-operatives needed to be supplemented by commercial banks in a substantial way. The first step in this direction was taken through "social control" of commercial

banks in 1967. The National Credit Council was set up in December 1967 to determine the priorities of bank credit to different sectors of the economy. In October 1968, the National Credit Council appointed a Study Group under the chairmanship of Prof. D.R. Gadgil. The Group found that by the end of June 1967 the commercial banks had reached only 5000 villages. By that time, although about 39 per cent of the total credit requirements of agriculture were met by institutional credit agencies, commercial banks' share therein was negligible at less than one per cent, the balance of 38 per cent being met by the co-operatives.

3.04 The Study Group recommended that the main aim of future national policy should be to involve the commercial banks increasingly in rural credit through branch expansion and direct lending. According to the Study Group, increased involvement of the commercial banks in rural credit could be achieved mainly by a) broadening the branch banking base, particularly, in rural areas, b) direct lending in areas where primary co-operative credit structure was either weak or had not been effectively established; and c) providing credit support to the base level co-operative agencies i.e. PACSs where the central co-operative banks (CCBs) were not financially and operationally strong enough to provide credit support. The recommendations of this Study Group formed the basis for further expansion of the commercial banks in the rural sector. The All-India Rural Credit Review Committee (1969) also supported the view that commercial banks should increasingly extend finance in rural areas.

3.05 This process was accelerated by the nationalisation of 14 major commercial banks in July 1969 and another 6 banks in 1980. The Committee to Review Arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD) 1981, which assessed the role of commercial banks in rural credit endorsed the view that commercial banks could play a significant role in the various programmes of rural development and made a series of recommendations to improve the quality of lending through commercial banks. The public sector banks numbering 28 (20 nationalised banks and State Bank of India and its 7 associates) now account for more than 90 per cent of the total business of all scheduled commercial banks. The progress of public sector banks since nationalisation is shown in table 1.

Table 1**Progress of Public Sector Banks since 1969**

Item	June 1969	December 1986
1. Total No. of offices in India	6,596	36,264
2. Rural	1,505	16,557
Semi-Urban	2,622	8,386
Urban	1,176	6,248
Metropolitan	1,293	5,073
3. Population per office	65,000	13,000
4. Deposits (Rs. crores)	3,897	92,515
5. Advances (Rs. crores)	3,035	56,779
6. Priority Sector Advances (Rs. crores)	441	23,811

Source : Consultant's Study No. II - Chapter V.

3.06 This unfolds a story of rapid expansion of commercial banks as well as their loan operations. The total number of branches increased over five times and the rural branches eleven times. The growth in deposits and loans and advances also kept pace, recording an increase of about 23 times and 19 times respectively. Consequently the rural people have come to be served quite extensively both for their investment credit and working capital requirements. Thus while the growth was rapid, the growth in its wake gave rise to several problems. Some of these were problems of expansion itself but others were those of management and the structural aspects of rural development. In this Chapter, we limit discussions mainly to their role in rural lending.

Progress in Rural Lending - Targets and Achievements

3.07 After nationalisation of commercial banks certain sectors which were hitherto neglected were given a priority status and the banks were asked to provide credit to these sectors in a more concerted way. These sectors included agriculture (direct and indirect), small-scale industry, small road and water transport operators, retail trade and small business, education, self-employed persons etc. It was mandated that the involvement of commercial banks in the identified priority sectors should reach a level of 33.3 per cent of outstanding credit by March 1979 and 40 per cent by March 1985.

3.08 Currently commercial banks are required to achieve certain targets and sub-targets under priority sector lendings. These are listed below :

- i) The overall target of 40 per cent of the total credit in respect of identified priority sectors was to be achieved by March 1985 and the same is expected to be maintained thereafter.
- ii) Direct finance to agriculture and allied activities is expected to reach a level of 17 per cent of total credit by March 1989. In February 1989, this target was further raised to 18 per cent to be achieved by March 1989.
- iii) A target of 10 per cent of net bank credit for weaker sections i.e. small and marginal farmers, share croppers, tenant farmers, landless labourers, artisans, village and cottage industries, IRDP beneficiaries, SC/ST borrowers etc. should be maintained.
- iv) Advances granted under differential rate of interest scheme (DRI) should form one per cent of the total advances outstanding as at the end of the previous year; atleast 40 per cent of such advances should go to SC/ST borrowers and at least two-thirds DRI advances should be provided through rural and semi-urban branches.

3.09 The latest available data show that most of these targets have been achieved. In fact the percentage of priority sector advances to net bank credit has crossed 45 per cent. The overall achievement of these targets and sub-targets as at the end of March 1988 in respect of public sector banks is indicated in table 2.

Table 2
Achievement of Targets/Sub-Targets in
respect of Public Sector Banks-March 1988

		(Rs. crores)
i)	Net Bank Credit	62,118
ii)	Priority Sector Advances	28,468
	Percentage to Net Bank Credit	45.8

		(Rs. crores)
iii)	Direct Advances to Agriculture	10,438
	Percentage to Net Bank Credit	16.8
iv)	Advances to Weaker Sections	7,310
	Percentage to Net Bank Credit	11.8
v)	Advances under DRI Scheme	622
	Percentage to outstanding advances at the end of December 1987	1.0

3.10 A detailed analysis of lending by all commercial banks to priority sectors and the comparative position of advances under different sub-sectors as on June 1969 and June 1986 is presented in table 3. It would be seen that as on June 1986 agriculture accounted for 41.5 per cent in terms of amount and 65.3 per cent in terms of number of accounts in the priority sector. As on the same date, small scale industries constituted 36.5 per cent of the amount and 7 per cent of the number of accounts. Advances to agriculture stood at Rs.9,483 crores, of which direct advances were Rs.8,117 crores or 85.6 per cent of the total agricultural credit spread over 16 million accounts. The southern and northern regions together accounted for Rs.4,648 crores or 57.3 per cent of direct agricultural advances as on June 1986 covering 8.8 million accounts (55.8 per cent of the total number of accounts). The eastern and the north-eastern region having 27.3 per cent of rural population accounted for 14 per cent of the priority sector, while the Western and Southern regions together having 36.8 per cent of the total rural population accounted for more than 51 per cent of the priority sector credit as on June 1986.

3.11 Some other highlights of commercial banks' advances to agriculture are indicated below :

- i) As at the end of June 1985, the direct advances to agriculture by commercial banks amounted to Rs.5,257 crores, spread over 10.0 million accounts. Of this direct short-term advances to agriculture stood at Rs.1964 crores spread over 6.3 million accounts. This accounted for 63 per cent of the number of accounts and 38 per cent of the amount of credit outstanding for agriculture. As against this their term-loan outstanding as on that date stood at Rs.3293 crores (62 per cent) spread over 3.7 million accounts (37 per cent).

- ii) As regards term loans as on June 1985 small and marginal farmers accounted for 68.2 per cent of the number of accounts and 33.3 per cent credit outstanding. The medium and large farmers, on the other hand, accounted for 31.8 per cent of the term-loan accounts but as much as 66.7 per cent of the outstanding credit in term-loan accounts.

Table 3
Advances by All Commercial Banks to Priority Sectors

Sr. No.	Sector	June 1969		June 1986		Average advance per A/c. (Rs.)
		No. of A/cs.	Amt.	No. of A/cs.	Amt.	
						(A/cs. in thousands)
						(Rs. crores)
1.	Agriculture					
	Direct	256	54	15,988	8,117	
	Indirect	11	134	967	1,366	
	Total	267	188	16,955	9,483	5,593
	(Percentage to total Priority Sector Advances)	(81.4)	(38.6)	(65.3)	(41.5)	
2.	Small Scale Industries	57	286	1,812	8,321	45,921
	(Percentage to total Priority Sector Advances)	(17.4)	(59.1)	(7.0)	(36.5)	
3.	Retail Trade and Small Business	NA	NA	4,449	2,003	4,502
	(Percentage to total Priority Sector Advances)			(17.1)	(8.7)	
4.	Other Sectors	4	9	2,766	3,037	10,979
	a) Road and Water transport operators	3	8	618	2,109	
	b) Professional and self-employed	-	0.3	1,759	787	
	c) Education, Housing loan to weaker sections and consumption loans etc.	1	0.5	389	231	
	(Percentage to total Priority Sector Advances)	(1.2)	(2.3)	(10.6)	(13.3)	
5.	Total Priority Sector Advances	328	483	25,982	22,844	8,792
	Total Credit		3,599		55,651	
	(Priority Sector Advances as percentage to total credit)		(14.0)		(41.0)	

Source : Consultant Study No. II, Chapter V.

- iii) Assuming that each short-term loan account represents a farm holding, commercial banks can be estimated to have covered at the end of June 1985, 1.44 million marginal farmers (2.6 per cent), 1.09 million small farmers (6.8 per cent) and 1.18 million medium and large farmers (5.2 per cent). There were 55.52 million marginal, 16.08 million small and 22.75 million medium and large farmers in the country.
- iv) The relative shares of marginal, small and medium and large farmers in land-area of holdings and their share in total short-term credit outstanding of commercial banks are given in table 4.

Table 4
Category-wise Share in Area and Credit

(Position as on June '85)

Category of farmers	Share in area of operational land holding (Per cent)	Share in Credit
Marginal (Upto 2.5 acres)	12.2	33.0
Small (2.5 acres to 5 acres)	14.1	29.1
Medium/large (above 5 acres)	73.7	37.9
	<u>100.00</u>	<u>100.00</u>

It will be seen that the proportion of the short-term credit given to the marginal and small farmers (33.0 per cent and 29.1 per cent respectively) by the banking system is much higher in relation to their proportion in the area under operational holding (12.2 per cent and 14.1 per cent respectively)

Poverty Alleviation Programmes

(i) **Integrated Rural Development Programme**

3.12 We have discussed IRDP and related poverty alleviation programmes in detail in Chapter XXI. However, the significant involvement of commercial

banks therein, progress in disbursement, failures etc., are briefly referred to here to emphasise their impact on the lendings of commercial banks.

3.13 One of the purposes of the nationalisation of commercial banks was to ensure that there was a rational deployment of credit in various sectors based on priorities necessitated by state policy and increased flow of credit to weaker sections of the community has from the start been a high priority area. Accordingly, the banks were mandated to lend at least 10 per cent of the net bank credit to weaker sections. Since IRDP became the major credit linked programme for the weaker sections, the commercial banks were required to involve themselves actively in the financing of this programme. During the Sixth Plan itself 16.6 million beneficiaries were assisted under IRDP and the aggregate term credit disbursed under the programme by all agencies was Rs.3,120 crores. The share of commercial banks in this was about 49 per cent. Their share has since increased substantially. The concurrent evaluation of IRDP for October 1985 to September 1986 has shown that the commercial banks accounted for 69 per cent of the loans RRBs 23 per cent and Co-operatives 8 per cent. More or less the same pattern was observed during January-September 1987. The region-wise distribution of credit outstanding under IRDP lending as at the end of June 1986 is given in table 5.

Table 5

Lending under IRDP by Commercial Banks - June 1986

Region	No. of Accounts ('000)	Amount outstanding (Rs. Cr.)	Average per account (Rs.)
Northern	776	175	2,255
North-Eastern	174	38	2,183
Eastern	1,224	205	1,675
Central	1,439	329	2,286
Western	833	174	2,088
Southern	2,050	346	1,687
Total	6,496	1,267	1,950

The outstandings under IRDP advances amounted to 18 per cent of the total outstanding advances at the rural branches as on 30th June 1986. In terms of incremental outstandings at the rural branches of commercial banks during the year 1985-86, IRDP outstandings contributed to 22.2 per cent of the total. During the year 1985-86, 14.91 lakh beneficiaries were accounted for under IRDP as against 51.60 lakhs for direct agricultural advances. IRDP disbursement during this period at Rs.376 crores formed 16 per cent of total disbursement for direct agricultural finance at Rs.2,366 crores. But these achievements in disbursements do not, however, reflect, it must be conceded, the quality of performance. Nor does it indicate that everything is moving well with the IRDP. The targets are achieved mainly because the banks have been compelled to do so. In fact, considerable importance has been attached by Government of India and other authorities to ensure that IRDP targets are achieved by banks without fail and this message has percolated to the field level. Several relaxations have been made by RBI in respect of eligibility criteria, procedures, rate of interest, collateral security and guarantee for the loan etc. in view of the special status accorded to IRDP loans and these concessions have been extended despite the fact that viability of many of these loans is open to question and recovery performance has been none too satisfactory. The attitude of Government officials has over the years hardened and they do not now hesitate to coerce bankers to give such loans under IRDP. This excessive concern with target achievement has resulted in marginalising the function of branch managers. They have been reduced to the position of mere instruments to carry out the instructions of Governmental functionaries at the local level and are obliged to lend even if the usual norms of lending and reasonably sound banking practices are to be overlooked, if not altogether ignored. The culture of casualness and permissiveness which is thus emerging in the sanctioning of loans needs to be arrested lest it affects the outlook and attitudes of bank functionaries in handling their other lendings.

(ii) Differential Rate of Interest Scheme

3.14 The 'Differential Rate of Interest (DRI) Scheme' was introduced in 1972 to give an added thrust to loans granted to the lowest-rung of the weaker sections. The scheme envisages provision of credit upto Rs.6,500 at a highly concessional rate of interest of four per cent for specified activities to the weakest of the weaker sections i.e. whose family income from all sources

does not exceed Rs.7,200 in urban and semi-urban areas and Rs.6,400 in rural areas. The advances under the scheme, it was stipulated, should form one per cent of total advances outstanding as at the end of the previous year and further that at least 40 per cent of such advances should go to SC/ST borrowers. At least two thirds of such DRI advances were to be issued through rural and semi-urban branches. As at the end of June 1986, credit to DRI beneficiaries by public sector banks aggregated Rs.523 crores, spread over 46 lakh accounts and formed 1.02 per cent of their total credit. The region-wise disbursement of DRI advances is given in table 6 .

Table 6

Region-wise Disbursement of DRI Advances

<u>Region</u>	<u>No.of Acc- ounts ('000)</u>	<u>Amount (Rs. Cr.)</u>	<u>Amount as percentage to total</u>
Northern	457	79	15.1
North-Eastern	91	11	2.1
Eastern	1,023	82	15.7
Central	629	86	16.4
Western	770	89	17.0
Southern	1,630	176	33.7
Total	4,600	523	100.0

The DRI Scheme was introduced during the early 70's primarily to increase the lending by commercial banks to the weakest of the weaker sections. As at present, however, the commercial banks are participating substantially under IRDP and other poverty alleviation programmes where the lendings are directed to the poorest and hence the initial logic for the introduction of DRI is no longer relevant in the present context. Recent instructions stipulate that DRI and other poverty alleviation programmes have to be mutually exclusive. Implementation of DRI, however, creates anomalous situations as, for instance, commercial banks have to finance the same clientele i.e. the weaker sections under two parallel programmes one at a higher rate and another at a lower rate. Further, co-operatives are not covered under the DRI scheme, on the ground that they are not, sufficiently strong to absorb the losses on account of lending at the rate of 4 per cent. Also, it seems

that no worthwhile purpose is served by extending a favoured treatment to only a very small proportion of the weaker sections of the farming community. Considering these factors, we are of the view that there is no need for the continuance of the DRI scheme and hence we recommend that the scheme may be discontinued forthwith.

(iii) **Self-employment Scheme for Educated Unemployed Youth (SEEUY)**

3.15 The Self-employment Scheme for Educated Un-employed Youth (SEEUY) was introduced by the Government of India during 1983-84 with the objective of encouraging the educated unemployed youth to undertake self-employment ventures in industries, service and business. The scheme covers all educated unemployed youth who are at least matriculates and are within the age group of 18 to 35 years. A bank loan upto Rs.35,000 at concessional rate of 10 per cent in backward areas and 12 per cent in other areas (loans above Rs.25,000 for industrial ventures will carry higher rate of interest upto 13.5 per cent) and subsidy at the rate of 25 per cent would be available to the identified beneficiaries. The scheme has been extended till the end of the Seventh Five Year Plan.

3.16 The performance of banks under the scheme since its introduction is indicated in table 7.

Table 7

(Year ended March)

<u>Yearwise performance of Banks under SEEUY</u>					
	<u>1983-84</u>	<u>1984-85</u>	<u>1985-86</u>	<u>1986-87</u>	<u>1987-88</u>
1. Physical target (in lakhs)	2.50	2.50	2.50	2.50	1.25
2. No. of applications sponsored to banks (in lakhs)	4.27	3.68	3.42	3.31	1.98
3. No. of loans sanctioned (in lakhs)	2.42	2.28	2.20	2.27	1.13
4. Amount of loans sanctioned (Rs. in crores)	401.54	429.52	429.99	469.91	237.18

The District Industries Centres (DIC) have the overall responsibility of implementing the programme. The selection of borrowers under the scheme is done

by a task force set-up by DIC where representatives of the banks are members. There have, however, been several complaints about the operation of the SEEUY scheme. One is that the selection of borrowers was often done by the task force without properly assessing the candidate about his capabilities, aptitudes and skills. Secondly, the scheme, in many cases, did not take into account the backward and forward linkages. Thirdly, the borrowers selected did not have the aptitude for the activities for which loans were given. Further, since DIC had several other functions, they could not give the required degree of attention to the implementation of SEEUY. Above all, as in other Government sponsored poverty alleviation programmes, the thrust was more on achievements of targets rather than on the quality of loans. As a result, the recovery of loans in this scheme has been extremely bad. In several cases it has been reported that borrowers were missing; they had either misutilised the loans or disposed of the assets. A recent study by RBI revealed that there were several deficiencies in the implementation of the scheme such as selection of ineligible candidates, misutilisation of bank finance, inadequate income generation from the assets etc. It was also found that the recovery position was unsatisfactory due to irregular income of borrowers, wilful defaults and lack of proper follow-up.

(iv) Self-employment Programme for Urban Poor (SEPUP)

3.17 The Self-employment programme for urban poor (SEPUP) was introduced by Government of India in 1986-87 and has been extended till the end of Seventh Five Year Plan. The objective of the programme is to assist poor people (family income upto Rs.600 per month) living in metropolitan, urban semi-urban areas and not covered under IRDP, with bank loans upto Rs.5,000 at 10 per cent interest and subsidy at 25 per cent from the Government of India. The target is to cover one beneficiary for every 300 population based on 1981 census. During the first year of its implementation, the banks disbursed Rs.101 crores in respect of 3.08 lakh loans.

3.18 The commercial banks were also asked to step up their advances to SC/ST beneficiaries. The progress in respect of advances granted by public sector banks to SC/ST beneficiaries is given in table 8.

Table 8
Advances of Public Sector Banks to SC/ST Beneficiaries

As at the end of	(No. of accounts in lakhs) (Amount in Rs. crores)				
	<u>Total Priority Sector Advances</u>		<u>Of which to S/C ST beneficiaries</u>		Percentage of 5 to 3
	No. of A/cs.	Amount outstanding	No. of A/cs.	Amount outstanding	
1.	2.	3.	4.	5.	6.
December 1985	241.94	20,647.81	56.81	1,350.29	6.5
December 1986	269.75	24,085.27	64.91	1,600.35	6.6
December 1987	297.88	27,810.04	71.09	1,814.28	6.5
March 1988 (Provisional)	303.92	28,467.79	72.95	1,957.04	6.9

There has been significant progress both in the number of accounts and quantum of credit granted by the banks to SC/ST beneficiaries. There is no specific target stipulated for loans to these sections. The weaker sections for which a target of 10 per cent of advances has been prescribed include, among others, SC/ST beneficiaries. However, under special Government programmes like IRDP, SEEUY and SEPUP it has been stipulated that 30 per cent of the benefits should go to the SC/ST. The banks have achieved these targets except in the case of SEPUP. Under DRI Scheme as against the target of 40 per cent, the banks have lent 49.3 per cent of advances to SC/ST beneficiaries.

3.19 The commercial banks have been advised to initiate measures to ensure smooth flow of credit to the minority communities. The concerned lead banks have been asked to give wide publicity to the various anti-poverty programmes among minority communities, particularly in the 40 identified districts with large concentration of minority communities. Lead banks have also been instructed to prepare suitable schemes for their benefit in collaboration with bank managers. At the end of December 1987 advances by commercial banks to minority communities amounted to Rs.2,964 crores under 4.15 million borrowal accounts, of which the priority sector advances amounted to Rs.429 crores under 0.79 million accounts.

Branch Expansion

3.20 The commercial banks have since nationalisation, made substantial progress in branch expansion in all states and regions of the country. This followed the recommendations of a Committee on Branch Expansion Programme under the Chairmanship of Shri F.K.F. Nariman appointed in August 1969 by RBI. The main task set for the Committee was to evolve a rational policy in regard to development of branch network of commercial banks, so that they could finance agriculture more effectively. The Committee recommended, among other things, the location of new branches of commercial banks in unbanked and under-banked centres. In the absence of reliable and updated information about economic potential of the centres for such branches, the Committee felt that RBI may be guided by population criterion (1 unit per 10,000 population) while granting licences. The Committee also recommended that each commercial bank should concentrate on certain districts where it should act as a Lead Bank. These recommendations facilitated the implementation of the Lead Bank Scheme and formulation and execution of area specific schemes under a concept of district credit planning.

3.21 The branch expansion policy of commercial banks thus got a fillip after their nationalisation in July 1969. As against 8,321 branches at the time of nationalisation, the banking system (including RRBs) had 53,397 branches as at the end of 1986. The major policies and guidelines of RBI on branch expansion during this period centred around :

- i) Preparation of banking plans initially by the banks themselves but associating State Government, District Consultative Committee, Lead Bank and RBI at later stages in identifying specific centres. These plans took into account several factors such as the need for banking facilities at the centre, removal of regional imbalances, reduction in the number of population served by a bank office etc.
- ii) Linking opening of new offices at unbanked rural/semi-urban centres to opening of branches in banked centres in urban and metropolitan centres.
- iii) Involving the Lead Bank on an intensive scale in opening branches in their respective districts.

- iv) Giving preference to RRBs in opening branches in their command areas and supplementing their activities in such areas by sponsor banks.
- v) Categorising banks into regional and all-India banks and giving preference to regional banks for opening branches in their area of operation and dissuading them from opening branches in far-flung areas.
- vi) Adopting a selective and need based approach in the matter of opening branches at urban and metropolitan centres.

3.22 The branch expansion policy of RBI during 1985-90 envisaged the opening of additional bank branches so as to achieve average population of 17,000 per bank office (as per 1981 census) in rural and semi-urban areas with development block as the basis. Besides, a rural branch was expected to be available within a distance of 10 kms. and cover an area of about 200 sq.kms. Hilly tracts and regions which were sparsely populated and tribal areas were to be given special consideration by relaxing the population norms. The banks were also advised to consider setting up of satellite/mobile offices in areas where the volume of business and other considerations did not warrant the setting up of a full fledged branch.

3.23 The spread of bank branches as at the end of December 1987 vis-a-vis the position as on 30th June 1969 is indicated in table 9.

3.24 The highlights of the branch expansion programme during the past 18 years are :

- i) The increase in the number of bank branches during the period 1969-87 is given in table 10. In most of the years (except when RBI followed a policy of consolidation) the number of branches opened in a year was of the order of 2,000 and above. In some years the number of branches opened exceeded 3,000.
- ii) Of the 45,135 branches opened during 1969-86, as many as 29,586 branches were opened in unbanked centres. This trend of opening more branches in unbanked centres was visible from 1977 onwards.

Table 9

**Bank Group-wise/population Group-wise Number of Branches of
Commercial Banks as on 30th June 1969 and 31st December 1987**

Sr. No.	Banks	30th June 1969					31st December 1987				
		Rural	Semi-Urban	Urban	Metro-politan/ Port Towns	Total	Rural	Semi-Urban	Urban	Metro-politan/ Port Towns	Total
1.	State Bank of India	462	795	162	150	1,569	3,557	2,150	1,070	760	7,537
2.	Associate Banks of State Bank of India	357	375	86	75	893	1,311	1,170	558	382	3,421
3.	Nationalised Banks	686	1,452	928	1,068	4,134	12,028	5,465	4,648	3,939	26,080
4.	Regional Rural Banks	-	-	-	-	-	12,259	946	133	3	13,341
5.	Other Scheduled Indian Commercial Banks	265	595	231	228	1,319	1,372	1,383	827	600	4,182
6.	Foreign Banks	1	2	9	118	130	-	2	9	125	136
7.	Non-Scheduled Banks	61	103	31	22	217	18	14	7	-	39
TOTAL :		1,832	3,322	1,447	1,661	8,262	30,545	11,130	7,252	5,809	54,736

Note : 1. Data based on information gathered from DBOD, RBI.

2. Nationalised Banks include banks nationalised at the reporting time.

Table 10

Year-wise Commercial Banks' (including RRBs) Branches

<u>Year</u>	<u>Net increase in number of branches</u>	<u>Year</u>	<u>Net increase in number of branches</u>
1969	1361	1979	2053
1970	2133	1980	3030
1971	1801	1981	3460
1972	1754	1982	2781
1973	1964	1983	3297
1974	1764	1984	3988
1975	2274	1985	4321
1976	3201	1986	401
1977	3341	1987	1339
1978	2508		
		Total	<u>46,474</u>

iii) As on 30th June 1969, rural (22 per cent) and semi-urban branches (40 per cent) accounted for 62 per cent of the total branches. However, at the end of 1987, rural (56 per cent) and semi-urban branches (20 per cent) accounted for 76 per cent of the total number of branches.

iv) As against the estimated population served by a commercial bank branch at 65,000 in 1969, the per branch population coverage in December 1986 was 13,000 (1981 census). Only in Assam and Manipur the population per branch was above the planned level of 17,000.

v) Of the 36,590 branches opened by Lead Banks upto 31st December 1986 since the introduction of lead bank scheme, 10,432 branches were opened by them in their lead districts.

3.25 The main objective of branch expansion has to a large extent been fulfilled in the last decade and half since nationalisation and the policy has lately shifted from expansion to consolidation and from quantitative to qualitative improvement. There may, however, be still pockets where banking

services are needed if not on a population criterion but on consideration of spatial gaps. The allotment of centres to commercial banks and RRBs on the basis of lists of identified centres received from State Governments for opening new bank offices under the branch licensing policy 1985-90 has almost been completed. RBI has allotted 4,958 rural/semi-urban centres to banks (2,046 to RRBs and 2,912 to commercial banks) upto June 1988. Banks have been advised that opening of branches at the centres allotted to them under the current programmes should be spread over the remaining period of the Seventh Plan. Another aspect is the understaffing in a large number of rural branches, many of which are working as two or three men offices. Related to this is the problem of training the staff in all facets of rural lending. This is very important from the point of view of ensuring quality of service to rural community.

3.26 We have elsewhere in this report recommended merger of RRBs with the sponsoring commercial banks. This would result in adding another 13,000 and odd branches. But with the rationalisation which is called for in view of the lead role assigned to rural branches of commercial banks or RRBs as the case may be under the Service Area Scheme, the number of branches may eventually get reduced. The reduction, however, is not likely to be substantial.

Deposit Mobilisation and Credit Deployment in Rural Areas

3.27 With the rapid expansion of commercial bank branches in the rural areas, it was thought necessary to emphasise local deployment of deposits, in order to allay apprehension that rural branches might become conduits for the flow of resources from rural to urban areas. Accordingly, certain norms regarding deployment of credit as a percentage of deposits mobilised from rural and semi-urban areas were prescribed by the RBI. The banks were advised that by March 1979 their rural and semi-urban branches should achieve a Credit Deposit Ratio (CD Ratio) of at least 60 per cent. While it was not envisaged that this ratio be achieved separately for each branch, district, or region, banks were asked to avoid wide disparity in CD ratio between different states/regions.

3.28 The public sector commercial banks could achieve this target in respect of their rural branches by June 1985, when the CD ratio stood at 61.0 per cent. As regards their semi-urban branches, the CD ratio was 48.9 per cent by December 1980 and 51.3 per cent by December 1986. The comparative position of CD ratio of Public Sector Banks in June 1979 and December 1986 is given in table 11.

Table 11

(Percentages)

Comparative Position of CD Ratio of Public Sector Banks *

<u>Population Group</u>	<u>June 1979</u>	<u>December 1986</u>
Rural	55.2	60.5
Semi-Urban	47.5	51.3
Urban and Metropolitan	80.0	64.8
	<u>67.0</u>	<u>61.4</u>

3.29 As at the end of December 1986, all the states in the southern region exceeded 60 per cent CD ratio in rural areas. In Andhra Pradesh, Karnataka and Tamil Nadu the ratio was 101 per cent, 99 per cent and 99 per cent respectively. Maharashtra (75 per cent) in western region, Madhya Pradesh (71 per cent) in central region and Orissa (102 per cent) in eastern region exceeded the 60 per cent level. The performance of Bihar and West Bengal was poor at 43 per cent and 36 per cent respectively. CD ratio of 60 per cent in semi-urban branches was exceeded only in Andhra Pradesh, Tamil Nadu and Karnataka.

3.30 In 245 out of the total number of 437 districts in the country, the CD ratio of rural branches as at the end of December 1986 was over 60 per cent, in 103 districts it was between 40 and 60 per cent, and in 89 districts between 20 and 40 per cent. The ratio was below 20 per cent in 20 districts, which were mainly hilly and tribal. In central, western and southern regions the proportion of districts with a satisfactory rural CD Ratio was fairly high. The CD ratio of semi-urban branches of CBs in 141 districts was above 60 per cent, in 123 districts between 40 per cent and 60 per cent in 114 districts between 20 per cent and 40 per cent and in 23 districts less than 20 per cent. While the CD ratio by itself is not an indicator of the total involvement of

* Source : Consultants Study II - Chapter V

banks in a region, as it does not take into account other investments by banks in the region by way of subscription to bonds floated by quasi-Government bodies etc., it is universally accepted as the true indicator of deployment of deposits raised locally in the shape of loans in the area. The low CD ratio in certain regions/states was mainly due to their low credit absorption capacity. This in turn was due to lack of infrastructural facilities and absence of profitable avenues for deployment of credit in these areas.

3.31 The regionwise position of rural branches of commercial banks, their deposits and advances are given in table 12.

Table 12
Commercial Banks (excluding RRBs)
Rural Branches Deposits and Advances : Region-wise Variations
(Position as on 30th June 1985)

Region	Offices	Deposits (in Rs. crores)	Credit	CD Ratio	Per branch		Per capita	
					Deposit (Rs.in laksh)	Advances	Deposit (Rs.)	Advances (Rs.)
Northern Region	3,087 (18.5)	2,400.62 (22.8)	1,173.97 (17.)	49.00	77.77	38.03	3780	1852
North Eastern Region	456 (2.7)	301.61 (2.9)	188.51 (2.7)	62.50	66.14	41.34	1173	733
Eastern Region	2,208 (13.2)	1,658.06 (15.8)	954.86 (13.9)	57.58	75.09	43.24	1225	705
Central Region	3,354 (20.1)	2,128.96 (20.2)	1,373.70 (19.5)	64.52	63.47	40.95	1480	955
Western Region	2,945 (17.6)	1,627.20 (15.5)	928.56 (13.5)	57.06	55.25	31.53	2304	1314
Southern Region	4,662 (27.9)	2,393.57 (22.8)	2,271.81 (33.0)	94.91	51.34	48.73	1824	1731
Total	16,712 (100.0)	10,510.02 (100.0)	6,891.40 (100.0)	65.57	62.88	41.23	1844	1209

Source : RBI, Report on Currency and Finance, 1986-87.

It could be seen that there are sharp regional variations in the growth of banking as between different regions. There is a concentration of offices, deposits and credit in the southern, central and northern regions while the north-eastern region has the smallest share followed by eastern region. Relative

to the share of branches, deposit mobilisation was marginally better in the eastern, north-eastern and central regions and significantly better in northern region. In the western and southern regions, however, the share of deposits was lower relative to the share of branches. In all regions, except the southern region the share of credit was lower than their share in deposits. The branches in the southern region had 33 per cent share in credit as against share in deposits at 22.8 per cent and share in office at 27.9 per cent. Consequently the the CD ratio is the highest at 94.91 per cent in the Southern region. The average deposit per rural branch for the country as a whole was Rs.62.9 lakhs. The northern, eastern, north-eastern and central regions had higher average per branch deposit. The average advances per rural branch for the country as a whole amounted to Rs.41.2 lakhs. Southern and Eastern regions had the highest average advances per branch. The average per capita deposit in the rural areas was Rs.184 for the country as a whole. It was the highest in the Northern region, at Rs.378. The per capita advances in rural areas amounted to Rs.121 for the country as a whole. It was the highest at Rs.185 in northern region followed by the southern region at Rs.173.

3.32 As at the end of December 1984, 48.7 per cent of the credit extended by rural branches (including RRBs) was for agriculture (direct advances). Priority sector advances covered roughly 75 per cent of the business of rural branches. In the semi-urban branches the share of direct agricultural advances was lower at 31.5 per cent and share of priority sector advances at 67.9 per cent. The average number of loan accounts per rural branch stood at 589 and amount of credit outstanding at Rs.24.5 lakhs. As regards direct finance to agriculture in rural branches, the average number of loan accounts stood at 345 and credit at Rs.11.9 lakhs.

3.33 There is marked regional variation in the deployment of credit and mobilisation of deposits. Perhaps this is only to be expected considering the widely prevailing regional differences in resource endowments and infrastructural facilities in the country: In addition to rural branches, semi-urban branches of commercial banks account for substantial lending for agriculture. The rural branches also lend significantly for non-agricultural and non-priority sectors. The proportion of such advances goes on increasing in semi-urban, urban and metropolitan branches in that order.

Staffing and Supervision Arrangements in Rural Branches

3.34 The bulk of the lending, much more than the stipulated norm of 40 per cent of the total lendings in rural branches of commercial banks, is to the priority sector and consists of a large number of small advances. The borrowers of these branches are located in far flung areas and commuting facilities for reaching such borrowers are very often non-existent. Obviously sanctioning and monitoring of advances to clients of this nature are time consuming and require proportionately more man power than what is necessary in urban centres. A single officer can supervise at the most upto 750 accounts. Even this norm is on the high side if the borrowers are scattered over a wide area. Our consultants have found that many of the rural branches visited by them were inadequately staffed. As many as 1700 accounts had to be managed by a single field officer in some branches. In view of the large number of accounts to be covered by field officers, supervisory work in many rural branches came to be neglected. The staff gave priority to the routine house-keeping work including submission of returns. Even the non-business working day was being utilised for clearing the arrears of the routine office work. Due to their reduced profitability, the controlling offices tried to economise the costs in rural branches in several ways and cutting down on the staff strength was most frequently resorted to. One view is that the additional expenditure on staff could be curtailed to a large extent by resorting to mechanisation at the larger branches, particularly in urban/metropolitan centres and diverting the surplus staff to the rural centres. There are however, several practical difficulties in implementing this in view of various pressures on the banking industry. NABARD has started a pilot project where it finances the cost of additional supervisors. Extension of this scheme to the entire banking system would be difficult in view of cost implications and Government restrictions on recruitment in banks.

3.35 Another issue that needs examination in this context is whether there is any need at all for a special cadre of staff to supervise agricultural lending. In the initial stages there was need for technical expertise not only in the appraisal and developing of agricultural finance, but also for providing technical advice to the borrowers and accordingly the staff specialised in agriculture were posted to the rural branches of commercial banks. At present, however, since the schemes are mostly prepared at the controlling offices, the specialised staff posted to the branch are generally being utilised for routine office work and to a limited extent for routine supervision. One view is that such work

at the branch level can be done by the general staff with some additional training. One has also to take into account the fact that extension officers of the State Governments' Agricultural Departments currently provide technical advice to many of the bank borrowers. In the circumstances the need for specialised staff in agriculture arises more at the controlling offices. Over a period of time, this core staff has to be built at the block level so as to guide all the branches within that block. At the branch level, what is important is to have, at all professional levels, staff, who have the necessary proficiency in handling all the different areas of activities and high degree of motivation. Such personnel should possess skills and motivation to interact with rural clients, besides skills in identifying, formulating and appraising projects and other services needed by the clients in agricultural production sub-system (APS), agricultural inputs sub-system (AIS) and agricultural marketing and processing sub-system (AMPS). Besides, it is also necessary that such staff are exposed to various programmes of training so as to upgrade their skills in handling all types of rural advances.

3.36 It has been the general experience that staff in the rural branches of commercial banks lack motivation. Most of the rural branch centres do not have the basic amenities. The officer posted to a rural branch compares his position with that of his colleague posted in cities and feels that he is being discriminated against. This affects his attitude to work and he may just bid his time to complete his compulsory stint at the rural branch, without any real involvement in the work. A realistic solution is to be found to this problem if the staff posted at the rural centres are to give their best during their tenure at such centres. The following are some of the suggestions made to us during our visits, to enhance the motivation of rural branch staff of commercial banks :

- i) Most of the problems associated with rural posting arise when the incumbents have families and family obligations. If they are posted at the early stage of their career before they get involved in such obligations, rural postings would not be so much resented.
- ii) It has been stated that many staff members escape rural posting through influence and this demotivates others. Hence, rural

posting should be made compulsory for all. A definite tenure should be fixed for such posting which should be strictly adhered to.

- iii) The staff posted at rural centres should be given special incentives so that the disadvantage associated with such posting can be off-set to some extent.
- iv) Creation of a 'banking community centre' for a group of village branches of commercial banks and locating it in a taluk headquarters. All the branch managers and staff could be suitably housed at this centre where facilities for education, health, recreation etc. could be created jointly by the commercial banks.

3.37 We feel that it is necessary to study the implications of these suggestions more closely to see how far they are practical in the present context of commercial banking. We are also of the view that merely exhorting the commercial banks to take up the challenge of rural work without concrete measures and incentives is not likely to yield results. At present there is no uniformity among the banks in regard to the facilities available to rural branch managers. There is a stipulation prescribing a minimum period of two years service in a rural branch for eligibility for promotion to higher grades. We are convinced that if commercial banks are to expand in the rural areas, they should have the right staff properly trained and motivated to man the rural branches. While recruiting staff in the rural branches of commercial banks, some weightage needs to be given to candidates from the rural areas. Some incentives both monetary and non-monetary are necessary for the staff posted in these rural branches to compensate the hardships of rural posting. It is important that they look forward to a rural posting with a sense of pride, instead of avoiding such postings as at present. We understand that the Indian Banks Association has set-up a committee to examine these and other related aspects with regard to service conditions of rural branch managers and make suitable recommendations for motivating them which can be uniformly applied to all banks.

Overdues in Commercial Banks

3.38 A detailed analysis of overdues in different institutional structures

i.e. commercial banks, RRBs and co-operatives and remedial measures thereof are presented in Part III "Overdues in the Agricultural Credit System". It is becoming increasingly clear that the overdues are an all pervasive malady and is neutral to the type of lending institution. For the institutional credit structure as a whole as at the end of June 1986 overdues from agricultural lending worked out to a total of Rs.4,262 crores of which Rs.1,744 crores related to commercial banks, Rs.413 crores related to RRBs and Rs.2,105 crores to PACSs and LDBs. Some special features of overdues and the emerging trends in the commercial banking system are discussed below :-

- i) Of late, there has been an improvement in the recovery performance of public sector banks in respect of their direct agricultural advances. The aggregate recovery for the year ended June 1987 in respect of the 28 public sector banks was 57.4 per cent of demand as compared with 56.5 per cent for 1985-86 and 54.2 per cent for 1984-85.
- ii) This improvement is due to a number of steps initiated recently by commercial banks to improve their recovery performance. This included gearing up of their organisational structure, increased adoption of schematic lending, improved pre-lending appraisal of schemes, launching of recovery drives in co-ordination with State Government machinery etc.
- iii) The state-wise recovery position of all scheduled commercial banks indicated that Kerala with 73.1 per cent recovery topped the list as at the end of June 1987, followed by Punjab with 69.8 per cent recovery. In 5 states i.e. Punjab, Kerala, Goa, Andhra Pradesh and Tamil Nadu the recovery was above 60 per cent of demand as on June 1987. The recovery was less than 40 per cent of demand in Assam (39.4 per cent), Manipur (21.9 per cent) and Meghalaya (30.3 per cent).
- iv) The recovery performance in respect of short-term loans has been generally better than term loans as indicated in table 13.
- v) Whenever commercial banks have lent without properly assessing the credit-worthiness of the borrower, his ability to productively use the asset and repay the loan, recovery has been poorer.

Table 13

Recovery Performance under Short-term and long-term loans

<u>June</u>	(In per cent of demand)	
	<u>Short-term</u>	<u>Term loans</u>
1981	58.7	46.8
1982	58.5	46.5
1983	58.8	48.1
1984	57.5	46.6
1985	60.2	49.6
1986	61.5	52.9
1987	63.6	52.3

Such cases have been more prevalent under poverty alleviation programme. For example the percentage of recovery under IRDP loans was 45.3 of demand on 30th June 1987 as against 57.4 under general agricultural advances for the 28 banks in the aggregate.

- vi) In several cases the average number of accounts handled by a field officer was beyond his capacity. Consequently he had neither time nor enthusiasm to plan his work according to the convenience of the borrowers. As mentioned earlier, increase in the average number of accounts handled by the field officer well above the reasonable norms has resulted in considerable slackening of recovery efforts. Quite a few of the branchmanagers interviewed by our Consultants were of the view that this extra burden on the field staff was one of the major factors responsible for poor recovery.
- vii) In the absence of minimum residential facilities, many field officers did not live at the centre where the branch was located but at the nearest town or city. This had slackened the recovery efforts as they could not visit the villages early in the morning or after nightfall, when the farmers were likely to be found at their residences.
- viii) The 'non-business working day' introduced by the banks was not fully taken advantage of by the field staff for recovery

purposes. They had often utilised it for clearing the arrears in desk work and documentation.

- ix) The case study conducted by the consultants revealed that in many branches the post of field officer was kept vacant for a number of years, by which time the overdue position had become very acute. In some other branches although field officers were posted in time, in the absence of clerical support they had to concentrate on desk work to the neglect of field duties. Due to paucity of staff many branches could not reschedule the loans well in time.
- x) A welcome trend, however, was organisation of 'recovery melas' where the bank officers camped in certain villages and invited the borrowers to repay their loans. Many times the concerned Government authorities also attended these melas and used their moral influence with the borrowers to repay bank loan. Borrowers in fact welcomed such melas as they saved their time and botheration of visiting the branches. Such efforts have improved the recovery in certain pockets quite significantly.

Lead Bank Scheme as a Mechanism to provide Credit for Rural Development

3.39 We have discussed the various aspects of credit planning in Chapter XVII on "Development Plans and Credit Planning". We are presenting here only an overview of the concept of LBS and the new 'Service Area Approach'. The adoption of 'area approach' for the development of credit and banking in the country on the basis of local conditions was first recommended in October 1969 by the Gadgil Study Group. The Group suggested earmarking of districts to commercial banks so that they could act as pace setters in these districts in providing integrated banking facilities. This idea was fully endorsed by the Nariman Committee. RBI accepted the recommendation and formulated the Lead Bank Scheme (LBS) towards the close of 1969. The LBS did not envisage a monopoly of banking*business to the Lead Bank (LB) in the allotted districts; instead the lead bank was to act as a group leader for co-ordinating the efforts of all credit institutions in the district for branch expansion and for meeting the credit needs of the rural economy. The allocation of districts to each bank was made taking into account factors

like size of the bank, adequacy of its resources, regional orientation of the banks, etc.

3.40 Firstly, the LBs undertook an impressionistic survey of districts allotted to them and identified the centres for opening branches. District Consultative Committees (DCCs) were set up in the districts to serve as forums for consultation and co-ordination among the banks on the one hand, and the district development functionaries on the other. The working of LBS was reviewed on a sample basis in Gujarat and Maharashtra by the Study Groups set up for the purpose. Their report submitted in December 1975 contained several recommendations regarding the implementation of LBS and preparation of District Credit Plans (DCP). Based on these recommendations, LBs prepared the first set of credit plans and launched them by July 1978. These first round credit plans were, however, deficient in many ways. RBI decided to terminate them at the end of December 1979 and issued fresh guidelines for preparation of DCP for calendar years 1980-82. A system of preparing Annual Action Plans (AAP) under DCP was introduced and the first such plan was launched in January 1980. CRAFTCARD assessed the implementation of LBS and suggested setting up of a Committee to review the scheme in detail. Accordingly a Working Group was set up in December 1981 to study the LBS. This Committee identified several deficiencies of LBs and made recommendations to bring about a qualitative change in the implementation of LBS and DCP. RBI issued guidelines in the year 1982 to LBs for the preparation of Third Round of DCPs covering the period 1983-85. Pending finalisation of Seventh Five Year Plan, RBI could not finalise the guidelines for the Fourth Round of DCPs. LBs were advised to prepare Annual Action Plans for the years 1986 and 1987. In April 1987, RBI issued fresh guideline for preparation of Fourth Round of DCPs covering the 3 year period beginning from January 1988 to December 1990. Thus, over the years LBS and DCPs/AAPs have become the main instruments for ensuring better deployment of credit for rural development by commercial banks. As at the end of December 1987, LBS covered 437 districts in the country.

3.41 The machinery to implement the LBS at various levels consists of (i) Lead Bank (ii) Lead Bank Officer appointed by LB (iii) District Co-ordinators of Non-Lead Banks (iv) Lead District Officers of RBI (v) Officers of NABARD (vi) District Consultative Committee and its Standing Committee which supervise

the implementation of the scheme at the district level (vii) District Level Review Committee which ensures participation of non-officials in credit planning (viii) State Level Bankers Committee which co-ordinates the activities of the financial institutions at the state level and (ix) State Level Co-ordination Committee which co-ordinates the activities of financial institutions with those of government departments.

3.42 LBS has no doubt created an awareness for better credit planning and resulted in better understanding of mutual problems at the ground level. Many of the LBS Committees, however, have tended to become more ritualistic than functional. Co-operation between banks and Government agencies have also not been achieved in the real sense, particularly in the context of large scale implementation of anti-poverty programmes where targets set by Government Departments have become more sacrosanct than the guidelines laid down under credit planning. Although the quality of the credit plans have steadily improved over the years as a result of increasing familiarity of the bank staff with the techniques of credit planning. The absence of reliable data at the block level still remains a major problem. The annual plan targets of various Government Departments are still not available block-wise in most cases. In the absence of proper district or block development plans, LBs struggle to give shape to credit plans on the basis of whatever information they could collect. Because of these limitations, current DCPs are at best only indicative of broad targets. Branch managers do not find DCPs/AAPs of much guidance in their lending operations. As our Consultants have pointed out "at the grass root level, in so far as branch managers are concerned they are not aware of the exact targets under the credit plan be it DCP or AAP". The tendency towards unplanned loaning to walk-in-customers or sponsored clients (IRDPA) etc. is on the increase. Branch managers generally ignore the plan and undertake loaning in a haphazard manner. Even if in some cases targets under DCP are achieved, it is more accidental than the result of realistic planning and conscious implementation. Though they are associated with the credit planning exercises, co-operatives generally feel that they are participating in a plan imposed on them by LBs. Another problem in credit planning is that Government Departments do not stand by their commitments to line up the various facilities as envisaged. This makes credit estimates in the plan go haywire. The Lead Bank Scheme and credit planning have no doubt

made considerable progress during the past two decades. But with too many banks, too many programmes with some degree of commonality of objectives and too many agencies involved, coordination has become a major problem. Further, in the absence of district development plans, credit planning has become somewhat of a loosely structured planning exercise. To improve the quality and mechanics of credit planning and make it more meaningful to participating branches, RBI recently suggested a new concept known as the 'Service Area Approach'.

Service Area Approach to Rural Lending

3.43 On a review of commercial banks' performance, the available evidence show that the steep increase in institutional credit had not resulted in a corresponding increase in agricultural production and productivity. There was also a marked regional imbalance both in growth rate and levels of production. Against this background, RBI advised the Chief Executives of Public Sector Banks to personally undertake an in-depth study of their rural loaning in November/December 1987. Their studies confirmed that for various reasons bank credit could not achieve optimum results in increasing production as also productivity because (i) schematic and intensive area approach was gradually being replaced by scattered lending and (ii) the banks competed with each other for business in areas with good potential, often neglecting areas with inadequate business potential. A seminar on rural lending was held by RBI in January 1988 to discuss the findings of these studies. An important recommendation of the seminar was that with the large net work of rural and semi-urban branches, the time was opportune to adopt a system of assigning specific area to each bank branch. This would enable the branches to have developmental orientation and tone up the quality of lending in rural branches. The idea was to allocate a specific number of villages to each branch of commercial banks and RRBs and make it responsible for bringing about economic development in the areas assigned. The new approach known as 'Service Area Approach' was formalised by the Union Finance Minister in his Budget speech of 29 February 1988. The RBI issued comprehensive guidelines to all banks in March 1988 outlining the modalities of implementation of the new scheme.

3.44 The Service Area Scheme (SAS) involves five stages in its implementation, viz. (i) identification of the service area for each branch, (ii) survey

of the service area for assessing the potential for lending for different activities and selection or identification of beneficiaries, (iii) preparation of credit plans on an annual basis, (iv) co-ordination between credit institutions on the one hand and field level development agencies on the other, on an ongoing basis for the effective implementation of credit plans and (v) a continuous system of monitoring the progress in the implementation of the credit plans and individual schemes as also of recovery and proper recycling of funds.

3.45 The scheme envisages allotment of roughly 15 to 20 villages to each rural and semi-urban branch of commercial bank and RRB. Specialised branches like Agricultural Development Branch of the State Bank of India and Gram Vikas Kendras of Bank of Baroda are allotted a little more number of villages. A Committee headed by the Lead District Officer (LDO) of RBI was to supervise the branch-wise allocation of villages. Proximity to the branch, contiguity in geographical location and accessibility were the main criteria adopted by the Committee for allocation of villages. The co-operatives have not been brought within this exercise but they would be free to lend within their existing area of operation to their members. In the case of 'service area' allocated to RRBs, the lending for non-target groups is expected to be taken care of by another designated commercial bank branch, generally belonging to the sponsor bank of the concerned RRB. Most of the branches have reportedly been allocated their 'service area' villages and they have started the preparation of village profiles for assessing the potential for lending and schemes suited to the borrowers. The branch annual credit plans will be aggregated to make block plans and further to district plans on the basis of guidelines issued by RBI. A block level bankers' committee is expected to coordinate the activities of both the credit agencies and the development agencies. The intention is that credit should be supported by necessary infrastructure and other non-credit inputs so that there will be perceptible impact of the bank credit on the overall development of the rural sector.

3.46 The distinct advantages expected to accrue from the new approach are :

- i) The branch managers would be able to devote concentrated attention to the development of the designated area of each branch.
- ii) Duplication of efforts by several banks in the same area would be avoided.

- iii) Instead of scattered lending over wide areas and the consequent dilution in the standards of pre-disbursement appraisal and post-disbursement supervision of credit, lending will be more organised and systematic.
- iv) It would be easier for the branch to effectively monitor the end-use of credit and assess its impact on increase in the levels of production, productivity and income levels of the beneficiaries.
- v) The branch manager would develop a sense of involvement and commitment in the success of these plans, as he alone is responsible for its conception and implementation.

Great hopes are placed on 'service area approach' as a means of bringing about an overall improvement in the quality of lending, planned and systematic lending in place of scattered lending, optimising the use of credit by establishing better linkages with production and productivity and proper recycling of bank credit.

3.47 The crucial element of the scheme is the preparation of the branch credit plan. This is required to be prepared on a systematic and realistic basis for productive activities identified in the service area after taking into account financial support and infrastructural facilities available. The next task is to implement the plan with a focus on physical realisation of results in terms of output, productivity, incomes, employment and not merely on disbursement of credit. This would naturally require close monitoring of the end-use of the funds. By all means, this is a very challenging task for the branch manager.

A Critical Appraisal of Service Area Concept

3.48 The scheme has just begun and any assessment of it must necessarily await its implementation. It is only to be expected that such a massive endeavour of allocating villages in the entire country would meet with several implementation problems. In states such as Uttar Pradesh, Madhya Pradesh and North Eastern States where the branch net work of commercial banks is poor, the average number of villages allocated to some of the branches has become quite large. The villages are also spread over a wide area. In view of the shortage of manpower in many of these branches, they may not be able to effectively service the entire area. In such cases, it may be neces-

sary to open additional branches so that the service area of the existing branches could be reduced to a manageable level. Under the scheme, villages have also been allocated to many weak branches of RRBs and private sector banks. These banks may not be able to meet the credit requirements of the borrowers of the area fully, particularly under programmes like IRDP. Such borrowers would also not be in a position to go to other branches outside the service area. In fact, the new approach reduces the option to the residents of the area from going to another bank branch.

3.49 Preparation of credit plans implicitly involves preparation of development plans. A credit plan pre-supposes the existence of a development plan so that the former can subserve the objectives of the latter. The formulation of development plans is, however, the responsibility of the Government authorities at different levels. The Government of India is thinking of strengthening the Panchayat Raj System and entrusting the responsibility of District /Block planning to District/Block/Mandal Panchayats. Under this concept, it is contemplated that rural development plans at different levels - the district, block and village clusters - will be formulated by the elected representatives of the people at each level with the assistance of a responsive district administrative machinery. In such a situation, unless there is complete collaboration and co-ordination between the two, there might arise a confusion of roles between bankers and Government functionaries. As a result, development plans would effectively become conditional to credit plans, rather than the other way round. Preparing credit plans in isolation and without proper co-ordination with the development plans could be counter-productive. It may be necessary, therefore, to specify in more detail their respective roles and collaborative arrangements for preparing the plans more specifically so as to avoid overlapping at the field level. What is more important is that bankers and development agencies prepare their respective plans jointly. We feel that such collaborative aspect of rural planning should be given added emphasis under the new approach. We hope that the Block Level Committees proposed under the 'service area approach' would act as an effective medium for such collaboration between bankers and development planners.

3.50 Another aspect which causes us concern is that service area scheme seeking to undertake credit planning for a village is primarily related to

branches of commercial bank. It only takes into account the lending programmes of PACS in the village. It does not, on the face of it, envisage the association of such of PACSs in the preparation of credit plans. Credit planning for a village, or for that matter any area, will be more meaningful only if all the credit agencies in the area effectively coalesce in the preparation of the credit plan and each agency has a given role to perform in its implementation. Specifically the close association of PACSs and other co-operative agencies such as the DCCB or its local branch, particularly where the PACSs are weak is of crucial importance, since the co-operative credit system is still the most appropriate rural credit system close to the people. The efforts of the commercial banks should be to supplement rather than supplant the co-operatives in rural lending.

3.51 Finally, we would like to reiterate that the above comments on the 'service area approach' are not in the nature of an assessment of it in advance of its implementation, but (a) by way of indication of some of the problem areas of implementation perceived by us which need to be taken note of and attended to and (b) by way of addition to it so that the service area emerges not only as a service area for commercial banks alone, but for co-operative institutions as well as commercial banks. Hence, we would prefer to call it a 'development area approach', (discussed in detail in Chapter X on Development Plans and Credit Planning) especially because it emerges out of the Development Plan and development linked credit plan-both of which currently hinge at the district level and are split into block plans but will, in future, as the 'service area approach' succeeds and yields the socio-economic profile of the village, emerge from the village plans. The intention behind the 'service area approach' and its proposed expanded version, inclusive of the co-operatives, that is the 'development area approach' is wholly sound inasmuch as it seeks to make the banker at the grass root level determine the needs and potential of the likely clientele in a systematic way and develop a credit plan for the branch on that basis, which in turn will become the basis of credit plans at the block and district levels.

Profitability of Commercial Banks

3.52 The profitability of commercial banks has been under strain for sometime mainly due to the following factors :

- i) rise in costs of deposits following increased customer preference for longer term deposits.
- ii) declining yield on the advances particularly due to concessional finance to the priority sectors.
- iii) reduction in total lendable resources as a result of increased cash reserve ratio and statutory liquidity ratio.
- iv) opening of large number of branches in rural areas which do not have adequate business potential.
- v) rise in establishment expenses.
- vi) increase in non-performing advances.

3.53 The average yield on advances, average yield on investments, average cost of deposits and average cost of borrowings of 28 public sector banks during the past four years are given in table 14

Table 14
Average Yield on Advances and Investments, Cost of Deposits and
Borrowings of Public Sector Banks

		(In percentage)			
		<u>1983</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>
a)	Average yield on advances	13.72	13.59	13.55	13.42
b)	Average yield on investments	6.77	7.21	7.95	8.76
c)	Average cost of deposits	6.93	7.12	7.36	7.51
d)	Average cost of borrowings	8.34	9.33	9.47	9.57

As can be seen from the table above, the yield on advances declined over the years from 13.72 per cent in 1983 to 13.42 per cent in 1986. The average cost of deposits and borrowings however increased during the same period, reducing the margins available to the banks.

3.54 There has, however, been some improvements in the absolute net profits of public sector banks in recent years as shown in table 15. This has been primarily due to higher coupon rates on Government bonds, injection of additional capital, increased interest rates on cash balances kept with RBI and on food credit. Moderation of branch expansion as well as staff

growth, revised service charges and better cash management have also contributed to their profitability.

Table 15

Net Profits of Public Sector Banks

	(Rs. crores)			
	<u>1984</u>	<u>1985</u>	<u>1986</u>	<u>1987</u>
Profits	82.5	117.8	192.5	261.7

Profitability of rural lending

3.55 Profitability of commercial banks is the net result of a series of operations in the rural and urban sectors. Because of unitary structure, their funds from different sources and regions get pooled and disaggregated as advances depending on the potentials in different sectors, regions as also mandates from higher authorities. In view of the complexity and range of operations involved in resources mobilisation and lending, it would be difficult to estimate precisely the impact of one sector i.e. rural lending on overall profitability.

3.56 The composition of liabilities and assets of commercial banks as a whole as worked out by Consultants II is indicated in table 16. The pattern of deposits of rural branches of commercial banks show a slightly different trend i.e. current deposits six per cent of the total deposits, savings deposits 46 per cent and fixed deposits 48 per cent. Since deposits constitute a major share in their total liabilities, the overall cost of funds for the rural branches of commercial banks was estimated at 7.3 per cent in 1986 when interest rates on deposits ranged between 5 to 11 per cent. Loans and advances constituted 60 percent of deposits raised by commercial banks in rural areas and the remaining 40 per cent are lent to the head office for investment in cash, securities and other purposes. Fifty nine percent of total advances of commercial banks are lent to large and medium industries, wholesale trade, food procurement and other large sectors. Of the balance (41 percent) 17 per cent goes to agriculture, (of this 75 per cent as direct advances and the balance 25 per cent as indirect advances), 15 per cent to small scale industries and 9 per cent to rest of the priority sector. The advances of rural branches of commercial banks account for 12 per cent of their

Table 16

Composition of Liabilities and Assets of Commercial Banks

		(Percentages) (Year ended December 1986)	
<u>Liabilities</u>		<u>Assets</u>	
1. Owned funds	1.3	1. Cash and bank balances	14.8
2. Deposits	86.0	2. Call money	2.7
of which		3. Investments	25.6
a) Current	20.5	4. Loans and Advances	51.5
b) Savings	24.0	Of which	
c) Fixed	55.5	a) Agriculture	17
3. Borrowings	6.7	b) Non-agriculture	83
4. Other Liabilities	6.0	5. Other assets	5.4
	100.00		100.00

total advances. Of this, about 50 per cent is for agricultural purposes and the rest for non-agricultural purposes. For the rural sector of commercial banks, it is estimated by Consultants (II) that the interest earned on funds deployed works out to an effective rate of 11.5 per cent (Lending rate to priority sector advances ranged between 8.0 and 16.5 per cent as on 31st December 1986) and the average cost to 7.3 per cent. The average loss per Rs.100 of rural business (deposits + advances) would be 38 paise as shown in table 17.

3.57 On this basis at rate of interest on deposits in the range of 3 and 11 per cent and loans and advances as interest rates ranging from 8.00 and 16.50 per cent, the losses of rural branches on their total business of Rs.20,260 crores as at December 1986 are estimated at Rs.78 crores. At 1988 level of business and at rates of interest on deposits in the range of 3 to 10 per cent and on advances at rates of interest in the range of 10 to 15.50 per cent with substantial chunk of loans at 10 per cent, these losses are estimated to go up further to Rs.103 crores. Downward revision in lending rates in March 1988 has further reduced the margin and increased the loss from 38 paise to 47 paise per Rs.100 of business, as shown in table 18.

Table 17

Average Cost of Funds - Business of Commercial Banks

Sr.No.	Indicator	Rural branches of commercial banks
(1)	(2)	(3)
1.	Ratio of business to working funds	1.60
2.	Volume of business per employee	Rs. 14.5 lakhs
3.	Payout per employee	Rs. 29,000
4.	Manpower expenses per Rs.100 of business	Rs. 2.00
5.	Manpower expenses per Rs.100 of working funds	Rs. 3.20
6.	Other expenses per Rs.100 of business	Re. 1.00
7.	Other expenses per Rs.100 of working funds	Rs. 1.60
8.	Manpower plus other expenses per Rs.100 of business	Rs. 3.00
9.	Manpower plus other expenses per Rs.100 of working fund	Rs. 4.80
10.	No. of deposit accounts per employee	464
11.	No. of borrowal accounts per employee	143
12.	Total number of accounts handled per employee	607
13.	Manpower expenses per account handled	Rs. 44
14.	Average rate in percentage of earnings from funds	11.5
15.	Average cost of funds (per cent)	7.3*
16.	Loss per Rs.100 of working funds (14-15) - (9)	60 paise
17.	Loss per Rs.100 of business (16 + 1)	38 paise

Table 18

Loss of Commercial Banks per Rs.100 of Rural Business-March 1988

i)	Gross Margin (per cent)	4.05
ii)	Ratio of business to working funds	1.60
iii)	Manpower and any other expenses for Rs.100 working funds	4.80
iv)	Loss per Rs.100 of working funds	0.75
v)	Loss per Rs.100 of Business	0.47

* The financial cost at 7.48 (Chapter XVIII) is the average of three years.

The projected losses at 1988 level of rural business on the basis of these calculations would go up further to Rs.128 crores. These projections have been made by the Consultants based on certain assumptions.* The actual losses of rural branches of commercial banks during 1986, 1987 and 1988 were Rs.65.41 crores (in respect of 7706 rural branches), Rs.52.59 crores (in respect of 6591 rural branches) and Rs.36.17 crores (provisional) (in respect of 3769 rural branches) respectively. The impact of downward revision in lending rates effected in March 88 and March 89 is yet to reflect fully in the working results of rural branches.

3.58 Some of the factors responsible for poor profitability of rural lending by commercial banks identified by our Consultants are :

- i) lower rate of return available on agricultural lending due to administered interest rate policy. The average return on rural lending would be about 11.5 per cent as of December 1986, as against about 14 per cent for non-rural lending.
- ii) the sample study done by consultants indicates that lending under IRDP alone is contributing to nearly about 40 per cent of the total losses of rural branches of commercial banks. Currently IRDP advances of rural branches of commercial banks form about 15 per cent of their rural lending which is expected to rise to about 20% in 1988. At this level of IRDP lending, the losses are estimated at around Rs.54 crores
- iii) relatively poor deposit mobilisation by rural branches; although 43 per cent of the branches of scheduled commercial banks are in rural areas, rural deposits form only 12.5 per cent of their total deposits. As deposits are available at an average cost of 7.3 per cent, larger deposit mobilisation would increase the profitability of commercial banks.
- iv) average productivity in rural branches as measured by average rural business (deposits + advances) handled per employee at Rs.14.5 lakhs is very low as compared with Rs.21 lakhs per employee for non-rural branches.

* For details of these assumptions and calculations see Chapter VII of the Consultants' (II) Report.

- v) many rural branches retain balances much in excess of cash retention limit resulting in loss of revenue, due to locked up funds.
- vi) at present non-interest income of rural branches forms a very insignificant proportion of total income.

3.59 One important aspect of profitability of the commercial banking system needs to be emphasised here. It is true that as far as rural business is concerned some of the commercial bank branches incur a net loss particularly in respect of their lendings to weaker sections which carry a lower rate of interest. As we have explained earlier, the precise quantification of such losses would be difficult and they would vary depending upon the basic assumptions made while calculating the losses. This is partly because of the complexity involved in identifying costs and returns of resources mobilisation and lending exclusively in the rural branches. Nevertheless, as of now, commercial banks are in a position to absorb the losses of their rural branch operations through earnings from their more profitable business. Although the capacity for such cross subsidisation varies from bank to bank (in fact Consultant II found marked variations in the structure, staffing and quality of rural lending among banks depending on their ability to cross-subsidise rural lendings), it is the availability of such a mechanism of cross subsidisation which has enabled them to keep their head above water and show net profit for the system as a whole. Although an increasing share of weaker section lendings which carry lower interest rates puts strain on their overall profitability, commercial banks, as a whole, do make profits. We have made recommendations elsewhere in this report to merge RRBs with the sponsor banks and have explained in detail our rationale for such a recommendation. The basic point is that if lendings to rural and weaker sections are to be at concessional rates, there has to be some cross-subsidisation. Only a system like commercial banks has, in the Indian context, the capacity for such a cross-subsidisation. This explains our emphasis on the continuance of commercial banks as an important channel for rural credit.

Commercial Banking in India - An Assessment

3.60 The major objective of bank nationalisation in 1969 was to involve the banking system more directly for promoting economic growth along with social justice. Prior to nationalisation, the commercial banks were more

or less confined to urban areas catering to traditional clientele of persons/companies etc. dealing with industry, commerce and trade. The major tasks of the banking system immediately after nationalisation were :

- i) to build-up a banking infrastructure in rural and semi-urban areas through an extended branch network.
- ii) to reorient the system for handling a wide range of small customers particularly in rural areas, and
- iii) to upgrade their lending techniques from security based lending to development oriented lending.

3.61 By and large these tasks have been accomplished in the decades after nationalisation. However, several functional/organisational deficiencies arose as a result of this rapid expansion and diversification. They were mainly:

- i) inability of the management to control the large number of geographically far flung branches,
- ii) inability of the traditional banking system and procedures to handle the increasing volume of business and varied activities leading to delays,
- iii) lack of adequately trained staff with right orientation and attitudes.

3.62 The commercial banks have endeavoured to deal with these deficiencies through increasing decentralisation and delegation, streamlining of procedures, building up training infrastructure facilities, etc. However, many of these deficiencies still persist in the banking system, although the degree and extent thereof vary from bank to bank and region to region. Some of the recent developments in the banking sector such as external pressures to write-off loans, growing sickness of units, higher expenditure on security, etc. have exacerbated the problem. The banks have also found it both time consuming and costly to enforce their legal rights against defaulting borrowers. It is reported that as at the end of December 1986 there were as many as 13.53 lakh court cases, involving an amount of Rs.3,489.63 crores. This has led to freezing of a sizeable portion of banks' resources for a long period of time. With a view to tackling some of these problems, it was decided in 1985 to embark on a phase of consolidation and up-gradation of the quality of the working of

the banking system. Several measures have been initiated recently to improve the operational efficiency and financial viability of the banks. With a view to further strengthening the credit monitoring system in commercial banks, the banks have been asked to introduce a comprehensive and uniform grading system which will indicate the quality of individual advances. Under this system known as 'Health Code System', the banks are to classify their advances into eight categories with a health code assigned to each borrowal account above a cut-off point. Such an assessment will help the bank managements to know about the health of their advances portfolio so that they can institute appropriate control measures. The current branch licencing policy (1985-90) lays special emphasis on consolidation while paying due attention to coverage of spatial gaps in rural areas and underbanked centres and restricts opening of offices in urban and metropolitan centres. In fact, as against 18,966 branches opened during 1980-85 the number of branches planned to be opened during 1985-90 is only 7,500.

3.63 There have also been efforts to strengthen the capital base of public sector banks. The Government of India contributed Rs.1000 crores to their paid-up capital during the last three years i.e. Rs.400 crores each during 1985-86 and 1986-87 and Rs.200 crores during 1987-88. Another Rs.800 crores are expected to be contributed during the remaining two years of Seventh Plan. As at the end of 1987, the paid up share capital and reserves of public sector banks aggregated Rs.2684 crores and constituted 2.09 per cent of deposits. The year-wise position of owned funds as a percentage to deposits and working funds is given in table 19.

Table 19

**Owned Funds of Banking System and
their Percentage to Deposits/Working funds**

Year	Total owned funds	Total deposits	Total working funds	(Rs. crores)	
				Percentage of owned funds to Deposits	Working Funds
1984	795	79297	96611	1.00	0.87
1985	1447	94301	109342	1.53	1.32
1986	2084	111581	127423	1.87	1.63
1987	2684	128389	151270	2.09	1.77

3.64 Although the percentage of owned funds to assets (working funds) increased from 0.87 in 1984 to 1.77 in 1987, this is still low when compared with banks in developed countries. The ratio of capital to weighted risk assets, recommended by the Cooke Committee of the Bank of International Settlements, is 8 per cent, of which the core capital element should be at least 4 per cent, to be achieved by the year 1992. We feel that in view of the increase in risk bearing advances of commercial banks, there is need to gradually increase the owned funds at least to a level of two per cent of their assets by the year 1990, three per cent by 1995 and further to around four per cent by 2000.

3.65 In addition to these measures, banks were advised to draw and implement specific action plans with a view to improving the quality of their operations. At the instance of RBI, all the commercial banks had drawn up two year plans in 1985 identifying their deficiencies with corrective measures for improving their performance. The RBI Governor himself reviews these plans and performance periodically. In particular, specific steps have been initiated in the area of bank personnel to improve the productivity and profitability of banks. All the public sector banks were advised in January 1987 to undertake an in-depth assessment of their staff requirements and limit the staff expansion to 1-1.5 per cent per annum during the remaining period of the Seventh Plan. In view of these measures, staff increase has come down from 6.7 per cent per annum during the years 1983-85 to 3 per cent in 1986 and further to 1.5 per cent in 1987. Banks are also rationalising the staff pattern of their branches to identify surplus pockets and re-deploy the surplus staff at deficit centres. Banks face many problems in transferring persons from urban and metropolitan centres to other branches in need of staff. Such rigidities which have developed in the system over a period of time adversely affect the working of banks. These controls over staff recruitment have contributed to the increase in the volume of business per employee from Rs.16.32 lakhs in December 1985 to Rs.18.65 lakhs in December 1986 and further to Rs.20.96 lakhs in December 1987. The increase in establishment expenditure over the previous year has also come down from 18.7 per cent in 1985 to 11.7 per cent in 1986 and further to 10.6 per cent in 1987.

3.66 Initially commercial banks were reluctant to enter the field of rural finance and preferred to play only a supplementary role to co-operatives.

Over the years the position has changed and they have forged ahead of co-operatives and today they play a more dominant role as shown in table 20.

Table 20

Direct Institutional Finance for Agriculture

<u>Agency</u>	<u>(Year ended June)</u> <u>(Rs. crores)</u>				
	<u>1981</u>	<u>1984</u>	<u>1985</u>	<u>1986</u>	<u>1987 *</u>
Co-operatives	4613 (58.1)	5735 (45.8)	6367 (46.6)	6947 (42.8)	7478 (41.8)
Commercial Banks	3043 38.3	5280 50.1	6613 48.4	8416 51.8	9355 52.3
Regional Rural Banks	286 (3.6)	509 (4.1)	693 (5.0)	871 (5.4)	1062 (5.9)
Total	7942	11524	13673	16234	17895

(Figures in brackets indicate percentage to total finance provided). *Provisional

3.67 By and large the various obligations imposed on banks in the matter of priority sector lending, agricultural advances, advances to weaker sections and credit-deposit ratio have been responsible for the significant rise in their rural lending. But for the introduction of those norms at that stage, commercial banks would not have involved themselves substantially in rural lending. Now that the banking system as a whole and most of the banks individually have achieved the overall targets and sub-targets in quantity, if not in quality, a review of these norms, is called for with more emphasis on quality than on quantity.

3.68 An important development in the field of rural lending by commercial banks has been the adoption of schematic lending, as against the normal pattern of lending based on the assessment of individual borrowers. The agricultural credit schemes of commercial banks were reviewed by an Expert Group in April 1978. The Group pointed out various shortcomings in the modalities of scheme formulation by commercial banks. Perfunctory assessment of infrastructural facilities, unrealistic assumptions relating to economic viability of the schemes, lack of proper assessment of scope of lending etc. were some of the deficiencies noticed. In view of these short-comings the Expert Group had come to the conclusion that despite the so called area approach, many credit schemes were stereotyped in content without reflecting

the area specific realities. Although there has been some improvement in the quality of scheme preparation over the years, most of these defects still persist particularly under the schemes prepared in respect of poverty alleviation programmes.

3.69 The quality of lending is also found to vary from bank to bank and area to area. Of late, the large number of proposals under Government sponsored schemes have significantly changed the complexion of rural lending and diluted the quality of loan appraisal. Under these target-oriented programmes, a large number of applications are sponsored within a short span of time exerting considerable pressure on banks. In the process, neither the Government agencies nor the banks are in a position to observe the norms which can ensure quality lending. Loaning without ensuring proper linkages have resulted in the schemes becoming, by and large, non-viable. Such borrowers gain an impression that banks are mere cash disbursing agencies. Once the process of identification of beneficiaries is completed by the sponsoring agencies, any attempt by the banks in subjecting the applications to further scrutiny, particularly with regard to their bankability, is not only resented but also resisted; quite often such resistance results in friction. In order to improve the quality of scheme preparation, commercial banks should have a team of specialised officers at the Head Office and other controlling offices, exclusively for the work of preparation of schemes for the areas where the bank has significant rural presence. This specialised staff serving a group of branches should be posted at controlling offices to supplement those at the branches, so that together they can meet the needs of technical assistance of the area.

3.70 The deterioration in the quality of lending was also due to the heavy work load of day-to-day house-keeping at the branches without commensurate increase in supporting clerical and other staff. Of late, the number of returns which are essentially statistical in nature has increased. The branch manager has to deploy staff for book-keeping, balancing, preparation of returns, etc. Most of the staff get tied up to this work and have limited spare time to visit villages and look after the business of rural lending. Some of the banks have one-man branches where there is only the branch manager assisted by one clerk-cum-cashier and one member of sub-ordinate staff. In such branches, the branch managers get tied down to the desk work thus limiting their ability

to handle rural lending. The commercial banks should discontinue such one-man branches as close supervision and follow-up of large number of small borrowers would not be possible through such branches or upgrade them. They also need to strengthen their post-investment monitoring of the schemes. Their evaluation should be periodically extended to the economic impact of such schemes also. If necessary, professional firms or personnel may be commissioned for such impact studies.

3.71 The cumulative effect of the phenomenal expansion of branch network in the rural areas, paucity of trained officers combined with reduced profitability in rural lending at concessional rates of interest has been the neglect of staffing in the rural branches. Posts are being sanctioned but some of them remain vacant for long duration. Vacancies are sometimes filled up by internal promotions at the branch level without proper regard to the adequacy of experience and skills of the persons. In view of this increased pressure on staff, the technical officers are being asked to do more and more desk work relating to agricultural accounts. This prevents them from spending more time on field visits. One gets an impression that in staff matters, the branch manager is left alone to fend for himself.

3.72 During their case studies the Consultants found that almost all branches irrespective of the bank to which they belonged depended mostly on walk-in business or sponsored loan applications. Branch Managers completed the targets allotted to them largely through these walk-in and sponsored applications. Any short-fall in targets was made good through canvassing business, particularly for equipment finance i.e. machinery/tractor finance in the case of agriculture and transport/truck finance in the case of small business. There was no evidence to show that the branch managers studied the area of their operation in terms of credit needs of the people and the opportunities available for provision of credit. Branch budgeting has become by and large a routine exercise.

3.73 The banks were found to be adopting the standard unit costs prescribed by NABARD and other agencies. Such standardisation has however, led to over dependence on stipulated norms without any flexibility in individual cases. Very few branch managers assessed the credit needs of the borrowers with the help of technical officers.

3.74 By and large term loans sanctioned by commercial banks were not supported by production finance. The case studies conducted by the Consultants revealed that in many cases, particularly in minor irrigation and farm mechanisation, the term loans from commercial banks were not supported by production credit. There were also cases where working capital loans were sanctioned with unduly long delays. There was also a common complaint that the period of medium-term loans granted by commercial banks was generally inadequate. The branch managers often adopted a conservative attitude and fixed shorter repayment schedules than what was warranted by the flow of incremental income from the project and repayment capacity of the borrowers. While working out repayment schedules for medium and long-term loans, commercial banks should take into account the life of the asset, incremental income generated and the consequent repaying capacity of the borrower. The period of repayment fixed should in no case be shorter than what is warranted by these considerations.

3.75 The banks have introduced the simplified forms for term loans as well as for IRDP loans. By and large, loan documents were also taken according to the uniform system introduced by the RBI in this behalf. The banks have also introduced loan pass books for IRDP borrowers. However, there is scope for further simplification of systems and procedures in rural lending. Some of the areas which require simplification are the format of the loan applications, mortgage/legal documents, reporting systems, etc. The accounting system and maintenance of books at the branches also need to be simplified. In order to prevent double financing and bringing about co-ordination in lending, pass books should be issued to each cultivator by the Government. A pass book can serve as record of land holdings as well as borrowings from banks. We suggest that the concerned Government agency should furnish in the pass book basic information regarding the farmer such as his name, house number, land owned, land rented in and/or out, type and value of other assets owned, family size etc. The lending agency could thus fill up in the same pass book the information about his loans and deposits. One copy each of the consolidated pass book could be kept with Government, bank and the farmer.

3.76 The major problem in respect of IRDP loans was that the loan applications were being sponsored from different villages without taking into consideration the market potential or infrastructure facilities available. The BDO

decided the activity for the beneficiary instead of the beneficiary himself and this had resulted in a mismatch between skills and the activity pursued. There was over-crowding in some activities and inadequate income generation. Adequate attention was also not paid to availability of suitable assets and consequently the size of the unit sanctioned was lower than that according to the prescribed norms. All these factors affected the income generation under IRDP and consequently recovery. Many branch managers had felt that the sponsoring authorities should also assume responsibilities for recovery and targets for recovery should be given to them.

3.77 In many cases the lead bank forums were found to be ineffective in sorting out the problems of the banks in regard to provision of infrastructural facilities by government agencies. Government authorities did not adhere to their commitments for various reasons. The commercial banks are at times called upon to open branches at centres which do not have basic infrastructural facilities like all weather roads, police presence etc. Banks cannot be expected to operate effectively when such essential infrastructure facilities are lacking. It is, therefore, imperative that the states provide such facilities before commercial banks are asked to open branches in those places.

3.78 It was found that the rural branch manager was being given detailed instructions on every aspect of rural lending to an extent that he was placed in a strait-jacket. There was hardly any discretion left to him and he was being reduced to the position of having to do his work in a mechanical way. The branch manager had instructions relating to the rate of interest, cost of assets, security, margin etc. and had little freedom or discretion, to use his own initiative or exercise his judgement. Even minor deviations from these instructions brought on him the displeasure of controlling offices and other higher authorities. There is need to re-examine and streamline these instructions and give sufficient discretion to the branch managers. Credit decisions will have to be taken by the managers within the overall framework of guidelines, and they should be made accountable for their decisions.

3.79 There has been a substantial increase in the routine work of the branches due to large increase in the number of loan accounts. There has also been substantial increase in the number of returns to be submitted by a branch. According to the report of the Working Group on Accounting Proce-

dures and Maintenance of Records at Bank Branches submitted in 1982, over 100 returns of different periodicity are to be submitted by a branch. Taking into account the periodicity, a branch has to compile on an average 1,300 returns in a year. In some cases it is as high as 2,600. This enormous increase in routine house-keeping work and submission of returns has considerably reduced the time available for personal contacts with the borrowers. This points to the need for a reduction in the number of returns, simplification of procedures and increasing mechanisation where feasible. Mechanisation can also help improved collection, recording and usage of data, and hence data could be used more effectively for policy decisions.

3.80 A majority of the commercial bank branches in the rural areas is making losses in spite of the fact that quite a few of them also handle non-agricultural business. Administered interest rate structure, inadequate volume of business, high cost of handling a large number of small accounts, non-availability of high interest earning business etc. have contributed to this situation. One predominant factor which affects the profitability of rural branches is the volume of business i.e. deposits and advances. It is necessary that rural branches improve the volume of business handled per employee. According to our Consultants the present ratio of business per employee is Rs.14.5 lakhs in rural branches of commercial banks, as against Rs.21.0 lakhs per employee for non-rural branches. According to their calculations, even if this ratio goes up by Rs.1 lakh per rural branch employee, it is expected to bring down the losses by about 20 paise per Rs.100 of business i.e. about Rs.41 crores on rural business of Rs.20,260 crores as at the end of December 1986. Thus it is imperative that commercial banks should aim at improving the level of efficiency of staff serving in the rural areas measured in terms of the volume of business handled per employee. This indicator should be watched carefully and monitored branchwise by the management.

CONCLUSION

3.81 We would in sum say that the commercial banks could achieve substantial quantitative expansion of rural credit, despite several external and internal constraints. The fixation of targets for priority sector lending particularly the ambitious targets fixed under the anti-poverty programmes which carry lower lending rates, have, however, imposed strains on the system, as commercial banks today account for nearly 70 per cent of lending under

IRDP. The banks have to function under a system of administered interest rates, conceding to them unremunerative returns and resulting in low profits insufficient to build up their reserves. The average productivity per employee has been low in their rural branches. There are surplus pockets mostly in urban areas and deficit in other areas calling for a rationalisation of the staff deployment pattern. Staff cost, accounts for a substantial portion of the banks' total establishment cost and successive wage revisions of the employees further add to this cost. These apart, another disturbing factor which is eroding the profitability of the commercial banking system is the rise of non-performing advances both in the rural and urban sectors. An amount of Rs.4,222 crores was involved in sick units at the end of June 1987. The position has not been much better regarding agricultural advances inasmuch as their overdues under agricultural advances at Rs.1,744 crores as on December 1986 formed 43 per cent of the demand. The overdues above 3 years at Rs.934 crores formed 53.5 per cent of their total agricultural overdues. The banks have found enforcement of their legal rights against defaulting borrowers both time consuming and costly. In view of legal requirements and even otherwise, banks do not disclose either the bad debt position or the amounts actually written off. Though in the case of small advances under some categories, some estimates are possible on the basis of claims preferred by banks on DICGC, these do not give any indication of bad debts in respect of larger advances. However, our impression has been (particularly from the large number of claims submitted to DICGC) that such bad debts are on the increase and would have an adverse impact on the viability of the structure in the coming years. We have also observed progressive deterioration in the autonomy of these institutions particularly under anti-poverty programmes. The commercial banks have been subject to several external pressures in the form of loan melas etc. Certainly one would not disagree with the need for setting overall targets for these banks in conformity with national objectives and priorities and the bank's capacity to bear the load. But if directions are given on the day-to-day functioning of these banks as to the areas and people to whom loans should be given, these would affect the overall efficiency of the system, resulting in bad loans.

3.82 The multi-agency system, although it was able to enlarge the flow of credit quantitatively to the rural areas, has not acquired the desired quality. This approach was intended to provide an alternative source of credit to

borrowers and bridge the credit gaps especially because the co-operatives by themselves were unable to meet all the credit requirements. In actual practice, however, the system has in some cases led to proliferation of branches of different commercial banks in already well-banked areas to the relative neglect of other needy areas. Too many targets, mandates, instructions, etc. have detracted from the efficiency of the system and made coordination, monitoring and management difficult with consequent decline in the recovery performance. Professionalism in banking has been the biggest casualty as most of the credit decisions are made in a mechanical way. Too much emphasis on standardisation has impaired the credit judgement capacity of branch managers. There has also been a general deterioration in the quality of staff of the rural branches. As we have already mentioned, finding personnel to man their rural branches has been one of the intricate problems faced by commercial banks. Welfare orientation seems to have substituted commercial judgement and branch managers have almost become subservient to Government Departments, lest they may be branded as anti-poor. The client-bank relationship has undergone a substantial change due to mass loaning particularly under the anti-poverty programmes. Sadly, people have started perceiving loans as any other public service to be availed of, irrespective of whether they have the capacity to utilise it properly or not. This culture of casualness in the handling of loan approvals is gradually spreading to their other lendings. This is a trend which as we see is dangerous and needs to be arrested.

3.83 If the commercial banks have to emerge as a strong system to be able to purvey credit effectively and efficiently in rural areas in the years to come, we feel that all the foregoing issues will have to be tackled boldly and with a sense of urgency. First and foremost, there is the need to make the system cost effective by improving staff productivity through rationalisation of staff deployment and proper man-power development. Secondly, the commercial banks should take concerted measures to recover their advances both in the agricultural sector and non-agricultural sector, which will ensure the necessary recycling of funds. We have elsewhere made several recommendations to improve the recovery of advances to the rural sector. We have also made recommendations to strengthen the credit guarantee scheme. Thirdly, we feel that the public sector banks should be accorded greater autonomy in their functioning. The emphasis should be on

making them accountable for results, rather than imposing on them too many guidelines and stipulations which might result in hindering their smooth functioning. Fourthly, there has to be a programme for the rehabilitation of the banks' branches many of which are weak specially in rural areas and need to be strengthened; this we have dealt with in another chapter. Fifthly, commercial banks should be allowed to have a higher margin for which we have made recommendations in yet another chapter in the Report. In this context, we welcome RBI's recent relaxations relating to lending rates for non-priority sectors wherein only a minimum rate of 16 per cent has been fixed, giving the banks freedom to charge higher rates according to the credit record of customers. Better returns on business and adequate margins will enable the banks to appoint the necessary specialised and technical staff for appraisal of loans and adequate field staff to ensure monitoring of loans and recovery thereof. This will also augment their profitability and strengthen their reserves. Sixthly, the equity base of the commercial banks has to be substantially fortified to enable them to enlarge their operations with a degree of safety and security. Seventhly, the targets fixed for financing the weaker sections and the rural poor should be reasonable such as the system can bear, particularly in the context of the large demand for credit estimated by us over the next decade or so, which can be successfully achieved only by a strong credit system capable not only of disbursing loans but also of monitoring and recovering them. Finally a good banking system must be in a position to protect the interests of its depositors at all times and extend guarantee cover for the deposits placed with it. The Deposit Insurance Fund with the DICGC, accumulated over a number of years, has recently been siphoned off almost entirely to meet the increasing claims of the client banks on their loans and advances. We have, therefore, recommended in Chapter XVII that this fund be kept in tact as far as possible to meet the claims of the depositors and built up adequately once again.

3.84 The commercial banks had, over a period of time, built up a magnificent edifice which of late has shown signs of developing cracks. The situation is no doubt grave but the position is certainly not beyond remedy. We would, therefore, sound a note of caution so that urgent action is taken to put the house in order and the system can meet the challenges facing it in the stupendous task of financing the rural sector.

CHAPTER IV

REGIONAL RURAL BANKS

Genesis

Initially under the social control policy introduced in 1967 and subsequently with the nationalisation of fourteen major commercial banks in 1969, a special obligation was laid on the banks to step up their advances for agriculture and allied activities. There was a specific reservation of a prescribed percentage of loans outstanding for this purpose. However, a widely shared impression in many quarters was that even after a lapse of five years of nationalisation, these banks could not reach the rural population, especially the weaker sections in sufficient measure. It was thought that this was because the manner of functioning of these banks was not conducive to lending to weaker sections. The Government of India (GOI), therefore, appointed a Working Group by notification dated July 1, 1975 with Shri M. Narasimham, the then Additional Secretary, Department of Economic Affairs as Chairman, to examine in depth the setting up of new rural banks as subsidiaries of public sector banks to cater to the needs of the rural people. The notification stated that unless such new institutions were started on the basis of attitudinal and operational ethos entirely different from that obtaining in the public sector commercial banks, the mode of functioning of the public sector banking system would not only not change, but on the other hand, would be perpetuated. The idea in setting up the new institutions as set out in the Government resolution was two fold :

- (i) to provide employment to the rural educated youth who were properly oriented to look after the needs of the rural folk, unlike the urban oriented personnel of the public sector banks; and
- (ii) to bring down the costs of rural banks by recruiting staff for these banks on the same scale of pay and allowances as for employees of state government/local bodies.

4.02 The Working Group proceeded with their enquiry reckoning the multi-agency approach as a solution to problems of institutional credit in the rural sector. Consequent to the entry of commercial banks, more particularly after

nationalisation of the 14 major banks, considerable progress was made in providing credit for agriculture. During the period which followed, direct lendings to agriculture by commercial banks rose from Rs.54 crores in June 1969 to Rs.540 crores in December 1974 and rural branches to 6697 in March 1975 as against only 1833 in June 1969. Despite such massive step up by commercial banks both in the provision of credit and its wider reach to rural areas, the bulk of it tended to benefit the bigger farmers to the neglect, besides the rural artisans and agricultural labourers, of farmers whose holdings were either too small or belonged to the lower bracket of the middle sized farmers. In other words, the benefit of increased credit flow from the commercial banks almost bypassed the relatively weaker sections of the community.

..03 It was to meet the needs of these sections of the community the Working Group felt, that attention was required to be paid in extending institutional credit in rural areas. They also felt that neither the co-operatives which were weak and trailing behind, nor the commercial banks though strong, were institutionally equipped to purvey credit to these sections. Nor was the task of a nature or dimension that a restructuring of either of the two or both the systems could have tackled. The answer, it was thought, lay in a fusion of such of the characteristics of the two systems as were conducive to facilitating smooth and effective flow of credit to the new areas and clientele, to make for a new institutional device. In the context of the areas and the clientele these institutions were expected to serve, it was necessary for these institutions to be fully familiar with the local problems, operate on a low cost basis unlike the commercial banks but observe normative business efficiency as in commercial banks, if accessibility of the new class of borrowers to these institutions and smooth flow of credit to them were to be ensured.

4.04 The Working Group which submitted its report on 30th July 1975 recommended the setting up of 'Regional Rural Banks' (RRBs) as full-fledged scheduled banks. These banks it was expected, would while combining the local feel and familiarity with rural problems which the co-operatives possessed and the degree of business organisation, ability to mobilise deposits, access to central money markets and modernised outlook which the commercial banks had, also maintain a low cost profile. These banks were to be sponsored by commercial banks with equity participation by the GOI, the sponsor bank (SB) and the state government.

Following this, the Government promulgated the RRBs Ordinance on 26th September 1975 (subsequently replaced by the Regional Rural Banks Act, 1976) and the first five RRBs were established on the 2nd of October 1975.

Organisational Structure

4.05 The issued and paid up share capital of RRBs at Rs.25 lakhs was to be held by GOI, the SB and the concerned state government in the proportion of 50 per cent, 35 per cent and 15 per cent respectively. The SB was required to provide managerial and financial assistance to the RRBs, sponsored by it for the first five years and thereafter on the basis of mutually agreed terms.

4.06 The management of the RRB was to vest in a Board of Directors headed by the Chairman who was usually an Officer of the sponsor bank but appointed by the Government of India. In addition, the Central Government nominated three directors (of whom one was from the RBI). The concerned state government had two Directors, while the sponsor bank nominated the balance of three directors. In some cases non-officials were nominated as Government or sponsor bank directors. In terms of a later amendment to the RRB Act, following the recommendations of the Kelkar Working Group (1986), the composition of Board in addition to a Chairman is to be as under :-

Government of India	- 2 non-officials
Reserve Bank of India	- 1 official
NABARD	- 1 official
Sponsor bank	- 2 officials
State Government	- 2 officials

4.07 An RRB was normally expected to recruit its own staff, but in the initial years, the SB provided the necessary staff particularly at the senior levels. In consonance with the principle of low cost profile, the remuneration of the staff (other than those on deputation) recruited for an RRB was to be so fixed as to correspond to the salary structure obtaining in the concerned state government for comparable cadres at the district level.

4.08 The RRBs were required to confine their lendings mainly to the weaker sections of the rural community. This 'target group' comprises basically the small and marginal farmers, agricultural labourers, artisans, small entrepreneurs

and persons of small means in trade, commerce or industry or other productive activities within the area of operations of the bank. Financing the clientele outside the target group by the RRBs was to be exceptional.

4.09 To enable the RRBs to keep their costs low, they were extended several concessions relating to maintenance of Statutory Liquidity Ratio, refinance facilities from NABARD and SBs etc. RRBs were allowed to maintain a lower level of Cash Reserve Ratio (CRR) and Statutory Liquidity Ratio (SLR) i.e. CRR of three per cent and SLR of 25 per cent of their demand and time liabilities. With a view to helping them mobilise deposits, they were also allowed to pay 1/2 per cent more interest on deposits. They were eligible to avail themselves of refinance from NABARD to the extent of 90 per cent of their schematic lending and 50 per cent of non-schematic lending at 6-1/2 per cent and 7 per cent respectively. The sponsor bank provided refinance upto 30 to 35 per cent of non-schematic lending of RRB at 8-1/2 per cent. These concessions were reviewed by the Kelkar Committee in 1986. To further improve the financial position of RRBs they recommended that the paid-up capital of each RRB be raised from Rs.25 lakhs to Rs.100 lakhs. They also recommended that the SLR requirements of RRBs should be invested in Government securities yielding higher returns with the help of the sponsoring banks. The Sponsor Bank was to provide refinance upto 20 per cent of non-schematic lending of RRBs at 7 per cent p.a. Further while the quantum of the refinance in respect of non-schematic lending to be provided by sponsoring banks was reduced from 30-35 per cent to 20 per cent, the interest rate on such refinance was brought down from 8.5 per cent to 7 per cent.

Progress of RRBs

4.10 The Working Group on Rural Banks (1975) had recommended the setting up, in the first instance, of only five RRBs to serve as pilot institutions in their respective areas. It had in particular pointed to the need for careful planning in organizing these banks and had further suggested that future expansion may be considered depending upon the performance of the pilot institutions and the experience gained on the basis of their working. Despite this, even during the very first year itself 34 new RRBs were established. In fact, the Working Group set up in 1977 under the Chairmanship of Professor M.L. Dantwala to review the working of RRBs observed that the expansion of the RRB system

was unnecessarily hurried. By the end of 1986 there were 194 RRBs as shown in table 1. Seven states i.e. Uttar Pradesh with 39, Andhra Pradesh with 15, Madhya Pradesh with 24, Bihar with 22, Rajasthan with 14, Karnataka with 13 and Maharashtra with 10 accounted for much as 137 out of the 194 RRBs. At the end of 1986, 351 out of 436 districts in India were covered by RRBs. Again out of 115 tribal districts, 94 were covered by RRBs.

Branch Expansion

4.11 The branch expansion of RRBs has been even more phenomenal. As at the end of 1986, 194 RRBs had opened 12,838 branches. The yearwise data regarding the opening of branches are shown in table 2 .

Table 1

Progress in setting up of RRBs

<u>Year</u>	<u>No. of RRBs</u>	<u>District covered</u>	<u>Year</u>	<u>No. of RRBs</u>	<u>District covered</u>
✓1975	6	12	1981	107	182
1976	40	84	1982	124	214
1977	48	99	1983	150	265
1978	51	102	1984	173	307
1979	60	111	1985	188	333
1980	85	144	✓1986	194	351

Table 2

Number of branches opened by RRBs

<u>Year</u>	<u>Opened during the year</u>	<u>At the end of the year</u>	<u>Average No. of branches per RRB</u>
✓1975	17	17	2
1976	472	489	12
1977	698	1187	25
1978	566	1753	34
1979	667	2420	40
1980	859	3279	39
1981	1516	4795	45
1982	1396	6191	50

<u>Year</u>	<u>Opened during the year</u>	<u>At the end of the year</u>	<u>Average No. of branches per RRB</u>
1983	1604	7795	52
1984	2450	10245	59
1985	2361	12606	67
1986	232	12838	66

As many as 6,415 branches or about half of the total, were thus established during the 3 years 1983-85. At the end of December 1986, out of 30,177 branches of commercial banks at the rural centres, 42.5 per cent were those of RRBs.

Deposit Mobilisation

4.12 By December 1986, RRBs had mobilised Rs.1,715 crores as deposits. The average deposits per RRB and per branch were Rs.8.8 crores and Rs.13.4 lakhs respectively. The average amount of deposit per account was Rs.871 only. The progress of RRBs in deposit mobilisation over the years is shown in table 3.

Table 3
Deposits mobilised by RRBs

<u>Year</u>	<u>Number of Accounts</u>			<u>Amount (Rs.)</u>		
	<u>Total (lakhs)</u>	<u>Per RRB (000)</u>	<u>Per Branch (No.)</u>	<u>Total (crores)</u>	<u>Per RRB (crores)</u>	<u>Per Branch (lakhs)</u>
1976	1.89	4.7	386	7.58	0.18	1.5
1980	37.01	43.5	1129	199.83	2.35	6.1
1986	196.93	101.5	1534	1,714.94	8.84	13.4

Lending Operations

4.13 The total loans advanced by 194 RRBs stood at Rs.1,785 crores as at the end of December 1986. The average loans per RRB and per branch were Rs.920 lakhs and Rs.13.9 lakhs respectively. The average number of borrowal accounts per RRB and per branch stood at 41,898 and 633 respectively. The average loan amount per borrowal account worked out to Rs.2,195. Of the 194 RRBs, 7 had loans outstanding of over Rs.40 crores. The average Credit Deposit (CD) ratio of all RRBs worked out to 104. However, in the case of 30 out of 194 RRBs the CD ratio was less than 50, while in the case of 6 RRBs the ratio was above 200. The purpose-wise distribution of outstanding loans of RRBs as at the end of

December 1986 is given in table 4. Retail trade and small business accounted for 26.7 per cent of total outstanding loans, followed by agricultural term loans accounting for 21 per cent. The loans issued under the special programmes like IRDP, DRI and others at Rs.307 crores constituted 46 per cent of the total loans issued during the year 1986.

Table 4

Purposewise distribution of outstanding loans of RRBs - December 1986

Purpose of loan	Amount out-standing (Rs.Crores)	Percentage to the total out-standing loan	Average amount out-standing per account Rs.	Percentage to the total no. of accounts
S.T. (Crop) loans	331.9	18.6	1,843	22.1
Agr. term loans	375.6	21.0	2,912	15.8
Allied activity term loan	296.6	16.7	2,150	17.0
Rural Artisans etc.	108.0	6.0	1,645	8.1
Retail trade etc.	476.0	26.7	2,115	27.7
Consumption loans	15.9	0.9	1,260	1.6
Other purpose loans	143.2	8.0	2,461	7.2
Indirect advances	37.6	2.1	9,255	0.5
Total	1,784.8	100.0	2,195	100.0

An Overview of Progress

4.14 Between 1975 and 1986, the RRBs increased from 6 to 194, their branches from 17 to 12,838 and districts covered from 12 to 351. The average number of branches per RRB similarly increased from 2 in 1975 to 66 in 1986. During the same period, deposits increased from Rs.0.20 crore to Rs.1,714.94 crores and deposits per branch from Rs.1.18 lakhs to Rs.13.4 lakhs. Regarding lending operations, the total loans outstanding rose from Rs.0.10 crore at the end of 1975 to Rs.1,784.8 crores at the end of 1986.

A Review of the Performance of Regional Rural Banks

4.15 The performance of RRBs during the last 12 years in terms of expansion in numbers of banks and their branches, and in many cases their loan operations

as well as deposits collection, has been per se impressive. Admittedly, the RRBs have achieved considerable degree of success in taking the banking services to the very remote areas which had hitherto remained unbanked, and made available institutional credit to the weaker sections in these areas. Their achievement in coverage of the tribal blocks has also been equally significant. Further, in making available credit to the far-flung rural areas, they have facilitated the flow of credit from the central money market to these areas through re-finance from National Bank for Agriculture and Rural Development (NABARD). Nevertheless, a closer look at their performance would be needed for a proper evaluation of their impact on the rural credit structure and to adjudge their success or otherwise in fulfilling the objectives with which they were set up. The indicators of performance in the event would obviously be different from the mere increase in the number of branches or even quantum of loans issued and deposits mobilized.

4.16 The objectives and policy indicators regarding RRBs have been dealt with by the first Working Group (1975). The two Working Groups, since set up, one by the Reserve Bank of India under the Chairmanship of Professor M.L. Dantwala in 1977 and the other set up by GOI under the Chairmanship of Shri S.M. Kelkar, the then Additional Secretary, Banking, in 1984, reviewed the position of the working of these RRBs. The CRAFTICARD (1981) also had occasion to look at some aspects of RRBs' performance. Both the reviews on RRBs had brought out the various deficiencies in the working of the RRBs and in particular their inability to operate on a viable basis. The Kelkar Working Group which was the last of the reviews undertaken, had come to the conclusion that non-viability was built into the very concept of RRBs. Despite this inherent weakness, both the Groups as well as the CRAFTICARD were of the view that RRBs should continue as an integral part of the rural credit system. However, the Dantwala Working Group and CRAFTICARD had made a package of recommendations so as to improve their viability but this involved major restructuring of the RRBs. Also in some of the functional areas, restructuring meant negation of the very basic assumptions which provided the rationale for setting up of the RRBs. Many of the recommendations implied virtually, the conversion of the RRBs, de facto, into fullfledged commercial banks, albeit with limited area of operation and in the process eliminating both competition and complementarity. In all cases, the commercial bank branches were to hand over all their rural business to

the RRBs. For instance, the Dantwala Working Group recommended extension of loans to the non-target groups as well as the handing over of all rural business of the commercial banks to the RRBs. A transfer of business on a selective basis was recommended by the CRAFTICARD also. The Kelkar Working Group, on the other hand, recommended the continuance of RRBs on the lines as originally envisaged. They re-emphasised the need to maintain the image of the RRB as a 'poor man's bank'. The Working Group also recommended, besides increased doses of share capital by Government, a variety of other concessions and subsidies, including the three partners sharing the losses in such a manner that there was a long term underwriting, in fact, of all losses of RRBs because they believed that even with such subsidies and concessions, in addition to periodical additional equity provided for in their recommendation, the RRBs could not be brought to a viable status on a durable basis.

Critical Areas

i) **Profitability :**

4.17 Disquieting feature in the functioning of RRBs has been their unsatisfactory working results, giving rise to mounting losses over the years. During the year 1986, out of 194 RRBs only 46 earned profits, while as many as 148 had incurred losses for the year 1986. The accumulated losses of all the RRBs put together by the end of 1986 amounted to Rs.94.31 crores. The accumulated losses in the case of 117 RRBs as on 31st December 1986 had wiped out their entire share capital. In the case of some, the losses had eroded even a part of their deposits. A number of RRBs was not able to comply with the statutory requirements in respect of liquidity and cash reserves. The year-wise profit and loss position as also the accumulated losses of the RRBs are given in table 5 .

4.18 As already pointed out, the Kelkar Committee made several recommendations to improve the profitability of RRBs. However, even with these concessions, the number of RRBs incurring losses further increased from 148 in 1986 to 151 in 1987 and accumulated losses from Rs.94.31 crores to Rs.133.10 crores. The factors which contribute to the erosion of the profitability of RRBs are many. In our view, these are endemic to the system structured as it

Table 5

Profit and loss position of RRBs

Year	Total No. of RRBs	Profit		Loss	
		No. of RRBs	Amount	No. of RRBs	Amount
1976	40	26	10.92	14	2.55
1977	48	27	33.42	21	36.88
1978	51	22	63.88	29	54.45
1979	60	36*	147.53	22	61.97
1980	85	56	217.80	29	103.59
1981	107	62**	311.97	43	219.49
1982	124	48	352.00	76	601.00
1983	150	50	357.00	100	969.00
1984	173	43	318.33	130	1,585.90
1985	188	36	326.00	152	2,990.00
1986	194	46	432.12	148	3,354.83

(Note : * In 1979, 2 RRBs neither earned profits nor incurred losses.

** in 1981 information on profit and loss was not available in respect of 2 RRBs.

Accumulated losses of all RRBs

Year ended	Amount	Year ended	Amount
1982	981.00	1985	6,136.18
1983	1,733.09	1986	9,430.88
1984	3,171.26		

is. Firstly, the RRBs are mandated to confine their lendings to weaker sections where the interest earned on loans is the lowest in the banking system. Low interest margins and the high cost of servicing a large number of accounts, coupled with low volume of business on account of their restricted clientele are some other factors which make for unprofitable working of these banks. Non-availability of competent and trained staff also pose serious problems in expanding the business of RRBs. In sum, low margins, low level of business and high operating costs all of which are built into the system, account for the inescapable losses in RRBs. The question of interest rates, costs and margins

for different systems is dealt with in detail in Chapter XVIII. As indicated therein, with a financial cost of 7.80 per cent per annum and transaction cost of 8.65 per cent per annum, if RRBs have to break even, they have to charge interest at atleast 16.45 per cent per annum. This is obviously not possible in the present system, as RRBs are to cater to the weaker sections at concessionary interest rates, with also no scope for cross-subsidisation, in the absence of loans which could yield higher returns.

4.19 We also examined the position of 46*RRBs which were working at profit as at the end of December 1986. But we found that the factors which have contributed to profits of these banks have not been their earnings through lending to the target group. In the case of 18 banks which were started during 1984, 1985 and 1986 their profits were mainly due to deposits of initial share capital contribution etc. with the SBs. Of the remaining 27 banks, in 22, the balances with SBs and investments, similarly ranged between 35 per cent to 95 per cent as against the SLR and CRR requirement of 28 per cent. The profit in these cases was also mostly due to the interest earned on these deposits and investment and not on lendings for the weaker sections. Of the balance five banks, three had very low CD ratio i.e. less than 68 per cent as against the all India average of 104 per cent, which again points to their restricted lending to the target group. In the case of the remaining two banks, although they had a higher CD ratio, a larger component of their lending was for non-agricultural sector.

(ii) **Management**

4.20 A sample study by our consultants revealed that the Boards of Management of RRBs did not meet regularly. Board meetings were often adjourned for lack of quorum and resolutions were approved by circulation. In some cases the representative of the GOI was not even nominated. It was found that non-official directors did not evince adequate interest in the affairs of the RRBs. Reportedly many irregularities and sensitive issues were not brought to the notice of the Board. Quite often most of the time was taken up for discussion of personnel and recruitment matters. The time spent on discussions relating to financial health of the bank was marginal. In general, the working of these Boards left much to be desired.

* Of these, one RRB neither earned profit nor incurred loss.

(iii) Recovery of loans

4.21 As on June 1986, recovery in RRBs was 49 per cent. Frequency distribution of RRBs according to percentage of recovery to demand for the year ended June 1986 is given in table 6. The recovery performance was more than 60 per cent of demand in the case of RRBs in Punjab, Kerala, Tamil Nadu, Meghalaya and Mizoram. The position was very unsatisfactory in respect of RRBs in Nagaland, Tripura, West Bengal, Orissa and Bihar.

Table 6

Recovery of loans by RRBs as on June 1986 **

<u>Percentage of recovery to demand</u>	<u>Number of RRBs (Percentage to total)</u>	
25 and below	9	(5.0)
26 to 35	20	(11.4)
36 to 50	52	(28.6)
51 to 75	72	(39.6)
Above 75	28	(15.4)
	<hr/>	<hr/>
	181	100.0
	=====	=====

† Total *

4.22 The case studies conducted by our consultants showed that the high overdues in some RRBs have been due, among other factors, to irregular and benami advances. The agitation by the staff of RRBs for wage parity with the staff of commercial banks also affected recoveries in some banks. While droughts and floods and consequent damage to the crops affected recoveries in some years, wilful default, misuse of loans, lack of follow-up, improper identification of borrowers under IRDP etc. were found to be some of the other reasons for the high level of overdues in RRBs. Political intervention in sanction of loans under IRDP on the one hand and announcements about write off of the loans by local leaders on the other, have been cited as reasons for unsatisfactory recoveries in some of the RRBs. Recoveries by and large were poor in respect of loans sanctioned under

* of the balance of 13 RRBs, 12 were established after 1st January 1985 and in respect of one bank data was not reported.

** Source : Statistics of RRBs, June 1988, NABARD.

IRDP and other poverty alleviation programmes. It is true that the other agricultural credit systems also suffer from these weaknesses but their overall profitability enables them to absorb these losses. It was also found that loans for minor irrigation, animal husbandry, horticulture, handicrafts etc. had been granted without ensuring adequate supply and marketing arrangements and these resulted in the loans going bad. Purposewise, repayment was comparatively poor in the case of long term agricultural loans (40 per cent) and loans for Industry, Service and Business (ISB) activities (41 per cent).

(iv) **Staff Position**

4.23 The main problems relating to staff in RRBs were (a) inadequacy in relation to workload, (b) difficulties in recruitment, (c) lack of training, and (d) lack of motivation. Often it was found that disproportionately large staff was posted at the Head Office. In some RRBs, recruitment of staff was not fast enough to take care of the requirements of additional branches. There was also some problem in recruitment of the staff after it was entrusted to Banking Services Recruitment Boards (BSRB). However, in some RRBs there was surplus staff due to conversion of uneconomic branches into satellite branches. Recruitment of more qualified persons had in some ways added to the difficulties of RRBs since some of the well-qualified staff was constantly on the look out for better positions elsewhere. In the result, the turn-over in officer cadre was as high as 25 per cent in some RRBs while in the clerical cadre it was 15 per cent. Frustration among the staff arising from lack of promotional avenues was also quite visible in many RRBs, leading to agitations in some.

**Future of Regional Rural Banks
in the Rural Credit System**

4.24 Poor quality of lending, bad management and large scale defaults have thus led to the poor performance of RRBs. But these are weaknesses the RRBs share with the rest of the institutional structure in the credit system. What really places RRBs on a different footing is as the Kelkar Working Group termed 'the built in non-viability' of the structure. Viability in our view means not merely the ability of the institutions to break even, but the ability also to expand. While recommending the continuance of RRBs as part of the Rural Credit System, the Kelkar working group had conceded that even with the whole of the package of concessions, subsidies and equity accretion, not more than half the number

of banks could turn the corner even temporarily. Provision of subsidies and other financial as well as non-financial assistance almost on a continuing basis was, as the figures in the report of Kelkar Committee bring out, necessary to keep the institutions going, even on, what one of our Consultants termed 'starvation diet'. This is not to suggest that the function of financing the weaker sections should be given up or slowed down. On the contrary, our concern is that credit to these sections is not in any way clogged on account of the weakness of the structure which finances them. Credit flow to the weaker sections cannot be ensured if the lending institutions are themselves weak structurally or otherwise; it is only a financially strong bank that could absorb the shocks implied in financing the weaker sections. What is, in fact, needed is a financial system which serves the poor well and not a system which can extend only poor service. In other words our objective is 'Service to the poor and not poor service'. Experience has shown that this objective could be achieved only by self-sustaining credit institutions. RRBs, structured as they are, in our view are not the institutions which could fulfil this function.

The Rationale and Expectations

4.25 While taking a view of the future set-up of RRBs, it does seem necessary to also look at the considerations which weighed with the Working Group on Regional Rural Banks (1975) in recommending this new institutional set up within the framework of the multi-agency system in India. Only then could there be a proper appreciation of the issues involved, and judgement whether or not the RRBs have been able to live upto the expectations, the founders had of them.

4.26 The Report of the Narasimham Working Group has set out in detail the rationale of setting up the RRBs. One of the important considerations was, as the Working Group had pointed out, the inadequacies of the co-operatives and the commercial banks which were the two institutional structures then responsible for credit delivery operations in the rural areas in reaching the rural poor. In the view of the Working Group, the co-operatives suffered from certain disabilities, such as their limited absorptive capacity of refinance from the higher tiers of finance because of their inadequate non-overdue cover. These disabilities themselves were as a result of their inability to mobilise adequate deposits, their managerial weaknesses and ineffective supervision of credit. Equally important, was their inability to cover adequately the small and marginal farmers. As

for the commercial banks, the Working Group felt that attitudinally their disposition to rural credit operations at the delivery point was totally different from that which should guide the functioning of local level institutions. One of the reasons for this was the high cost structure of the commercial banks and their style of functioning. The Working Group, therefore, felt that by a combination on the one hand, of such of the characteristics of the co-operatives which made them an ideally suitable institutional frame-work in the context of Indian rural ethos, and operational efficiency of commercial banks on the other, a new institutional structure that could provide for a healthy credit delivery system to rural poor could be moulded. Such an arrangement would also help to remove the disabilities/inadequacies, which characterised the co-operatives and commercial banks and thereby enable the new structure to speed up the progress of institutional lending with its focus on meeting the committed needs of the small farmers and other weaker sections. The Working Group thought that such an institution would provide for a sturdy and vibrant organisational structure which could face the new challenges in the fast changing and dynamic rural credit scenario.

4.27 The Narasimham Group was, however, cautious not to suggest its adoption as a permanent pattern of rural credit system in the country; in their view it was basically an experimental institution. It envisaged that in organising the new institutional structure, considerable planning will be necessary and that to start with, only five such banks may be set up and that their further expansion should be conditional to their justifying the various assumptions underlying the objectives with which these institutions were set up. The Working Group also outlined the broad indicators of future policy and approach as is evident from the rationale they had spelt out for the setting up of the RRBs. The Report laid special emphasis on generation of viability among the small borrowers, as one of the goals the new institution had to keep in view. To this end, they stressed the need for adopting proper loan appraisal systems so that recovery of loans became a by-product of this process. (The Working Group had also made it abundantly clear that it was certainly not their intention that the RRBs should remain non-viable for all times to come.) They stressed the need to keep in view the fact that viability had a time dimension as well. A major consideration with the Kelkar Working Group in recommending the continuance of the RRB system was that in its absence commercial banks would not have

expanded their branch network in rural areas. In the event they thought that many of the remote corners would have remained unbanked, denying accessibility to credit for large numbers of small and marginal farmers and the weaker sections. Secondly, the Group shared the feelings of the Narasimham Working Group that the commercial banks lacked the necessary personnel with the requisite skills and aptitude for rural lending. A third factor was that RRBs would continue to remain, as the Narasimham Working Group assumed, a low cost institution.

Expectations Belied

4.28 The changes, which the last few years have witnessed in the rural credit scene have been qualitatively different from what had been experienced in the past. These changes have belied the basic assumptions of the Narasimham Group (1975) and the expectations of the Kelkar Group (1986). As for branch expansion, the commercial banks have registered considerable progress and reached out to remote rural areas. As of March 1988, the commercial banks had 18,282 rural branches as against a mere 8,300 in 1976. The figure would have been much higher if the commercial banks had not been pre-empted from opening more branches in pursuance of the policy of priority to RRBs in the sanction of rural branches.

4.29 While on the subject of branch expansion of commercial banks, we should not fail to add that the Narasimham Working Group had emphasised the point that the new institution (RRB) should aim at supplementing rather than supplanting the existing institutions. The Dantwala Committee had also noted "In our view the most relevant criterion for the selective extension of the RRB system is the state of co-operative credit structure at the district level. As referred to in our earlier paragraph, in as many as 182 districts, the DCCBs are weak. The 48 RRBs cover 55 of these districts. To start with, the programme of establishing new RRBs may be implemented in the remaining 127 districts". In other words, there was a re-emphasis of the principle of complementarity which is the basic philosophy underlying the multi-agency approach to rural credit. The Working Group had suggested that the setting up of the RRBs should not in any way lead to a let-up in the pace of either rural branch expansion or extension of rural credit by the commercial banks and the progressive widening of the area of credit coverage by the cooperatives. In retrospect, however, it would appear that neither of the two suggestions was followed up. Contrary

to the recommendation regarding the rural branch expansion of commercial banks there was not only no significant expansion in recent times, but on the other hand, there was an embargo on new rural branches in pursuance of the policy of sanctioning such branches exclusively to RRBs, save in exceptional cases. As for increase in the area of credit coverage by the co-operatives, there has been a widely shared feeling that the RRBs at the district level and their branches at the village level led to a general weakening of the cooperative credit system.

4.30 Secondly, in the wake of the expansion of their rural branches in the late seventies and for a while thereafter, the commercial banks had inducted staff at different levels with the necessary technical qualifications, aptitude and training in rural lending. As regards cost, there has been in fact, a steady narrowing down of the differences between the emoluments pattern in RRBs and the commercial banks, as a result of the hike in salary and allowance structures in many state governments e.g. West Bengal and Maharashtra. In many cases at least near-parity if not total parity has already been reached. In the matter of cost structure, however, it is not the emoluments of individual employees or the numbers of employees which matter so much as the total operational costs of rural lending and more so lending to the weaker sections, which involves a large number of small accounts. The costs in servicing them, monitoring them and recovering the loans are much higher than making loans to other segments of society. A sample study on costs and margins carried out by one of our Consultants has shown that the transaction costs in RRBs are somewhat higher than those in the rural branches of commercial banks. One obvious reason is, in commercial banks with a broader loan mix and relatively higher level of efficiency, the economies of scale tend to bring down the costs.

4.31 As regards the local feel, there is a qualitative difference as between a Co-operative and an RRB. Firstly, in a co-operative membership itself is local and it participates in the management of the institution. In the case of RRB on the other hand, the local feel is sought to be achieved merely by recruiting middle and lower level staff within the district.

4.32 Another area of weakness in the co-operatives which the RRBs were expected to overcome was the lack of absorptive capacity for refinance from

higher tiers for want of adequate non-overdue cover. Today, however, most of the RRBs share the same weakness, perhaps with much higher intensity since on account of mounting overdues many RRBs have either only restricted eligibility for refinance or no eligibility at all. As on 30th June 1987, only 30 out of 196 RRBs were eligible for unrestricted lending, or in other words had adequate absorption capacity under the NABARD schematic assistance.

4.33 Based on the analysis we are convinced that the logic and rationale which justified or perhaps even necessitated the setting up of RRBs in the mid-seventies do not any longer exist. In today's context, these considerations do not seem relevant, howsoever rational the approach and lofty the intention might have been a decade ago.

4.34 We are aware that there has been a lot of emotional and populist appeal which has come to be associated with these institutions. As a Committee engaged in assessing the strengths and weaknesses of the various components of the credit system and recommending measures for strengthening the system in its totality, we are called upon to look at the future of RRBs on empirical considerations in the context of the future framework of the rural credit system in the country, which we have outlined in this Report. At the same time, we do recognise that the emotional undercurrents are a factor which cannot be altogether ignored. Therefore, in the search for alternative mechanisms, we have taken due note of this. The discussion which follows, explaining the rationale for the option we have chosen, would bear this out.

4.35 The working of RRBs in the last 12 years and their deficiencies show that the weaknesses of RRBs are endemic to the system and non-viability is built into the system as such. We are, therefore convinced that constituted as they are at present, the RRBs would not be able to serve the interests of their target group in the manner expected of them. We, therefore, see neither logic nor propriety in the present context, in continuing with a losing financial structure. As the Kelkar Group itself has brought out, RRBs cannot be made viable institutions through internal reorganisation and strengthening. An analysis of the profit and loss position of RRBs on the basis of secondary data undertaken by us for a two year period viz. 1985 and 1986 has shown that of all the variables such as the age of the banks, number of branches, deposits, credit etc., the CD

ratio alone has some significance in explaining the profit and loss of an RRB; but this coefficient carries a negative sign, which means that the more an RRB lends the more it loses. This amply bears out the statement of the Kelkar Working Group that non-viability is built into the RRB system itself.

4.36 We have examined the possibilities of letting the RRBs continue with various improvements such as enlargement of their share capital, provision of bad debt reserves, providing somewhat larger access for them to higher income groups and more resilient customers and even giving them a subsidiary status to the commercial banks. But on a close examination of each such possibility we found insurmountable difficulties. All in all, we found these alternatives to be unsatisfactory half-way houses which do not solve the problem of service to the rural poor and do not meet the need of effective credit to the weaker sections of the community. We must also state that our commitment is not to any particular institution, but to the idea of providing effective lending service to the down-trodden and bringing an ever enlarging segment of the less well-to-do in the fold of credit and through credit, among other things, in the realm of growth and development.

4.37 In view of these factors, we clearly see no place for RRBs in the country's rural credit system for the future and we so recommend. But we should hasten to add that it is of utmost importance that the different components of the future credit system effectively serve the target groups of RRBs and the purposes for which they were originally established.

Alternative Mechanism for Financing of Weaker Sections

4.38 Having come to the conclusion that RRBs as a system, have no justifiable case for continuance and accordingly recommended their discontinuance, it is necessary to consider how the objectives for which RRBs were set up could continue to be subserved. Our concern is to ensure that the failure of the RRB system and hence its discontinuance do not jeopardise the cause of the target groups. Our recommendations for the discontinuance of RRB system itself arise from our concern for the weaker sections, since the RRB system has failed to subserve the interests of these sections. Therefore in our view the question of tackling the existing RRBs is only of secondary concern; the major concern is

the building of a mechanism which would effectively perform the functions which the RRBs were expected to do.

4.39 One of the propositions we considered was making the existing RRBs as either fully owned or substantially owned subsidiaries of the sponsor banks. We could not, however, support this as a solution, since the subsidiaries would also continue to be separate corporate bodies having to face the same problems as RRBs themselves have faced. In the event, reorganisation of these RRBs into subsidiaries of the sponsor banks would be self-defeating in purpose.

4.40 The second option would be to merge the RRBs and their branches with the concerned SBs; the Head Offices of RRBs being either merged with Regional or Zonal offices or where such offices do not exist, converting them as Zonal/Regional Offices of the sponsor banks and the branches becoming the branches of the sponsor banks. As legal provisions stand at present, there is no enabling provision for the RRBs to be taken over or merged with SBs. Necessary amendments to existing laws will have to be brought about. While the mechanics of merger and post-merger problems will have to be handled carefully, we do not see any major hurdle in a merger arrangement. Functionally, the public sector banks are involved in a much larger way in lending to rural areas as well as to weaker sections. As of March 1988, the total lendings of all RRBs stood at Rs.2,318 crores as against Rs.10,438 crores as direct advances to agriculture and Rs.7,310 crores as advances to weaker sections by the commercial banks. Similarly, the public sector banks have given Rs.28,468 crores as priority sector advances as on that date. So far as branch set-up is concerned, the public sector banks today (March 1988) have 16,916 rural branches spread over the length and breadth of the country as against 12,235 rural branches of RRBs. But for the branch expansion policy followed in the recent past of sanctioning rural branches on a priority basis to RRBs, the rural branches of public sector banks would have been much higher than the existing 16,916 and RRBs would have had less than their present 12,235 branches.

4.41 The merger as we have recommended would involve the question of absorption of the accumulated losses of RRBs. Consistent with the existing principles in this regard, the losses necessarily would have to be borne by the shareholders. We, therefore, recommend that the net loss of each RRB should

be shared between GOI, sponsor bank and state government in the same proportion as their share holdings. We suggest that a case-by-case analysis of each RRB should be made to assess its net worth i.e. realisable value of assets and outside liabilities. The general principles of bank merger adopted by RBI under Section 45 of Banking Regulation Act can be adopted while merging RRBs with sponsor banks. Since the accumulated losses are likely to increase in future, as trends in this regard point to, there is a sense of urgency in giving effect to our proposal on merger. Delay in giving effect to our proposal would also make the problem of staff absorption by sponsor banks more complex.

4.42 As can be seen from table 7, as at the end of December 1987, RRBs had 13,090 rural/semi-urban branches. The branches accounted for 32 per cent of the total number of rural/semi-urban branches of the banking system (commercial banks and RRBs put together) at 41,316. However, the share of RRBs in rural lending was barely 9 per cent and in total business 6.4 per cent, whereas the commercial banks which accounted for the balance of 68 per cent of the branches had as much as 91 per cent of the share of rural lending and 93.6 per cent of the total business. The share of RRBs in the total business as well as in rural lending is so small as compared to the share of the commercial banks that the merger as we have proposed would not only leave no void but on the other hand the commercial banks which are the stronger institutions may be in a position to step up the share in rural lending so far catered to by the branches of RRBs. Therefore, the merger as we have proposed would only facilitate a smoother flow of credit to rural areas than before.

4.43 In giving effect to the proposal for merger of RRBs with commercial banks there is one more aspect to be dealt with. This relates to the permanent staff of RRBs. With the general rise in salary scales and allowances in many state governments, the differential between the emoluments structure in commercial banks and the RRBs is not a significant one as of now. A merger which would involve a corresponding addition to the rural branches of commercial banks would provide to the banks concerned, a complement of staff with necessary orientation and with the levels of educational qualification now prescribed for recruitment, their skills can be upgraded to the extent called for. Reference has already been made elsewhere in this Chapter to all-India agitation by the staff of RRBs for hike in emolument structure as well as promotional opportunities

Table 7

Share of RRBs and Commercial Banks in Rural Credit as on December 1987

(Rs. crores)

	No. of Branches		Total	Deposits	Gross Credit	Total Business
	Rural	Semi-Urban				
Commercial banks	18,370	9,856	28,226	40,699	21,627	62,326
RRBs	12,215	875	13,090	2,123	2,162	4,285
TOTAL	30,585	10,731	41,316	42,822	23,789	66,611
Share of RRBs (Percentage)	39.9	8.1	31.7	4.9	9.1	6.4
Share of CBs (Percentage)	60.1	91.9	68.3	95.1	90.9	93.6
	100.0	100.0	100.0	100.0	100.0	100.0

Source : Banking Statistics - Quarterly Handout - December 1987
published by Banking Statistics Division, DESACS, RBI

and to this end they have been demanding some percentage of higher posts in the sponsor banks being reserved for RRB staff. The Kelkar Working Group recommended such a reservation to provide for adequate opportunities for staff in RRB for career progression. This problem would automatically get solved through merger. The only question that still remains would be fixation of seniorities. This should pose no problem since there have been in recent times cases of merger of smaller private sector banks carrying lower scales of pay with nationalised banks in which the staff carry higher scales. The same modalities as in these cases can be applied while merging RRBs with the sponsor banks. Since the modalities have already been worked out and have been given effect to, we do not propose to go into further details in this regard.

4.44 In recommending that the RRBs be merged with sponsor banks, we have other considerations as well which are even more important. Firstly, the sponsor banks would in this process be acquiring the branches of the RRBs, which will ultimately strengthen not only their delivery system but also enhance their deposit raising capability. Secondly, the new concept of 'service area

approach', (discussed in Chapter X) is intended to facilitate integrated development of identified areas, an identified branch being made responsible for it. Under the service area concept where commercial bank branches do not exist and there are RRB branches in their place, we apprehend that weak as the RRBs and their branches are, the area allocated to them would suffer not only in comparison but in absolute terms also, so far as service expected of the branch to which the area is allocated is concerned. Further, under the service area approach, in cases where RRB branches become the identified focal institutions, the non-target group in the area has to be catered to by the nearby branches of commercial banks. This would defeat the unity of command which is an integral aspect of the service area scheme. On the other hand, if RRBs become commercial banks' branches they would be able to meet the entire credit needs of the area, including those of the weaker sections which is the target group for RRBs.

4.45 Yet another consideration is that, once the RRBs are merged with the commercial banks with their wide range of lending, the scope for internal cross-subsidisation also widens and the losses on account of having to service the weaker sections can be offset by earning from the higher interest yielding loan portfolio of the banks.

Impact of Merger on Sponsor Banks

4.46 While the mechanics of merger in its detail will have to be worked out by the Reserve Bank of India in consultation with the GOI, it would be useful at this stage to take a look at the emerging scenario. This is necessary for a critical appreciation of the ability of the sponsor banks both to absorb their share of the losses and to effectively take over the functions presently discharged by RRBs.

4.47 Firstly, as for their financing of the weaker sections is concerned, the total loans outstanding the whole of which represents loans for weaker sections, stood at Rs.2,318 crores as against loans outstanding of Rs.7,310 crores for weaker sections in public sector commercial banks as on 31 March 1988. The total advances to weaker sections by commercial banks and RRBs put together at Rs.9,628 crores constituted 15 per cent of the aggregate net bank credit of both RRBs and commercial banks at Rs.64,436 crores i.e. Rs.2,318 crores

plus Rs.62,118 crores. The commercial banks are expected to lend 10 per cent of the net bank credit to weaker sections under the current stipulation. They have however, exceeded the target as lendings to weaker sections at Rs.7,310 crores formed 11.8 per cent of the net bank credit on 31 March 1988. To maintain the current levels of lending to weaker section after merger of RRBs with commercial banks, we would recommend that the current target of 10 per cent may be raised to 15 per cent of the net bank credit i.e. net bank credit of the entire commercial banking system including RRBs. This increase would take care of the annual incremental advances of around Rs.400 crores of the RRB system to weaker sections. The achievement of the target should be monitored in respect of each sponsor bank.

4.48 The erstwhile branches of RRBs will become branches of sponsor banks under the new arrangement. While these new (merged) branches would finance all types of customers as in any other branch of commercial banks, their focus should continue to be servicing of the weaker sections. With a view to ensuring that there is no slackness in lending to the target groups by these individual branches, we propose that in no case lending to target groups in these merged branches should be less than what was achieved prior to merger. In addition, we would recommend that these branches in the post-merger period should maintain not only the past growth rate but also progressively step it up depending upon the extent of coverage of target group in their respective areas of operation.

4.49 We have earlier recommended that the losses of RRBs should be shared between Government of India, sponsor banks and state governments in the same proportion as their existing shareholding in the RRBs i.e. 50:35:15. We have examined whether the profitability of these sponsoring public sector banks is adequate to absorb their share in the accumulated losses of RRBs. Out of 196 RRBs as at the end of December 1987, 192 RRBs have been sponsored by 26 public sector banks - 2 banks i.e. State Bank of Travancore and Oriental Bank of Commerce have not sponsored any RRBs. Of this, 154 RRBs had accumulated losses of Rs.130 crores and the remaining 38 RRBs had accumulated surplus of Rs.30 crores as at the end of December 1987. Thus, the net losses to be absorbed in respect of 192 RRBs work out to Rs.100 crores, the share of the sponsoring public sector banks being Rs. 35 crores. As against this, the profits earned by these sponsoring public sector banks were Rs.189 crores and Rs.257 crores

during the years 1986 and 1987, respectively. If the losses of these RRBs have further increased during 1988 which is likely, so also would the profits of sponsor banks which as a whole would be able to absorb their proportionate share in the accumulated losses of RRBs from their current profits, without much difficulty.

4.50 The entire staff of RRBs (15,570 officers, 9,129 field supervisors, 22,584 clerks and 2,410 subordinate staff making a total of 50,693) who will have to be absorbed by the sponsor banks in suitable scales, may need further orientation in general banking besides rural banking. We, therefore suggest that the staff so absorbed be kept in a separate pool in sponsor banks for some time, say for three years. This will enable sponsor banks to identify their training needs and placements. As we have stated earlier, the head office of each RRB could be converted into a controlling office of sponsor bank. If there is already a controlling office of sponsor bank at that centre, the head office of the RRB could be merged with the controlling office.

4.51 NABARD has been providing refinance to RRBs both for schematic and non-schematic lending including short term loans from RBI's General Line of Credit. To the extent of schematic lending, sponsor banks will continue to get refinance from NABARD. Since NABARD has not been providing refinance to commercial banks for non-schematic lending including short-term loans, the existing outstanding under these heads in respect of RRBs (at Rs.489 crores as on December '87) would have to be repaid to NABARD. Since advances by RRBs form only less than four per cent of net bank credit, we do not envisage any resource constraint to meet this commitment by the sponsor banks. In the new context NABARD will be relieved of its responsibilities of inspection and refinance of RRB system with consequent savings in cost to the NABARD. Incidentally this would also enhance NABARD's capability to monitor the co-operative credit sector.

A Strong and Viable Credit System to Serve the Rural Poor

4.52 Finally, but not any less importantly, we would like to add that our concern in recommending merger of the RRBs with the sponsor banks is that, there should be at the delivery point a strong institution to serve the small man. In the new situation when the commercial banks will take over the activity of the RRBs, it is not only imperative that the bank's volume of credit given to

the weaker sections in the erstwhile RRBs be maintained but that the planned growth rate of lending to the poor should also be adhered to.

4.53 One of our major concerns bears repetition; the merger recommendation does not mean any dilution of either the institution's, the government's or our concern for the small man. On the contrary, the intention is to give the small man a stronger institution to serve his needs more efficiently. Only the separate legal or corporate identity of the RRB would be lost and not the functions for which RRBs were created. In view of this, as a transitory measure, we would recommend, more on psychological grounds rather than on economic considerations, that branches which were former RRB branches may be treated as specialised commercial bank branches and the name board may carry the legend to show that it was the former branch of such and such RRB.

4.54 In fine, we would like to restate the rationale of our recommendations for merger of RRBs with commercial banks. Firstly, it will offer a solution to the problem of the insolvency and the in-built non-viability of the majority of RRBs. Out of the 194 RRBs at the end of 1986, in the case of 117, the accumulated losses have wiped out their entire share capital and reserves rendering them in a technical sense insolvent institutions. This number was only 50 out of a total 173 RRBs as at the end of December 1984, when Kelkar Working Group reviewed the working of RRBs. In the normal course from the banking point of view, these are institutions which should go into liquidation. In their case, therefore, consistent with the social policy followed in such cases, they have necessarily to merge with a stronger bank. The remaining 77 RRBs though not immediate candidates for liquidation are potential candidates. In these cases also there will be no option left other than merger sooner or later. This is evident from the fact that the number of loss-making RRBs as well as the quantum of losses have been steadily on the increase. As at the end of December 1982, the losses of 76 RRBs were of the order of Rs.9.81 crores only. The accumulated losses as at the end of December 1984, with reference to which date the Kelkar Working Group examined the position, amounted to Rs.31.72 crores in respect of 130 banks. As of December 1987 these have risen to Rs.133.10 crores in respect of 162 banks. In addition there may be other losses including losses on account of loans not fully covered. The merger we have recommended would solve this problem of accumulated losses also. Secondly, the merger would

be a solution to the innate weaknesses of the RRBs, by providing a structural arrangement which will have a built-in self-strengthening and as already referred to, internal cross subsidisation capability. Above all, the merger will in due course take us closer to achieving the goal of creating a strong, viable credit system, in which the interests of the small man would be better served.

CHAPTER V

CO-OPERATIVE BANKING SYSTEM - AN OVERVIEW

Evolution of Co-operative Credit - An Historical Background

Promotion of credit co-operatives in its present day corporate form was the first ever effort in the country at institutionalising credit for the rural areas. It also marked the culmination of a series of measures initiated by the Government in the last three decades of the 19th century to combat usury and the resultant indebtedness and alienation of land, all of which were eating into the vitals of an already stagnant rural economy. These earlier measures ranged from post-office savings banks with a view to encouraging thrift, subsidised state loans known as Taccavi, legislative steps to provide debt relief together with general settlement of debt as well as curbing of usury and legislative measures to prevent alienation of land. But all these proved to be mere palliatives and failed to provide a long term solution. It is in this context and in their search for new measures that the Government eventually turned their attention to co-operatives as the most hopeful method of combating the complex problems of usury and indebtedness and the consequent alienation of land from the tillers of the soil. By then, co-operative organisations established on the principles of 'self-help' and 'mutual-help' by Friedrich Wilhelm Raiffeisen for providing loans to small farmers and by Shulze for providing relief in sickness and for purchase of raw materials to small artisans had met with some measure of success in Germany. Some headway had been made around this period in Italy also by Luzzati in organising Peoples Banks. As was natural then, it was to these experiences in Europe, that the Government looked for guidance when it turned its attention to co-operatives as a long-term solution. In particular, the Government found the German experience of special relevance to the Indian context. Accordingly, in 1896, the then Provincial Government in Madras deputed one of its officers, Sir Frederick Nicholson to study the experience of land banks in Germany so as to explore the possibility of adopting the system in Indian conditions. He recommended the organisation of Raiffeisen type of co-operative societies as a lasting solution to the problems in the Indian context. The Madras province provided an ideal ground for the experiment with its long tradition even then of indigenous societies known as 'nidhis'. Around this time, another

Civil Servant in the then United Provinces (presently Uttar Pradesh), Mr. Dupurnex published the results of his study in the Province and recommended the establishment of 'Peoples Banks of Northern India', as the most hopeful solution to the problem of indebtedness, usury and stagnant rural economy with a large peasantry. Drawing inspiration from these two studies, several societies came to be organised in various parts of the country.

5.02 It was, however, soon realised that any significant advance in the organisation of co-operative societies was possible only with the necessary legislative support. Accordingly, the Government of India appointed a committee under Sir Edward Law to examine the question. This committee drew up model schemes for the management, both of rural and urban co-operative societies and a framework of the legislation needed to provide to the societies the required privileges for their effective functioning. Sir Edward Law's recommendations provided the basis for the bill which was passed into law in 1904 as the Co-operative Credit Societies Act. With the passing of the Act, the co-operative credit system soon emerged as the premier institutional agency for provision of agricultural credit in the country. In 1912, some major amendments were brought about in the Act with a view to broad-basing it to enable organisation of non-credit societies as well. With the constitutional reforms popularly known as Montague Chelmsford Reforms and the passing of the Act of 1919 for the purpose, Co-operation became a transferred subject. Following this, many provincial governments replaced the Central Act with their own legislations. Notable among these were Bombay, Madras, Bihar and Orissa which replaced the Central Act with their own legislations in 1925, 1932, 1934 and 1935 respectively. Several provincial governments simultaneously initiated a number of other measures as well for the development of co-operative credit movement. As a consequence, the co-operative credit system had by the twenties become the principal institutional agency for the provision of agricultural credit, both for production and investment. The Royal Commission on Agriculture (1928) thus observed that 'if co-operation fails there will fail the best hope of rural India.'

5.03 The co-operative credit movement, however, suffered a serious setback as a result of the economic depression of the thirties. The debt burden in-

creased not only in money terms but also in real terms. In turn, the co-operative credit system had to bear its share of the onslaught of depression. Defaults of earlier loans became unavoidable and they mounted. In fact, payment of interest as well as of principal practically remained frozen. However, the position changed dramatically as a result of rise in prices with the start of the Second World War. This was a period of economic recovery and as available data show, the agriculturists began to liquidate their old debts, the co-operatives sharing their part of the benefits.

5.04 The Agricultural Finance Sub-Committee (1945), nevertheless, entertained some doubts about the capability of the co-operative credit system to cope with the emerging credit needs fully, although it recognised that the expansion of co-operative movement provided the best and lasting solution to the problems of rural economy and agricultural credit in particular. They were of the view that if the co-operatives' share in agricultural credit had to increase, as it ought to, certain corrective measures were necessary to reorganise and improve their working and recommendations including certain institutional innovations were made. The Co-operative Planning Committee in its Report (again in 1945), however, took an entirely different view. They believed that not only in provinces where the co-operative credit system had registered a high degree of development, but in others also, the system could provide the cultivator with all the facilities which were needed or any new institutional innovation could provide. They, therefore, recommended that whatever assistance, financial and otherwise, which the Agricultural Finance Sub-Committee felt was necessary for the alternative institutional framework should be given to the provincial co-operative banks, thus obviating the need to duplicate institutional structures for the same purpose.

5.05 With the co-operatives being able to recover substantially from the reverses they went through in the depression period, the co-operative banking system at all levels was in a position, despite the shocks of partition, to acquire a place of importance in the Indian Banking System by the late forties. In its review of the position of banking facilities in the country the Rural Banking Enquiry Committee (1950) in fact made special reference to the role of the Provincial (now the State Apex) Co-operative Banks as well as

the District Level Central Co-operative Banks. The Committee had come to the conclusion that on the face of it, the position was such that a sound and satisfactory co-operative banking structure had come to stay, albeit in some states only. In other states, it was the Committee's view that the structure was in the process of reorganisation, consolidation and rehabilitation. In the words of the Committee, 'they had no hesitation in dispelling the 'misgivings' about the ongoing efforts in this direction expressed by some people/parties before the Committee and they did not see any 'reason why given favourable circumstances, government support and popular co-operation, the structure should not develop on right lines The primary societies at the village level had come to be regarded in the words of the Committee as 'miniature banks' and the Committee felt convinced that these were the only appropriate organisations through which banking facilities could reach out to the vast masses of rural population. Nevertheless, the Committee recognised and agreed with the Agricultural Finance Sub-Committee (1945) that reasonable facilities should be afforded to the commercial banks also without in any way hampering the growth of the co-operative credit system, to play an important part in rural credit organisation. It was their view that in regard to functions as well as clientele there could be a broad division of labour between commercial banks and co-operative banks.

Rural Credit Survey Committee and after

5.06 Various expert committees which examined the problem of agricultural credit during the last seven decades or more have, while recognising the role of commercial banks, come to the one and the same conclusion without exception, that in the Indian context, there is no alternative from the point of view of structural appropriateness, to co-operatives at the village level for provision of agricultural credit. Thus in a manner echoing sentiments of the Royal Commission on Agriculture (1928), the Rural Credit Survey Committee (1954), the first comprehensive enquiry into problems of rural credit after independence, summed up its findings after detailed examination of the entire gamut of issues connected with the problem including the social ethos of rural society, in the celebrated dictum that 'Co-operation has failed, but Co-operation must succeed'. The Committee which was set up by the Reserve Bank of India in 1951 diagnosed the failure of co-operatives in purveying agricultural credit as under :

- i) It fell short of the right quantity, related as it was to the value of land taken as security and limited by shortage of available funds with societies.
- ii) It was not of the right type unrelated as it was to any specific period determined by the repaying capacity of the borrower.
- iii) It did not serve the right purpose unrelated as it was to any productive purpose materialising in the annual harvest.
- iv) It failed to reach the right people as credit was granted to those persons only who could offer land as security but not to others who really needed it.

The Committee's prescriptions to correct the position were :

- i) State partnership through contributions by the state governments to the share capital of co-operatives;
- ii) effective integration of credit with marketing and processing; and
- iii) management through adequately trained personnel responsive to the needs of the rural population.

5.07 The Committee also recommended the conversion of the then Imperial Bank of India with a view to ensuring that the new State Bank of India with its subsidiaries would, as the largest commercial bank and state owned, supplement the efforts of the co-operatives in providing the needed credit support for the commercial transactions of co-operatives, such as marketing, processing, warehousing etc. In pursuance to its recommendation that co-operation must succeed, notwithstanding its failure in the past, it recommended a series of further measures so that necessary conditions were created in which the co-operatives could succeed in place of the usurious money lender, nevertheless distinct from either the government directly dispensing loans to agriculturists or the commercial banks doing so with their wholly urban orientation, an agency which would be owned and managed by the farmers themselves. To this end the Committee recommended a whole package of measures. The Reserve Bank was required to constitute (since established) a National Agricultural Credit (Long Term Operations) Fund to enable the bank to provide long term loans to state governments for subscribing to the share capital of the

co-operatives. The larger equity base, it was felt, would make the co-operative structure commercially viable and it, with the financial strength so gained, would be able to mobilise rural savings and meet the bulk, if not the entire credit needs of the rural sector. Other institutional measures recommended were the setting up of National Co-operative Development Corporation under the aegis of the Central Government to extend the support for processing and marketing and storage facilities in the co-operative sector, central and state warehousing corporations, National Agricultural Credit (Stabilisation) Fund in the RBI to provide medium-term loans for the purpose of rescheduling the short-term loans in the event of crop failures on account of natural calamities and setting up of a national network of training institutions to train the co-operative banking personnel. In the two decades which followed, both policy and effort, at the national as well as the state levels were geared to the development of co-operatives as an exclusive institutional agency for purveying agricultural credit.

Co-operative Credit and the Multi-agency Approach

5.08 However, in the review undertaken by the All India Rural Credit Review Committee (1969), also set up by the Reserve Bank of India, it was found that inspite of the massive efforts made in implementing the various recommendations of the Survey Committee (1954), the performance of the co-operative sector had not measured up to expectations, either in mobilising deposits or retailing credit. The same weaknesses, such as mounting defaults, lack of trained personnel and the like, which had been the major malaise continued to be the bane of co-operative structure. In the result at the end of the third plan, it was found that the credit dispensed by the co-operatives considerably trailed behind the increasing demand for credit in the rural sector. The Review Committee had thus come to the conclusion that without abandoning any of the measures taken to upgrade the co-operatives, there was need for some supplementary effort so that the agricultural production did not suffer. Thus, in recommending a larger role for commercial banks in the provision of agricultural credit and a multi-agency approach to rural credit so as to plug the gaps in the credit system, the Committee felt that it was necessary to ensure that the co-operative structure was not in any way damaged. In the light of this, the Committee recommended a series of measures to

reorganise and strengthen the co-operative credit structure as a part of an integrated approach to multi-agency system. It also noted that under the social control policy introduced in 1967 and subsequently the nationalisation of 14 major commercial banks in 1969, the banks had been given a special responsibility to step up their advances for agriculture and allied activities.

5.09 The Working Group on Regional Rural Banks (1975) had briefly reviewed the performance of commercial banks in agricultural credit under the multi-agency system as also that of the co-operative credit system. The Report makes special mention of the impressive record, in terms of coverage and credit disbursal by the co-operatives, but was of the view that if supply of credit increased, so too the demand leaving a large gap unfilled. Besides, the progress in all the states had not been uniform. The selective record of progress had in fact according to the Group contributed to widening regional disparities in the functioning of co-operatives. Equally strongly, they felt, that even where the co-operatives had done well, their credit did not reach all strata of cultivators. Similarly, in regard to commercial bank credit to the rural sector, the Working Group has referred to the rapid expansion of rural branches following nationalisation and the phenomenal increase in the quantum of credit disbursed. Even so, it accounted for only a small portion of the total requirement of credit. Also the expansion of commercial banks in rural areas was a high cost operation. The Working Group, therefore, felt that there was a need for an institution which shared the local feel and low cost profile of the co-operatives combined with the degree of business organisation, ability to mobilise deposits, access to central money markets and modern outlook which the commercial banks possessed. The Working Group accordingly recommended the setting up of state sponsored, regionally based and rural oriented commercial banks to be known as Regional Rural Banks. The Working Group also felt that while a certain amount of financial loss in the initial period was inevitable in the case of Regional Rural Banks and was a price worth paying for the achievement of the larger social objective of widening area of credit coverage, the success of these banks in the long run should be judged as much by their ability to achieve financial viability. In other words social objectives ought not to provide an umbrella to inefficiency. The Working Group had in particular emphasised that as they envisaged it, the role of the new institution would be to supplement and not supplant other

agencies in the field. In fact, they had assumed as a datum that at the base, the Farmers Service Societies would be organised and said "Indeed we cannot stress too strongly the importance of strengthening the base level of credit, for even if the commercial banks - the existing and the proposed Regional Rural Banks - were to open a much larger number of rural branches than now, they still will leave uncovered a vast number of Indian villages. In this sense, a revitalised and strengthened base level co-operative system is a necessity"

5.10 Thus the refrain of all committees and working groups which have looked into the performance of the co-operative credit system either directly as part of their enquiry for the specific purpose or indirectly in enquiring into other related matter has been that the co-operatives have not done as well as they should have, but there is no question of getting away from this system in the long run. One reason for the indictment of co-operatives' performance has been that it was the sole purveyor of agricultural credit until the 1967. Arising from this, the blame for all ills of rural credit - the heavy overdues, under-financing, over-financing, procedural complexities leading to inevitable delays, have all been laid on the doors of the co-operatives. Experience stretching over nearly two decades now of the performance of commercial banks and a decade and a half of RRBs has, however, shown that the weaknesses which were considered as endemic to the co-operative system have in fact not been the weaknesses of the co-operative system itself but the ones associated with the clientele they had been exclusively serving in the past and a host of other factors. That the causes lie elsewhere, has been amply borne out by the performance of the commercial banks and the RRBs since their entry into this area. The weaknesses, in fact arise from such deficiencies as those relating to the structure of agricultural production itself.

Progress of Co-operative System

5.11 No credit system has been subjected to as much experimentation at the dictates of those outside the system as the co-operative credit system has been. Each time the system has been subjected to review by a committee or a working group, it has been made to follow newer prescriptions. The history of co-operative credit system has thus been the history of alternating periods

of growth, stagnation and reorganisation and yet quantitatively the achievements of the co-operative system have by no means been insignificant. These pertain not only to the credit sector in the system, but others as well.

5.12 In evaluating the achievements, one could clearly demarcate for purposes of comparison, if not for anything else, three different stages in the chronology of the progress of the co-operative system. First stage might readily be upto 1950 which also is the base year of India's series of quinquennial plans. The next two stages could be (i) the period of two decades thereafter upto 1970-71 and (ii) the latest, viz., from 1971-72 upto 1985-86 which is the latest year upto which data are available. Numerically in terms of membership, the co-operatives have spread widely in the country. The percentage of rural population covered by the agricultural credit co-operatives was a mere 7.8 in 1951 but by 1960-61 it increased to 36 per cent and further to about 65 per cent in 1985-86.

5.13 Agricultural credit - short, medium and long-term - constitutes of course, one of the most important sectors of rural co-operation. Short and medium-term credit in combination, recorded a five-fold increase from 1970-71 to 1985-86. The figure is Rs. 3,140 crores for the latter year. The pre-plan, which incidentally is the pre-rural credit survey figure (i.e. for the year 1950-51) was as low as Rs.22 crores. These figures indicate what could aptly be described as the phenomenal expansion that has taken place over the successive plans of co-operative credit. Long-term agricultural loans by the co-operatives in 1985-86 had similarly gone up to Rs.533 crores, representing a more than three-fold increase over the advances in 1970-71, the corresponding figure for 1960-61, the base level adopted for this analysis was a mere Rs.12 crores. (Please see tables 3 and 4 of Chapter 1). Likewise fertiliser distribution through co-operatives increased to nearly three times from about 13 lakh metric tonnes in 1970-71 to 40 lakh metric tonnes in 1985-86. This represents, in fact, more than 45 per cent of the total fertilisers sold in the country. Another area in which co-operatives have made an indelible impression is in milk production which increased from 17.41 million metric tonnes in 1951 to 20.74 million metric tonnes in 1969-70. The figure for 1969-70 is given here for the purpose of comparison as against 1970-71 in other areas, in view of the fact that from the year when 'Operation Flood'

on the Anand pattern commenced. As of now, the milk production in the sector has reached 42.3 million metric tonnes, i.e. two-fold increase as compared to what it was a decade and a half ago. Again in sugar, production by co-operatives represents about 60 per cent of the total production in the country and the number of co-operative sugar mills is around 200. The godown capacity of co-operatives, in the aggregate, is of the order of 8.56 million tonnes*. There are also nearly about 200 co-operative cold storages. Consumer goods distributed by co-operative agencies are assessed to be of the value of Rs.1,675 crores in rural areas.

5.14 The movement which has made such impressive progress in diverse fields and under numerous handicaps within its own structure on the one hand and in relation to the state on the other, cannot be wished away, nor can it be relegated to a position of no consequence although it is a fact that the growth and achievement of the co-operatives has not been uniform in all states. As a result, while in some states like Punjab and Kerala the system is strong, in many others it has failed to come up to the desired levels of expectation. Thus looking to the state of the movement even in the limited sphere of credit, the classic assertion of the Rural Credit Survey made 35 years ago still seems valid that Co-operation has failed but Co-operation must succeed.

The Lost Spirit of Co-operatives in India

5.15 It may be useful at this stage to look for the reasons for the weakness of the system in India whilst it has registered phenomenal success in the more competitive societies, such as Japan, South Korea, Netherlands and West Germany. It has been said of co-operation in India that it has failed to grow because it has been both state sponsored and state patronised; but so too has it been in many countries to cite only two examples, South Korea and Japan. It has also been said and in their evidence before us one of the voluntary organisations committed by its charter to the promotion of co-operatives as co-operatives that with the acceptance of the recommendations of the AIRCS and the measures taken in pursuance thereof, ended true spirit of co-operation and state partnership in equity became the thin end of the

* With NCDC assistance

wedge. Further, that it opened the 'flood gates' for excessive government intervention/interference in the affairs of the co-operatives and authentic non-official leadership along with democratic management disappeared altogether. That state partnership was envisaged to impart financial strength in co-operatives which served the weaker sections and not for replacing democratic control by state control is evident from the mechanics of the operation of state participation in equity as spelt out in the Survey Committee's Report. It is not necessary for us to paraphrase these again. That the import and intention of state participation in favour of the weak in their competition with the more-powerful sections of society is amply clear from the address of the then Prime Minister Shri Jawaharlal Nehru, at the conference of State Ministers of Co-operation in October 1961. He said "I hope that I have made you appreciate my own rather strong feelings on the subject of co-operation. I think it is a basic thing for our agriculture, for our industry and, still more for our whole attitude to life, national and international. It is not a government directed show, although it is government-assisted, of course. There are to be no big bosses of the Government sitting in big offices with big chap-rasis outside, directing and controlling the whole thing. That would be quite objectionable. In co-operation there is mutuality, a feeling of comradeship, fellowship, a feeling that any ordinary peasant can walk in, unafraid of the big boss". The fault then lies not with the principle enunciated but the change in the governmental ethos and mood. When he met us, Shri B. Venkatappiah, the patron saint of the agricultural credit movement and co-operation today, in the long and glorious tradition of the late Shri Vaikuntbhai Mehta, Prof. D. R. Gadgil, Shri Wajahat Hussain and other luminaries, ruefully mentioned that when the Rural Credit Survey Committee recommended a substantially enlarged role for institutional credit and state participation in equity, till institutions gained financial strength, the continued 'respect for institutions' was assumed.

5.16 The change of mood which has resulted in excessive state interference that has come to dominate the co-operatives is not limited to this field. The strength of the co-operatives unlike many other institutional structures, however, lies in the fact that in the ultimate analysis, they have a base and their strength is derived from their membership at the base. And, once the

membership gets enlightened on their rights as members of a democratic organisation managed and controlled by them, the tidal wave it could generate against external interference cannot only stem but also overpower the efforts at undue state interference.

Co-operatives as a Total System

5.17 However, the awareness of the membership of their rights is of any consequence only if the co-operatives at different levels could function as parts of a total system and are self-reliant. The basic requirement for the various tiers working as a part of a total system is that the higher tiers should look upon the lower tiers and more particularly the primary societies as the mother institutions, the secondary tiers deriving their strength from the primaries, the state level organisation deriving its strength from the secondary level organisations and together all of them providing within a sector, mutual support on the one hand and on the other, the higher tiers exercising effective leadership role through an efficient system of supervision and management of all the tiers by professionals skilled in the relevant tasks and trained for the purpose. Also a cohesive system can be built only if there is organic relationship between the lower and the higher tier, apart from the share capital obligation which only invests the ownership rights of the lower tiers in the higher tiers. For the structure as a whole to work as a system, the organisational ties have to be far stronger than they are at present. This can come about only when there is a commonly shared interest in deposit mobilisation, as well as in profits and reserves. The leadership role of the higher tier has to be buttressed by due authority as well vested in them. Cohesiveness has to be built, above all, around mutual accountability. In other words the lower tier ought to have some accountability as well as obligations in regard to the higher tier even as the higher tiers will have the same degree of responsibility to extend support to the lower tiers apart from being considered merely as shareholders. As we see it, progressively the responsibilities which lie with the Registrar today should be vested in the higher tier organisation so far as the lower tier is concerned. The higher tiers would also have to take the responsibility for evolving appropriate training systems for the non-official office-bearers and the professional managers of the lower tier institutions.

5.18 The organisational set up for the short-term credit in every state thus consists of three tiers - SCB, DCCBs, and PACSs - the lower tiers being members and shareholders of the immediate higher tier. It also needs to be recognised that each of the higher tiers will have certain rights as well as obligations with regard to the lower tiers, more particularly in the area of leadership, at the district level, this vesting in the DCCB and at the state level, in the SCB. The higher tier will also have the responsibility for the performance of the lower tier including the protection of their democratic structure. The higher tier must thus have as already alluded to, the right to issue instructions/directives to the lower tier which will have to be followed up, approve important decisions, prescribe conditionalities in certain situations and exercise supervision over the performance of the lower tiers. Arising from the responsibility in regard to shared interests in profits and reserves, the higher tier must be able to share in the losses of the lower tier for which purpose a separate fund may need to be established within the system funded by contributions out of the profits of PACSs, DCCBs and SCB, and managed by SCB. The higher tier should have also the right to convene the general meeting of an institution in the lower tiers, if found necessary with a view to bringing up some critical issues before the general body of the lower tier institution. The DCCBs should also, besides exercising supervisory functions over the PACSs, extend to them legal and other help when needed. DCCBs will of course continue to function as the liquidity reservoir and balancing centre for PACSs. At the same time the DCCBs have a task to operate as a bank for other co-operative societies in the district and to finance them.

5.19 The task of the DCCB, in promoting the activities and performance of the PACSs, is closely connected with the development activities in the area and, therefore, the DCCBs will have to play an important role in district development planning and the district credit planning.

5.20 As far as the SCBs are concerned, they will have to function as the effective leader of the short-term co-operative credit structure in the state. It should be able to develop policies relating to the organisational matters of not only DCCBs but also PACSs and take care of the implementation of this task. Besides, it will be the special responsibility of the SCB to provide refinance for DCCBs and extend assistance in the development activities

of DCCBs. It will also have to provide management assistance to DCCBs where the latter are weak. Among its other responsibilities will be approval of appointment of chief executive, training of secretaries and staff of DCCB, providing assistance in publicity and public relations, approval of the yearly budget, directives for liquidity and solvability. Needless to say, it will continue to be the liquidity reservoir and balancing centre for DCCBs. Development of personnel and salary policy for all tiers will be other important area of responsibility of the SCB. Flowing from all this, the SCB, in discharging its lead role responsibility of the co-operative credit organisation in the state has also a crucial role to play in the development and credit planning at the state level.

5.21 Such a cohesive structure would need to be built up in all other sectors as well. Thus in the marketing sector such cohesion has to be built around producer members who would resist temptations to sell their produce except through their marketing societies and in milk production, around the milk producers and so on. In this context, it is equally important that there is also co-operation amongst co-operatives and there are national systems for each of the spheres evolved as has materialised in marketing, milk production, consumer activities and handicrafts etc. with strong support from the co-operative credit system at all levels. In extending this support, to the rest of the co-operative structures, there is however, a gap at the national level inasmuch as, unlike in the area of marketing, milk production, consumer activities or handicrafts and other spheres where there are national apex organisations, some quite strong, there is no such institutional structure at the national level for the co-operative credit system as of now to extend that support to the other national level co-operative organisations or to the credit structure itself which are today federated only up to the state apex level. Apart from national level apex organisations such as the NAFED, NCCF, etc., there are other co-operative enterprises as well, such as, fertiliser co-operatives etc. which also need credit support and this today is met by the commercial banking system. In the result, the more viable national level co-operative organisations and the larger co-operative enterprises with their country wide spread, are on the one hand required to depend on the commercial banking system and on the other, they in this process provide to the commercial banks, economically stable clientele from the co-operative system itself.

The need to fill this systemic gap at the national level in the co-operative credit sector is dealt with separately.

5.22 Another major weakness in the co-operative system today in India is that there is very little effort except in certain parts of the country to strengthen the base level unit, viz., the primaries. It is often little realised that unless the base level structure is strong, it is difficult to perceive the upper tier becoming strong. Looking to the credit sector alone, the tendency has been for the secondary level institutions at the district level to secure for itself higher margins even at the cost of the primaries; the state apex organisations doing so similarly even at the cost of secondary level institutions. In their search for financial strength, the district and apex level organisations have so far looked up to margins on refinance from NABARD and legal mandate requiring the lower tiers to keep their surplus resources with them. The co-operative credit system has woefully neglected its basic responsibility in mobilising deposits, the lower tiers looking up to the higher tiers for refinance at all levels and the higher tiers neglecting the interests of the lower tiers. In short, the higher tiers have failed to provide effective leadership to the lower tiers.

Certain Other Aspects of the Malaise

5.23 It is clear that while the magnitude of most variables in the co-operative system seem to be expanding in absolute terms and even as percentage, the system is not expanding impressively in real terms and certainly not in its qualitative aspects. Deposit mobilisation, either short or long-term, has not been a strong point with the co-operative banks, which means that the banks' wherewithal for lending operations has been seriously constrained. Various factors which have contributed to rural agricultural stagnation in many areas of the country on the one hand and with the institutions' own weaknesses on the other, have stood in the way of effective lending to worthwhile borrowers. More importantly, the arrival of commercial banks on the rural agricultural scene with their impressive branch expansion and vast resources and personnel has increased the state of competition and has done creditably both in the area of deposits and lending. Again, in the co-operative banking system the overdues have continued to be around 40 per cent of demand and the figure in the case of SLDBs has actually worsened in recent years.

Bad debts too have mounted. Inability to adhere to the eligibility criteria has been disqualifying many co-operative institutions from obtaining refinance from higher institutions. All in all, the co-operative banks are in no better shape than they ever were and their survival and expansion now requires a new approach, new strategies and new initiatives.

Organisation and Leadership in the Co-operative System

5.24 The changes required call for active help and guidance in the case of primaries by both the DCCBs and the SCBs and in the case of the latter by a national apex. Simultaneously some structural changes also have to take place in those institutions and the emphasis of their work has to be altered. Co-operatives constitute an organically linked organisational system, imbued with a distinct philosophy. Their higher tiers cannot look upon their own interests as paramount. Their primary concern should above all be to strengthen the PACSs just as the emphasis of the SCB has to be on strengthening and helping the DCCBs. Only on the basis of strong PACSs can there be strong DCCBs and a strong SCB. That mutual dependence and mutual support requires an organisational change with all the consequences of that change, whereby an SCB operates as leader of the whole co-operative credit in the state and DCCBs as the leader of the PACSs in the districts. Those responsibilities require fundamental changes in the relations between the three tiers. Organisational and financial ties have to be designed to make it possible that the whole co-operative credit structure moves cohesively in the same direction, that each of the tiers feel responsible for each other, that rights and obligations between the different tiers come into existence and that stronger mutual financial ties are designed so that each tier strengthens the other. Only in such a coherent structure can the co-operative credit system be rebuilt in a co-operative organisation. Where the force of all the ties is combined, it can lead to a real revival of co-operative credit.

5.25 It is for this reason that we have devoted a lot of attention to a new organisational set up describing the tasks of SCB/DCCB in their relation to PACSs and vice-versa. Also, we have formulated financial ties in designing a liquidity scheme within the whole organisation, with the consequence that not only the PACSs can become self supporting but also that DCCBs and

SCB can grow if the PACSs grow and development of PACSs can assist in developing the DCCBs and SCB.

5.26 We also strongly believe that PACSs have to do more than merely savings, credit and commodity business. It has a task in helping its members to take up new economic activities which are profitable and to assist, guide and help them in doing so. When a PACS can carry out this task, it will be of utmost importance not only to the members but for the economy of the whole village as well.

Self Reliance - Key to Successful Co-operatives

5.27 The essence of the co-operative banking system as evolved in the Raiffeisen model, is that savings from people are collected initially and are utilised to give credit to small borrowers. If these resources are not sufficient then and only then some loans are taken from the higher co-operative institutions. The basic feature of this model which is applied extensively in Western Europe and in some countries in the East such as Japan and South Korea, and is as much applicable in India is that of a large horizontal self-reliance, i.e. reliance on resources mobilised locally and a small vertical dependence on higher credit institutions. The other essential feature of this system is a shift of emphasis from maximising profitability to maximising service to the members of the system, viz., paying best possible interest to the depositors and lending at as low an interest as possible, consistent with viability, to the borrowers, selling commodities and services at as reasonable a price as possible and making profits basically to add to the reserves - insofar as these reserves are necessary for good performance and continuity and to pay a modest dividend to shareholders. These principles have worked wonders in Western European countries and in Japan and South Korea in the East. For instance, the co-operative banking system under the leadership of Rabo bank, Netherlands, the DG bank in West Germany, the Nurinchunkin Bank in Japan and the National Agricultural Co-operative Federation (NACF) in South Korea have succeeded in bringing a very large percentage of farmers into the fold of the co-operative system and these national apexes have become some of the biggest banks of the world, the Nurinchunkin Bank having emerged as the sixth largest bank in the world. The extent of their services is enormous.

5.28 In India, on the other hand, when the co-operative movement was started in the early part of the century, while thrift was the corner stone of its philosophy the savings actually mobilised, particularly at the primary level, were small because of the poverty of the peasantry. Later, when the movement was made to expand fast as an instrument of state policy, primarily to serve the credit needs of agriculture, considerable resources by way of refinance were provided to it to enable it to do so. Savings from the impoverished rural areas, at that stage of the country's development, would not have been able to meet even a small part of the credit needs. In the process unfortunately, the philosophy of thrift and savings got de-emphasised. It was as though the starting point had faded away. Under these circumstances, as there was pessimism about the mobilisation of savings, dependence came to be on the higher financial institutions, the district central co-operative banks, the state co-operative banks and the RBI, now replaced by NABARD for co-operative and other refinancing. Under these conditions, co-operative institutions ceased to be an example of horizontal self-reliance but came to be a case of vertical dependence. The philosophy and the strategy of local resource mobilisation hardly came into its own.

5.29 The effects of this non-self-reliance on the part of the co-operatives in general and the PACSs in particular have been far-reaching and regressive. Barring exceptions here and there, the co-operative system either lost its resilience or in most cases never acquired it in the first place. As dependence came to be on vertical financing and refinancing by higher institutions like the SCBs, the RBI/NABARD and the government, the members of the co-operatives seldom thought of the funds as their own assets but more often than not regarded these as government funds. The interest they would have taken in their own institutions, the democratic control they would have exercised on the use, recovery and nurturing of the funds and the check they would have brought to bear on the functionaries of the co-operatives, all ceased to exist. Neither effective lending, nor speedy recovery nor profitability came to be insisted upon. The members became disinterested parties or permitted colossal inefficiencies. The other effect of the vertical dependence of co-operative institutions was an encroachment on their territory by higher institutions and the governments and thereby hangs a tale. These interferences are many, as

we have listed later, and range from vetos of local decisions to supercessions of whole network, from directives by Registrars to making the co-operative secretaries and managers responsible to non-co-operative organisations and governments. Such institutions have also brought in their wake, political interferences of several sorts. The non-responsibility of the secretaries and managers to the co-operatives further created a lack of interest by the members in their own institutions. The cumulative and self-reinforcing negative effects of all these factors made the co-operatives a mediocre, inefficient and static system.

Deposit Mobilisation Vital to Self Reliance

5.30 There is a distinct change now in the savings scenario. In recent years, it has been noticed that the Indian rate of savings has risen from 10 per cent in 1951 to more than 23 per cent in 1983 and is still as high as 22 to 23 per cent. Such a high rate is an envy of many a developing country which have far lower rates. Moreover about 17 per cent out of this 23 per cent rate of saving comes from the household sector, and that includes the rural and agricultural households in a substantial measure. Saving, therefore, is ceasing to be a real bottleneck today.

5.31 Thus at present in India it is not as though savings in rural and agricultural areas are not available. Only a shift of strategy is required in order to divert local savings into the co-operative system. The day has certainly come for the system to give itself a goal and develop a method of mobilising local resources in a big way. Techniques of mobilisation have to be sharpened and the agents for this mobilisation have to be trained and put in position. Such mobilisation of local resources will reduce the dependence of the co-operatives on higher institutions on the one hand, and on the government on the other. Co-operation will then begin to come into its own.

5.32 The point of significance is that if co-operative institutions like the PACSs begin to work on the deposits of local people rather than on resources lent by the government and higher institutions, the savers and the depositors, i.e. the members of the co-operative system will get more concerned about the safety of their deposits and will keep a critical eye on lending and recovery. At present, in the belief that the resources are coming from the government

and other institutions, the members are seldom concerned and do not exercise their democratic right to keep the lending and the recovery in check. The whole system will become more dynamic and self-assertive, if the local deposits were to be the starting point of the lending and the recovery process. Thus the first and the primary improvement that we suggest in the co-operative credit system is to openly shift the emphasis on local savings mobilisation.

Re-emphasis on Savings Deposits

5.33 There is much scope for mobilising small savings in savings bank accounts by PACSs. Bulk of the people in rural areas, who at all have savings, only have small savings. Such people are likely to be concerned more with the ready "accessibility" and "liquidity" of their banked savings rather than with higher interest income and would, therefore, be inclined to put their savings in savings bank accounts in preference to term deposits which offer higher rates of interest. Mobilisation of savings through savings accounts from as large a number of persons as possible will undoubtedly call for much greater effort by the PACS. The workload of managing the large number of accounts which will be frequently debited and credited would also be more than if there were to be mainly a few term deposits. But the needed effort must be made in consonance with the basic philosophy of the credit co-operatives to promote thrift and savings. Further more, from the point of view of the viability itself, savings deposits have very beneficial implications for the PACS. As the existing margins between deposit rates and lending rates are very narrow and the operational costs are high owing to lack of scale economies and overdues etc., the system often runs into losses and hence does not expand. In order to widen the margins, it is essential that in deposit mobilisation greater emphasis be placed on securing bulk of deposits by way of savings bank accounts with a relatively lower interest of 5 to 6 per cent rather than of deposits on which higher interest rates going up to 10 per cent or more are paid. It would be better to keep the weightage of these other deposits with high rates relatively small. The effect of this would be to reduce the outgo on account of interest payment and hence to increase the margins of co-operative business and enhance its profitability, besides generally inculcating the savings habit in the members.

5.34 There is another significant point in favour of this strategy. As the interest paid on small savings is smaller than the interest on loans refinanced

by the higher institutions, a shift of emphasis from vertical refinancing to horizontal small savings mobilisation, is also a shift from a higher to lower interest paid and hence a shift from a lower to higher margin of business. Moreover, we are concerned with what will happen to co-operatives if government or the RBI or NABARD, as a consequence of budget constraints, have to diminish refinancing. Then no or insufficient funds would be available with the co-operatives to lend and the whole system will be under great constraint, at best and in danger of collapsing at worst.

5.35 A strategy focussed initially on deposit mobilisation will also free the co-operatives from an overdependence on governments and from subjection to excessive conditionalities generally imposed by governments. Thus, from whatever angle we look at the matter, a renewed emphasis on deposit mobilisation would seem to be inevitable.

Officialisation of the Co-operative Credit System

5.36 A consequence of the absence of self reliance and dependence on the higher tiers and government has been that over a period of time, the state has gained considerable financial stake in the higher level organisations through participation in the equity and in many other ways. In turn, this has been made use of as an alibi for gaining control over the co-operatives. Thus, irrespective of the political persuasions of the party in power, in the last two decades it has been a story of collective supersessions of co-operatives at all levels and in place of democratically elected management, government officials, or non officials nominated by the government manning them - the lower grade officials, the lower level co-operatives and the more senior level officials the higher tiers of co-operatives. Consequently at the district and state and at the national level, the federations which have been organized for assisting the lower level co-operatives to become more democratic and fostering mutual co-operation among co-operatives, have virtually become federations of Assistant Registrars at the lower level, federating into federations of Deputy Registrars and they in turn federating into one of Registrars or equivalent officials as the national level federations. Even where supersession has not taken place, the show is managed by invoking powers of the government and deferring of elections. In the result, co-operative federations have virtually become a government

directed, government controlled and government regulated enterprises. The inroads into the co-operative federalism and self-government have been possible through officialisation largely on account of the progressive intensification of powers vested in the government and through the abuse of these powers. One example may be cited, wherever massive supersessions of co-operatives have taken place, it often has been through the exemption clause in the relative Act. There is a clause in every Act which vests in the government the right to exempt an action from the purview of the normal provisions of the Act. It is through invoking this exemption that the governments have short-circuited the normal procedures for supersession and to foist on them government officials or the political proteges of the party in power as administrators of co-operatives.

5.37 Even otherwise, the control which vests in the government under the law is so over-riding and complete that even for a minor decision such as declaration of dividend, the society requires prior approval of the Registrar of Co-operative Societies. The law again vests in the government, the power to withhold elections. In many states the government has been vested with the power to nominate the chairman and managing director of a co-operative even when a society has a fully elected board. And above all, the government nominees in the Board have been vested with the power to veto any decision of the Board, not to speak of the power in the government even otherwise to annul any proceedings of the committees or sub-committees of the society. The government can issue directives to the co-operatives to act in a particular manner or not to do certain things. The provisions of the Co-operative Acts, intended solely to prevent malfeasance in individual cases, and that too by the due process of law are today being misused to gain control over these democratic institutions. Several Committees, which have looked into this growing phenomenon have recommended measures to eliminate it, but no worthwhile action has been taken on these. In our view it is high time that these powers to regulate and intervene where situation warrants are vested in the higher tier co-operatives.

5.38 Earlier in this Chapter, we have recommended the vesting of the powers of government in regard to organisational matters with the higher organisation. This as we have suggested, should include the power to convene the general body meetings of PACSs if the managements of the societies are not functioning properly and advise the general meeting about the corrective action

to be taken. Where supersession becomes absolutely necessary and interim administration has to be taken over till a new managing committee is elected, the power to appoint the administrator should vest in the DCCB and the term of the administrator should not exceed six months. Similar powers if any to be exercised over DCCBs will vest in the SCB. Likewise, the functions as regards institutional promotion of primary co-operatives will also be that of DCCBs and of DCCBs with SCB and so on and not of the Registrar of Co-operative Societies.

Politicisation in the Co-operatives

5.39 If the progressive officialisation of the co-operatives making them totally government directed organisations have distorted the principles of self-government and federalism in co-operatives, their politicisation in the last few decades has caused even greater damage to the system. The CRAFTICARD in their report emphasised the need for depoliticisation of the co-operative credit system. Similarly, the Venkatappiah Committee in their report on the Role of National Co-operative Societies recommended depoliticisation of co-operatives. In both the cases the term depoliticisation has been used with reference to the management of the institutions. Referring to the need for such depoliticisation in the national federations, the Venkatappiah Committee has quoted the view expressed in this connection by the then Prime Minister (Pandit Jawaharlal Nehru) during his address at the Sixth Co-operative Congress where he spoke of the 'widespread feeling that co-operators in India are too much mixed up with politics'. The Prime Minister also advised that steps should be taken to depoliticise the movement.

5.40 The need for depoliticisation of the co-operatives cannot be too strongly over emphasised because by their very nature and objects they are basically apolitical. But efforts at gaining control over the co-operatives by politicians, have over the years become quite perceivable and their infiltration has come to be strongly felt. Politicisation has not confined itself to management area, it extends to the conduct of the business also. One clear example of this in the co-operatives which has been referred to in the CRAFTICARD Report is the general write off of co-operative dues resorted to by state governments.

5.41 Co-operatives being democratic organisations, it needs to be recognised that their membership cannot be totally insulated against their political persuasions. Consequently, neither the entry of politicians into the ranks of co-operative leadership nor the emergence of non-official co-operators as political leaders in themselves need be construed as an altogether undesirable development but what needs to be guarded against is that decisions concerning the conduct of the business of the co-operatives are not taken on political considerations. In other words what would be open to objection would be the temptation to use co-operatives as instruments for promoting political interests, because when this happens it spells danger to the functioning of co-operatives and their main objective, viz., pursuing the economic interests of their members in the process gets lost.

5.42 Where there are rival political groups at the village level, politicisation in its elementary form manifests itself in the domination of co-operatives by one group which often results in serious distortions in the credit disbursement and recovery process. Groupism and rivalries in different political parties are likewise, reflected in the party-wise panels contesting the elections of the co-operative societies/banks, largely on political considerations. At the higher level, it is not an unusual experience to see the fortunes of co-operatives administered/managed by a group belonging to a particular political party, suffering serious setbacks when another party comes to power in the state. A phenomenon observed of late, is that close to general elections to the state legislative bodies or Parliament, several state governments show not only total indifference to effecting recovery of co-operative dues and totally bar coercive measures, but also exhort people, from political platforms, not to repay their co-operative dues. There have also been instances, (as in Haryana recently), where the election manifestos of political parties contained promises to write-off co-operative dues, as a bait to voters. About a decade ago, under more or less similar circumstances, Government of Maharashtra wrote off co-operative dues to the extent of about Rs.50 crores. Similarly, Government of Tamil Nadu had written off Rs.57 crores. No doubt, a government measure such as write off may not put the credit system into any loss because the government concerned makes good the amount, but the Reserve Bank of India and Government of India have taken serious exception to such measures by state governments, because it generates a general psychology of non-repayment, totally vitiating the recovery

climate which besides putting the state exchequer to avoidable financial burden is in the long run likely to jeopardise the financial interests of credit agencies.

5.43 One contributory factor to greater politicisation in recent times has been the incorporation of certain provisions in the Co-operative Societies Acts of various states and Rules framed thereunder. Till the early fifties, the provisions in the Co-operative Societies Acts were largely confined to registration, amalgamation, winding up and management structure etc. of the co-operative societies, more or less on the lines of those in the Companies Act, except for provisions relating to one member one vote etc. But this position changed considerably with the introduction of the policy of state partnership in the share capital of co-operatives and consequential state participation in their management, recommended by the All India Rural Credit Survey Committee (1954). Although the Survey Committee's intention was that with state partnership, and consequent sharing of risks of business, not only the financial strength of co-operatives will be enhanced, but this will also be a confidence booster to the clientele of co-operatives. It was also envisaged that the Government share capital would be gradually repatriated over a period of time. On the question of government control, the Committee was altogether opposed to such control. In fact in order to ensure that such control was not exercised that the Committee provided only for not more than a third of the managing committee being nominated by government. It also did not interfere with the one-member one-vote principle although government contribution to share capital was envisaged at 50 per cent of the total share capital.

5.44 Paradoxically, however, state partnership which was conceived, as already stated, as a measure for strengthening the co-operative credit institutions, had paved the way instead for ever-increasing state control over co-operatives, their increasing officialisation and politicisation culminating in virtually depriving the co-operatives of their vitality as well as their democratic and autonomous character. Over a period of time they have been made fully dependent on the state governments and reduced to the position of being merely a tool in the hands of the political and administrative functionaries of the state. No wonder that in the prevailing situation the state governments are still looked up to, to provide further share capital contribution and other financial assistance for reviving the 'weak' credit co-operatives, not to speak of repatriation of

government share capital which is only a distant possibility in the case of most of the credit co-operatives. In the circumstances, the restoration of the autonomy in co-operatives now depends entirely on the extent to which it (the state government) is willing to give up the powers it has acquired over the co-operatives.

5.45 Another area where there has been progressively increasing politicisation is in the determination of interest rates on considerations other than financial, that is to say, with an eye on populist appeal. One example could be cited; there has of late been a growing tendency to progressively reduce interest rates on certain types of loans, to an extent that the credit system increasingly finds it difficult to compensate itself for the losses on account of such lending, from the higher returns on those lendings which carry a higher rate. The reduction in the interest rate of crop loans across the board recently is one example under which the national apex institution, viz., NABARD, itself is in effect left with no margin at all affecting its viability in the long run. What is worse is a considerably low rate of interest not justified by the state of the economy which results in beneficiaries equating the loans more or less with grants from government. In its turn, this psychology results in an all round delinquency in the repayment of loans.

5.46 It needs to be recognised that politicisation has led to damaging results on the credit institutions as the CRAFTCARD had also pointed out in their Report. Unless this is recognised and there is awareness at the highest levels in government that politicisation of the co-operative system is fraught with serious danger to the capability of the co-operatives to function effectively in the long run and survive in a reasonably healthy state, there is a clear danger that politicisation would not only destroy the system but may defeat even the purpose for which it is resorted to. As experience of last two decades has shown, politicisation has assumed such serious proportions that it has in itself become the bane of the agricultural credit system in general and co-operative system in particular. We are convinced that the time has come to reverse this process.

Recapturing the Co-operative Spirit

5.47 The net outcome of all these factors and in particular, the politicisation, officialisation, mass supersessions, low margins and lack of professionalisation

in the managerial infrastructure at all levels as an inevitable consequence of excessive officialisation, in the co-operative banking system has been to import a great deal of inefficiency, high costs, low or negative profitability, inefficient service and non-self-reliance in the co-operative organisations especially at the level of the PACSs. It is thus necessary that the country recaptures the spirit of co-operation, its culture, its discipline and above all, its ethos and this cannot be achieved unless a mutually supportive and cohesive structure based on a strong foundation at the primary level drawing support and inspiration from the higher tiers which are professionally managed under a dynamic and highly motivated leadership comes to be established.

5.48 In the chapters which follow, we proceed to discuss in detail the working of the various segments of the co-operative credit structure and their strengths and weaknesses as well as measures to overcome the weaknesses so that a strong and dynamic co-operative credit system is developed in the country.

CHAPTER VI

SHORT-TERM CO-OPERATIVE CREDIT STRUCTURE

The co-operative system in the country, though federal in its organisational structure is integrated vertically on the basis of functional responsibilities of the various components of the system. The short-term co-operative credit structure has at its base, the primary societies of all kinds, viz., the primary agricultural credit societies (PACs) which are expected to be multi-purpose in character but in a large number of cases deal mainly in credit, the farmers service (co-operative) societies generally referred to as FSSs which are, in fact, multi-purpose primary societies but with a larger area of operation and larger membership, large-sized adivasi multi-purpose societies in tribal areas known popularly as LAMPSs, urban co-operatives such as the urban co-operative banks and employees credit societies in large organizations of different kinds, all federated into district central co-operative banks (DCCBs) at the district level, which in turn are federated into the state co-operative banks (SCBs) at the state level, known popularly as the apex banks. As on 30th June 1986, there were 92,408 primary agricultural credit societies, 352 district central co-operative banks and 31 state co-operative banks supplying short-term and medium-term agricultural credit. Their coverage extend to remotest parts of the country. They have come a long way since the first primary co-operative society was set up in 1904. They have over the years played a very significant role in making institutional credit accessible to the farmers, and were, indeed, till about the early seventies, the only institutional credit agency available to the farmer. Though themselves nascent, they managed to hold their ground against the established power structure, of which the money lender was an integral part, during these early decades of country's independence and steadily widened the clientele of production credit for agriculture. If in the earlier period they attended more to the needs of the comparatively larger farmer, it was because the extension agency itself was at the stage directed more towards this class of farmers to achieve quicker results in food production. It was again these co-operatives which provided the vital credit support to the new agricultural technology, the so called "green revolution", in its early dynamic years. Even today they continue to occupy the leading position in the sphere of production finance, despite

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the very strong presence that the commercial banks have now come to acquire in the rural areas with their vastly larger resources. Nevertheless, while recognising the role played by the co-operatives in the cause of the agricultural community, one cannot remain oblivious to their weaknesses - weaknesses which would in course of time prove fatal to them in a severely competitive environment. They do not in general seem to be showing the will or the inclination to re-shape their horizon and goals to cope with the changed context. There has been an upward trend in overdues in the last few years and consequently their borrowing membership is declining. Management continues to be an area of serious weakness. Undoubtedly, the blame for all their weaknesses cannot be placed at their door alone. While some weaknesses are internal to them, many others flow from the dictates of external agencies which are for ever controlling and regulating them, and from the larger socio-political environment in which they are working. These factors have been discussed by us earlier. At this stage we consider it germane to take a close look at the performance of the various tiers of the short-term co-operative credit system with a view to identifying the principal operational shortcomings and devising measures for strengthening the delivery system. Indian agriculture has a vital stake in the success of the co-operatives because we believe that there is no better or more responsive and cost effective credit system than the co-operatives to serve the ever growing and diversifying needs of agriculture.

6.002 For the purpose of review of progress, we have used the data furnished in the Statistical Statements relating to Co-operative Movement in India which give comprehensive details on the business of co-operative credit societies (published for the year upto 1981-82), the data on credit and non-credit co-operatives - important items, (published by NABARD upto the year 1985-86) and also the basic data on performance of DCCBs (published by National Federation of SCBs for the year 1984-85 and 1985-86). The last publication gives a more detailed break-up of data on DCCBs as compared to the important items of data published by NABARD for the same period. The review has been made on an All India basis for a period of 10 years from 1975-76 to 1985-86 with state-wise analysis wherever necessary and feasible. The data furnished in the study reports I and II of our consultants on the basis of their field studies have also been made use of.

A. Primary Agricultural Credit Societies (PACs)

6.003 Table 1 below gives at a glance certain vital statistics relating to PACs over a ten year period.

Table 1
Progress of PACs

Sr. No.	Particulars					(Rs. crores)
		1975-76	1983-84	1984-85	1985-86	Annual Growth rate during 1975-76 to 1985-86 (per cent)
1.	Number	1,34,838	92,496	91,749	92,408	
2.	Societies with full time paid Secretaries	58,628 (43.5)	N.A.	68,224 (74.3)	N.A.	
3.	Membership (in '000)	39,521	66,669	69,182	72,117	6.19
4.	Borrowing membership during the year (in '000)	17,851 (45.2)	22,470 (33.7)	21,649 (31.3)	19,657 (27.3)	0.96
5.	Own resources					
	a) Share Capital	327.31	720.75	778.66	831.54	
	b) Reserves	109.55	235.81	255.60	296.08	
6.	Deposits	113.31	463.93	524.06	571.98	17.57
7.	Borrowings	1,154.44	3,163.73	3,743.12	3,927.22	
8.	Total Loans and advances outstanding	1,299.21	3,498.19	3,980.65	4,323.20	
9.	Loans issued	1,023.44	2,499.31	2,693.01	3,140.37	11.86
10.	Overdues	560.51	1,574.65	1,630.25	1,806.08	12.41
11.	Percentage of overdues to demand	41.4	43.6	41.6	41.8	
12.	Profit making Societies					
	a) Number	78,328	N.A.	51,878*	N.A.	
	b) Percentage to total	58.1	-	56.5	-	

Data for the years 1983-84, 1984-85 and 1985-86 provisional.

Figures in brackets shows percentage to the total number of societies and membership respectively.

* Data for 1982-83

Source : Statistical statements relating to Co-operative Movement in India.
Data on Credit and Non-Credit Co-operatives - Important Items.

As a result of the reorganisation of societies undertaken during the period 1975-76 to 1985-86, the total number of PACSs has decreased from 1,34,838 to 92,408. They covered 5.71 lakhs villages* or 98.2 per cent of the total number of villages in the country. The average coverage per society was 6 villages for the country as a whole, and ranged from 3 in Gujarat, Haryana, Tamil Nadu, 17 in Uttar Pradesh and Madhya Pradesh, 22 in Tripura, 27 in Meghalaya to 171 in Arunachal Pradesh. The total membership of PACSs increased from 39.5 millions in 1975-76 to 72.1 millions in 1985-86. The membership of PACSs has been growing every year because of membership drives from time to time. The growth has been seen even in PACSs where overdues are very high and the scope for fresh lending is very limited. The annual growth rate of membership of PACSs during the last 10 years was 6.2 per cent. The case studies conducted at our instance have revealed that in many PACSs more than one person from the same family have been enrolled as members. Non-farmers have also become members of PACSs in large numbers for various reasons. This is particularly seen in Assam, Haryana, Madhya Pradesh, Maharashtra and Tamil Nadu. The membership of PACSs includes more than ten per cent belonging to Scheduled Castes and six per cent belonging to Scheduled Tribes on an All India basis. The average membership per society increased from 293 in 1975-76 to 780 during 1985-86, though in many states it is much lower, e.g. in Gujarat (288) and Maharashtra (351), where PACSs have still not been reorganised on viability basis, in Himachal Pradesh (336), Jammu & Kashmir (394), Manipur (264), Arunachal Pradesh (368) and Sikkim (389) where density of population is low, and West Bengal (352), etc.

Borrowing Membership

6.004 Although there is a substantial increase in the total membership of PACSs, the borrowing membership i.e. the number of members borrowing from the society during the year concerned has shown a mixed trend increasing from 17.8 millions in 1975-76 to 22.5 millions in 1983-84, thereafter declining to 21.6 millions during 1984-85 and 19.6 millions in 1985-86. The average growth rate of borrowing membership during the last 10 years was only 0.9 per cent. This does not compare favourably with the annual rate of growth of total membership during the same period at 6.2 per cent. The percentage of borrowing membership to the total membership had shown a steady decline from 45.2 in 1975-76 to 27.3 in 1985-86. In 1985-86, the borrowing membership, as a percentage of total membership, was below the All India percentage

* Data relate to 1981-82

at 27.3 in several states as may be seen from the examples given below :

<u>State</u>	<u>Percentage of borrowing membership to total membership</u>
Assam	14
Andhra Pradesh	24
Karnataka	16
Maharashtra	26
Bihar	20
Orissa	17

Madhya Pradesh and West Bengal had 29 per cent borrowing membership to total, Kerala and Haryana had achieved 49 per cent and 46 per cent respectively, and in Punjab their proportion was above 60 per cent.

6.005 The state-wise position of membership and borrowing membership during the last five years is given in table 2. It will be observed that although the total membership has generally increased over the last five years, in Andhra Pradesh and Assam it has shown a declining trend (the latest data available for Assam related to 1983-84). In the case of Gujarat, although the total membership increased from 18.27 lakhs to 22.17 lakhs as at the end of 1984-85, it declined to 19.72 lakhs by the end of 1985-86. The reasons for reduction of membership can be attributed to the stagnancy of the co-operative credit structure in Assam and availability of other avenues for borrowing under the multi-agency system for agricultural credit. The borrowing membership during the last five years has shown a mixed trend. In the states of Bihar, Haryana, Orissa, Rajasthan, Tamil Nadu and Uttar Pradesh, there was a declining trend. In Karnataka and Madhya Pradesh although there was an increase in the borrowing membership from 1981-82 to 1983-84, it has declined thereafter. The high level of overdues ranging from 30 to 66 per cent in these states has drastically curtailed the eligibility of a large number of members from fresh borrowings and this has probably caused the decline in the number over these years.

6.006 The very slow growth in the proportion of the borrowing members in the last decade, and in some states a net decline in the same, is a phenomenon which seems to transcend to some extent the internal weakness of

Table 2
Membership and Borrowing Membership of PACSs

(In thousands)

STATE	Total membership as at the end of the year				Borrowing membership during the year			
	1981-82	1983-84	1984-85	1985-86	1981-82	1983-84	1984-85	1985-86
Andhra Pradesh	7,988	7,998 [●]	7,604 ⁺	7,522 ⁺⁺	1,655(20.69)	1,655 [●] (20.69)	2,659 (34.97)	1,746 (23.88) ⁺⁺
Assam	2,318	2,218	2,218 ⁺	2,218 ⁺	39(1.68)	302 (13.62)	302+(13.62)	302+(13.62)
Bihar	5,662	5,806	5,818	5,824	2,719(48.02)	2,809 (48.38)	2,810 (48.30)	1,190 (20.43)
Gujarat	1,827	2,003	2,217	1,972	701(38.37)	745 (37.19)	770 (34.73)	782 (39.66)
Haryana	1,196	1,291	1,356	1,384	651(54.43)	687 (53.21)	714 (52.65)	641 (46.32)
Himachal Pradesh	625	673	692	709	109(17.44)	113 (16.79)	249 (35.98)	120 (16.93)
Jammu & Kashmir	417	417*	N.A.	N.A.	164(39.33)	164*(39.33)	N.A.	N.A.
Karnataka	3,801	3,250	4,074	4,412	627(16.50)	717 (22.06)	714 (17.53)	688 (15.59)
Kerala	4,667	5,172	5,171	5,767	1,621(34.73)	2,461 (47.58)	2,120 (41.00)	2,807 (48.67)
Madhya Pradesh	3,935	4,500	4,572	5,023	1,297(32.96)	1,445 (32.11)	1,400 (30.62)	1,420 (28.27)
Maharashtra	5,586	5,883	5,950	6,450	1,557(27.87)	1,560 (26.52)	1,575 (26.47)	1,650 (25.58)
Orissa	2,419	2,747	2,826	3,149	627(25.92)	860 (31.31)	784 (27.74)	540 (17.15)
Punjab	1,733	1,756	1,764	1,772	1,044(60.24)	1,086 (61.85)	1,089 (61.73)	1,090 (61.51)
Rajasthan	3,602	3,737	4,140	4,289	1,496(41.53)	1,362 (36.45)	1,431 (34.57)	1,435 (33.46)
Tamil Nadu	5,330	5,676	6,334	7,052	2,380(44.65)	2,569 (45.26)	1,701 (26.86)	1,792 (25.41)
Uttar Pradesh	9,062	10,092	10,795	10,953	3,040(33.55)	2,984 (29.57)	2,585 (23.95)	2,328 (21.25)
West Bengal	2,391	2,823	2,771	2,720	730(30.53)	762 (26.99)	508 (18.33)	802 (29.49)
All India Total	63,171	66,669	69,182	72,117	20,520(32.48)	22,470 (33.70)	21,649 (32.74)	19,657 (27.26)

● Data relate to 1981-82

* Data relate to 1982-83

+ Data relate to 1983-84

++ Data relate to 1984-85

Figures in bracket show percentage of borrowing membership to total membership

Source : Important Items of Data on Credit and Non-Credit Co-operative Societies.

the co-operatives. Undoubtedly, the high delinquency rate in recovery of loans has depressed the growth of borrowing membership and will continue to so affect it till the channels of credit recycling are unclogged by better recovery performance. Nevertheless, the data thrown up by the decennial All India Rural Debt and Investment Surveys and other studies also reveal that while there has been a very significant shift of borrowers from non-institutional to institutional sources of credit, there has been no significant enlargement in the proportion of borrowers. In other words, the widening of credit has not taken place, at the desired rate. One reason for this could be that the absorption capacity of credit still continues to be poor because the bulk of the cultivated area is unirrigated. This is partly due to lack of availability of superior agricultural technology for a wider spectrum of crops and partly due to the weaknesses of the agricultural extension agencies. Where agro-climatic conditions are more stable, more particularly where irrigation is available, the proportion of members' borrowing is also generally larger.

Share Capital

6.007 It may be seen from table 1 that the total paid up share capital of PACSs increased from Rs.327.3 crores in 1975-76 to Rs.831.54 crores in 1985-86 showing an annual growth rate of 9.8 per cent. The average of owned funds per society which was Rs.0.32 lakh during 1975-76 increased to Rs.1.22 lakhs during 1985-86. However, when seen state-wise, there are wide variations with West Bengal (21,240), Bihar (25,277), Manipur (12,846), Nagaland (9,060), Meghalaya (45,555), Assam (40,098) and Andhra Pradesh (89,575) having an average share capital much less than the all India average. The other major states like Gujarat, Haryana, Punjab, Karnataka, Orissa, Rajasthan and Uttar Pradesh are having an average share capital of more than the all India average of Rs.1.22 lakhs but less than Rs.2 lakhs. Punjab and Kerala had an average of Rs.2.16 lakhs and Rs.5.59 lakhs respectively. The government contribution to the share capital amounted to Rs.135.1 crores, averaging about Rs.14 to 15 thousand per PACS. The government share capital contribution in some states averaged to more than Rs.20,000 per society. While it was more than Rs.44,000 per society in Kerala, in Assam due to merger of societies to form Panchayat level societies, the government contribution has gone up to the extent of Rs.60,000 to Rs.70,000 in respect of these societies.

6.008 Besides the share capital contribution by the state government, the main accrual to the share capital of a PACS is from its members through a linkage of share capital with the loan advanced. In other words, the share capital of a member determines his borrowing power. The ratio required is generally 1:10. However, in the case of the weaker sections of the community the ratio of share capital requirement is five per cent. A majority of the membership of the PACSs is from these sections. Moreover, what is somewhat harsh on the PACSs is that they are required to invest almost the entire share capital collected from their members in the shares of higher financing agencies.

Deposits

6.009 The vast bulk of PACSs had very little to show by way of deposit mobilisation except in a few states. The average deposits of PACSs as on 30 June 1986 in the major states are given below in table 3.

Table 3
Average Deposits of PACSs

State	No. of Societies	Total Deposits	Average Deposits per Society
		(Rs. crores)	Rs.
1. Andhra Pradesh*	7,051	15.25	21,628
2. Bihar	6,757	0.44	651
3. Gujarat	6,839	18.92	27,665
4. Haryana	2,339	4.62	19,752
5. Karnataka	4,911	12.25	24,944
6. Kerala	1,574	325.69	20,69,186
7. Madhya Pradesh	5,573	13.70	24,582
8. Maharashtra	18,374	14.50	7,891
9. Orissa	2,796	4.30	15,379
10. Punjab	3,058	31.32	1,02,420
11. Rajasthan	5,267	9.74	18,492
12. Tamil Nadu	4,674	51.05	1,09,220
13. Uttar Pradesh	8,601	41.40	48,134
14. West Bengal	7,719	5.13	6,645
All India	92,408	571.98	61,897

* Data relate to 1984-85

The averages, however, by no means represent the general effort in deposit mobilisation of that order by most PACSs in a given state. It is the effort of a few which has been averaged out for all. Most societies were not even conscious of their role as promoters of thrift and had made no efforts for deposit mobilisation. Kerala, of course, is a class apart, and the average of Rs.20.69 lakhs truly reflects the high level of performance in this respect by all PACSs. Next in line, though much below Kerala, come Tamil Nadu, Punjab, Uttar Pradesh, Gujarat and Karnataka which have a reasonably wider spread with average deposits of Rs.1.09 lakhs, 1.02 lakhs, Rs.0.48 lakh, Rs.0.27 lakh and Rs.0.25 lakh respectively. In other states the effort was restricted to a small number of PACSs. The total amount of deposits of PACSs in the country as on 30.6.1986 was Rs.572 crores of which Rs. 325.7 crores were with PACSs in Kerala alone and Rs.123.8 crores with PACSs in Tamil Nadu, Uttar Pradesh and Punjab. A reason often cited for PACSs not mobilising deposits is that they do not have the appropriate infrastructure of an office building, strong room and deposit counters etc. for want of resources. Many, of course, do not even have one whole time person who could handle this nature of banking service on a regular basis.

Loans and Advances

6.010 The total loans issued by PACSs increased from Rs.1,023 crores in 1975-76 to Rs.3,140 crores in 1985-86 of which Rs.2,747 crores were for short-term purposes and Rs.394 crores were for medium-term purposes. The total loans issued had shown an annual growth rate of 11.8 per cent during the past 10 years. The average loan business of PACSs in principal states as on 30th June 1986 is given below :

Table 4

Statewise Average Loan Business of PACS

(Rs. lakhs)

<u>Name of State</u>	<u>Average loan business</u>
Andhra Pradesh	3.94
Assam	0.40
Bihar	0.93
Gujarat	5.42
Haryana	8.46
Karnataka	4.87

<u>Name of State</u>	<u>(Rs. lakhs)</u> <u>Average loan business</u>
Kerala	33.22
Madhya Pradesh	5.68
Maharashtra	3.64
Orissa	5.89
Punjab	7.93
Rajasthan	5.03
Tamil Nadu	8.19
Uttar Pradesh	4.96
West Bengal	1.63

It will be observed that the average loan business of PACSs in Kerala was Rs.33.22 lakhs while PACSs in Tamil Nadu, Haryana, Punjab, Orissa, Madhya Pradesh, Gujarat and Rajasthan had an average loan business ranging between Rs.5 lakhs to Rs.10 lakhs while in the other states the PACSs had average loan business of less than Rs.5 lakhs. The PACSs in Assam, Bihar, West Bengal had very low average loan business. Although the average loan business may not reveal the actual position of the majority of the PACSs in the state, it will indicate the comparative position of societies between different states. The co-operatively well developed states of Maharashtra, Andhra Pradesh rank below Orissa, Madhya Pradesh and even Rajasthan in respect of the average loan business of PACSs. One of the reasons for this poor loan business of PACSs in Maharashtra and Gujarat is that reorganisation of PACSs has not been taken up in these states as envisaged by the Government of India and Reserve Bank of India.

6.011 The norm of viability for PACSs was laid down at Rs.2 lakhs loan business as early as in 1973 by the Working Group on Co-operation for the Fifth Five Year Plan. The Reserve Bank of India had issued detailed guidelines for a programme of reorganisation of PACSs on the basis of this norm through a process of amalgamation of the large number of primary credit societies then existing into viable/potentially viable units. The programme was implemented in all states with the exception of Maharashtra, Gujarat, Jammu & Kashmir. Some state governments had laid down even higher loan business say Rs.3 lakhs (Haryana), Rs.5 lakhs (Punjab and Uttar Pradesh) and Rs.6 lakhs (Kerala) as a norm for viability. This norm itself needs to be revised in the changed context of interest margins and operational costs. However, even

after a period of 10 years since the state governments had taken up reorganisation of PACSs, a large number of PACSs continue to have a loan business of even less than Rs.2 lakhs. For example, in Andhra Pradesh where the reorganisation was completed by 1978, the societies having loan business of less than Rs.2 lakhs in 3 districts studied by the state level task force on integration of co-operative credit structure in 1985-86 numbered 493 and formed 55.9 per cent of the total number of reorganised societies as on 30th June 1985. The details are given below :

**Classification of Societies According to
Short-term Loans Outstanding as on 30.6.1986**

	<u>Guntur</u>	<u>Nizamabad</u>	<u>Anantapur</u>
i) Less than Rs.1 lakh	90]	16]	248]
ii) above Rs.1 lakh and below Rs.2 lakhs]45.7 79]per cent]19.7 24]per cent]92.2 36]per cent
iii) above Rs.2 lakhs and below Rs.3 lakhs	58	19	11
iv) above Rs.3 lakhs and below Rs.5 lakhs	55	31	5
v) above Rs.5 lakhs and below Rs.10 lakhs	57	66	5
vi) above Rs.10 lakhs	<u>31</u> <u>370</u>	<u>47</u> <u>203</u>	<u>3</u> <u>308</u>

6.012 The statewise position of loans issued by PACSs per hectare of total cropped area is indicated in table 5.

**Table 5
Loans Issued per Hectare of Gross Cropped Area**

<u>State</u>	<u>1975-76</u> Rs.	<u>1985-86</u> Rs.
Haryana	7.65	364.31
Himachal Pradesh	5.98	156.95
Punjab	10.74	524.30
Rajasthan	3.16	82.57
Assam	N.A.	10.03
Manipur	2.28	21.73
Tripura	1.35	28.00
Bihar	2.14	31.63

Table 5 (contd.)

<u>States</u>	<u>1975-76</u> Rs.	<u>1985-86</u> Rs.
Orissa	2.16	60.58
West Bengal	2.71	93.54
Madhya Pradesh	3.07	119.64
Uttar Pradesh	3.79	107.88
Gujarat	12.72	280.86
Maharashtra	8.04	173.92
Andhra Pradesh	5.48	173.09
Karnataka	7.11	138.47
Kerala	16.41	1,294.16
Tamil Nadu	14.8	363.31

Although the above averages have been arrived at by dividing the total loans given by the total hectareage cultivated in the state, whether all the members were borrowers or not, it all the same shows that loans per hectare issued in most of the states were very low even against the background of considerable increase in the scale of finance during the ten year period. The scales of crop loans per hectare for principal crops, fixed often on ad hoc basis, ranged between Rs.1,000 to Rs.3,000 per hectare. Only states such as Punjab and Kerala had issued somewhat reasonable amounts per hectare but in all other states the gap in the credit requirements and the actual loans advanced continues to be very wide. The scales of finance for paddy and wheat per hectare in some of the sample districts visited by our consultants are as under :

<u>Name of District</u>	<u>Scale of finance</u> Rs.
Anantnag (J & K)	1,100
Kangra (HP)	1,850
Birbhum (WB)	2,306
Faridkot (PJB)	2,500
Gorakhpur (UP)	3,000
Ranchi (BHR)	3,720
Nanded (MHR)	1,752
Raichur (KTK)	2,541

Overdues

6.013 The overdues of PACSs increased from Rs.560.5 crores in 1975-76 to Rs.1,806 crores during 1985-86. The percentage of overdues to demand, however, remained around 41 during the 10 years under review except that there was a marginal increase during 1983-84 at 43.6 per cent. High delinquency rate in recovery of loans is the key retarding factor in both, the widening and the deepening of credit by the PACSs. A detailed analysis of this important issue has been made by us in Chapter XV of the Report.

Profits

6.014 The percentage of societies making profits to the total number of societies declined from 58.1 in 1975-76 to 56.5 during 1984-85. Statewise position which is available for the year 1981-82 revealed that the percentage of profit making societies to total in Assam (14.6), Tamil Nadu (35.8), West Bengal (44.7), Karnataka (46.1), Bihar (50.1), Maharashtra (51.4) and even Kerala (51.9) was less than the all India position of 56.5 per cent. Punjab, Rajasthan, Orissa, Uttar Pradesh were some of the states where the percentage of PACSs making profit to the total was above 67.

Non-credit (multi-purpose) Activities

6.015 Though it was envisaged that the PACSs would not only provide short and medium-term agricultural credit but would also undertake services like distribution of inputs, supply of consumer goods and more importantly the marketing of agricultural produce, the number of societies undertaking all such activities is not large. According to the Statistical Statements relating to Co-operative Movement in India 1981-82, the PACSs engaged in sale of inputs and supply of consumer goods numbered 45,789 and 48,503 as at the end of June 1982, forming 48.7 and 51.6 per cent of the total number of PACSs. The value of agricultural inputs supplied by PACSs amounted to Rs.944.75 crores during 1981-82. This compares favourably with the total amount of short-term agricultural loans issued by PACSs during the year at Rs.1,696.7 crores. PACSs in some of the states had distributed inputs proportionately much higher than the kind component of crop loans e.g. Gujarat, Himachal Pradesh, Jammu & Kashmir, Punjab, Uttar Pradesh and Madhya Pradesh. However, in many other states, viz., Andhra Pradesh, Bihar, Haryana, Maharashtra, Orissa and West Bengal, the proportion of inputs distributed

through PACSs was low as compared to the crop loans issued. The number of societies undertaking such activities was also small in these states except in Haryana and Orissa. As for the societies undertaking marketing and processing activities, their number was very small, i.e. 2,241 and 74 respectively forming only 2.3 and 0.07 per cent of the total number of societies as on 30th June 1982. The number of PACSs having their own godowns as on 30th June 1986 was only 37,812 forming 41 per cent of the total number and the capacity of the owned godowns was 58.75 lakh tonnes. The number of societies having hired godown was 15,815 forming 17 per cent of the total.

Farmers Service Societies (FSS)

6.016 There were only 2,535 FSSs as on 30th June 1986. They are mainly concentrated in Assam, Bihar, Karnataka, U.P. and to some extent in M.P. and Manipur. There are very few FSSs in the other major states. The comparative position of FSSs and PACSs in several states reveals that although the membership, owned funds and loans outstanding showed a comparatively better position in FSSs as compared to PACSs, mainly because of their larger size, in respect of mobilisation of deposits and recovery of dues there was no significant difference between the two. The multi-purpose functions envisaged in the FSSs were also absent in most of the FSSs. Overall, their performance has not been very encouraging. They are beset by the same problems of recovery. They have not been able to appoint technical staff as they were expected to. The commercial banks have also been chary of adopting them, which was an essential part of the scheme of their establishment. The state governments have also often defaulted on promised subsidies. In the circumstances, they seem presently to be at a dead end, and there is little inclination on the part of any one to establish any new FSS.

Large-sized Adivasi Multi-purpose Societies (LAMPS)

6.017 The LAMPSs were organised for meeting the total credit requirements and services like supply of essential commodities, marketing of minor forest produce collected by tribals from the forests and giving technical guidance for the adoption of modern methods of cultivation etc. However, these objectives have not been properly served by these societies. Out of 2,961 LAMPSs in the country as on 30th June 1986 nearly 40 per cent are in M.P., 17 per cent in Bihar and between 7 and 10 per cent in Gujarat, Maharashtra, Orissa and

Rajasthan and the remaining in other states. LAMPSs have not been organised in Andhra Pradesh, Kerala and hilly states of Himachal Pradesh, Meghalaya and Mizoram. The membership of 43.2 lakhs comprised 26.3 lakhs tribals, 6.7 lakhs scheduled castes and 10.2 lakhs others. The average membership ranged from 12 in Nagaland, to 5,500 in Tamil Nadu. The borrowing membership formed less than 30 per cent of the total except in Bihar and Gujarat where it was more than 40 per cent. The average loan per borrowing member worked out to about Rs.1,000, a major portion of which was for cultivation. Investment credit formed less than 30 per cent of the total loans outstanding. The percentage of overdues to demand is about 45. Since the tribal economy was mainly based on income from collection of minor forest produce, it was envisaged that the LAMPSs would integrate marketing of minor forest produce with production credit and the recovery of production credit would mainly come out of the sale proceeds of minor forest produce. However, in actual practice there was total absence of such integration. The case studies revealed that the LAMPSs functioned more or less as credit societies and multi-purpose functions were almost absent.

Management of PACSs

6.018 Before the reorganisation of primary agricultural credit societies, their management was done by the elected managing committees with the help mainly of part-time secretaries or honorary secretaries (often one of the members of the committee acting as a secretary). Only a few societies had full-time paid secretaries. One of the important considerations in the criteria of viability for the programme of reorganisation was that each reorganised society should have the potential to generate enough business to be able to afford at least one full-time qualified paid secretary. As all reorganised societies did not initially have income enough to pay the salary of the secretary even with the assistance of managerial subsidy given by the state governments, many state governments introduced cadre schemes of PACSs secretaries backed by cadre secretaries Salary Fund constituted at the DCCB level, out of which salaries could be paid to them irrespective of the income of individual PACSs. Regular contributions were required to be made to the district level fund by PACSs, DCCBs and SCB at specific scales and for a certain number of years by the state governments. The cadre scheme and the cadre fund scheme showed promise in the beginning, but

unfortunately did not do well over years. The state government contribution stopped after the stipulated time. All the potentially viable PACSs did not become actually viable soon enough, so much so that their contribution remained low. It was, therefore, not possible to sustain the Salary Fund largely on the basis of contribution of the DCCBs and SCB. Resultantly, all the societies could not retain full time secretaries. In many cases the secretaries started irregularly deducting their salaries from the loan recoveries made. The total number of PACSs as on 30th June 1984 that did not have a full time paid secretary/manager was 23,525 forming 25.7 per cent of the total. The position for a later date is not available but it could not have substantially improved. Further, 50 per cent of the paid secretaries of PACSs studied by our consultants have not undergone any training owing to constraints of resources and non-availability of substitutes. The need for at least one full time official in each PACS to manage its day to day affairs cannot be overstated. It is not possible for the elected management to conduct and further the business of the society without such full-time assistance.

B. District Central Co-operative Banks (DCCBs)

6.019 The progress of DCCBs during the last ten years can be seen from table 6. As against 435 districts in the country there are 352 DCCBs. There is no DCCB in Union Territories as also in some other small states. The SCBs in these states function as DCCBs and directly deal with PACSs. In a few states such as Assam and Himachal Pradesh where DCCBs were found to be too weak to continue as separate institutions, they have been amalgamated with the SCB. The DCCB normally covers one revenue district.

Share Capital

6.020 The share capital of DCCBs is contributed by the primary societies, mainly PACSs on the basis of definite ratios of linking of share capital to borrowings. According to the present policy, the linking of share holding to borrowings of PACSs is five per cent in respect of borrowings for financing short-term and medium-term agricultural credit for small, marginal and economically weak farmers. In respect of borrowings for financing other farmers, the ratio is ten per cent. In respect of cash credit to PACSs, marketing societies, consumer stores, etc. the share linking is two and half per cent. In respect of salary earners societies and urban co-operative banks share linking is generally ten per cent except for small scale industrial advances.

Table 6

Progress of DCCBs

(Rs. crores)

Sl.No		1975-76	1980-81	1984-85	1985-86
1.	2.	3.	4.	5.	6.
1.	Number	344	337	350	352
2.	Owned funds	360.45	669.87	954.77	1,006.67
3.	Deposits				
	(a) From Cooperative Societies	371.49	857.84	2,048.14	1,987.27
	(b) From public and individuals	613.43	1,565.28	2,274.22	3,005.19
	Total	984.92	2,423.12	4,322.36	5,088.20
4.	Borrowings Outstanding	570.32	1,187.33	2,163.78	2,287.73
5.	Loans issued	1,721.66	3,210.77	6,475.71	7,333.09
6.	Loans Outstanding				
	(a) ST	1,076.25	2,163.68	3,698.98	2,470.30
	(b) MT	137.24	343.96	0	0
	(c) Conversion	214.67	478.97	1,376.05*	1,017.21*
	Total	1,428.16	2,986.61	5,075.04	5,475.30
7.	Overdues				
	(a) Amount	459.56	939.64	1,463.34	1,696.07
	(b) As percentage to demand	25.0	32.5	36.9	37.8
8.	No. of banks under rehabilitation	181	127	166	173

Source : Statistical statements relating to Co-operative Movement in India. Data on Credit and Non Credit Co-operatives, Important Items. Data for the years 1984-85 and 1985-86 provisional.

* Includes conversion loans

6.021 Even though the paid-up share capital has increased from Rs.236 crores in 1975-76 to Rs.506 crores during 1985-86, it cannot be said that every DCCB has adequate share capital. The adequacy of the share capital is judged on the basis of requirements of share capital of each DCCB vis-a-vis its lending programmes. The share capital and owned funds of a DCCB are required not only for providing adequate borrowing power (m.b.p.) which is fixed at 15 times the owned funds but also for investment in certain fixed assets such as buildings, vaults, fixtures and fittings and also for absorbing the overdues so that the bank is not put to difficulties in meeting its commitments to its creditors. The total working capital of DCCBs in 16 states as on 30.6.1986 and the owned funds required for raising the resources at 15 times has been worked out in table 7. It is seen that the owned funds are adequate for raising the required amount of resources in all the states. It will, however, be observed that the total owned funds required for investments in shares of SCB at five per cent and for absorbing overdues at the level of 20 per cent of the outstanding are inadequate in all the states except in Kerala, Gujarat and Himachal Pradesh where the percentage of overdues to outstanding is less than 20. It will not, therefore, be possible for the DCCBs in all other states to absorb the overdues fully within their owned funds. Further, some amount of owned funds are also required for investment in fixed assets, such as buildings, furniture, fittings and fixtures etc.

Reserves

6.022 The major reserves of DCCBs consist of statutory reserve fund, agricultural credit stabilisation fund and bad and doubtful debt reserve. Of the total reserves of DCCBs at Rs.348.69 crores as on 30.6.82 for which statewise break-up figures are available, the statutory reserve fund amounted to Rs.75.79 crores, stabilisation fund Rs.46.83 crores and bad and doubtful debt reserve Rs.93.78 crores. The total of the three reserves worked out to 62 per cent of the total reserves. The total reserves of DCCBs had increased from Rs.124.34 crores on 30.6.76 to Rs.501.08 crores as on 30.6.86. The statutory reserve fund comprised Rs.111.54* crores and stabilisation fund Rs.71.38* crores as on 30.6.86. The break-up of the other reserves is not available. Out of these three major reserves, the agricultural credit stabilisation fund and bad and doubtful debt reserve are constituted for specific purposes; the first one for meeting the DCCB's share in conversion of short-term agricultural

*Source: Basic data on performance of DCCBs - National Federation of SCBs.

Table 7

Owned funds of DCCBs (position as on 30.6.1986)

(Rs. crores)

Sr. No.	Name of State	Paid up Capital			Total owned funds	Total Working Capital	1/15 of Col.7
		Govt.	Others	Total			
1.	2.	3.	4.	5.	6.	7.	8.
1.	Gujarat	7.04	42.04	49.08	139.26	1114.26	74.28
2.	Maharashtra	8.12	72.76	80.88	169.71	1926.13	128.41
3.	Kerala	5.80	14.15	19.95	42.44	440.43	29.36
4.	Haryana	6.36	11.43	17.79	38.84	286.18	19.08
5.	Uttar Pradesh	14.94	46.79	61.73	97.06	859.10	57.27
6.	Karnataka	6.68	27.99	34.67	54.73	454.02	30.27
7.	West Bengal	5.64	10.32	15.96	33.07	223.32	14.89
8.	Orissa	9.53	13.56	23.09	47.06	256.47	17.10
9.	Tamil Nadu	9.94	33.09	43.03	103.60	904.26	60.28
10.	Punjab	7.11	21.77	28.88	53.96	429.64	28.64
11.	Andhra Pradesh	9.25	34.85	44.10	76.18	486.65	32.44
12.	Bihar	6.50	6.22	12.72	25.47	169.16	11.28
13.	Himachal Pradesh	0.31	0.41	0.72	3.69	54.25	3.62
14.	Jammu & Kashmir	0.55	0.23	0.78	1.34	11.33	0.76
15.	Madhya Pradesh	9.32	25.98	35.30	61.08	627.92	41.86
16.	Rajasthan	10.49	26.42	36.91	59.18	420.29	28.01
Total		117.58	388.01	505.59	1006.67	8663.41	577.56

Borrowings from apex bank	5 per cent of Col.9	Total loans outstanding	20 per cent of Col.11	Total of Col.10 & 12	Surplus/Deficit (-)	Over dues to outstanding-percentage	
9.	10.	11.	12.,	13.	14.	15.	
1.	215.49	10.77	665.82	133.16	143.93	- 4.67**	17.8
2.	215.90	10.80	1064.39	212.88	223.68	- 53.97	23.4
3.	84.86	4.24	297.66	59.53	63.77	- 21.33@	10.1
4.	124.81	6.24	221.14	44.23	50.47	- 11.63	45.3
5.	282.25	14.11	457.33	91.47	105.58	- 8.52	49.7
6.	117.04	5.85	297.07	59.41	65.26	- 10.53	33.3
7.	35.99	1.80	116.03	23.21	25.01	+ 8.06*	54.6
8.	131.82	6.59	187.34	37.47	44.06	+ 3.00++	40.1
9.	225.98	11.30	680.35	136.07	147.37	- 43.77	22.8
10.	123.61	6.18	264.51	52.90	59.08	- 5.12	48.7
11.	231.91	11.60	336.08	67.22	78.82	- 2.64	46.0
12.	64.15	3.21	96.32	19.26	22.47	+ 3.00£	62.1
13.	1.73	0.09	16.98	3.40	3.49	+ 0.20	11.7
14.	3.99	0.20	7.53	1.51	1.71	- 0.37	49.9
15.	232.82	11.64	442.13	88.43	100.07	- 38.99	25.3
16.	195.38	9.77	293.66	58.73	68.50	- 9.32	40.1
2287.73		114.39	5444.34	1088.88	1203.27	- 196.60	

* on the basis of actual overdues at Rs.63.36 crores, there is a deficit of Rs.32.09 crores in owned funds.

++ On the basis of actual overdues at Rs.75.19 crores, there is a deficit of Rs.34.72 crores in owned funds

£ On the basic of actual overdues at Rs.59.81 crores, there is a deficit of Rs.37.55 crores in owned funds.

** On the basis of actual overdues at Rs.118.40 crores, there is a surplus of Rs.10.09 crores in owned funds.

@ On the basis of actual overdues at Rs.29.96 crores, there is a surplus of Rs.8.64 crores in the owned funds.

loans into medium-term loans and the latter reserve is for writing off bad debts. The adequacy of these two reserves can be seen from the state-wise position indicated in table 8. It can be seen that the agricultural credit stabilisation fund of the DCCBs in the drought affected states is not adequate. These funds have to be augmented by government contributions since the capacity of the DCCBs to allocate adequate amounts from out of profits is very limited. The bad and doubtful debt reserve is also quite inadequate in the context of the likely bad and doubtful debts of these banks.

Table 8
Agricultural Credit (Stabilisation) Fund and Bad and Doubtful Debt Reserve - Position as on 30.6.1982

(Rs. crores)

Sl. No.	Name of State	M.T. Conversion loans outstanding	15 per cent of col.3 (Share of DCCB in conversion loans) ⁴	Stabilisation fund	Surplus/Deficit Col.5-4	Bad and doubtful debts estimated	Bad and doubtful debt reserve	Surplus/Deficit Col.8-7
1.	2.	3.	4.	5	6.	7.	8.	9.
1.	Gujarat	91.25	13.69	9.73	-3.96	27.99	15.35	-12.64
2.	Maharashtra	41.68	6.25	8.36	+2.11	15.29	15.71	+0.42
3.	Rajasthan	67.75	10.16	0.37	-9.79	9.76	6.19	-3.57
4.	Haryana	17.53	2.63	1.93	-0.70	2.85	3.76	+0.91
5.	Uttar Pradesh	91.50	13.73	1.72	-12.01	18.27	7.59	-10.68
6.	Karnataka	22.84	3.43	3.03	-0.40	7.37	2.97	-4.40
7.	West Bengal	7.96	1.19	0.80	-0.39	4.77	1.57	-3.20
8.	Orissa	9.10	1.37	0.65	-0.72	5.76	3.72	-2.04
9.	Bihar	14.91	2.24	0.45	-1.79	7.34	2.71	-4.63
10.	Tamil Nadu	36.84	5.53	8.48	+2.95	9.63	12.18	+2.55
11.	Madhya Pradesh	25.17	3.78	3.29	-0.49	9.06	5.82	-3.24
12.	Andhra Pradesh	69.73	10.46	2.96	-7.50	12.49	5.31	-7.18
13.	Assam	-	-	(2)	+(2)	0.29	(15)	-0.29
14.	Himachal Pradesh	0.04	0.01	0.32	+0.31	0.54	0.61	+0.07
15.	Jammu & Kashmir	0.75	0.11	0.05	-0.06	1.19	0.27	-0.92
16.	Kerala	0.05	0.01	1.06	+1.05	4.47	4.80	+0.33
17.	Punjab	6.19	0.93	3.64	+2.71	14.14	5.22	-8.92

Figures in brackets show amount in thousands.

Source : Basic data on performance of DCCBs - National Federation of SCBs.

Deposits

6.023 The growth of deposits in DCCBs during the last 5 years may be seen from table 9. The trend in deposit mobilisation, as would be seen has been a continuously rising one. However, when seen against the growth rate achieved by commercial banks and RRBs, the performance of DCCBs looks a bit sluggish.

Table 9
Deposits of DCCBs

	(Rs. crores)				
	<u>1981-82</u>	<u>1982-83</u>	<u>1983-84</u>	<u>1984-85</u>	<u>1985-86</u>
Received from individuals	1,490.08	1,843.52	2,372.22	2,274.22	2,664.81
Received from co-operatives	1,020.43	1,340.21	1,393.30	2,048.14	2,267.19
Received from others	<u>259.62</u>	-	-	-	-
Total	<u>2,770.13</u>	<u>3,183.73</u>	<u>3,765.52</u>	<u>4,322.36</u>	<u>4,932.00</u>
Growth Rate	14.3	15.0	18.2	15.0	14.1

The trend in rural deposits of commercial banks, RRBs and co-operatives over the last 20 years can be seen from table 10.

Table 10
Trends in Deposits

Year	Rural Sector of CBs	RRBs	Co-operatives			Total
			SCBs	DCCBs	PACs	
1969	329	-	216	351	57	624
1976	1,564	8	724	985	113	1,822
1980	4,444	200	1,500	2,100	270	3,870
1986	12,660	1,715	3,385	4,932	572	8,881

Source : Report of the Consultants on Study II.

The deposits of commercial banks in rural areas increased at an average annual rate of 27 per cent during the seventies and this rate came down to 19 per cent in the first six years of the current decade. The deposits collected by the co-operatives increased at an average annual rate of 18 per cent in the seventies and 15 per cent in the first six years of the eighties. We are conscious of the fact that there is an element of double counting in the deposits with different constituents of the co-operative credit structure consisting of SCBs, DCCBs and PACs since the lower tiers are required to keep their surplus resources with the higher tiers though in practice this is not so in all cases. It is, however, difficult to calculate the exact extent of such double counting. The deposits are often used for lending by lower tiers and with a view to reducing their dependence on refinance. Even the liquid assets

maintained by DCCBs are not necessarily invested always with the SCBs and some portion gets invested in Government/trustee securities, etc. also. Therefore, there may not be much variation in the growth rate of deposits even if the overlapping is avoided. We have ignored the element of double counting in deposits of co-operative banking system for the reasons explained in paragraphs 23-24 and 23-25 of Chapter XXIII on "Supply of Agricultural Credit : Estimates of Resources". A comparison of the growth rate of deposits of rural sector of commercial banks with that of co-operatives does not seem to place the co-operatives in a much inferior position considering the fact that the commercial banks provide other banking services which the co-operative banks are not in a position to provide now. Nevertheless, the performance of DCCBs in deposit mobilisation, though positive, still continues to be lower than what could be achieved. Moreover, there is considerable variation from state to state. The per branch deposits of all types in respect of ten DCCBs studied in different states ranged from Rs.10.6 lakhs in the case of a DCCB branch in Bihar to Rs.108.1 lakhs in the case of a branch of DCCB in Indore in Madhya Pradesh. The fixed deposits and other deposits representing statutory reserves of primary societies accounted for a greater proportion of the deposit portfolio of a majority of DCCBs. As on 30.6.1986, the total fixed and reserve fund deposits of all DCCBs in the country at Rs.2,837 crores, formed about 56 per cent of the total deposits. Such deposits generally carry higher rates of interest than the rate at which the DCCBs borrow funds from the SCB for financing agricultural operations as well as investments in agriculture and allied activities.

6.024 The DCCBs in general do not appear to have made all the possible efforts for mobilisation of larger deposits. Their staff have not been adequately motivated and trained in various techniques of deposit mobilisation especially since there is a stiff competition from commercial banks in deposit mobilisation from individuals. It has, of course, to be recognised that the DCCBs are not able to offer comparable facilities to their clientele as are available to the depositors from commercial banks. They also cannot accept deposits from trusts, institutions, etc. since they are not "scheduled banks" and are, therefore, deprived of collecting deposits of institutions which can invest their surplus funds only in a scheduled bank. All the same, a number of DCCBs are too weak to be able to create the confidence so essential for attracting deposits, from their potential clientele.

6.025 It will also be useful to examine the proportion of deposits in the working capital of DCCBs. Table 11 shows statewise position of deposits during the last ten years (1975-76 to 1985-86) and the percentage of deposits to working capital during the period. It will be seen from the table that the percentage of deposits to working capital has shown an increasing trend in most of the states indicative of greater self reliance than in earlier years. This is a positive development. The percentage has declined only in Haryana, Himachal Pradesh, Orissa and Punjab during 1985-86 as compared to 1975-76. However, the position during the last two years has shown some improvement in Haryana and Punjab. In 11 out of 17 states, the deposits constituted more than 50 per cent of the working capital during 1985-86 of which in six states the deposits accounted for more than 60 per cent of the working capital (Maharashtra, Himachal Pradesh, Assam and Kerala with 71.5 per cent, 78.6 per cent, 81.8 per cent and 69.6 per cent). States which have low deposits as compared to working capital were Orissa 26.9 per cent, Rajasthan 34.9 per cent, Andhra Pradesh 36.2 per cent and Haryana 37.8 per cent. States which had shown significant progress in increasing the percentage of deposits to working capital during the last ten years were Assam, West Bengal, Karnataka, Madhya Pradesh, Tamil Nadu and Kerala. These percentages, though seemingly not too unsatisfactory, cannot obscure the fact that the working capital itself is far too inadequate to meet the needs of agricultural production and allied activities and to the extent still larger deposit mobilisation is undertaken, the working capital will increase adequately to look after those needs.

Loans and Advances

6.026 The statement showing classification of advances of DCCBs state-wise as on 30.6.86 is given in table 12. The issue of short-term agricultural credit is the single major purpose of co-operative banks. Marketing of agricultural produce alone or in conjunction with processing activities, financing input supply activities as also the industrial co-operatives are other purposes for which loans are issued by co-operative banks depending upon the absorption capability of concerned co-operatives in the states. It will be seen that out of the 16 states, DCCBs in seven states had issued more than 50 per cent of the total loans for short-term agricultural purposes and three more states had issued short-term agricultural loans more than 40 per cent of the total.

Table 11
DCCBs - Deposits as a Proportion of Working Capital

(Rs. lakhs)

STATE	Total Deposits					Percentage of Deposits to Working Capital				
	1975-76	1981-82	1983-84	1984-85	1985-86	1975-76	1981-82	1983-84	1984-85	1985-86
1. Andhra Pradesh	4,385	11,282	14,936*	14,936*	17,627	34.10	31.23	36.11	36.11*	36.22
2. Assam	133	137	192●	192●	593£	11.41	59.05	66.20●	66.20●	81.79£
3. Bihar	1,438	3,999	5,370	6,629	7,037	27.77	32.39	35.52	39.89	41.59
4. Gujarat	16,596	44,447	61,167	68,531	69,566	50.99	62.31	61.99	62.80	62.43
5. Haryana	2,758	6,896	7,930	9,470	10,818	42.62	33.41	30.30	36.40	37.80
6. Himachal Pradesh	1,084	2,309	3,268	4,094	4,267	85.29	80.36	80.21	87.53	78.65
7. Jammu & Kashmir	315	1,631	2,389	N.A.	N.A.	31.37	64.90	70.36	N.A.	N.A.
8. Karnataka	5,744	15,496	19,683	23,549	26,495	42.69	52.31	53.62	60.01	58.35
9. Kerala	4,391	13,277	25,446	23,704	30,676	56.19	53.80	68.66	63.32	69.65
10. Madhya Pradesh	5,119	15,691	19,445	26,559	31,636	36.08	45.62	45.41	52.36	50.38
11. Maharashtra	24,752	68,938	98,066	1,20,476	1,37,662	63.52	69.09	70.45	72.22	71.47
12. Orissa	1,406	5,355	5,807	7,729	6,899	33.83	29.05	23.85	31.85	26.89
13. Punjab	7,911	15,831	18,475	18,478	22,832	61.05	50.77	42.24	40.79	53.14
14. Rajasthan	2,753	8,459	7,406	8,757	14,667	32.87	31.07	21.97	23.85	34.89
15. Tamil Nadu	7,966	27,213	39,819	47,727	50,304	40.26	52.27	55.07	50.96	55.63
16. Uttar Pradesh	9,477	27,903	36,613	38,888	47,935	49.47	46.89	48.33	49.83	55.79
17. West Bengal	2,255	8,138	10,540	11,971	14,233	41.71	48.88	50.54	56.32	63.73

* Data relate to 1983-84

● Data relate to 1982-83

£ Data relate to 1986-87

Source : Statistical Statements Relating to Co-operative Movement in India -
Important Items of Data - Credit and Non-Credit Co-operative Societies

Table 12
Classification of Loans Issued by DCCBs during 1985-86

(Rs. crores)

Sr. No.	Name of State	Total loans & advances	Of Col.3 S.T. Agr	Of Col.4 Seasonal agricultural Operations	Marketing of crops	Others including Input supply	S.T. Non-Agr.	M.T. Agr.	M.T. Non-Agr.	Other loans & advances
1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.
1.	Andhra Pradesh	242.06	130.57	129.97	0.30	0.30	25.79	19.81	13.20	52.68
2.	Bihar	29.09	17.80	16.47	0.22	1.11	5.82	4.27	0.64	0.84
3.	Gujarat	1,728.95	318.12	194.83	87.28	36.01	613.96	46.19	15.41	735.26
4.	Haryana	274.39	200.12	196.57	-	3.55	30.27	7.97	0.33	35.68
5.	Himachal Pradesh	36.70	17.23	0.78	7.44	9.01	12.54	1.27	0.62	5.03
6.	Jammu & Kashmir	63.35	8.33	8.33	-	-	29.99	1.61	0.49	22.92
7.	Karnataka	389.71	147.62	105.81	5.73	36.08	80.61	36.07	7.01	118.38
8.	Kerala	417.14	129.52	105.93	13.68	9.91	179.54	6.75	34.65	66.77
9.	Madhya Pradesh	629.04	331.62	243.43	3.64	84.55	59.39	35.30	10.06	192.67
10.	Maharashtra	2,219.14	353.59	325.69	8.12	19.78	1,508.31	93.30	29.94	233.99
11.	Orissa	96.06	61.54	48.37	6.49	3.78	11.96	15.43	4.48	2.65
12.	Punjab	573.28	413.97	335.32	0.40	78.25	52.24	7.53	0.99	98.52
13.	Rajasthan	204.91	120.88	87.23	11.81	21.84	24.44	38.32	0.93	20.33
14.	Tamil Nadu	885.79	252.70	126.08	3.31	123.31	360.62	24.01	63.21	185.23
15.	Uttar Pradesh	712.05	341.50	214.61	2.91	123.98	181.30	51.71	10.44	127.59
16.	West Bengal	40.95	16.93	16.80	0.05	0.07	16.13	0.48	3.33	4.07

Table 12 (Contd.)

	As percentage of							
	Col. 4 to 3 12.	Col. 5 to 4 13.	Col. 6 to 4 14.	Col. 7 to 4 15.	Col. 8 to 3 16.	Col. 9 to 3 17.	Col. 10 to 3 18.	Col. 11 to 3 19.
1.	53.94	99.54	-	-	10.65	8.18	5.45	21.76
2.	61.19	92.53	-	6.23	20.00	14.68	-	-
3.	18.40	61.22	27.43	11.31	35.51	2.67	-	42.53
4.	72.93	98.22	-	-	11.03	2.90	-	13.00
5.	46.95	4.52	43.18	52.29	34.16	3.46	-	13.70
6.	13.15	100.00	-	-	47.34	2.54	-	36.18
7.	37.88	71.68	-	24.44	20.68	9.25	-	30.37
8.	31.05	81.78	10.56	7.65	43.04	1.61	8.3	16.00
9.	52.72	73.40	-	25.49	9.44	5.61	-	30.62
10.	15.93	92.11	-	5.59	67.96	4.20	-	10.54
11.	64.06	78.60	10.54	6.14	12.45	16.06	-	-
12.	72.21	81.00	-	18.90	9.11	1.31	-	17.18
13.	58.99	72.16	9.77	18.06	11.92	18.70	-	9.92
14.	28.53	49.89	-	48.79	40.71	2.71	7.13	20.91
15.	47.96	62.84	-	36.30	25.46	7.26	-	17.91
16.	41.34	99.23	-	-	39.38	1.17	8.13	9.93

Note : Percentages working out to less than 5 not indicated except in respect of M.T. (Agricultural)

Source : Basic Data on performance of DCCBs during 1985-86.

National Federation of SCBs.

Haryana and Punjab had issued more than 70 per cent of the total loans for short-term agricultural purposes while Bihar and Orissa had issued more than 60 per cent of the loans for the same purpose. Gujarat, Maharashtra and Jammu & Kashmir had issued less than 20 per cent of the total loans for short-term agricultural purposes. Most of the states except Himachal Pradesh and Tamil Nadu had issued more than 60 per cent of the short-term agricultural loans for seasonal agricultural operations. Gujarat, Himachal Pradesh, Kerala and Orissa had advanced a portion of short-term agricultural loans (above 10 per cent) for marketing of agricultural produce while Himachal Pradesh, Karnataka, Madhya Pradesh, Tamil Nadu and Uttar Pradesh had issued more than 25 per cent of the total short-term agricultural loans for other purposes including supply of inputs. Punjab and Rajasthan had financed about 19 per cent and 18 per cent of short-term agricultural loans for the same purpose. The performance of other states in financing marketing and input supply is very insignificant. The performance of DCCBs in Maharashtra, Jammu and Kashmir, Kerala, Tamil Nadu, Gujarat and Himachal Pradesh in financing short-term non-agricultural purposes is good as they have financed more than 1/3rd of the total advances for these purposes. Out of the short term non-agricultural purposes, loans for industrial purposes (working capital for industries including processing industries like sugar factories, cotton mills, oil mills etc.) were granted by Andhra Pradesh, Gujarat, Kerala, Maharashtra, Orissa, Tamil Nadu and Uttar Pradesh. The percentage of such loans exceeded five per cent of the total loans advanced.

6.027 The DCCBs are not able to diversify their loan portfolio. The major portion of the loans and advances of DCCBs consists of short-term agricultural advances. Till recently the eligibility criterion for NABARD refinance for schematic lending to DCCBs was a recovery performance of 60 per cent of the demand and therefore, many DCCBs were not eligible for such finance. Further, there were restrictions in the State Co-operative Laws in financing long-term loans by the short-term credit structure. DCCBs were allowed to lend for periods upto five years. Some of the states have amended the Co-operative Societies Rules to enable DCCBs to finance for longer periods. NABARD has since relaxed the conditions of eligibility on par with that of PLDBs and hence the DCCBs can now take up schematic lending in a larger way.

6.028 The major deficiencies found in financing agriculture during the studies conducted by our consultants are (a) delay in sanction and disbursement of loans, (b) inadequate scales of finance and unit cost, (c) insistence of disbursement of kind component in kind even where infrastructure facilities for supply of inputs are not adequate, (d) repayment schedule fixed without synchronising with the cash flow or fixing instalments without taking into account repaying capacity and (e) lack of follow up or monitoring loans and advances. These are discussed later for remedial steps.

Overdues

6.029 Poor recovery performance is one of the major weaknesses of DCCBs which affect recycling of loans. High overdues have affected the ability of the DCCBs in many cases to avail themselves of adequate refinance from higher financing agencies. Further the profitability of many banks has been adversely affected where even interest is not fully/partially recovered.

6.030 The statewise position of overdues of DCCBs as on 30.6.1986 is given in table 13.

Table 13
Statewise Overdues of DCCBs as on 30.6.1986

Name of State	No. of DCCBs	Total overdues (Rs. crores)	Percentage of overdues to demand
Andhra Pradesh	27	154.74	45.3
Bihar	34	59.81	52.4
Gujarat	18	118.40	36.2
Haryana	13	100.12	32.3
Himachal Pradesh	2	1.98	55.7
Jammu & Kashmir	2	3.76	39.0
Karnataka	19	98.91	41.7
Kerala	13	29.96	16.9
Madhya Pradesh	45	111.78	35.6
Maharashtra	30	248.86	42.8
Orissa	17	75.19	51.4
Punjab	15	128.84	22.5

Table 13 (contd.)

Name of State.	No. of DCCBs	Total overdues (Rs. crores)	Percentage of overdues to demand
Rajasthan	25	117.69	48.1
Tamil Nadu	17	155.41	33.0
Uttar Pradesh	57	227.26	43.8
West Bengal	17	63.36	53.4

It will be seen that the percentage of total overdues to demand in respect of DCCBs in four states was above 50, in five states between 41 to 50, and in five other states between 31 to 40. Hence out of 16 states only in two states the DCCBs had total overdues of less than 30 per cent and only in one state namely Kerala the overdues were less than 20 per cent.

Weak Banks

6.031 A DCCB is considered weak when its estimated bad and doubtful debts, other overdues above three years and accumulated losses exceed 50 per cent of its paid-up capital and reserves. The banks are identified as weak or otherwise every year by NABARD with reference to their latest financial position. The programme of rehabilitation for improving the working of weak DCCBs under the three-tier structure and weak SCBs under two-tier structure was launched by RBI in 1971. As on 30.6.86, 173 banks have been identified as weak and placed under the scheme of rehabilitation. Banks which are found unlikely to become viable are not taken up for rehabilitation under the scheme. From 1975-76 till 1985-86, the number of banks under rehabilitation, remained more or less stationary although there was some reduction in the number during the years 1977-78 and 1978-79. Although the scheme has been in operation for more than 15 years, as on 30.6.86 there were 43 DCCBs under rehabilitation for periods between 5 and 10 years continuously and 58 banks for more than 10 years. Further, there was a large number of DCCBs which emerged operationally successful from the rehabilitation programme only to slide back into "under rehabilitation" status one or two years later.

C. State Co-operative Banks (SCBs)

6.032 Salient data of the state co-operative banks since 1975-76 upto 1985-86 can be seen from table 14.

Table 14
Progress of SCBs

		(Rs. crores)			
Sr. No.		1975-76	1980-81	1984-85	1985-86
1.	Number	26	27	30	31
2.	Deposits				
	(a) Co-operatives	557.34	1,318.45	2,401.85	2,856.48
	(b) Others	166.34	355.80	564.29	528.93
	Total	723.68	1,674.25	2,966.14	3,385.41
3.	Borrowings (Outstanding)	343.73	608.47	1,076.20	1,227.00
4.	Loans outstanding	893.60	1,836.45	3,150.17	3,852.79
5.	Overdues	43.60	161.74	244.96	291.76
6.	Percentage of Overdues to demand	7.0	10.0	10.5	9.2
7.	No. of banks under rehabilitation	5	8	9	8

In pursuance of the policy of having one apex level credit institution each for the short-term co-operative credit structure in each state and union territory, SCBs have been organised in all the states and union territories except Lakshadweep and Dadra Nagar Haveli. In smaller states and Union territories there is a two-tier structure where SCBs function also as DCCBs. In states where the three-tier structure exists, the membership of the SCBs is generally restricted to DCCBs, state level co-operative institutions and some primary level institutions such as urban co-operative banks. In states where the two-tier structure is operating, the primary co-operative societies of all types are the members. The individuals continued to be members in some SCBs though as a matter of policy individual membership is discouraged. The state government is a member of every state co-operative bank.

Share Capital and Reserves

6.033 As at the close of 1985-86, the share capital of the SCBs increased

to Rs.148.5 crores including government share capital of Rs.27.3 crores. The government share capital formed 18.4 per cent of the total. The reserves and other funds amounted to Rs.487 crores, raising the owned funds to Rs.635.5 crores. The government share capital at 18.4 per cent is much less than the 51 per cent share recommended by the All-India Rural Credit Survey Committee (1954). Since the maximum borrowing power of a SCB is generally fixed at 20 times its owned funds, the owned funds of SCBs can be considered as adequate.

Deposits

6.034 During the last 10 years the deposits of SCBs registered a substantial increase from Rs.723.68 crores in 1975-76 to Rs.3,385.41 crores in 1985-86. The deposits of the 28 SCBs maintaining accounts with RBI, as at the end of March 1988 had further increased to Rs.3,885 crores. Of the deposits on 30th June 1986, Rs.494.78 crores and Rs.313.19 crores aggregating Rs.807.97 crores represented low cost deposits, viz., current and savings deposits. The fixed and other deposits mainly represented funds of the co-operative institutions especially the statutory reserves of DCCBs and surplus funds of other co-operative institutions which are compulsorily required to be invested with SCBs. The deposits collected from the public constituted only 16 per cent of the total deposits as on 30th June 1986. The efforts of the SCBs towards deposit mobilisation are somewhat handicapped as the SCBs are not allowed to open branches outside the state capital except where there is no DCCB or the DCCB is very weak or there is large scope for deposit mobilisation or there are large co-operative units like sugar factories and spinning mills to be financed. On the other hand, in the state capital, a DCCB of the concerned district operates and competes with the branches of the SCB. Another factor demotivating the SCBs (and some of the DCCBs also) in their efforts to collect more deposits is the refinance policy adopted by the NABARD in the sanctioning of refinance limits to DCCBs/SCBs. NABARD provides only supplementary finance and hence sanctions refinance to the extent of the deficits in the resources of DCCBs. The more the deposits of a DCCB/SCB, the lower is the refinance available to it from NABARD. Since the refinance from NABARD is at concessional rate of interest, collection of deposits affects the profitability of the banks in two ways. The cost of raising deposits by co-operative banks is higher as they offer 1/4 to 1/2 per cent higher interest and secondly, this reduces the amount of concessional refinance from NABARD. Thus the cost of raising resources required for lending goes up on both counts. However,

NABARD has recently announced certain measures to compensate the loss of income to DCCBs and SCBs for deploying their own resources for short-term agricultural loans. In respect of those DCCBs which are not availing of refinance from NABARD or those banks which are availing very meagre amount as refinance but are having adequate surplus funds for investment, NABARD has of late arranged for the deployment of such surpluses in remunerative investments fetching a reasonable return of 13.5 per cent so as to compensate the losses incurred on loans for short-term agricultural purposes.

Borrowings

6.035 The borrowings of SCBs are mainly from NABARD and the major purposes for which funds are drawn from NABARD are for seasonal agricultural operations (SAO) and for medium-term agricultural purposes or for conversion and rephasing of SAO loans. The borrowings of SCBs from NABARD for SAO during the last 10 years have been increasing as may be seen from table 15. Though the borrowings from NABARD are increasing in absolute amounts, the proportion of borrowings to the loans issued at PACSs level during the last 10 years has declined from 40.6 per cent to 31.8 per cent indicating that more and more internal resources are being used for lending. However, there are considerable variations from state to state as may be seen from the state-wise position of borrowings of SCBs from NABARD for SAO during 1985-86 in table 16.

Table 15
Borrowings of SCBs

Year	Amount sanctioned	Maximum outstanding	Outstanding as on 30th June	Loans issued by PACSs during the year	Loans outstanding at the level of PACSs	(Rs. crores)	
						Percentage of Col.3 to Col.5	Percentage of Col.3 to Col.6
1	2	3	4	5	6	7	8
1975-76	611.89	372.85	146.60	916.62	1,012.09	40.68	36.84
1980-81	796.67	475.59	291.46	1,513.60	1,914.96	31.42	24.83
1983-84	1,244.87	802.63	584.50	2,157.85	2,554.30	37.19	31.42
1984-85	1,234.52	867.71	446.41	2,323.35	2,835.90	37.35	30.60
1985-86	1,308.82	872.97	550.47	2,746.87	3,237.00	31.78	26.97
1986-87	1,425.29	936.37	660.12	2,833.00	3,293.00	33.05	28.43
1987-88	1,999.68	1,307.04	909.77	3,116.00	3,589.00	41.95	36.42
1988-89	2,553.07	1,801.33	1,778.30*	3,250.00 (estimate)	4,355.00 (estimate)	55.41	41.35

* March 1989

Table 16
State-wise Position of Borrowings of SCBs for
Seasonal Agricultural Operations - 1985-86

(Rs. crores)

Sr. No.	Name of the State Co-operative Bank	Limit Sanctioned	Maximum outstanding	Outstanding as on 30th June 1986	Short-term loans issued by PACSs during the year	Percentage of Col. 4 to 6
1	2	3	4	5	6	7
1.	Andhra Pradesh	156.20	111.71	70.59	197.46	56.6
2.	Bihar	33.52	30.23	27.53	31.76	95.2
3.	Gujarat	97.50	85.83	20.66	249.60	34.4
4.	Haryana	112.40	109.35	82.19	200.01	54.7
5.	Himachal Pradesh	-	0.16	0.07	4.57	3.5
6.	Jammu & Kashmir	4.35	3.58	3.58	8.34	42.9
7.	Karnataka	74.50	35.38	19.69	134.36	26.3
8.	Kerala	46.00	43.89	Nil	313.27	14.0
9.	Madhya Pradesh	145.20	106.25	92.41	252.19	42.1
10.	Maharashtra	56.25	Nil	Nil	312.50	-
11.	Orissa	66.75	57.09	46.92	47.19	120.9
12.	Punjab	143.85	84.34	Nil	363.29	23.2
13.	Rajasthan	91.60	76.03	50.91	104.31	72.9
14.	Tamil Nadu	67.00	56.69	45.11	207.01	27.4
15.	Uttar Pradesh	188.79	140.07	78.67	243.40	57.5
16.	West Bengal	22.75	10.12	9.74	71.93	14.1
17.	Manipur	-	0.66	0.31	0.37*	178.4
18.	Nagaland	0.60	0.60	0.60	2.60	23.1
19.	Pondicherry	0.90	0.90	0.90	2.10	42.9
20.	Tripura	0.50	0.50	0.50	0.55	90.9
21.	Andaman & Nicobar	0.16	0.13	0.09	0.09	144.4
	Total	1,308.82	872.97@	550.47	2,746.87	31.8

* Data relate to 1983-84

@ All India maximum outstanding

It will be seen from table 15 that there has been a substantial increase in the quantum of short-term agricultural credit provided by co-operatives during the last two years viz. 1987-88 and 1988-89. This was the result of a massive rabi programme launched in many of the states where there had been extensive damage to kharif crops during the year 1987-88 due to the drought/floods. During 1988-89 the increase in the aggregate short-term credit provided by co-operatives was due to the special drive for new membership in co-operatives under the food production programme and provide them crop loan assistance, greater thrust on NODP and other programmes like special rice production programme etc. To enable implementation of this policy thrust, additional refinance facilities were made available by NABARD, by waiving where necessary or relaxing existing norms governing such refinance to co-operatives. Consequently, the short-term credit limits sanctioned by NABARD and the utilisation thereof indicates a sizeable quantum increase. The co-operatives were directed to grant increased credit under these programmes even though in view of the reduction in the lending rates for short-term agricultural loans from 1st April 1988 credit institutions suffered losses in the process. Since the reduction in the lending rates was imposed on the co-operatives and other credit institutions, NABARD also worked out a scheme for compensating the co-operative credit institutions, a portion of the losses sustained by them in such lending. While sanctioning the short-term credit limits to SCBs during 1987-88, NABARD had taken into account the massive rabi programme launched in many states and also additional requirements of credit under NODP, SRPP etc. While sanctioning credit limit for 1988-89 to SCBs, NABARD had taken into account, besides the requirements under special agricultural production programmes the need for larger share of concessional refinance following the decline in their earnings due to reduction in lending rates. It would not therefore, be correct to infer that the higher quantum of credit limits and their utilisation during the two years had, in any way, set in a trend towards greater reliance on refinance from NABARD since these measures were of a temporary nature and it is expected that the position would stabilise soon around the levels noticed earlier. Statewise position shows that the proportion of borrowings to loans issued at PACSs level in 12 out of 21 SCBs is less than 50 per cent, six SCBs viz. Bihar, Orissa, Rajasthan, Manipur, Tripura and Andaman Nicobar Islands relied heavily on borrowings from NABARD with the proportion of borrowings to loans issued were upwards of 72.9 per cent.

Efforts should be made by these banks to reduce their reliance on borrowings from NABARD by increasing their internal resources.

6.036 The borrowings for medium-term agricultural and for conversion/ rescheduling purposes during the last three years is given below :

Table 17
Borrowings for Medium-Term Purposes

(Rs. crores)

Year	M.T. Agricultural			M.T. Conversion/Rephasement			Total drawals Col.3 + Col.6	Medium- term loans issued by PACs
	Limits sanctioned	Drawals during the year	Outstanding at the end of the year	Limits sanctioned	Drawals during the year	Outstanding at the end of the year		
1.	2.	3.	4.	5.	6.	7.	8.	9.
1983-84	31.36	18.73	37.42	56.64	54.69	119.95	73.42	341.46
1984-85	25.03	17.11	38.13	123.69	72.64	119.50	89.75	369.66
1985-86	24.27	13.02	35.35	116.67	88.39	141.85	101.41	393.50

The drawals under medium-term agricultural loans have shown a decline during the past three years. These loans were under non-schematic lending which NABARD has been lately discouraging. The medium-term conversion/rephasement loans have increased steadily during the last three years due to successive natural calamities experienced in many parts of the country. The borrowings from NABARD formed only 18 per cent of the working capital of SCBs as on 30th June 1986. The state-wise position however indicates that SCBs of Orissa (60.2), Haryana (55.2), Rajasthan (51.3) and Andhra Pradesh (41.2) had relied heavily on borrowings while states such as Maharashtra (2.7), Assam (2.2), Himachal Pradesh (6.2), Gujarat (10.2), and Karnataka (11.6) had been able to reduce their dependence on borrowings to a very large extent.

Loans and Advances

6.037 The total loans advanced by SCBs increased from Rs.1,516.80 crores during 1975-76 to Rs.5,514.42 crores during 1985-86, registering over 300 per cent increase. The short-term loans issued during 1985-86 comprised Rs.5,129.41 crores and term-loans Rs.385.01 crores. The percentage of term loans issued to the total loans was only seven. However, the percentage of

outstandings under term loans as on 30 June 1986 to the total loans outstanding was 23.5. Viewed statewise, a few states, such as Rajasthan (58.5), Meghalaya (64.3), Goa (72.1), Orissa (41.5), Tripura (44.6), Andhra Pradesh (38.8) and Uttar Pradesh (33.7) had a higher proportion of term loan outstandings than the All India proportion.

6.038 The classification of loans outstanding as on 30 June 1986 of some of the SCBs (table 18) will show the proportion of agricultural and non-agricultural loans financed by them.

Table 18
Classification of Loans of State Co-operative Banks

(Rs. crores)

Name of SCB	Total loans out-standing	Loans for SAO	M.T. (agr.)	M.T. (con.)	Total of cols. 3,4&5	Percentage of col.6 to col. 2
1	2	3	4	5	6	7
Assam @	48.32	5.33	10.44	-	15.77	32.6
Bihar	98.84	36.94	23.96	5.71	66.61	67.4
Maharashtra	859.48	70.09	13.97	22.23	106.29	12.3
Madhya Pradesh	287.28	144.45	9.15	25.60	179.20	62.4
Tamil Nadu	322.58	51.81	21.13	7.38	80.32	24.9
Haryana	156.33	107.51	9.30	-	116.81	74.3

@ State having two tier system

It will be seen that the proportion of agricultural loaning to the total loan portfolio was small in some of the states such as Maharashtra, Tamil Nadu and Assam which have avenues for financing allied and non-agricultural activities including marketing and processing industries organised in the co-operative sector.

Overdues

6.039 The percentage of overdues to demand of SCBs as on 30 June 1986 is generally low i.e. less than ten, except in respect of SCBs where the two-tier system is prevalent and SCBs function as DCCBs dealing with PACSs directly. This may be seen from the table given below :

Table 19
Overdues of SCBs as percentage to demand

<u>States</u>	<u>Percentage of overdues to demand</u>
Assam	45.3
Bihar*	36.6
Himachal Pradesh	50.0
Manipur	90.4
Meghalaya	70.2
Andaman & Nicobar Islands	58.0
Arunachal Pradesh	54.0
Chandigarh	78.1
Dadra & Nagar Haveli	76.1
Goa, Daman & Diu	76.1
Pondicherry	50.0

* State having three tier structure

The overdues arising out of agricultural financing are mostly absorbed by DCCBs and the overdues at SCB levels are in respect of non-agricultural loans granted by them directly to other co-operative institutions. In some bigger states, the percentage of overdues to demand is, however, high e.g. Andhra Pradesh (24.2), Rajasthan (25.0) and West Bengal (23.4)

D. Overall Assessment

6.040 It will be seen from the above review that the progress of the short-term co-operative credit structure has been uneven in most states of the country. Notable progress has been achieved only in a few states like Kerala and Punjab, where the banks have been able to provide reasonable credit, mobilise substantial resources by way of deposits and diversify the loan portfolios through both agricultural and non-agricultural lendings. In Maharashtra and Gujarat deposit mobilisation at the DCCB and SCB level has been quite good and has given strength to the system. The performance of Tamil Nadu also in this respect is better than the remaining states particularly at PACS level. Close behind is Uttar Pradesh. However, by and large the progress made by the structure in most of the states cannot be considered adequate. Regional imbalance, both in terms of structural strength and flow of finance to members for agricultural production, therefore, constitute a major problem area.

6.041 The problems and weaknesses which beset the structure continue to be substantially the same as were identified earlier by the first two major Reviews, viz., All India Rural Credit Survey Committee, 1954, and the Rural Credit Review Committee, 1969. The Rural Credit Review Committee had discussed in depth the problems of the short-term co-operative credit structure in the context of the implementation of the recommendations of the AIRCS Committee report, 1954. They had pointed out that owing to certain structural weaknesses, failure to mobilize adequate deposits, the mounting overdues, and lack of trained staff, the co-operatives had failed to come up to expectations. Recommending supplementary efforts through commercial banks, the Review Committee observed that firstly there had been serious and avoidable failures on the part of those who implemented the policy. For instance, the paramount need to establish a viable primary structure was lost sight of and confusion prevailed at this all important level of the co-operative credit organisation. Secondly, the co-ordinated pattern of marketing and credit which was an important postulate for the success of the integrated scheme of rural credit was not achieved except in a marginal measure. The most disquieting feature in the working of credit co-operatives still continues to be the high rate of credit delinquency. The high level of overdues is the single most important factor affecting the flow of credit and virtual stagnation in some regions. Since the borrowers in default are not to be given fresh finance, there is a decline in the growth rate of lendings by the PACSs. The overdues at the end of June 1986 at PACSs' level were 41.8 per cent of the demand and have remained around this level since 1975-76. Another important weakness of the co-operative credit structure is the state of health of the PACSs. Several corrective measures were taken, both by the Government and the Reserve Bank for the reorganisation of primary agricultural credit societies (and also for rehabilitation of central co-operative banks). However, despite all the efforts, the PACSs are even to-day not strong or efficient enough to discharge their responsibilities. Similarly, at the central banks level both their own resources and their eligibility of refinance from the higher financing agencies continue to be limited. This has led to the choking of credit lines and denial of financial assistance to agriculturist members of affiliated PACSs.

6.042 As in dispensing institutional rural credit, so in mobilising rural deposits the co-operative agency initially had been the pioneer. Over the years, however,

despite the emphasis on thrift in the basic philosophy of co-operative organisation, the attempts made in this direction particularly by the primary level organisations have continued to be half-hearted. Table 20 gives the data on the owned funds, deposits and borrowings in the institutions at the three tiers of the co-operative credit structure, as at the end of 1961-62, 1975-76 and 1985-86, together with the relevant proportions of each of these as a component of the total working funds. It will be seen from the table that in the case of state co-operative banks and DCCBs, there has been a gradual increase in self reliance due to increase in the proportion of deposits to the total working funds and a gradual decrease in the proportion of refinance to the total working funds. As at the end of June 1986, the reliance of all state co-operative banks taken together on refinance was as low as 23.4 per cent and in the case of DCCBs the proportion was only 27.8 per cent. The deposits constituted 64.8 per cent in the case of SCBs and 60.0 per cent in the case of DCCBs of the total working funds. However, in the case of PACSs, the deposits constituted only 10.2 per cent. All the same, the seemingly increasing self-reliance of even the DCCBs and SCBs, though a trend in the right direction, cannot obscure the fact that this is self-reliance at a low level of financing, considering not only the potential but also the growth trends of other credit institutions. In point of fact, the resource mobilisation efforts of the co-operatives have not been satisfactory. This has kept the total working funds restricted to much less than the desired levels. It must, however, be recognized barring in few states, that the comparatively sluggish performance of DCCBs in deposit mobilisation is as much a matter of lack of their will and inclination as of the weakness of their infrastructure. Indeed, one gets a feeling in talking to the representatives of most of the DCCBs that they are hesitant to raise deposits beyond a point for fear of incurring losses. The deposits raised by them are at a higher cost, which will necessarily be so in a highly competitive money market, than the rates at which they have to lend to PACSs. It is only in a few states that significant potential exists for direct lending to other co-operative institutions at remunerative rates of interest to cover the losses incurred by them on their lendings to PACSs for short-term agricultural operations. They also cannot, by their very charter, give the kind of facilities and banking services to individuals as can be done by commercial banks, thereby somewhat restricting the circle of their depositor-clientele. Their branch net-work too is somewhat meagre and their staff

Table 20
Proportion of Owned Funds, Deposits and Borrowings to the Working Capital

(Rs. crores)

	1961-62		1975-76		1981-82		1985-86	
	Amount	percentage of working capital	Amount	percentage of working capital	Amount	percentage of working capital	Amount	percentage of working capital
<u>STATE CO-OPERATIVE BANKS</u>								
Owned funds	28.85	11.3	158.71	12.9	396.80	12.4	615.94	11.8
Deposits	81.44	31.8	723.68	59.0	1,879.84	58.7	3,385.41	64.8
Borrowings	145.79	56.9	343.73	28.1	927.88	28.9	1,227.00	23.4
Total	256.08	100.0	1,226.12	100.0	3,204.52	100.0	5,228.35	100.0
<u>DISTRICT CENTRAL CO-OPERATIVE BANKS</u>								
Owned funds	61.80	17.5	360.48	18.8	737.11	14.6	1,006.67	12.2
Deposits	124.46	35.3	984.92	51.4	2,770.13	54.9	4,932.00	60.0
Borrowings	166.39	47.2	570.32	29.8	1,534.87	30.5	2,287.73	27.8
Total	352.65	100.0	1,915.72	100.00	5,042.11	100.0	8,226.40	100.0
<u>PRIMARY AGRICULTURAL CREDIT SOCIETIES</u>								
Owned funds	88.62	27.2	436.86	25.6	838.71	21.5	1,127.62	20.0
Deposits	17.64	5.4	113.31	6.6	316.44	8.1	571.98	10.2
Borrowings	219.07	67.4	1,154.44	67.8	2,754.53	70.4	3,927.22	69.8
Total	325.33	100.0	1,704.61	100.0	3,909.67	100.0	5,626.82	100.0

not fully oriented to the task. Therefore, while it is essential for them to raise larger resources by way of deposits, their genuine problems of deposit raising will also need to be sympathetically looked into and appropriate solutions provided.

6.043 Professionalisation of management is again an area where the co-operatives have failed to make any real progress, in spite of much discussion on it from time to time. More blame in this area of weakness attaches, in fact, to the external controlling and guiding authorities, viz., the state governments, than to the co-operatives themselves, because the latter have rarely been allowed any say in the conduct of their own management. It hardly needs to be emphasised that with the expansion and diversification of the co-operative movement, skilled management assumes special significance. A related area is staff training which forms an essential element in the development of co-operative management. It is necessary that the training of management personnel has to keep pace with the growth and diversification of the co-operative movement.

6.044 Besides attending to the problem areas brought out above, a number of steps also need to be taken in the nature of rationalisation and loosening of certain lending procedures and policies, which in the present context have become operationally constrictive and are hampering initiative and growth. Some of the general issues impinging on the healthy development of the co-operative credit structure as a whole, have already been dealt with by us in the earlier chapter. The most pressing issue of high credit delinquency is also being dealt with by us in a separate chapter. Here we propose to discuss certain measures to tackle other weaknesses specific to short-term credit system with a view to strengthening the co-operatives involved in the system at different levels and thereby facilitating more effective delivery of credit.

E. Recommendations

L Primary Agricultural Credit Societies

(i) Viability

6.045 The concept of three tier hierarchy for the short-term co-operative credit structure already existing was accepted as the appropriate pattern following the A.I.R.C.S.C. recommendations in 1954. The reorganisation of

co-operatives at the level of each of the three tiers has been, more or less, completed except in some states at the primary level. There are thus the state co-operative banks at the apex level in all states and district central co-operative banks at the district level serving an area of by and large one district. A view is sometimes expressed that a three tier structure adds to the cost of purveying credit and that therefore, there might be a case for eliminating at least one tier. Generally the abolition of the middle tier is recommended by the proponents of this view. We have examined this suggestion and do not find ourselves in agreement with it. At the primary level a co-operative has to be as proximate as possible to its membership and therefore its area of operation has necessarily to be limited. This itself imposes certain limitations on the extent to which a primary unit can mobilise its resources. It is in recognition of this that it has been found necessary, not only in India but elsewhere in the world including the developed countries where co-operatives have registered phenomenal success that the primary units need to federate themselves at the secondary level to form a secondary tier. This tier will have a wider area to operate in and extend better services to the clientele. In the Indian context the district has increasingly been recognised as a viable unit for planning, implementation and monitoring. In the co-operative credit structure the secondary level organisation which is the District Central Co-operative Bank, has its area of operation limited to the district. It has been found necessary for the DCCBs in their turn to federate themselves at the state level to form the state co-operative banks to gain access to a wider money market and refinance from the Reserve Bank of India and for providing supervision and effective leadership to the co-operative credit structure as a whole in the state. Such a federal unit at the state level will also supplement the efforts of the DCCBs in mobilisation of additional deposits and function as a balancing centre for the constituent banks. Looking at the cost aspect only, it does not seem that there is scope for any saving, since in the absence of a secondary level organisation the state organisation will have to have regional or zonal offices for discharging the functions not merely for monitoring and supervision but also of providing leadership. A detailed study was undertaken in one of the states by the Reserve Bank of India in regard to the cost reduction aspect consequent on elimination of any one or the other of the three tiers and it was found that even with fine tuning, the cost saving may not be more than 0.25 per cent of the total cost

now incurred by the system as a whole or in other words, by all the three tiers together, but the intangible advantages which accrue to the system far outweigh this meagre saving. Considering also the large territorial and population sizes of the major states in the country, which are in fact larger than many countries in the world, supervision and guidance of the primary level directly from the apex level may not prove a viable proposition. It is in this context that the three tier system has been recognised as central to the principle of federation which governs the organisational structure of the co-operative system in general. Smaller states and Union territories do, of course, have a two tier structure. Even from the point of view of the national level refinancing organisation viz. the NABARD, the meagre margin that the State Co-operative Bank retains on the refinance provided is justified since the repayments to NABARD of its refinance to the co-operative structure is fully guaranteed in this process. Similarly at the state level, the district central co-operative bank insulates the system considerably against the incidence of defaults at the primary level. We, therefore, do not see any advantage in abolishing any one of the tiers. On the other hand, there are positive advantages in continuing with the three-tier structure as it exists today.

6.046 As regards the size of the primary level unit, there have been differences of view which persisted for long time ever since the All-India Rural Credit Survey Committee's recommendations in this regard came to be accepted. The concept of a large sized society underwent several changes till the report of the Committee on Co-operative Credit (1960) and the acceptance of its recommendations by the Central and state governments. This Committee had recommended that, while, as a general rule, co-operatives should be organised on the basis of the village community as the primary unit, where villages were too small, the number to be served by the co-operative society might be increased in the interests of viability. In the words of the Committee one of the main aims of future endeavour should be the promotion of a viable unit of co-operative services and business. A viable unit according to this Committee was one which might be expected within a reasonable time to render the more important of the services expected of credit societies adequately and to as large a number of producers as possible without depending upon financial assistance from the Government except for a limited period. The conference of State Ministers for Co-operation held at Hyderabad in

1964 summarised the guidelines to be followed in pursuance of the above approach. These indicated that the minimum criteria of viability could be put down as the ability to (a) appoint full-time paid secretary, (b) set up a regular office in a building owned or hired, (c) contribute to statutory and other reserves on the scales considered necessary and (d) pay a reasonable dividend. According to the above guidelines the minimum credit business of the society was fixed at Rs.2 lakhs in 1973. Looking at it from the potentiality angle, the Reserve Bank of India had advised that the area of operation of society should cover cultivated area of 2,000 hectares to enable the society to have adequate short and medium-term agricultural business. The process of reorganisation on these basis has already been completed in all the states, except in Gujarat, Jammu & Kashmir and Maharashtra. It is understood that in Jammu & Kashmir also it is now under way. One of the reasons for hesitation in these states in doing so is stated to be the unwillingness of non-viable PACSs to merge with others. This hesitation will have to be got over and the societies reorganised as early as possible. The states of Maharashtra and Gujarat have had a long tradition of co-operative development, but in the present day context their primary societies, due to their attenuated state, have become incapable of meeting the rising demands of a growing agricultural economy and are to that extent failing to exploit the potential.

6.047 In spite of reorganisation of PACSs in most of the states, a large number of societies continues to have low borrowing membership, low business turnover and high level of overdues resulting in accumulation of losses. Although the latest position of viable and non-viable primary societies is not available, the data indicates that a large number of societies are still functioning at a non-viable stage. This is clear from the fact that out of 92,000 societies only 68,000 societies had a full-time secretary. Further, at the end of June 1985, only 56.5 per cent societies were working at profit. It is, therefore, necessary that the state governments take a fresh look at the primary societies in their states and implement the various suggestions made in this report for improving the viability of the societies. According to the guidelines for identification of potentially viable PACSs, it is necessary that a society should have a minimum gross cultivated area of 2,000 hectares in its area of operation. Since the scales of finance for different crops as well as the unit costs of different kind of medium-term agricultural investments has been continuously

going up, the loan business potential of financing an area of 2,000 hectares itself has increased substantially by now. Taking a diverse crop mix (both irrigated and non-irrigated), at an average scale of finance of Rs.1,500 per hectare, the 2,000 hectare area will bring in a business of Rs.30 lakhs as short-term agricultural loans. Even if the coverage of members is one-third, the loaning will be Rs.10 lakhs. Even at the assured margin of 2.5 per cent which is available at present on the funds borrowed from CCB, the PACSs should be able to make an annual income of more than Rs.20,000 if overdues do not exceed 20 per cent. This together with the efforts made by the PACSs for generating larger non-credit business, besides intensifying the coverage of members, i.e. enlarging borrowing membership and increasing the quantum of lending consistent with the requirements of agricultural technology can place most of the PACSs in a comfortable position of viability and give them confidence enough to undertake an ever expanding package of services to their members. Studies conducted by our consultants have indicated that the optimum size of a society at which the income is maximum is a volume of business of Rs.25 lakhs to Rs.30 lakhs per annum and the break even level of credit operations is Rs.17 lakhs. The optimum levels of credit and non-credit operations, thus, are at Rs.17 lakhs and Rs.8 lakhs to Rs.13 lakhs respectively. It will however be naive to expect that the large number of PACSs which still continue to be non-viable inspite of their reorganisation on the criterion of potential viability, will actually attain reasonable viability on their own momentum in the near future. The trends that we see from the data are discouraging in this respect. A very large number of PACSs has continued to stagnate at a low level of business in spite of more than a decade of their functioning as "potentially viable" societies. It is, therefore, necessary that a determined and a clearly programmed effort be made to upgrade their level of functioning. We propose the following lines of action in this behalf.

6.048 Firstly, a programme of action has to be drawn up for each PACS. A macro approach in the form of broad guidelines and general directions alone will not suffice. We are of the view that all PACSs which have not so far reached a loaning business of Rs.10 lakhs should be taken up for specific attention. A programme of development should be drawn up for each of these PACSs in the context of its specific potential and possibilities by the DCCB with appropriate assistance from the SCB and the Department of Co-operation

of the State Government. The programme of development for each PACS should particularly deal with increasing its loan business, enlarging its package of profitable non-credit activities, augmentation of resources (deposit mobilisation etc.) and reduction in overdues, with a view to reaching a volume of business indicated in the previous paragraph. The programme should be a phased one extending over a period not exceeding 5 years, which we believe is a period reasonable enough for even the weakest of the PACSs to reach an acceptable level of business and consequent viability. In fact, as we see it, the period of the Eighth Five Year Plan, beginning 1990 should be the period devoted to reviving and strengthening all the PACSs at least to a level that they come to acquire a sustained momentum of growth and resolutely the capacity to adequately handling the challenges of a growing and diversifying agricultural economy. The implementation of the programme for each PACS, needless to say, will have to be closely monitored and the required guidance given from time to time. The states of Maharashtra, Gujarat and Jammu & Kashmir which have not so far taken up the programme of reorganization of PACSs at all, must undertake this programme at the earliest and simultaneously proceed with a programme of development of the reorganized PACSs.

6.049 Secondly, it is of the utmost importance that each PACS should have at least one full-time paid official, namely the secretary, who can handle its business activities on a regular basis. One of the principal reasons for all PACSs not being able to engage a full-time Secretary is their incapacity to pay his salary. Secretaries' cadre and Salary Fund Schemes were devised specifically with a view to getting over this difficulty of weaker PACSs. In practice, however, these schemes have failed to meet the problem and many PACSs still do not have a full-time Secretary. In fact, the data indicating a number of PACSs having a full-time Secretary also needs to be taken with a pinch of salt. The impression we got during our visits was that many of these so-called full-time Secretaries were so poorly paid that they took up side jobs and, were, in fact, no better than part-time Secretaries. It is patent that a sizeable number of PACSs will not be able to engage a Secretary at a reasonable pay in their present state of financial health. But a solution has to be found to the problem, because it is critical to the entire scheme of viable functioning of the PACSs. We are making some recommendations in this behalf later in the chapter.

6.050 Thirdly, the process of reorganisation must not stop short at what had been brought about more than a decade ago at the instance of the Reserve Bank of India and the state governments. The needs and postulates of a growing economy call for flexibility. They must continue to change in line with the dynamics of the situation, calling not only for different viability requirements but also for enlarged scope and volume of services that they must render to their members. In this context, we are of the view that the number of reorganised PACSs must continue to get reduced, with each PACS covering a larger area than now and thereby becoming financially and operationally stronger in the process. However, our intention in saying this is not to recommend another state-sponsored programme of reorganisation of PACSs (except in the three states mentioned earlier), which in our view will be straitjacketed in nature and, therefore, not a satisfactory solution. Further reorganisation must come through voluntary effort and through an emerging awareness among PACSs to amalgamate with their neighbours with a view to attaining a more competitive and viable size. The endeavour on the part of the higher level co-operative organisations and the state government should be to create this awareness among members and managing committees, so that interaction and thinking can develop in the PACSs on these lines. Results will come gradually to begin with, but in course of time, the pressure from members will force the pace. As we see it, significant development in this direction will start taking place only around the Ninth Five Year Plan, i.e. after the basic programme of rejuvenation of the existing PACSs has been successfully undertaken during the Eighth Plan. Motivation for bolder organisational changes, in response to heightened expectations of members for still better services, will come when the PACSs have first broken through to a reasonable level of performance.

(ii) Strengthening of Share Capital

6.051 One of the conditions stipulated by NABARD while sanctioning the loans to state governments from NRC(LTO) Fund for share capital contribution to PACSs is that the societies should not have overdues exceeding 40 per cent of the demand, except in respect of certain category of societies including societies affiliated to weak CCBs under a scheme of rehabilitation for which loans could be granted for share capital contribution upto Rs.25,000 irrespective of the percentage of overdues to demand. Recently, as a measure of drought

relief, the NABARD had relaxed for the year 1987-88, the conditions regarding eligibility for share capital assistance such as level of overdues, level of business etc. on merits of each case. Since most of the societies have overdues above 40 per cent except in a few states, the state governments are unable to avail of the facility of long-term loans from NABARD for share capital contribution to the extent required. Since the share capital required for various purposes by PACSs is now higher in the present context when the viable business norm itself has to be pegged at a higher level than what was envisaged earlier, we are of the view that the share capital requirement may be worked out for each PACS in the light of the programme of action for PACSs' viability recommended by us earlier and additional share capital contribution provided by the State Government to them to the extent of their minimum requirement. The minimum essential requirement must be provided by NABARD irrespective of overdues and other such considerations. The problem of overdues is such as has to be tackled by itself through the programme of action and should not be made a constraint on other essential requirements.

6.052 At present the entire share capital collected by PACSs from members is invested with the DCCB. In other words, it appears that the PACSs exist for the DCCB and not the other way round. The current trend of higher level federal institutions looking after their own interest at the cost of their federating constituents must be reversed in order to have a healthy federal structure. Since the present system leaves no share capital from members with PACSs we recommend that the ratio of share linking at the DCCB level for PACSs may be fixed at five per cent in respect of both small farmers and others. This will strike a reasonable balance between the interests of both the tiers.

6.053 At present the ratio of share linking to borrowings in respect of cash credits to PACSs, for marketing, consumer activities etc. is two and a half per cent. We recommend that the ratio of share linking in respect of cash credits to PACSs be reduced from two and a half per cent to one per cent. This will enable some more of the share capital received by PACSs from their members to be retained at their level.

(iii) Mobilisation of Deposits

6.054 Resource mobilisation is another major area of weakness in the primary

credit structure. At present most of the PACSs are totally dependent on the finance provided by DCCBs. In case the DCCBs are weak, the PACSs are starved of finance. This affects the expansion of both the credit and non-credit functions of PACSs. The branches of commercial banks and RRBs are able to mobilise rural savings. It should be possible for PACSs also to mobilise deposits from members and non-members in their areas of operation. The fact, however, is that having begun as thrift societies they have over the years deviated from their original philosophy, except in a few states. The fault is not entirely theirs. Their whole culture has been shaped by the dictates and directions of those who regulate them. The main emphasis by the State Departments of Co-operation in the development of primary credit societies since the early fifties has been on their ability to become successful channels of refinance. Consequently, they came more and more to function merely as post offices for routing of refinance and themselves also began seeing their own role as such. This culture must change and realisation must dawn that without own resource mobilisation the scope and size of agricultural lending by PACSs will continue to remain far short of requirements. Indeed, with the progressive reduction in the proportion of refinance, as seems inevitable in the years to come and when the total demand for credit will be much larger, their very survival will be at stake in the absence of augmentation of their resources through deposit mobilisation. Refinance will not only remain limited in volume, but will in the ultimate analysis prove more expensive affecting their viability. We do not minimise the difficulties in making a beginning in this direction. Bedraggled as most of them are, the societies do not even have the essential wherewithal for handling deposits. The weak, and more particularly the unprofitable ones, have poor image and credibility which is so essential for inspiring the confidence of a potential depositor. Nevertheless, we consider deposit mobilisation to be vital for the future growth and strength of PACSs. We urge that they should be enabled and equipped to undertake this function in a significant way. All PACSs will not be able to straightaway take it up because of lack of appropriate infrastructure and suitable personnel. It will, therefore, be necessary to draw up a phased programme whereunder, to begin with, those PACSs which have the necessary wherewithal and are somewhat better equipped are encouraged to start taking deposits and those which already have some experience of handling deposits may intensify their efforts in this direction, and in subsequent phases, year

by year, the rest of the PACSs are also brought within the fold. Considerable guidance and assistance will need to be given to equip and orient them to this onerous field of activity.

6.055 The SCB/DCCB could help in building up infrastructural facilities like banking counters and a safe for holding cash/valuables etc. in the case of those societies having a building, either own or hired, with adequate security arrangements. Some of the SCBs/DCCBs in the states of Madhya Pradesh, Uttar Pradesh, Tamil Nadu and Andhra Pradesh have introduced schemes for providing PACSs with grants ranging from Rs.6,000 to Rs.10,000 for providing modern counters, for purchase of safe etc. However, the number of PACSs assisted under these schemes is small in view of the meagre funds allocated by the banks. PACSs require to be provided with adequate assistance in the form of grants/loans from the higher level institutions viz. DCCBs and SCBs which are entrusted with the responsibilities of leadership in developing the ground level structure. CRAFTICARD had recommended that DCCBs and SCBs should create a primary co-operative development fund (PCDF) for helping the PACSs to emerge as fullfledged multi-purpose co-operative societies. It was also recommended by CRAFTICARD that the banks instead of making ad hoc lumpsum appropriation out of the general resources for the fund should make regular systematic contributions, at stipulated rates from their annual profits. However, the recommendation has not been implemented by most of the DCCBs/SCBs. We reiterate that SCBs/DCCBs should create a primary co-operative development fund as recommended by CRAFTICARD without delay and should make regular contributions so that assistance could be given to PACSs for erection of modern counters, purchase of safe etc. for taking up banking activities and also to present a better image on depositors and members as a credit institution.

6.056 We are aware that PACSs are handicapped as compared to RRBs and branches of commercial banks for want of deposit insurance while mobilising rural deposits, particularly when they have to compete with the rest of the banking system which enjoy the advantage of insurance cover. We understand that the question of DICGC extending deposit insurance cover to PACSs was earlier examined but this did not materialise due to various difficulties in view of their very large number, tasks involved in ensuring

their financial strength, etc. by a national institution like RBI and problem of statutory inspections and collection of periodic returns regarding deposits and collection of premia from PACSs. But all the same, the PACSs cannot altogether be left without any insurance cover whatsoever for their deposits since we envisage massive deposit mobilisation efforts on their part in future. We recognize the difficulties on the part of DICGC in extending insurance cover at this juncture. We would therefore recommend that to start with SCBs in co-ordination with the respective state governments should formulate suitable schemes for insuring deposits of PACSs in their states. The state-wise schemes, we feel, will be more manageable than one on an All-India basis.

6.057 Since PACSs do not come under the purview of the B.R. Act as applicable to co-operative societies, interest rate directives issued by the Reserve Bank of India are not applicable to them. They can, within limits, offer rates of interest higher than those offered by commercial banks and RRBs. We would, however, emphasise that the PACSs should endeavour to mobilise more savings deposits which can be profitably used in its own credit and non-credit business since they constitute low cost resources as compared to term deposits and borrowings from higher financing agencies.

6.058 As PACSs are not governed by the Banking Regulation Act, the norms prescribed for the maintenance of liquid assets are not applicable to them. Of course, all surplus resources that a PACS may have at any point of time are required under the state co-operative law to be invested with the DCCB. In our view, it is necessary that some definite liquidity norm should be stipulated for PACSs also as a policy directive. We have placed considerable emphasis in our report on the imperative need for vigorous deposit mobilisation by PACSs. In that context a definite pattern of liquidity cover will be extremely desirable. This liquidity may be maintained in the form of a special deposit account with the DCCB. Our intention also is that by doing so a newer and a more mutually supportive relationship will be brought about between the DCCB and PACSs, for while it is the duty of the DCCB to assist the PACSs, it is also the obligation of the PACSs to strengthen the resources of the DCCB so that it would serve the PACSs better. In our view, a liquidity cover of 15 per cent of the deposits will be appropriate to begin with. In other words, the special deposit account will be allowed to be so operated

that at any point of time the balance should not be less than 15 per cent of the PACS' deposits. The PACSs may withdraw from the special deposit account any amount in excess of the minimum liquidity cover to be maintained by them. If the PACS wants to have more funds for its business operations, it will have to resort to borrowing/refinance facility from DCCB. This special deposit account should earn an interest at one and a half per cent higher than the rate of interest on savings deposits, because though in nature a savings deposit account, it also has an element similar to a fixed deposit in respect of the minimum 15 per cent balance to be maintained.

(iv) Lending Policies and Procedures

6.059 An important area of concern is that which is ultimately associated with the lending policies and procedures of co-operative credit institutions. The crop loan system has been by now accepted and implemented in all of its essential characteristics for financing SAO though a few deviations are still noticed in certain states which operate as restrictive practices. For example, in West Bengal for short-term agricultural loans in excess of Rs.1000 mortgage of land is insisted upon though the State Government and Registrar of Co-operative Societies (RCS) have issued instructions not to insist on such security. The five essential features of the crop loan system are : (i) determination of the quantum of credit in relation to the production needs, and repaying capacity, (ii) disbursement of substantial portion of the loan in kind, (iii) seasonality in the advancing and repayment of loans, (iv) advancing the loans against the security of crop (to be raised) rather than against the security of land, (v) streamlining of procedures for sanction and disbursement of loans.

6.060 In the light of experience gained over the last two decades, certain modifications in some aspects of the system as formulated in the crop loan manual are necessary either generally or in particular areas to suit local conditions and changed environment.

(a) Cash Credit System

6.061 For financing crop loans, fixed short-term loans are granted for a period not exceeding 12 months. It had been urged on us by many that the fixed loan system for crop production was not suitable for agriculture and should be replaced by cash credit system. The arguments made in favour

of introducing cash credit system for agriculture are : (i) the term loan system does not meet adequately and timely the cash requirement of borrowers, (ii) the fixed due date system of the term loan forces the farmer to sell his produce earlier even at non-remunerative prices if he has to avoid the default, (iii) the borrower is ineligible to draw further funds even if a small portion of his short-term loan has not been repaid on the due date.

6.062 The pre-requisite of cash credit system are : (i) The borrower needs cash and receives cash frequently during the year as the production and sales of the unit go on throughout the year, (ii) the lending bank has close supervision over the borrowers' operations in the account and (iii) the lending institution has requisite infrastructure to maintain accounts and watch the borrowers' activities closely. The system has already been introduced in some parts of the Kerala, Tamil Nadu etc. where there is perennial irrigation with a multiple cropping pattern and for crops like arecanut, coconut, betelwines where expenditure is not related to seasonal pattern and yields and cash flows are seen almost throughout the year. Therefore, the situation lends itself to a reasonably successful operation of the system. Cash credit system is a sophisticated and personalised type of credit arrangement and it is necessary for the credit agency to enforce proper disciplines to ensure that (a) draws on the cash credit limits are for making genuine payments connected with the cost of cultivations, (b) the outstandings against the limit are backed by agricultural inputs/supplies on hand, standing crops and unsold agricultural produce and that (c) the sale proceeds of the agricultural produce when received are promptly credited to the cash credit account (d) the outstandings under the sanctioned limits are brought down to a minimum at least some time during the year when there are neither agricultural produce on hand nor any standing crops in the fields and (e) sanction and renewal of the cash credit limits is done after proper scrutiny of the cash inflows and outflows.

0.063 Under the system, detailed production plans will have to be drawn up for each cultivator covering the whole year, showing the calendar of different crops raised, the package of practices followed to estimate the cost of supplies required from time to time as well as the particular harvesting and marketing seasons of the concerned crops and the expected cash realisation by way of sale proceeds of the agricultural produce. This would enable the

credit agency to determine the quantum of cash credit limit required to be sanctioned and the manner in which credit would be used and repaid.

6.064 These precautions are necessary to avoid the likelihood of (i) misuse of credit for meeting consumption needs, expenses connected with religious/social functions, etc. and (ii) the outstandings turning out to be a permanent loan without commensurate repayments in the account. In that case instead of facilitating production credit and making it more flexible, the accommodation may become non-productive and the arrangement a means of camouflaging the position of overdues.

6.065 Another essential pre-requisite for introduction of the cash credit facility is that the credit agencies are strong and well managed. Thus in the case of PACSs, they should firstly have not only full time qualified secretaries but also adequate support from CCBs while in the case of branches of commercial banks, arrangements should exist for adequate supervision. The field survey data given by Consultants entrusted with Study II indicates that as against the norm of 500 agricultural accounts per supervisor (in commercial bank branches), in most of the branches the supervisor had a heavier charge ranging from 1,000 to 2,400 accounts.

6.066 In the light of the above and after considering the advantages and disadvantages of introducing the cash credit system in financing short-term agricultural needs, we are of the view that the cash credit system may be introduced only in areas where perennial irrigation is available and multiple cropping is in practice and not in other areas where only one crop is grown during the year and the agricultural practices do not require frequent operations on the loan account. Our studies relating to agricultural credit in general on the one hand and on the effectiveness of lending institution on the other have convinced us, and this is borne out by the findings of the Consultants conducting Study I and II, that cash credit system could operate successfully only in areas where perennial irrigation is available and multiple cropping is in practice. We recommend that the system may be progressively introduced in multi-cropped areas, beginning first with those PACSs which have the personnel and the capability to handle it satisfactorily. The same consideration applies to the branches of commercial banks. As for single-cropped areas,

the answer lies not in the adoption of the cash credit system but in modifying certain procedures under the existing system in a manner that facilitates quicker fixation of credit limits and timely flow of credit. Indeed, it is these time consuming procedures which are at the back of the desire to have the present system changed to cash credit one.

(b) Normal Credit Statement

6.067 In terms of the crop loan system, the societies are required to prepare a normal credit statement for all the members once every year well before the beginning of the Kharif season in which the maximum credit limit of each individual member is fixed. As far as the short-term agricultural loans are concerned this is a very important and basic document. It indicates the acreage under cultivation (irrigated/non-irrigated) of each member under the kharif, rabi and other crops; and also the split up of the loan into cash and kind components for each financing season based on the acreage and scales of finance. The acreage shown under various crops is to be checked by the secretary with the land register prepared on the basis of village revenue records.

6.068 Experience so far has shown that the preparation of a normal credit statement each year is a time consuming exercise and since it has to be prepared in the months of January/February every year, (which coincides with the recovery season) the attention of the staff gets diverted. Since no material changes take place in the cropping pattern, in the case of most of the members every year, the exercise becomes mainly duplicative of the previous one. The requirement of obtaining each member's signature or thumb impression also takes time and in view of these reasons, the statements do not get prepared by the societies in time, leading to delays in the disbursement of credit, or where prepared they are not complete in all respects. We have considered the question and recommend that the normal credit statements need be prepared once in three years, subject to the proviso that if the scale of finance is changed in any year, the normal credit statement will have to be prepared afresh for that year. Otherwise the society will only have to prepare a supplementary credit limit statement in respect of new members admitted in the society during the year, or if there are any changes in the land holding/cropping pattern of the existing members, the same will have

to be indicated by preparation of a new statement for such members or corrections carried out in the last year's statement against their names.

(c) Disbursement of Kind Component

6.069 An important feature of the crop loan system is the insistence on disbursement of kind component in kind only. The stipulation was initially prescribed to ensure that the loan was not misutilised as also to popularise the use of fertilisers, pesticides etc. This discipline over the years has substantially served its purpose. Indian farmers have since taken to the new technology and are extensively using fertilisers, pesticides, etc. In areas, therefore, where the use of these inputs has been firmly established, there does not appear to be much need for issue of inputs in kind for promoting their compulsive use. On the contrary, in areas where their use has not become widespread, it has been observed during the field studies that the members have either not lifted the kind component at all or instances have been noticed where some members have later sold off the inputs so received in kind. Resistance also arises in lifting the kind component in societies where adequate arrangements do not exist for supply of fertilisers, pesticides etc. of farmers' choice. Our study has shown that in such areas where cultivators have become increasingly fertiliser conscious, it is not necessary to disburse credit in kind. The farmers should have a choice to purchase inputs of their liking from any available source. Nevertheless, we do recognise that the system of disbursement of credit for inputs in kind has served a very useful purpose. It not only has acted as a promotional measure for the use of these inputs with an assured credit support, but has by providing the clientele for these inputs also enabled the PACSs to undertake the stocking and sale of these inputs. Private trade generally goes only to those areas where the use of these inputs has been well established and the sale prospects are quick and substantial. Most of the areas in which private retailers are operating today are the ones which were opened up initially by the efforts of the co-operatives. There are still vast areas of the country where the private trade does not find worth its while to establish its outlets, and the input supplies have to be mainly arranged by the co-operatives. There the continuance of the 'B' component system in kind will still be needed. Considering all these factors it is recommended that the societies may not insist on disbursing the input component in kind in areas where the farmers are already accustomed to the use of these inputs.

The decision whether to disburse this component in kind only or otherwise may be left to the discretion of the DCCB in the light of the local situation and if the DCCB feels that such insistence is not necessary, it could be waived.

(d) Recovery - Fixing of Due Date

6.070 At present the stipulated financing periods for kharif and rabi crops with due date of repayment are as follows :

	<u>Kharif</u>	<u>Rabi</u>
1. Financing period	May to September	October to March
2. Marketing season	October to December	April to June
3. Due date of repayment	31 March	30 June

The above discipline has been prescribed in order to ensure proper seasonality in the lending and repayment of loans and thereby minimise the possibility of misuse of funds. It allows the cultivator a reasonable period to market his produce while avoiding distress sales to repay the debt. It also facilitates the planning of recovery efforts, i.e. to contact borrowers when they are in funds. Calculation of overdues is rendered easier as the system is simple to operate.

6.071 The weaknesses noticed over the last few years are : (i) cropping pattern of farmers has undergone a change and repayments are not necessarily made out of the sale proceeds of the crop(s) for which loans are contracted (ii) marketing season of some crops lasts for a longer period as the farmer's holding power has increased, (iii) in the case of rabi crop the period of three months is considered too short for marketing, collecting sale proceeds and making repayment; and (iv) the default in repayment of the loan by June end or even a part repayment of rabi loan renders a farmer ineligible for his kharif requirements from 1st July onwards.

6.072 While the seasonality schedule prescribed for disbursement of kharif loans and recovery thereof has a virtual universal acceptance, the suggestion that the rabi due date may be shifted to a later date instead of June-end needs consideration. This will give sufficient time to the borrower of a rabi loan for the marketing of his produce and repaying the loan. It is a normal experience that the prices of agricultural commodities are comparatively higher during July and August as compared to those in May or June.

6.073 At present when the kharif loan is outstanding the borrower is eligible to draw a rabi loan though to the extent of kind portion of loan only. After repayment of the cash portion of the kharif loan, he becomes eligible for the cash component of rabi loan, even though the due date of the kharif loans falls later. We consider that this stipulation comes in the way of full rabi financing and favour its removal. Likewise, we also do not favour the stipulation that the cash component under rabi loan should be repaid before disbursing the cash component of kharif loan. Kharif crop normally requires a larger cash component than that of rabi crops, and hence such a stipulation would come in the way of meeting the requirements of the farmers. We have observed that there is a tendency in banks in rabi areas to finance kharif requirements heavily in the month of June itself mainly because after 30th June i.e. the due date of rabi repayment, there may not be eligibility of the borrowers or the society and the DCCB for a fresh limit to draw upon. If the due date for rabi itself is shifted to a later date such tendencies to bypass the discipline will be avoided.

6.074 In view of the above, we recommend that the due date of repayment for rabi loans should be changed to 31 August instead of the present one of 30th June. By thus allowing another two months in setting the date of repayment of the rabi loan, the rabi farmers will have been given reasonable time for the marketing of their crop at more remunerative prices. This, in our view, is the most important consideration in giving a somewhat longer period, than presently allowed, for the repayment of a rabi loan. By doing so we will be giving to the rabi borrowers the same marketing period as is available to the kharif borrowers.

(e) Scales of Finance

6.075 According to the crop loan system a district level technical committee (DTC) consisting of representatives from Agriculture and Co-operation Departments of the State Government, the DCCB, selected PACSs and a few successful and enterprising agriculturists in the area is to be constituted to fix the scale of finance every year. The Committee has been later enlarged to include representatives of the Lead Bank and one or two major commercial banks in the district. The task of this essentially technical body is to determine the norms of lending, keeping in view the resource position of the lending agencies and experience in regard to the use of fertilisers and adoption of

improved agricultural practices. The scales of finance under the crop loan system as a whole are to be fixed for compact areas covering one or more talukas depending upon variations in natural conditions such as rainfall, irrigation facilities, types of soil, improved agricultural practices in vogue etc. Separate scales are required to be laid down for irrigated and non-irrigated areas. The Reserve Bank of India had reiterated these guidelines in 1979 when it came to its notice that many of the DCCBs were not following the guidelines in the crop loan manual. While fixing the scales of finance on the basis of the cost of cultivation of major crops grown in the district, the Committee has also to take into account the repaying capacity of the cultivator. Normally 50 per cent of the value of the gross yield is taken as the total repaying capacity from the crop and only 2/3rd of it can be taken as available for short-term agricultural loans, the balance 1/3rd being left for repayment of medium-term agricultural loans.

6.076 It has been pointed out by some representatives of financial institutions that the present scales of finance fixed by the District Level Technical Committee (DTC) of the DCCBs and accepted by commercial banks are generally inadequate. Some of the studies undertaken at our instance indicate that the scales of finance as determined by the DTC for major crops were found to be falling short by about 50 per cent of the farmers' requirements. One reason cited for this was said to be the general practice presently followed, of the scales of finance being fixed on an adhoc basis taking into account the availability of resources with DCCBs rather than the requirements of the crops in question. The actual disbursements to borrowers are generally even below the scale of finance sanctioned. The net result has been, allround underfinancing. From our field visits and the sample survey conducted by our consultants, it appears that the principal authority for finally fixing the scale of finance in most of the states is the Registrar of Co-operative Societies. The Registrar fixes the scale not so much in the light of the investment needs of the crops worked out by DTC or field workers conference, but on consideration of rationing of the available resources. The commercial banks and the RRBs also generally follow the same scales of finance as decided for the co-operatives although whenever pressure was brought by the branches concerned, they were able to obtain clearance from their Regional Offices for an enhanced scale but not to the full extent.

6.077 There is thus admittedly, a general feeling that the scales of finance fixed by the DTC in many states are not adequate. Our considered view is that the resources crunch experienced by any one or the other of the components of the credit system should not be the determining factor in fixing the scale of finance as such. Underfinancing is very often a cause for mis-utilisation and consequent overdues. The scales must be fixed strictly in the light of the instructions contained in the Crop Loan Manual (which also takes repaying capacity into account) by the widely representative DTC. If, however, there is shortage of resources with a particular credit institution even after availing of all facilities of refinance etc. and a reduction in the total quantum of credit required by the clientele has necessarily to be resorted to, the remedy should lie not in tinkering with the recommended scales of finance but in distributing the available funds equitably to different classes of borrowers. For instance, larger farmers who have own resources and savings may not need to be given credit on full scale whereas the small farmer cannot do without credit to the full extent. Such a prioritisation can be done at least in respect of the "cash component" in terms of classes of borrowers. When the scales themselves are reduced because of resources constraint, no one gets according to need and everyone suffers. But when prioritisation is done in terms of capacity, those who are the most needy get what they require and those who can do with less get less. Moreover if the scales of finance are kept at the level they ought to, good co-operatives having adequate resources will be able to lend to all according to the recommended scales and only those co-operatives which have resources constraint will need to resort to some kind of rationing.

(v) Management

6.078 A major area of weakness of the primary co-operative credit structure is the quality of its management. No programme of development can fructify without there being properly qualified personnel handling the day to day operations of the PACSs. Appointment of at least one full-time qualified and trained manager, known generally as the Secretary, is therefore critical to the development of the society. Appointment of such a functionary in each reorganised PACS was envisaged in the scheme of reorganisation. As it was not possible for most PACSs in their current stage of development and financial standing to engage a full-time secretary on a reasonable salary, most of the state governments devised a Cadre Scheme where under centralised recruitment of

secretaries was done at the district level and persons so selected were placed in the PACSs as secretaries. Those of the existing secretaries who were found suitable on the basis of their performance and other factors were also included in the cadre. The district cadre was either managed by the DCCB or by a specially constituted cadre society. To give financial backing to the cadre scheme, a cadre fund was also constituted at the district level to which contributions were required to be made at stipulated scales by the SCBs, DCCBs and the PACSs, besides such managerial subsidy as was available from the state governments. The salary of the cadre secretaries posted to the PACSs was paid out of this fund. It was felt that this scheme would take care of the problem of appointment of a full-time secretary to each PACS. Arrangements were also made for the training of these secretaries on a phased basis. However, after showing initial promise the scheme faltered. Cadre fund was not constituted by many DCCBs and where constituted contributions required were not often made regularly by the PACSs and DCCBs. The State Government contribution also ceased after some years. The secretaries appointed under the cadre scheme were thus left high and dry. Many of them left, some took up side jobs neglecting their commitment towards the society. Only those who were working in societies which were making good profits functioned on a regular full-time basis. Another fall-out of the cadre scheme was the unionisation of the secretaries leading to mass agitations and strikes at such crucial times as the recovery or the lending seasons, thereby disrupting the working of the societies.

6.079 Whatever the problems may have been of the cadre scheme, the main objection to such an arrangement, to our mind, is the lack of accountability of the secretary to the managing committee of the society. He is selected and appointed by an outside authority. The managing committee has no disciplinary control over him. He, therefore, does not see himself as accountable to the society but to the cadre controlling authority. This is a situation which is totally alien to any management or administrative concept. We are firmly of the view that the power of appointment of the secretary must fully vest in the PACSs and not in any outside authority. The obligation of the higher levels is to assist the PACSs in finding the right persons and not in taking over the management itself through this device. One of the ways in which the DCCB can assist the PACSs in this regard is by preparing panels of suitable candidates from which the appointment can be made by

PACs if they so choose. We strongly recommend that the existing cadre system should be given up and the PACs should be allowed to recruit their own secretaries. The SCB should only prescribe qualifications, selection procedures to ensure objectivity and scales of pay, in consultation with the Registrar of Co-operative Societies. Adherence by PACs to the qualifications and selection norms should be monitored and ensured by the DCCBs. Scales of pay will require to be prescribed for different gradations of societies, say, upto Rs.5 lakhs credit business, Rs.6 lakhs to Rs.10 lakhs business and above Rs.10 lakhs business etc.

6.080 The present day secretaries of PACs are often chosen under the cadre system from applicants with low motivation, with limited expertise and limited education. These secretaries are generally not committed to the management of the co-operatives but are responsible to the cadre. They are either ill-trained or not trained at all for the task they are called upon to handle. We have, therefore, suggested a package of recommendations to improve the calibre of the secretary, the selection process and the training. The secretary being the kingpin of the primary agricultural credit organisation, should be an able and dynamic person for the survival and improvement of the co-operative society. The secretary should be trained by the DCCB early in his career and should have frequent opportunities for further training through refresher courses. We have seen the importance given to training during our visits in Holland where the primary banks send their staff for training almost at regular intervals. We have given our recommendations in this regard in Chapter XIII on Staff Training and Manpower Development.

6.081 One of the reasons for the PACs not being able to get good candidates for appointment as secretaries is the lack of opportunities for upward mobility for them. It is necessary that a system should be developed which will provide them avenues of promotion. The cadre system did take care of this need to some extent, but we have for more important reasons brought out above, disfavoured the cadre system. Promotion opportunities have, therefore, now to be provided in a different manner. We suggest a two-fold approach in this behalf. On the one side, a regular procedure needs to be developed under which the DCCB informs all incumbent secretaries of PACs in lower business classifications whenever a particular PACS intends to recruit a secretary, so that the secretaries in other PACs may choose to compete for

the post in the PACS of higher classification with its higher emoluments. On the other side, a specific quota of appropriate posts may also be earmarked in the DCCB itself, to which recruitment may be made on merit only from the secretaries of PACSs. Thus one is a procedure for informing the secretaries of the opportunities available in other PACSs, so that they can take their chance if they so wish, and the other is a specific reservation of posts in DCCBs to which the secretaries could be appointed offering higher career prospects.

6.082 The question, however, of ensuring payment of the prescribed salary to the secretaries by all PACSs still remains. Roughly half the societies are running in loss and even out of the profit-making societies there are many whose level of business is low and profits are only marginal. Thus, for a large number of PACSs it is beyond the capability of their present financial resources to pay the secretary's salary at an appropriate scale. Therefore, till such time as all PACSs reach a reasonable level of viability, arrangement in the nature of a District Fund at the level of the DCCB will have to be maintained. However, the Fund that we are now recommending is somewhat different from the present salary fund. The present fund envisages payment of full salary of the cadre secretary in the case of all PACSs from out of the fund, consequently contribution has also to be made by all PACSs at graded scales to the fund. As we see it, the obligation to pay the salary to the Secretary must necessarily be that of the PACS concerned. However, recognising that many PACSs are weak, and thus not in a position to pay the full amount from their own resources, they would need assistance. This fund will provide that assistance to the extent of the deficit in their capability to pay the full salary. The assistance or conversely the deficit, will be determined by the DCCB after a careful assessment of the financial position of the PACSs concerned. The contributors to this fund would be the State Co-operative Bank, the Central Co-operative Bank of the district concerned, stronger PACSs and also the State Government. We postulate contribution from PACS also, many of whom will in any case be meeting the full salary commitments of the secretary from out of their own resources because in line with the principles of co-operation all must contribute according to their capacity and also because it is in the interest of the whole system that all work well. In this context it will be desirable to classify PACSs into at least three categories on some reasonable set of criteria, say, very good, good and weak, in a manner

of speaking. The weak PACSs will be required to make a small contribution to the fund, and the very good ones will be required to contribute at a somewhat higher scale than the good ones. We do not intend to indicate here the proportion in which the SCB, CCBs, PACSs and the State Government should share the contribution towards the fund because there cannot be one uniform set of scales for all the states in the country with their diverse conditions and levels of development. This proportion can more appropriately be decided upon by the SCBs in consultation with the others concerned, though as a general guideline we would suggest that the DCCB and SCB may contribute 1/4 per cent and 1/8 per cent of their outstandings respectively for the purpose. The deficit, if any, in the fund should be met by the State Government through its contribution. The State Government has a vital stake in good management and viability of the PACSs, and must therefore give the required financial backing. The district fund may be administered by a committee with representatives of SCB, DCCB, PACSs and the Registrar of Co-operative Societies.

6.083 In regard to the salary of the secretary, we are of the view that considering the paying capacity of the PACSs on the one hand and the developmental role that the secretary is required to play in business development of the PACSs on the other, his salary structure should be conceived in two parts : Part I will comprise the basic salary which ought to be reasonable yet generally affordable by the PACS concerned, Part II will be in the nature of incentive payment, related directly to his performance in generating additional business and profitability in different areas of the PACS' activity, e.g. improving recovery performance, mobilising deposits, additional loaning and profitable non-credit business, so that he comes to acquire a definite stake in the business development of the society. The basic salary scales will naturally be different in different states. These may be fixed by each SCB in consultation with the Registrar and others on relevant considerations. As mentioned earlier, different salary scales will need to be fixed for different gradations of PACSs, classified on the basis of their business turnover.

6.084 We would like to add here that the two-part salary structure, one basic and one variable related to improvement in performance, that we have recommended for the secretary is mainly in the context of the incapacity of most of the PACSs to pay higher scales of basic salary. It, of course, also has the merit of linking to some extent wages with performance. There

may, however, be a number of PACSs, though not a very large percentage of the total, which already have achieved a fairly high volume of business of all kinds and are earning good profits. Such societies are in a position to pay adequate salary to the secretary. A two-part salary structure may not, therefore, be necessary in their case. Moreover, such societies are likely to have a number of other employees also besides the secretary. Incentive salary to the secretary alone would, in their case, create problems and may not be tenable. We are conceiving of the two-part salary structure mainly for the bulk of the PACSs, which are likely to have the secretary as the sole full-time employee dealing with management and promotional matters. In case more than one employee has contributed to the growth in any such society, the incentive amount should be suitably shared by them.

6.085 While the mechanics of the two-part salary system may be worked out by the appropriate authority i.e. the SCB in consultation with the Registrar and others concerned. Such incentives may be thought of in four major areas of the work, viz., recovery of dues, deposits mobilised, additional loan business undertaken and additional profitable non-credit business generated. The incentive for each of the specified areas of work could be by way of additional remuneration related to the basic salary. Similarly, a measure of performance incentive related to salary could be built in for additional loaning also. But, it may be difficult to devise such a system of performance incentive for deposit mobilisation or additional non-credit business generated. For these, the incentive could well be related to additional deposits mobilised or additional profitable non-credit business generated and not as a percentage of basic salary. One final over-riding condition should be that the total incentive salary to be given during the year should be well within the increase in the profits, or reduction in losses, of the society over the previous year so that the society in the ultimate analysis is better off in doing so. We are also of the view that the incentive salary once earned should continue if the level of performance in subsequent years remains the same and should get reduced only if there is a decline in performance. Of course, if there is still better performance in subsequent years, the incentive salary will keep going up correspondingly.

6.086 Lastly, but not less importantly, we would like to refer to the role of the managing committee of PACSs. They determine the overall policy,

appoint, support and supervise the secretary, decide on loans and credits and are accountable to the general body of the society for the management of all its affairs. We found that in a great many PACSs little or nothing was done by the members of the committee about recovery of loans or deposit mobilisation or stimulating other profitable activities for the society as well as members. Their role was in most cases altogether passive. Where the members of the committee have played an active role not only in the management of the society but also in maintaining contacts with the members, the results on all counts have been most encouraging. An active managing committee should advise the members personally about the conduct of the business of the society, exercise supervision on the end-use of credit, convince members of the need for timely recovery and motivate them in this regard. Even members of the managing committee should take the responsibility of contacting a group of farmers and advising them about various economic activities that could be taken up individually or collectively. In case of any problem in the implementation of schemes due to delay on the part of governmental agencies, they should try to solve it and if necessary seek the help of the DCCBs. At present, the managing committees of PACSs are mostly the exclusive domain of men. The committee should involve women in the activities of the societies since they also contribute in the economic development of the community. An active committee also supervises the secretary effectively and gives him the needed support. It is, therefore, important that appropriate orientation programmes are conducted by the DCCB for the members of the managing committees of all PACSs. The content and coverage of the "education" programmes presently conducted by the District Co-operative Union for them are too perfunctory and inadequate. The DCCB needs to undertake this responsibility in a more effective and meaningful way, not only as part of its obligation towards its constituent units but also in its own interest of having a well-functioning base. In order to help the managing committees to actively involve in the development of societies, the DCCBs should periodically inform the managing committee about the changes in the organisational policies, regulations and the various schemes which could be taken up for the development of the PACSs. The DCCBs should also evolve a regular system of meetings with the PACSs, say about twice a year at which the chairman, directors and the executives of the DCCBs and the chairmen and secretaries of PACSs, could interact on mutual problems and development activities.

(vi) Office Premises and Godowns

6.087 It is necessary for all PACSs to have proper office premises and godown space, so that they can conduct their diverse activities as multi-purpose societies including marketing of agricultural produce (which very few PACSs are currently undertaking) in a proper and meaningful way. In order that the depositors should have the confidence to keep their savings with the co-operative societies, the PACS should look like a bank. The present day physical structures in which PACSs are lodged except in a few cases, cannot be considered good enough to attract deposits and even for gaining confidence of potential members who will be contributing to their share capital for joining as a member. In many cases, the godowns and the office premises are not separated even by a partition wall and the premises are not kept in a clean and tidy condition. The office should have certain minimum facilities including modern cash counters.

6.088 Presently the assistance schemes available in this behalf are the ones operated by the National Co-operative Development Corporation (NCDC). There is no specific scheme of assistance for construction of office building, but the godown assisted by them also include the basic office space for the PACSs. The published data available to us is quite outdated, i.e. as on 30th June 1982, according to which only 32 per cent of the PACSs had own godowns and 16 per cent had hired godowns. The position seems to have somewhat improved since then. The provisional data shows that, as on 30th June 1986, 41 per cent of the PACSs had come to have their own godowns, and another 17 per cent had hired godowns.

6.089 NCDC provides financial assistance to primary agricultural co-operative societies at the village level and to marketing co-operatives at the mandi, state and national levels under two categories of schemes.

- (a) The Centrally Sponsored Scheme for the development of co-operative marketing, processing and storage in co-operatively under developed states/U.Ts.
- (b) IDA (NCDC-I/NCDC-II/NCDC-III) and EEC aided co-operative storage projects and NCDC sponsored scheme for co-operatively developed states.

6.090 Under the Centrally Sponsored Scheme, the Corporation provides 50 per cent of the cost of godowns as loans, 25 per cent is provided by the state government as subsidy. NCDC has a further liberalised pattern of assistance in respect of co-operatively least developed states viz. Assam, Meghalaya, Manipur, Sikkim and Tripura where the pattern of assistance is 70 per cent of the cost of godown as loan and 25 per cent as subsidy to the state government. The state government in its turn is to provide assistance to the societies as 50 per cent loan and 50 per cent subsidy. This revised liberalised pattern would reduce the strain on the state plan resources from 25 per cent of the cost to a merely 5 per cent.

6.091 For storage programmes in co-operatively developed states, the NCDC provides 60 per cent of the cost as loan and the state government meets the balance 40 per cent as subsidy from the state plan funds. With the coverage of most of the states under internationally aided projects, the Corporation sponsored scheme is now applicable only to a few states viz. Tamil Nadu, Kerala and Gujarat and to spillover programmes in other states. For Union Territories the NCDC itself meets the full cost, providing 50 per cent of the cost as loan and the balance as subsidy.

6.092 For IDA/EEC assisted storage programme, the NCDC provides 75 per cent of the cost as a loan and of the balance, 20 per cent is contributed by the state government as share capital contribution from budgetary resources and 5 per cent is to be met from the own resources of the beneficiary society. The assistance from NCDC is granted in two parts; the first part of 50 per cent of the cost is granted as a loan through the state co-operative bank/state land development bank and the remaining 25 per cent as a loan by NCDC to the state governments. State governments in their turn, contribute this amount together with the contribution from budgetary resources (20 per cent of the cost) as share capital of the PACSs, making a total contribution of 45 per cent to the beneficiary society. At the level of the beneficiary societies, a 1:1 debt equity ratio is ensured under the projects. The loan granted under the schemes is for a period of 15 years with a moratorium on repayment of principal for the first three years. The rate of interest charged to PACS is 10.25 per cent with a rebate of 0.25 per cent for timely repayment. The rural godown for PACSs are of two types viz. 50 tonnes capacity and 100 tonnes capacity.

6.093 The progress of construction of rural godowns under internationally aided projects as on 31-3-1987 is given below :

<u>Projects</u>	<u>State</u>	<u>Net Programmes sanctioned</u>	<u>Godowns completed</u>
NCDC I 1978-84	Haryana, Orissa, Uttar Pradesh	5471	5445
EEC 1979-86	Madhya Pradesh, Rajasthan	4449	4440
NCDC II 1980-87	Andhra Pradesh, Bihar, Himachal Pradesh, Maharashtra Punjab, Uttar Pradesh	5819	5152
NCDC III 1984-89	Karnataka, Madhya Pradesh, Orissa, Rajasthan, Uttar Pradesh, West Bengal, Haryana	3761	1839
	TOTAL	<u>19500</u>	<u>16876</u>

Evaluation study conducted by the NCDC recently in Uttar Pradesh has come out with the finding that the working of NCDC storage projects in Uttar Pradesh has fulfilled the basic objectives of strengthening the infrastructure base of co-operative societies at the primary and apex level and has enabled them to service the needs of the farmers in a better way. The project as a whole and most of the sub-projects have been found financially viable by the societies and have strengthened their competitive position. The project has been considered economically viable and socially desirable to the farmers. The utilisation of the godowns has also been significantly good though there still exists some scope for further improving the same. This is an encouraging finding and it would be of interest to know the results of similar studies in other states, which we hope will be undertaken. The impression that generally seems to prevail is that in many states the godown capacity of PACSs. is grossly under-utilised. We recommend that Government of India should extend the scheme to cover all the viable societies in the country to have own godowns-cum-office. The NCDC could also consider granting exemption on the eligibility criteria in individual cases, not exceeding 10 per cent of the total project approved for any state. Presently the eligibility for participation in the scheme is based on the financial viability and a recovery percentage not less than 55 per cent of the demand in the case of PACSs.

6.094 We have suggested a combination of various measures viz. (1) a facelift of the society (2) enhancement of the calibre and the selection process of the secretary and his training (3) the need for managing committee to become more effective (4) an incentive system for the secretary to perform better (5) the restructuring of the co-operative credit organisation at the base level with organisational ties with the higher tiers with mutual rights and obligations to each other and (6) the development task of the managing committee and the secretary with regard to the members. We consider that this package of measures should be implemented as a total package since one part of the package is relatively ineffective without the others being adopted and implemented to bring about the required results.

(vii) Loans for Purposes other than Production

6.095 We have elsewhere stated our views on consumption credit in the chapter on 'Overdues'. Loans for social obligations and consumption needs are not available to the farmers from the co-operative credit system. Yet, these needs are often their pressing needs. Small farmers and landless workers who have meagre resources of their own have therefore to take loans from non-institutional sources at very high rates of interest for this purpose. Having borrowed from two sources, the inclination of the borrowers is naturally to first repay the loan which has been borrowed at a higher rate of interest with the result that they default on the repayment of production loans to the credit institution. Theoretically speaking, it may be argued that the consumption credit needs of the members of the co-operatives must be met out of their own savings and it is not the function of the co-operatives to finance their consumption needs. However, in the present stage of development of the agrarian economy it is futile to expect that the large mass of the rural people in lower income deciles will have savings enough to meet their financial needs for non-productive purposes without resort to borrowing. In this context, therefore, we consider it desirable that the PACSs should give credit for consumption purposes also. No doubt, there is an element of consumption finance deliberately built into a short-term production loan but that is really in the nature of interim finance against his own labour in production activity, expected to be repaid when harvest comes. What we are talking of here is his requirement of funds for some consumer durables and social obligations outside of this production activity. We recommend that the PACSs should be allowed to give credit for such non-production purposes also upto a pres-

cribed limit. These loans in our view should be only against tangible security. The Jawahar Rozgar Yojana has come to acquire an extensive coverage and millions of poor persons are being given employment under it. If an arrangement could be worked out by the DRDA/JRY authorities of making repayment to the PACSs on behalf of the borrower out of the wages to be earned by him, that could also become an acceptable security. It is not our intention to suggest that the funds for such loans should come by way of refinance from higher institutions. The PACS, should finance this lending out of its own resources.

6.096 In some parts of India, particularly the southern and eastern parts, the practice of giving loans against the security of ornaments and jewellery is quite common. In our discussions with both the borrowers and bankers during the course of our visits to various states, where this system is prevalent, we not only found no objection to such loans, but in fact appreciation that this way the needy persons were enabled to raise credit on reasonable rates of interest as against the usurious rates charged by the money lenders. As the loans are secured, the bankers are assured on the count that they will not become bad. The only thing that can happen is that the repayment sometimes may not be on schedule, but then they are getting the interest in any case. We should like to point out that these jewellery loans, wherever they are prevalent are also ostensibly for production purposes, but in practice we found that the productive purpose stated in the application was in most cases just a facade, the loan was really for meeting a non-productive need, though during our visit to Kerala we learnt that in some cases crop loans were also being taken on jewellery loan terms. Our recommendation, therefore, is that recognising that such needs exist and these needs are genuine and pressing enough to force the member to go to the moneylender, we should allow such consumption loans to be given in a straight forward manner by the PACS out of its own resources. These loans should be limited in quantum so that the resources of the PACS still continue to be mainly deployed on production loans. We suggest that a PACS should be allowed to give a maximum of 20 per cent of the deposits raised by it as consumption loans. The rate of interest applicable to such loans will be higher than the one for production loans. This will, therefore, give added viability to the PACS. Another advantage would be that by seeking to meet all the credit needs of the members, both productive and non-productive, it will be creating a closer bond with its

members. It, of course, goes without saying that the PACSs taking up such loans should have a proper building with safe-keeping and security facilities for the valuables, besides facilities for appraisal of the value of jewellery. The quantum of loan given will depend not only on the security offered but also on the repaying capacity of the borrower.

(viii) Allocation of Repayments

6.097 This is a matter of accounting policy and has been dealt with, among others, in the chapter on "Accounting Policies and Procedures". We, however, consider this matter of such importance to, and its effects so deleterious on, the financial position of the PACSs that we would like to highlight the problems created by this accounting policy, and the need for finding a way out of it, here also.

6.098 According to the accounting system generally prevailing in credit institutions, whatever amount is repaid by the borrower is first adjusted towards interest and the balance to the principal. Penal interest is also charged on the defaulted amount. This creates no problem at the society level. However, at the CCB level when the amount repaid by the society is first adjusted towards interest and then to the principal, irrespective of whether the amount represents payments made by individual members of the society towards interest or penal interest or principal, the anomaly arises. As long as the primary society is able to recover from its members enough interest so as to repay the interest payable to the DCCB, this practice does not create any problem. But when the interest collections from members fall short of its interest liability to CCB, a part of the principal recovered also gets adjusted towards interest by the CCB. This results in a situation :

(a) where the loans (principal) outstanding at the CCB level against a society appear larger than those at the level of the society. The position is illustrated by the data (Table 21) from a few states as at the end of June 1986. (b) the recovery performance of DCCB under principal appears poor though under interest it looks much better, (c) PACSs have to pay in succeeding years interest on loans outstanding which are higher than their own loans outstanding against members, (d) the profit position of DCCB is better than that of PACS at the cost of the latter. Over the years the gap continues to widen and the PACS has no means of meeting this gap except out of its own resources,

for the members who have already paid the principal (which has been adjusted by DCCB towards interest) have already cleared their liability. Of course, the problem arises and aggravates because of continued unsatisfactory recoveries from members of PACS.

Table 21
Loans outstanding and Borrowings

(Rs. lakhs)

State	ST loans outstanding against PACSs from DCCB	ST loans due from members to PACSs
Assam	1195	872
Jammu & Kashmir	1310	533
Madhya Pradesh	31804	31657
Meghalaya	247	239
Rajasthan	28881	26462
Uttar Pradesh	58354	42677

6.099 In view of the problem of long overdues and also because of the accounting system followed, the liability on this account is continuously increasing, leading to a progressive deterioration in the profitability of PACSs and increase in debt burden. The Working Group to Review the Flow of Institutional Credit for Rural Sector and other related matters (Shinde Committee) had recommended that the accounting system should be changed and the principal and interest collected by the society from members should be adjusted towards principal and interest in the same proportion at the DCCB level also. The Committee had, however, recognised the fact that if the present accounting system is changed, some of the DCCBs might face financial difficulties. The Committee has, therefore, suggested that the SCBs, state governments and NABARD should find ways and means to help those DCCBs, if necessary. We agree with the spirit of the recommendation of the Shinde Committee. We, of course, realise that it would be a major departure from the accepted accounting practice, but considering the special characteristics of the co-operative credit system, unlike that of the commercial banks which are unitary in nature, a departure in their case seems called for. The theoretical argument that a PACS should be treated by the DCCB on the same footing as the ultimate borrower vis-a-vis the PACS, because of its joint

and several responsibility on behalf of its members, cannot be too seriously pressed on practical considerations. The present system of accounting has landed the PACSs in a serious situation and is snowballing. The recommended system of allocation of repayment towards principal and interest in the same proportion in which it has been received will also need to be extended upto the SCB level. It could, however, be made applicable only prospectively, because if it were to be made applicable to past payments also, the DCCBs and SCBs will not be able to meet with the financial repercussions of the accumulated backlog. One beneficial effect of the recommended system will be that the DCCBs will then be motivated in their own interest to more vigorously assist the PACSs in making recoveries.

6.100 The issue, however, has other implications also. There is a justifiable apprehension that with the introduction of the new procedure suggested for appropriation of interest and principal, the DCCB would not receive the demand under interest fully i.e. at 7.5 per cent under the modified interest rate instructions of NABARD effective from 1st March 1988 and 1989 under which the lending rates to the ultimate borrowers have been reduced. In that situation the chances are that the DCCB may not be able to retain the margins suggested by NABARD for compensating losses on investment of its own resources as well as on refinance from SCB and pass on the balance to the SCB. At SCB level, this will further reduce the interest received from the DCCBs and there could be cases where unless they use their other resources, they may not be able to pay to NABARD even the minimum rate of interest of 3 to 5 per cent for the refinance obtained.

6.101 Therefore, though the change of accounting procedure recommended by Shinde Committee is aimed at removing the financial distortions which the present system creates for the PACSs, and we are ourselves in full sympathy with this object, we consider it necessary and prudent that the implications of such a change in procedure in all its aspects are first looked into by a group of experts before a final view is taken on the subject. The object of such an examination, we urge, should be to find a solution which is the most feasible in the circumstances, to protect the PACSs from the disability which the present system imposes on them.

(ix) Audit of PACSs

6.102 The audit of PACSs is done by the Registrar of Co-operative Societies through his own audit organisation in all the states, though there is nothing to bar the RCS nominating any higher tier co-operative organisation say the State or District Co-operative Union (if it has the capability), or any outside firm of chartered accountants, to undertake the audit. While we consider that, for the present, the audit may continue to be done by the RCS, we feel quite concerned with the high audit fees, in some states as high as 0.5 per cent of the working capital which are being charged for this statutory function. This eats heavily into the already tight margin of the PACS. We are strongly of the view that the audit may be done by the RCS free of cost as part of his obligation towards the co-operatives. If at all some fee has to be charged it should be a small fee.

II. Higher Tiers of the System

6.103 We have made a number of recommendations relating to specific problems and weaknesses in the operations of the DCCBs and SCBs at appropriate places in different chapters. Here we would like to highlight only those areas which we consider critical to the overall development of the short-term co-operative credit system as a whole, and to enable it to acquire greater capability and strength in the performance of its expected role. The main areas to our mind in this context are : (i) development of the leadership role of higher tiers, (ii) greater deposit mobilisation, (iii) development of project formulation and investment planning, capability for better and diversified project lending, and (iv) rehabilitation of weak banks.

Organisational Ties and Leadership Role

6.104 We have brought out in the earlier chapter the need for the development of the co-operative credit system into a functionally integrated organisational structure. Though the three tiers of the system have functioned with varying degrees of efficiency in different parts of the country, undoubtedly playing an important role in the disbursement of credit to the farming community, we find that there really are no functional ties among the different tiers. The relationship among them is mainly based on a share capital obligation and a refinancing dependency. The different tiers hang together rather loosely. The institutions in the higher tiers have barely any interest in the development of PACSs which are the cutting edge of the whole system. They are more

interested in their own profits and reserves, in their own deposit mobilisation, sometime at the cost of each other and similar other matters of self interest. Conversely, the lower institutions also see themselves as under no obligation towards their higher tiers, they only expect assistance and concessions from above. Bickerings, therefore, among tiers are not uncommon. In other words, the pervading ethos is that of 'each one for himself', rather than 'one for all and all for one' which is the basic philosophy of the co-operative movement. What we have to-day is only a credit system, not a co-operative credit organisation. It appears necessary to us that this ethos must change and a two-way system of obligations and rights must come about among institutions at different levels. The institution at the higher tier must assume certain obligations for the development and supervision of the institutions below. It should be the obligation of the higher level organisation to help and guide its constituent organisations in effective performance of the latter's functions. To do that it also must have the right to issue directives in specific matters and important decision-making areas and supervise the performance of the lower tier. In concrete terms, for instance, the set of obligations of DCCB in respect of PACSs would be, besides refinance, assistance to them in development and activity planning, assistance in deposit mobilisation and publicity in that behalf, assistance in recovery, training and education of secretaries and managing committee members, financial assistance by way of loans or grants in improving their accommodation and equipment, legal assistance when needed. The concomitant rights of the DCCB would be the authority to issue binding directives to PACSs on specific areas of their functioning to ensure their financial integrity, approval of their annual budget, approval of appointment of key personnel and their salary structure, laying down a reporting system. Likewise, the set of rights of the SCB, which is the leader of the short-term credit organisation in the State, in respect of DCCBs will broadly be the (a) power to issue directives in specific areas of functioning of DCCB, especially with regard to the manner in which they stimulate and assist the PACSs; (b) approval of important decisions of DCCB including the appointment of chief executive and its set of obligations will broadly be (i) assistance in the development activities of DCCB; (ii) management assistance in case DCCBs are weak; (iii) training of the staff of DCCBs and PACSs secretaries; (iv) assistance in the publicity and public relations; (v) to review and advise on annual credit programme and financial forecasts of the DCCBs; and (vi) approval of loans above specified levels.

6.105 However, while stating what is desirable we do realise that this kind of relationship among the three tiers in a state, entailing clearly defined responsibility of the higher tiers in respect of the lower ones in specific matters relating to the development of the system and correspondingly the rights of higher level organisation in specified matters vis-a-vis the lower ones, cannot come about just by wishing it so. It will require time and effort to build such bonds of mutuality. The most important requirement to bring it about is, first of all, to create an awareness among all tiers of the system that such a functional inter-relationship is needed for the development of the total organisation. We suggest that widespread discussions should take place at all levels in this behalf in conjunction with the higher ones. Let the need and the philosophy of it be understood first of all by all concerned. The state government has also to involve itself fully in this process, because many of the rights and obligations that we are talking of vis-a-vis different tiers belong at present to the domain of the Registrar. Most of these functions must come to the co-operative federal organisations and only then they can play the expected leadership role. The monitoring and supervision by the State Government or Registrar should be qualitatively of a different kind, and not in the nature of day-to-day control over policies, procedures and operations as now. We, therefore, suggest in this behalf that the SCB and the State Government should initiate this process of mutual discussions and interaction on the subject in each State.

Deposit Mobilisation

6.106 In our review of the performance of DCCBs and SCBs earlier in the chapter we have brought out the steady progress they have made in the mobilisation of deposits. However, their rate of growth of deposits continues to remain way behind the growth rate achieved by the rural branches of commercial banks and even regional rural banks. While their progressively reducing dependence on re-finance is a matter of satisfaction in so far as it goes, their total volume of credit would continue to remain restricted and far short of the needs of their agricultural clientele unless they do considerably more than what they have been able to do so far in the matter of deposit mobilisation. We have also brought out in the review some of the constraints of the co-operatives in respect of deposit mobilisation. Subject of deposit mobilisation by co-operative banks has therefore to be seen in two aspects : (i) the efforts that they must make to improve deposit mobili-

sation; (ii) policy constraints which demotivate them from greater effort.

6.107 In regard to their efforts to secure more deposits, there can be no set prescription except to say that they must make the needed efforts. They must come to realise that if they have to function as banks, with an expanding loans portfolio, deposits and not refinance will be their lifeline. A programme of greater deposit mobilisation will need to be chalked out by each DCCB with the guidance and assistance of SCB in the context of the local conditions, and the necessary efforts made to accomplish the programme. Various publicity and public relations techniques will have to be used, regular deposit mobilisation drives will have to be undertaken focussed more particularly on small savings. Some incentive packages will have to be adopted, for instance, a premium system, if possible, for opening a savings account with a minimum fixed amount. The look of the branches also will require to be improved to attract deposits on a competitive basis. The concerned staff will need to be trained.

6.108 We also consider it necessary to mention here the fact of competition within the co-operative structure itself, i.e. among various tiers, in deposit mobilisation. There needs to be a very clear understanding among all tiers of the co-operative credit structure that each one should have more or less an exclusive area of deposit mobilisation and that they should not attract deposits at the cost of the others as is happening now. During our discussions with the representatives of various SCBs, suggestions had been made to us that the SCB should be allowed to open more branches in the state or to open branches or extension counters at certain large agricultural processing units, such as co-operative sugar factories, co-operative spinning mills etc., so that the branch can become a deposit mobilisation centre besides meeting the credit requirement of these clients. We are not impressed by this argument. To our mind, if this were to be allowed this would lead to an encroachment on the area of mobilisation of the DCCB. Likewise we are quite clear that the DCCB should not have branches with a view to deposit mobilisation in villages which are within the area of operation of the PACS. Each one must make the efforts in its own area. We have no doubt that there is plenty of scope for each one of them to secure larger deposits. SCBs/DCCBs should be allowed to open more branches only at the place or in the area where they are already operating, depending on the potential and need for more branches.

6.109 As for the constraints which demotivate SCBs/DCCBs to higher efforts in deposit mobilisation, their genuine problems must be recognised and ways found to mitigate these constraints. In the given framework of interest rate structure, particularly the rate for ultimate borrowers for agriculture and other priority sector advances, deployment of resources raised through deposits, especially with a major portion consisting of fixed deposits, tends to become uneconomic for want of adequate margin between the deposit and the lending rates. In areas, and such areas are quite extensive, where marketing, processing and other relevant bankable activities are under-developed in the co-operative sector with a resultant low credit demand for these, the lending has to be more or less wholly on short-term agricultural operations at low rates of interest. There is little scope for intra-institutional cross-subsidisation in these areas. This acts as a disincentive for the banks to go in for greater deposit mobilisation. NABARD has, no doubt, lately agreed to compensate the loss of income to DCCBs/SCBs for deploying their own resources in short-term agricultural loans by providing higher margin in the refinance rate and by opening up new avenues for the deployment of the surplus resources in remunerative investment. We have yet to see the impact of this policy in practice. In any case, this cannot be a long-term approach in our view, because, firstly, it again creates a system of dependency on NABARD even for their profitability, and, secondly, there could be no guarantee that NABARD would continue to maintain such a compensatory arrangement for all time. In our view, measures have to be adopted independently of what NABARD might be able to do in this respect, which will take care of these major constraints of low profitability in the use of deposits for lending.

6.110 Under the present policy framework the DCCBs are not permitted to lend to individuals and non-co-operative institutions. There is a justification for such a postulation, inasmuch as the function of higher level federal institutions should in the main be the refinancing of the federating tier below or financing other co-operative institutions at corresponding level. This consideration must remain. However, to make it absolutely rigid could nullify the very object of strengthening the higher level institutions for them to help the tiers below in a more meaningful manner, more particularly in areas where the scope of lending for activities other than SAO is limited. The consideration of viability of the institutions is a paramount one, only then will they be able to play their role effectively in relation to their lower

level institutions. In this context, we are of the view and we so recommend it, that the DCCBs should be permitted to lend to non-members also, whether individuals or institutions, to the extent of not more than 20 per cent of the deposits raised by them. This lending would be at remunerative rates and would thus be able to give them higher profitability to compensate for the loss or low profitability on their lendings for agricultural operations and other traditional purposes. The restriction on lending to non-members only to the extent of upto 20 per cent of their own deposits will ensure that the bulk of their lending continues to be for priority purposes. The non-members so financed could be made nominal or associate members, without right of vote. Similar provision exists in South Korea and Japan. In South Korea lending to non-members is permitted to the extent of 33 per cent and in Japan upto the extent of 20 per cent. This has enabled the co-operative banks in South Korea and Japan to retain their profitability, secure high deposit mobilisation in line with the growth of the rural economy, and to emerge as the predominant credit system in the rural areas serving the diverse needs of the rural community. Co-operatives in India must also be enabled to do so.

6.111 In making this recommendation we are deliberately stopping short at the DCCBs. We would not like to extend it to the SCB, for the reason that the area of operation of the SCB being as large as a state, it would have within the state enough avenues of remunerative investment, even in comparatively more under-developed states, directly or in conjunction with the DCCBs.

6.112 We would also like to say that the maximum percentage of 20 that we have suggested for lending to non-members is an illustrative one and not intended to be rigid or uniform for the whole country. It can be fixed at different levels for different states or even for different DCCBs within a state, depending on the local context; only that it should not be too small to merely become a token gesture serving no meaningful purpose in the profitability of the bank. This facility to non-members, it is our belief, will also help in larger deposit mobilisation.

Project Formulation and Investment Planning Capability

6.113 This is the role which we envisage mainly for the State Co-operative Bank. Of course, DCCBs cannot also be altogether ruled out from this role,

because some of them may be in a reasonably developed and strong enough position to undertake it. But for the SCB it is necessary that as the leader of the co-operative credit system in the state, it develops the capability to perform this essential service in respect of its constituents.

6.114 Though lending under term loans by the short-term co-operative credit system have been steadily increasing, yet the term lending which the system has been traditionally doing so far is more in the nature of unsystematic scattered loans for animals, both milch and draught, minor irrigation, land development, and such like purposes. The quality of lending and appraisal is poor, and that perhaps is one of the reasons for their overdues under term loans being even higher than those of short-term loans. The scope of term lending in a meaningful way even for medium-term loans is vast. In some of the states the law has been amended to permit them longer term lending also. NABARD has now agreed to refinance investment lending provided it is on a schematic basis. The SCBs and DCCBs must necessarily, therefore, take greater initiative in identifying various types of schemes of investment credit for the development of agriculture and appropriate non-agricultural activities in the light of local potential. This can be done only if the SCB creates an appropriately staffed technical cell within itself, which will assist the DCCBs in formulating suitable projects for financing. When dealing with the commercial banks we have highlighted the need for the commercial banks to prepare projects under which financing can be done on a viable schematic basis. The need for the co-operative banks to do so is no less than that of the commercial banks. Many of the SCBs will be able to find resources from within for meeting the full cost of such a technical cell. However, assistance is also available from NABARD from its research and development fund for the appointment of technical staff. We understand that the NCDC also provides financial assistance to banks for the appointment of technical staff related to processing and marketing fields. In course of time we envisage that some of the DCCBs will also be able to set up such technical cells. We suggest that NABARD may examine the scope of its present assistance patterns in this behalf, and if necessary, make suitable modifications therein to enable the SCBs to build such a capability.

6.115 Besides credit planning and project formulation, there is need also for expertise to be developed, at least at the SCB level, for advising the

DCCBs on better investment portfolio management. Most of the SCBs and lesser still the DCCBs, have little realisation of the importance of resource deployment management. Better planning and management in this area will lead to better viability. This is an expertise which the SCB must develop not only for its own benefit but also for the benefit of the DCCBs.

Rehabilitation of Weak DCCBs

6.116 The programme of improving the working of weak DCCBs under the three tier structure and weak SCBs under two tier structure was launched by RBI in 1971. The programme envisages (i) Investigation of overdues (ii) Coercive action for recovery of overdues (iii) Relaxation of loan policy and procedures (iv) Selection of societies for intensive development and full finance (v) Assessing share capital requirements of the central banks and societies financed by them, (vi) Strengthening of supervision machinery (vii) Mobilisation of deposits (viii) Assistance from the state government in the form of term loans for maintenance of non overdue cover for borrowings from RBI/NABARD and (ix) Periodic review of the progress in the implementation of the programme by the Review Committee.

6.117 The identification of weak banks is annually done by RBI/NABARD by calling for the financial particulars of all DCCBs and assessing whether the bad and doubtful debts, other overdues above three years and accumulated losses have eroded more than 50 per cent of the paid-up capital and reserves. In all such cases the banks are included in the list of weak DCCBs and the state government is asked to take up the programme for rehabilitating the banks. The government is also required to constitute a Review Committee consisting of the representatives of RCS, the SCB and NABARD, with the General Manager of the bank as the convenor of the Review Committee. NABARD takes an active part in the implementation of the programme by deputing officers to the meetings of the Review Committee and calling for progress reports, advising the banks on areas in which the progress is not satisfactory and on the measures to be taken etc. However, in spite of these measures, it was found that there was no appreciable reduction in the number of banks under rehabilitation.

6.118 While preparing a programme for the rehabilitation of a weak DCCB,

it was assumed that the concerned bank and the state government would seriously take note of the deteriorating financial health and credit absorption capacity of the institution and would, therefore, be anxious to rectify distortions and restore it to its normal health. It was also assumed that banks will not only make concerted efforts in this direction but their efforts would be backed by the state government administratively, financially and politically. Unfortunately in practice all these expectations have been by and large belied. This is mainly attributed to (i) the lack of concerted and sustained efforts by the concerned DCCBs, apex banks and state governments, (ii) quite a few DCCBs had not even drawn a detailed action programme, in many cases the review committee which was to monitor progress of rehabilitation programme was either not constituted or if constituted did not meet regularly, (iii) in view of the large number of banks coming under rehabilitation programme, the state governments were unable to concentrate their manpower and monetary resources which got thinly spread over a large number of institutions, and (iv) recovery of overdues which was the crux of the programme but in almost all the cases, this did not receive the due attention. The vested interests within and outside these institutions did not promote any meaningful efforts for tackling this basic problem.

6.119 NABARD had initiated studies on the rehabilitation programmes in several states which were conducted by the Vaikunth Mehta National Institute of Co-operative Management (VMNICM). The studies have revealed that (i) The banks under rehabilitation have been able to augment the deposit resources and loan business to a substantial extent (average rate of growth is about 10 per cent in both cases). (ii) The banks have been making efforts continuously for decreasing erosion of owned funds but in majority of banks, the erosion in assets remained more than 50 per cent of the owned funds. The banks have not been able to make much improvement in the level of overdues also. (iii) The reserve for bad and doubtful debts of the banks continued to remain much less than the estimated value of bad and doubtful debts. (iv) The rehabilitation programme gave much emphasis on the rehabilitation of the DCCBs, while the rehabilitation of PACSs and ultimate borrowers was not given adequate attention. Hence the DCCB even after coming out of rehabilitation was not able to sustain and improve its business because of the weak nature of PACSs. (v) The banks under rehabilitation could seldom grant full finance to PACSs and hence the inadequate finance granted to

members tended to be diverted for non-productive purposes affecting the repaying capacity of the borrower. (vi) Intensive development of PACSs was seldom taken up seriously and full finance with adequate technical support was seldom given except in Maharashtra. (vii) The assessment of the requirement of the share capital of societies and DCCBs was not done for seeking government contribution to their share capital which would have enabled them to expand their borrowing power. (viii) Inadequate staff had affected timely coercive action on wilful defaulters and supervision and monitoring of loans (ix) Case by case analysis of overdues is a time consuming exercise and it requires some expertise which was lacking in the banks' staff. (x) The condition stipulated for sanction of Central Sector assistance for non overdue cover i.e. recovery performance of 50 per cent came in the way of availing such assistance in majority of the cases.

6.120 It appears from the studies that even though a bank is treated as a weak bank and brought under the scheme for rehabilitation, not much attention is paid to providing it with adequate resources for financing the non-defaulting and new members as well as to rehabilitate the non-wilful defaulters. Unless a multi-pronged attempt of providing finance adequately to the eligible borrowers, intensive deposit mobilisation drive, recovery of overdues and current dues, strengthening of PACSs etc. is made simultaneously, it may not be possible to make an impact on the functioning of the DCCBs. The Central Sector Scheme for providing financial assistance for creating non overdue cover has been limited to drought prone area/areas having predominantly SC/ST population and hence not available to all the districts. The share capital contribution to DCCBs from NRC (LTO) fund is subject to the condition that the level of overdues of the bank is within 40 per cent. of demand. The involvement of SCBs in providing assistance for case by case study of overdues, augmenting the staff, training of staff etc. is negligible. The involvement of the state government in providing the assistance required from their side is also not forthcoming as required. In these circumstances it will be difficult for the rehabilitation scheme to be successful.

6.121 NABARD had launched in 1987 a 12 Point Programme for restoring the eligibility of these banks to draw upon the short-term (SAO) credit limits. It comprises the same points as under the rehabilitation programme mentioned earlier but taken up as a time bound programme and will be in operation

for a period of three years. NABARD will be providing financial grants for training of staff, appointment of staff in rehabilitation cell, besides ad-hoc credit limits to the bank, provided respective state governments agree, in particular, for meeting the financial and other commitments on their part. The programme has started only recently and it is too early to judge its efficacy.

6.122 An improvement to the present scheme of rehabilitation has been suggested by us for implementation under the name of Institutional Strengthening Programme. The details of this programme have been given in Chapter XII on Programme for Institutional Development separately in the Report. Instead of the present schemes of rehabilitation prepared on the basis of the set guidelines issued by NABARD, institutionwise specific time bound institutional strengthening programmes would require to be drawn up for non-viable institutions.

CHAPTER VII

LONG-TERM CO-OPERATIVE CREDIT STRUCTURE

A separate institutional structure providing long-term credit in co-operative sector owes its origin to the report of the Maclagan Committee (1915). The Committee had observed that PACSs and their super structure at the district and state levels should, having regard to the pattern of their deposit resources, confine their lendings for periods not exceeding five years and that the issue of debentures was the best method for raising resources for long-term loans. It was, however, in the Registrars' Conference in 1926 that the idea of organizing land mortgage banks (LMBs) was finalised to purvey long-term credit to agriculturists. This arrangement was later endorsed by the Royal Commission on Agriculture in India (1928) and the Indian Central Banking Enquiry Committee (1931). As a consequence, the first Central Land Mortgage Bank was established in Madras in 1929. By the time India gained independence in 1947, there were only five central land mortgage banks (CLMBs) operating through 284 primary land mortgage banks (PLMBs) with loans outstanding at Rs.310 lakhs only.

7.02 Land mortgage banking really expanded following the implementation of the recommendations of the All India Rural Credit Survey (AIRCS) Committee (19> The Committee, in the first place, recognized the need to have a separate long-term co-operative credit structure and recommended the establishment of LMBs in all states. Secondly, it changed the role of LMBs from that of purveyors of credit for debt redemption to providers of credit for productive investment purposes. The principle of state partnership in the share capital of CLMBs was also recommended. Although the Committee favoured a separate structure for long-term credit in the co-operative sector, it wanted to have close co-ordination between the two wings. It recommended that SCBs and CLMBs should have a common building, common board of directors, if feasible, or at least some directors common to the two boards. The scope of lendings of the LMBs was substantially changed with the advent of economic planning through the Five Year Plans and they were assigned the role of providing long-term investment credit for productive purposes. Before nationalisation of major commercial banks in 1969, the LMBs were

the only institutional agency for purveying long-term credit for agriculture. With the setting up of the Agricultural Refinance Corporation (later ARDC/NABARD) the emphasis was shifted to schematic loans. Of late, the structure is financing not only agriculture related investments but also several allied developmental activities such as dairy, poultry, sheep rearing and fisheries which the farmers take up to supplement their income from agricultural activities. To further diversify the activities, the banks have made a beginning during the year 1987-88 in the non-farm sector too, by financing rural artisans, cottage industries and small enterprises in the rural areas. With these objectives the nomenclature of banks has undergone a change from LMBs to LDBs (Land Development Banks) and later to agricultural and rural developmental banks in some states.

7.03 Unlike the short-term credit (banking) institutions, the LDBs are not banks as they cannot accept deposits from the public withdrawable by cheque or otherwise on demand. Their own resources comprise share capital and reserves. Their borrowings include debentures which are guaranteed by the state governments and interim finance from SCB/CBs. Another difference is that the LDB structure has not evolved a uniform organisational pattern for the country as a whole; in certain states such as Tamil Nadu and Punjab it is a federal structure consisting of two tiers i.e. SLDBs and PLDBs, while in some states it is unitary with branches as in Uttar Pradesh and Maharashtra and in two other states, viz., West Bengal and Himachal Pradesh, it is mixed, that is to say, it operates in certain areas through a federal structure with PLDBs and in others through branches of the SLDB. There are, in addition seven states and six Union territories where SCBs/PACs look after the long-term credit requirements of agriculturists as there is no separate long-term credit structure in those states/union territories.

7.04 The performance of the land development banks under the Five Year Plans up to the end of the Sixth Plan is given in table 1. The LDBs have exceeded the targets under each Plan till the year 1968-69. Even thereafter the overall performance has been quite good and the progress in lending steady. However, after the multi-agency approach for agricultural credit was adopted and commercial banks entered the field in a big way, the performance of LDBs has shown a declining trend. Increasing overdues resulting in restricted

Table 1

Performance of Land Development Banks under the Five Year Plans
(Rs. crores)

Plan period	Target	Loans issued	Percentage achievement of the target	Average annual growth rate over previous plan
First Plan (1951-52 to 1955-56)	-	9	-	-
Second Plan (1956-57 to 1960-61)	25@	31	124.00	49.89
Third Plan (1961-62 to 1965-66)	150@	157	104.46	81.19
Annual Plan (1966-67 to 1968-69)	275	293	106.54	41.19
Fourth Plan (1969-70 to 1973-74)	900	783	87.00	28.58
Fifth Plan (1974-75 to 1978-79)	1,500	1,069	71.27	7.33
Rolling Plan (1979-80)	-	291	-	-
Sixth Plan (1980-81 to 1984-85)	2,150	2,047	95.20	13.62

@ Loans outstanding

Source : SLDB Federation

eligibility for lending in terms of NABARD discipline are among the many reasons responsible for the deceleration in the performance. The reduced scope for minor irrigation on account of utilisation of ground water resources to near saturation levels in many areas has also affected the growth of many LDBs.

7.05 As in the case of short-term credit structure, the long-term credit structure is also burdened at present with a high rate of delinquency, declining profitability for want of adequate margins between the cost of raising funds and the lending rates over which they have no control, excessive external interference and government intervention in the management leading to inefficiencies. These are discussed in greater detail in the following paragraphs.

Progress

7.06 At the end of 1985-86, the long-term credit structure consisted of SLDBs in 19 states and union territories with 2,447 PLDBs/branches of SLDBs. Of the 19 SLDBs, seven have unitary structure with branches, ten have a federal structure and in the case of remaining two states, viz., Himachal Pradesh and West Bengal, there is a mixed structure. In the federal structure of Madhya Pradesh and Rajasthan, the PLDBs are located at the district level with their branches at lower levels. In other states having federal structure, the PLDBs are at the sub-divisional/taluka/tehsil level and some of them have branches at the lower levels. As at the end of June 1988, out of the total such 718 banks, 102 had the district as the area of operation which included the integrated units in Andhra Pradesh, 66 had an area of less than a district, 432 banks had a taluka and 118 less than a taluka. The last category of banks was mainly in Tamil Nadu and Haryana. In the long-term structure, the base level unit is either a PLDB or its branch in the federal structure or a branch of the SLDB in a unitary structure. As on 30th June 1986, there were 2,447 branches of SLDBs and PLDBs/ branches and they were operating mostly at taluka/tehsil level serving in many cases more than 100 villages each. In seven states and six union territories a separate long-term structure did not exist and they were served by SCBs through their branches and PACSs. The progress of SLDBs during the last ten years may be seen from table 2. The SLDBs have made all round progress except in the matter of recovery of dues. The fresh advances of SLDBs, which increased from Rs.205 crores in 1975-76 to Rs. 533 crores in 1985-86 had shown an annual compound growth rate of 10 per cent. Since the debentures issued by SLDBs and the share capital collected from the members are interlinked to the loans issued, a corresponding growth rate in borrowings and share capital is also observed. The growth rate of fresh advances could have been higher but for the high level of overdues which increased from 37.5 per cent in 1975-76 to 45 per cent in 1985-86. This increase restricted the lending eligibility of the LDBs and consequently affected the borrowings and share capital growth. The rate of increase in term loans for agriculture by commercial banks and RRBs during the same period was much higher at 26.8 per cent; their advances increased from Rs.146 crores during the year 1975-76 to Rs.1573 crores during 1985-86.

Table 2

Progress of State Co-operative Land Development Banks

(Rs. crores)

Particulars	1975-76	1980-81	1983-84 [⊙]	1984-85 [⊙]	1985-86 [⊙]	Annual growth rate from 1975-76 to 1985-86
No. of Banks	19	19	19	19	19	
Membership*						
a) PLDBs and other Societies	2747	4335	4374	3849	3848	
b) Individuals (in thousands)	2171	2738	3307	3308	3468	
c) Total membership (in thousands)	2174	2742	3311	3312	3472	4.7
Owned Funds						
a) Share capital	99	154	174	181	193	6.9
Of which Government	23	48	46	45	46	
b) Reserves	55	141	204	247	280	
c) Total owned funds (a + b)	154	295	378	428	473	11.9
Deposits and other Borrowings	38	72	31	27	28	7.3
Debentures Outstanding	1,384	1984	2578	2579	2854	7.4
Working Capital	1,667	2,543	3,145	3,360	3,532	7.8
Fresh Advances	205	364	439	461	533	10.0
Loans Outstanding	1,068	1,697	2,236	2,386	2,625	9.4
Overdues						
a) Amount	64	243	283	268	323	-
b) Percentage to demand	37.5	47.8	41.4	42.8	45.0	-

⊙ Provisional Figures

*In the federal structure the membership consist mainly of PLDBs, while in the unitary structure the membership consist of individuals.

Source : Statistical Statements relating to Co-operative Movement in India published by RBI/NABARD.

Data on Credit and Non-Credit Co-operatives - Important Items

7.07 Further, the growth of SLDBs has been uneven in different states. A statewise review separately for co-operatively developed states and co-operatively non-developed states of the SLDBs is indicated in table 3. The first category of states consists of Andhra Pradesh, Gujarat, Haryana, Karnataka, Kerala, Maharashtra, Punjab, Tamil Nadu and Uttar Pradesh. The banks in these states have registered an overall progress in raising owned funds and expanding loan operations during the last 10 years. The increase in the owned funds was mainly due to the increase in the share capital from the members as well as increase in the reserves. Though the AIRCS Committee had recommended government contribution to the share capital of co-operatives upto 51 per cent of the total, contribution actually made to the share capital was not substantial. It formed only 23.8 per cent of the total and less than 25 per cent of the share capital of individual banks as on 30.6.1986 except in the case of SLDBs in Karnataka and Uttar Pradesh where it formed 35 per cent and 28.7 per cent respectively of the total. However, government contribution formed only 16.8 per cent and 13.4 per cent of the owned funds of banks in Karnataka and Uttar Pradesh respectively. The growth rate of share capital of SLDBs in Andhra Pradesh, Kerala, Punjab, Haryana and Uttar Pradesh was substantial as the same has more than doubled during the last 10 years while in those in Maharashtra and Karnataka, the percentage increase was 41.1 and 44.6 respectively during the same period. As regards resource mobilisation by way of debentures, whereas SLDBs in Andhra Pradesh and Punjab have shown a decline during the last 5 years, the increase is very nominal in respect of banks in Maharashtra and Uttar Pradesh, but SLDBs in Tamil Nadu, Gujarat and Karnataka have increased their resources very substantially. Loans issued by banks during the last four years have shown a declining trend in Andhra Pradesh, stagnancy in Maharashtra while the increase in Punjab was only nominal. There was a significant increase in lending by SLDBs during the last five years in Tamil Nadu, Gujarat and Karnataka.

7.08 In less developed states, namely, Assam, Bihar, Himachal Pradesh, Jammu & Kashmir, Madhya Pradesh, Orissa, Pondicherry, Rajasthan, Tripura and West Bengal, besides a few smaller states in the North Eastern region, while the owned funds of SLDBs increased in all states, the increase was noticeable particularly in Pondicherry, Orissa, Jammu & Kashmir and Madhya Pradesh. This was due to substantial government contribution to the share

Table 3

SLDBs in Co-operatively Developed States - Owned Funds, Resources raised and Loans Issued 1980-81 to 1985-86

(Rs. crores)

SLDBs	Share Capital			Owned Funds		Resources Raised [●]		Loans Issued	
	1975-76	1980-81	1985-86	1980-81	1985-86	1980-81	1985-86	1980-81	1985-86
Andhra Pradesh	6.44 (1.06)	10.78 (1.06)	14.45 (1.06)	29	49	66	61	71	63
Gujarat	12.13 (0.50)	9.76 (1.08)	10.86 (0.43)	14	38	5	23	6	27
Haryana	2.78 (0.70)	4.62 (0.70)	9.02 (0.70)	9	20	29	45	31	52
Karnataka	8.69 (3.44)	10.68 (4.45)	12.57 (4.45)	19	27	14	48	19	47
Kerala	1.08 (0.41)	3.51 (1.41)	6.22 (1.41)	6	17	21	39	24	41
Maharashtra	27.85 (6.03)	32.68 (6.03)	39.31 (4.93)	77	101	49	52	54	54
Punjab	3.78 (1.05)	5.18 (1.07)	8.94 (1.11)	7	21	34	33	36	49
Tamil Nadu	7.32 (1.70)	12.60 (6.85)	7.06 (1.70)	36	58	4	21	4	21
Uttar Pradesh	12.71 (1.91)	28.22 (9.63)	35.21 (10.12)	45	76	49	54	53	75

Note : Data for the year 1985-86 are Provisional.

● By way of Ordinary & Special Development Debentures.

Figures in bracket indicate the Government share capital

Source : Statistical Statements relating to Co-operative Movement in India, 1980-81 published by NABARD
Report of the Consultants on Study II

Table 3 (Contd..)

**SLDBs in Co-operatively Less Developed States -
Financial and other Particulars - 1980-81 to 1985-86**

(Rs. crores)

SLDBs	Share Capital			Owned Funds		Resources Raised		Loans Issued	
	1975-76	1980-81	1981-82	1980-81	1985-86	1980-81	1985-86	1980-81	1985-86
Assam	0.29 (0.21)	0.82 (0.64)	0.88 (0.64)	0.82	0.96	0.46	2	0.34	1.50
Bihar	5.42 (1.71)	15.69 (6.81)	22.19 (10.52)	17	23.27	12	29	14.28	31.09
Himachal Pradesh	0.40 (0.28)	0.73 (0.56)	1.07 (0.66)	0.75	1.09	0.29	1	0.28	1.54
Jammu & Kashmir	0.31 (0.10)	0.36 (0.10)	0.64 (0.25)	0.56	1.37	0.56	1	0.35	1.04
Madhya Pradesh	4.52 (2.10)	6.94 (2.35)	9.19 (2.35)	12	21.12	14	31	14.29	31.57
Orissa	1.45 (0.59)	3.35 (1.47)	4.56 (1.67)	2	9.07	11	7	9.89	7.62
Pondicherry	0.11 (0.05)	0.15 (0.08)	0.36 (0.25)	0.03	0.47	0.01	0.36	0.10	0.53
Rajasthan	1.80 (0.55)	3.77 (1.15)	5.69 (1.40)	8	11.14	17	20	18.87	19.17
Tripura	0.08 (0.06)	0.18 (0.12)	0.23 (0.13)	0.18	0.26	0.47	0.14	0.58	0.16
West Bengal	1.55 (1.01)	4.23 (2.66)	4.56 (2.67)	5	6.64	8	6	6.58	8.53

Source : Statistical statements relating to Co-operative Movement in India published by NABARD
Report of the Consultants on Study II
Data for the year 1985-86 are provisional

Figures in bracket show Government share capital

capital in the case of Pondicherry SLDB and building up of substantial reserves besides share capital from members in respect of Madhya Pradesh and Orissa SLDBs. The government share capital was substantial in the case of SLDBs of Assam (72.7%), Pondicherry (69.4%), Himachal Pradesh (62%), West Bengal (58.6%), Tripura (56.5%), Bihar (47.4%) and Jammu & Kashmir (39%). As regards loans issued and resources raised by way of debentures, SLDBs in Orissa, and Tripura showed a declining trend while the West Bengal SLDB had shown a decline in resources raised only. The Rajasthan SLDB has shown a decline from the year 1983-84 although its position had slightly improved during 1985-86 as compared to the previous year. There is no significant increase in floatation of debentures by SLDBs in any state except Madhya Pradesh and Bihar. As regards loans issued, while the banks in Assam, Bihar, Himachal Pradesh, and Madhya Pradesh had shown a significant increase, Rajasthan had shown only a marginal increase in lending during the period. In the smaller states such as Assam, Himachal Pradesh, Jammu & Kashmir, Pondicherry and Tripura, the level of lending is low as illustrated in table 4. It would appear that these banks are not earning enough which will eventually affect their capacity to function as viable apex level institutions.

Table 4

Particulars in respect of SLDBs in smaller states - position during 1985-86

Name of SLDB	(Rs. crores)			
	Resources raised	Loans issued	Loans outstanding	Percentage of overdues to demand
1. Assam	1.48	1.50	8.07	60
2. Himachal Pradesh	1.45	1.54	5.74	44
3. Jammu & Kashmir	1.44	1.04	5.42	51
4. Pondicherry	0.36	0.53	1.07	32
5. Tripura	0.14	0.16	1.40	74

Source : Report of the Consultants on Study II

7.09 In the eastern region states, viz., Bihar, Orissa, and West Bengal also the functioning of the banks is none too happy except in the case of Bihar where some improvement is seen in 1985-86. The working of banks in Orissa

and West Bengal is characterised by poor coverage of families, inadequate owned funds, poor resource mobilisation, low levels of lending operations and a rising trend in overdues. The financial and operational capabilities of land development banks in these two states have been affected due to lack of efforts on their part to undertake promotional work in identifying new items of investments and formulating schemes. Lack of necessary support from the state government, apart from poor infrastructure has also contributed to such a disquieting situation.

Primary Land Development Banks

7.10 The progress of PLDBs during the last 10 years is shown in table 5.

Table 5
Progress of Primary Land Development Banks

Particulars	1975-76	1981-82	1983-84*	1984-85*	1985-86*	(Rs. crores)
						Compound annual growth rate from 1975-76 to 1985-86 (per cent)
1. No. of Banks	890	880	885	890	910	0.2
2. Membership (thousands)	4,638	7,020	7,317	7,401	7,826	5.4
3. Owned Funds	72	145	181	189	199	10.7
4. Deposits and other Borrowings	574	1,088	1,083	1,234	1,461	9.8
5. Working Capital	704	1,361	1,600	1,709	1,777	9.7
6. Fresh Advances	136	260	277	312	390	11.1
7. Recoveries	119	236	429	433	462	14.5
8. Loans Outstanding	577	1,083	1,168	1,247	1,326	8.7
9. Overdues						
a) Amount	31	106	176	141	153	-
b) Percentage to demand	28.1	44.4		45.9	44.1	-

* Provisional

Source : Statistical Statements relating to the Co-operative Movement in India published by RBI/NABARD.

It will be seen that the membership had increased from 46.38 lakhs in 1975-76 to 78.26 lakhs in 1985-86 showing an annual growth rate of 5.4 per cent. The owned funds have increased from Rs.72 crores in 1975-76 to Rs.199 crores in 1985-86 showing an annual growth rate of 10.7 per cent. The borrowings increased from Rs.574 crores to Rs.1461 crores during the period 1975-76 to 1985-86. The fresh advances granted during 1975-76 which were Rs.136 crores, increased to Rs.390 crores by 1985-86, showing an annual growth rate of 11.1 per cent. The loans outstanding had increased from Rs.577 crores during 1975-76 to Rs.1326 crores in 1985-86 which showed an annual growth rate of 8.7 per cent. The overdues increased from Rs.31 crores during 1975-76 to Rs.153 crores by 1985-86. The percentage of overdues to demand in 1975-76 was 28.1 but in 1985-86 it increased to 44.1. The position of PLDBs shown by the above data refers to the 14 states where there are PLDBs while the states where the branches of SLDBs are purveying long-term credit to the agriculturists directly are not included in these figures. The major states thus excluded are Maharashtra, Uttar Pradesh and Bihar.

7.11 The position of PLDBs/branches of SLDBs taken together in terms of the range of overdues at the end of 1985-86 is given below :

<u>Percentage of Demand</u>	<u>No. of units</u>
Upto 25	588
Above 25 and upto 40	334
Above 40 and upto 65	467
Above 65	433

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Only 32.3 per cent of the total number of PLDBs/branches of SLDBs could have unrestricted lending eligibility while 23.7 per cent have a highly restricted eligibility during the year 1985-86.

7.12 In north-eastern region barring Assam, separate sections of the state co-operative banks are looking after long-term credit. However, there is no significant progress in the disbursement and recovery of loans in these states. Poor infrastructure, restrictions on transfer of land and shifting cultivation seem to have contributed to the poor lending operations in these states.

Inadequacies and Problems

Viability of PLDBs and Branches of SLDBs

7.13 The Sub-Committee of the Committee on Term Lending by Co-operatives (COTELCOOP) appointed by NABARD in 1983 recommended that a PLDB to be considered viable should have loans outstanding of Rs.70 lakhs to Rs.75 lakhs and that in the case of PLDB functioning at a district level, it should have an aggregate business of Rs.50 lakhs per branch. It was also recommended that this level should be reached within a period of three years. The high level working group on SLDBs (Rajgopal Committee) had suggested that the appropriate authority to decide the issue of viability of PLDBs and related matters would be a state level standing committee (recommended to be constituted by the working group) in view of the diversity in agro-economic conditions even within a state. However, this recommendation is yet to be acted upon by the state governments. On the basis of the norm suggested by the Sub-Committee of COTELCOOP, the number of PLDBs/branches of SLDBs which are not deemed viable was 539 as on 30-6-1986 forming 30 per cent of the total number of PLDBs/branches of SLDBs. As on 30th June 1982, the number of PLDBs working at profit was only 436, forming only 49.5 per cent of the total number of 880. One of the important constraints for banks to reach the viable status is the high level of overdues and consequent restrictions on fresh lendings. Since the fresh lending of PLDBs/branches of SLDBs is governed by the eligibility criterion based on the recovery of loans, the banks which are non-viable and weak are unable to improve their lending performance within the time frame of three years. It is observed from a review of the progress of the rehabilitation programme of PLDBs detailed in the subsequent paragraph that the improvement in recovery position is very slow during the three year period in respect of a majority of banks. Many banks have in fact showed a declining trend in recovery. Hence to bring a bank from a highly restricted category of lending to an unrestricted category of lending and thereby help it to improve its profitability is found to be an extremely difficult task with the existing regulations on fresh advances.

Rehabilitation of Weak PLDBs and Branches of SLDBs

7.14 NABARD has been operating, for the last three years, an action programme for improving the weak units. The Ten Point Programme for the rehabilitation of the weak PLDBs has the following main features :

- i) Selection of weak units for rehabilitation;
- ii) Investigation of overdues;
- iii) Strengthening of the organisation and management of the institutions;
- iv) Conducting of training programmes and workshops for the staff in the formulation of schemes, appraisal and recovery procedures;
- v) Review of loan policy and procedures;
- vi) Strengthening of resources;
- vii) Financial assistance from NABARD for appointment of technical staff;
- viii) Subsidy from NABARD for creation of rehabilitation cell;
- ix) District level rehabilitation review committee; and
- x) Constitution of state level rehabilitation review committee for reviewing the progress of implementation of the rehabilitation programme at the state level.

A chart showing the statewise position of the progress in the implementation of rehabilitation programme is given in table 6. It will be seen from the chart that (i) all the 14 states covered under the programme have constituted District Level Review Committees (working groups), District Level Rehabilitation Review Committees (DLRRC) and the State Level Rehabilitation Review Committees (SLRRC), (ii) investigation of overdues has been completed for all the states, (iii) rehabilitation programmes have been prepared for all the weak units and they have been approved by DLRRCs, (iv) comprehensive rehabilitation programmes have also been prepared in all the states and they have been approved by the SLRRCs except in the case of Madhya Pradesh and Maharashtra, (v) the Government of West Bengal, Rajasthan, Karnataka, Himachal Pradesh, Gujarat, Tripura and Uttar Pradesh have submitted a comprehensive rehabilitation programme to NABARD for approval and (vi) twelve SLDBs have constituted rehabilitation cells for preparation and implementation of the rehabilitation programmes. Madhya Pradesh and Jammu & Kashmir SLDBs have not so far, constituted the rehabilitation cells. (The cells will serve as the secretariat for the state level rehabilitation review committee). While the rehabilitation programme submitted by West Bengal, Rajasthan, Uttar Pradesh, Tamil Nadu, Karnataka, Gujarat and Himachal Pradesh state governments have been approved by NABARD, the progress made in respect of recovery of dues indicates that 118 banks/units have shown an increase in recoveries ranging from five per cent or less to ten per cent or more, 76 banks had shown a decrease

Table 6

Progress in Implementation of Rehabilitation Programme of Weak PLDBs/Branches of SLDBs

Sr. No.	State	No. of PLDBs/ Branches taken up for Rehabilitation	Constitution of Committees			Whether Investi- gation of overdues Taken Com- pleted		Whether action Plan prepared by DLRC	Whether action Plan approved by DLRRRC	Whether compre- hensive reh. plan prepared by SLDB	Whether compre- hensive plan approved by SLRRRC	Whether State Govt. has submitted CP to NABARD	Whether Reha- bill- ation cell Created by SLDB	Whether sanc- tioned by NABARD	Whether State Govt. acceptance to the terms and conditions of sanction received
			DLRC	DLRRRC	SLRRRC	5	6								
<u>Eastern States</u>															
1.	Bihar	23	C	C	C	C	C	C	C	C	C	NC	C	NS	NS
2.	Orissa	4	C	C	C	C	C	C	C	C	C	NC	C	NS	NC
3.	Uttar Pradesh (E)	4	C	C	C	C	C	C	C	C	C	C	C	S	NC
4.	West Bengal	6	C	C	C	C	C	C	C	C	C	C	C	S	NC
<u>Other States</u>															
5.	Gujarat	61	C	C	C	C	C	C	C	C	C	C	C	S	C
6.	Himachal Pradesh	3	C	C	C	C	C	C	C	C	C	C	C	S	C
7.	Jammu & Kashmir	5	C	C	C	C	C	C	C	C	C	NC	NC	NS	NC
8.	Karnataka	33	C	C	C	C	C	C	C	C	C	C	C	S	C
9.	Madhya Pradesh	3	C	C	C	C	C	C	C	C	NC	NC	NC	NS	NC
10.	Maharashtra	14	C	C	C	C	C	C	C	C	NC	NC	C	NS	NC
11.	Rajasthan	8	C	C	C	C	C	C	C	C	C	C	C	S	C
12.	Tamil Nadu	14	C	C	C	C	C	C	C	C	C	NC	C	S	NC
3A.	Uttar Pradesh (Others)	8	C	C	C	C	C	C	C	C	C	C	C	S	NC
<u>North Eastern States</u>															
13.	Assam	6	C	C	C	C	C	C	C	C	C	NC	NC	NS	NC
14.	Tripura	2	C	C	C	C	C	C	C	C	C	C	C	NS	NC

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Note : C : Complied

NC : Not complied

S : Sanctioned

NS : Not sanctioned

E : Eastern

Source : NABARD

in the recovery by up to five per cent to above ten per cent points during the year 1986-87 as compared to the previous year.

7.15 At the end of 30th June 1987, as against 186 banks in category IV (i.e. recovery up to 35 per cent) as on 30th June 1985, 12 banks moved up to category I (showing recovery of 75 per cent and above), 18 banks to category II achieving recovery between 60 per cent and 74 per cent, 79 banks to category III (achieving recovery between 36 per cent and 59 per cent) while 77 banks continued to remain in category IV.

7.16 As regards lending, out of 194 units under rehabilitation, 71 units registered an increase in the loans disbursed during the year 1986-87 as compared to the position during 1985-86; 123 units, however, had reduced lending during 1986-87 as compared to the previous year.

7.17 Since the ten point action programme has been in operation only during the last three-four years, it may be too early to judge the success/effectiveness of the programme. However, we have recommended elsewhere in this report an improvement in the rehabilitation programme of banks through a modified programme of institutional strengthening. The rehabilitation programme of PLDBs should also be replaced by an appropriate Institutional Strengthening Programme (ISP) in order to obtain better results, details of which are given in Chapter XII.

Co-ordination between Short-term and Long-term Co-operative Credit Structure

7.18 As a means of evolving co-ordination, many committees, mainly the Review Committee (1969), CRAFTICARD (1981), Rajgopal Committee (1985) to name a few, preferred functional co-ordination, with the PACSs acting as agents of LDBs for disbursing the long-term loans. From time to time since 1969, RBI had urged the state governments to bring about the functional co-ordination. As a follow up of CRAFTICARD recommendations, NABARD had advised the state governments in August 1982 to select, in each district on a pilot basis, at least five to ten viable PACSs equipped with full time paid secretaries, initiate a programme of training of secretaries in term lending procedures, create a cell at the apex bank level to monitor functional co-ordination, etc. But the scheme had failed to take off since most of the state

governments had not taken any action to implement the scheme and some of the state governments were not in favour of the scheme.

7.19 As a part of the functional co-ordination, NABARD had, in pursuance of the recommendations made by CRAFTICARD, introduced in August 1982, a scheme permitting the LDBs to issue, in areas of weak PACSs, short-term production credit to their borrowers of long-term credit. NABARD had also extended refinance facilities to SLDBs for the purpose on terms and conditions similar to those for SCBs. However, this scheme has not taken off as no SLDB has approached NABARD for short-term credit limits in the past five to six years.

7.20 Thus the measures taken for effective functional co-ordination between the two wings of the co-operative credit structure have not yielded results on the desired lines and functional co-ordination still remains a distant goal. The need for co-ordination hardly requires to be stressed all over again.

Legal Constraints

7.21 There are certain legal and other constraints which impede developing loaning operations by LDBs. The major constraints in diversifying the loans and broad-basing their operations are mentioned below :

- i) The membership of LDBs is restricted to land owners and that they cannot also admit non-farmers as members at present.
- ii) Mortgage of land is the only security provided for in the Co-operative Societies Acts and Rules and there are no provisions enabling the banks to finance loans without the security of mortgage of land. This restriction comes in the way of financing tenants, artisans, etc. for the purchase of machinery for investment in cottage and small scale industries, etc. where land may not be a major component of the project. The legal rigidity that has come to be built into the system, needless to say, would require to be removed if LDBs have to diversify their operations as they ought to.
- iii) There are no provisions for raising resources by way of loans.

This is again yet another rigidity which stifles the development of the LDB structure.

- iv) The existing provisions do not allow loans to be given for periods less than five years. Hence LDBs are not able to meet the working capital needs of the rural artisans, cottage and tiny industries in whose case NABARD has agreed to provide refinance by way of composite loans, for periods of less than five years.
- v) The embargo in the case of some banks except in a few states such as Madhya Pradesh, Uttar Pradesh and Maharashtra on LDBs providing financial assistance to statutory corporations such as state electricity boards, agro-industries corporations, land development corporations and corporations for agro-processing or for utilisation of post harvest technology.

7.22 It is thus imperative that the legal constraints are removed so that LDBs can diversify and lend for non-land based activities also. It needs to be recognised that the context in which landed security was prescribed as a legal obligation has changed and an ever expanding horizon is now opening up newer avenues of investment of finance for agriculture and allied activities. Further, the concept and sweep of security have vastly changed. It is now universally accepted that the assets created out of the loan itself are sufficient to provide adequate security. Although several committees have by now suggested amendments to the Co-operative Societies Acts, Rules and byelaws and recommendations had been endorsed by Government of India/RBI and NABARD, action is yet to be taken by many state governments. The Government of India had also written to state governments as early as in June 1986 in this regard. We would in the circumstances recommend that the state governments should without further delay initiate the necessary action for amending the Co-operative Societies Act and Rules suitably so that the legal restrictions which hamper the growth of LDBs and provisions of investment finance by them for the new areas of activity are removed.

Restricted Lending Eligibility

7.23 The lendings of LDBs are regulated according to the norms prescribed by NABARD with reference to recovery position of the PLDBs/branches of

SLDBs with an intention to improve the recovery performance of LDBs. These norms, although operative for more than a decade, have not made any significant impact on the recovery performance of these banks as has already been brought out in the review of progress of rehabilitation programme of PLDBs in paragraphs 7.15 to 7.17. Effective from July 1986, the regulations have been made even more rigid. It can hardly be said that the restricted lending eligibility has been instrumental in any way in improving the recovery position of banks; in fact it has even been counter productive. These aspects are discussed in some detail in Chapter XII which deals with the Programme for Institutional Strengthening (ISP). We have recommended in Chapter XII, the substitution of the present viability criterion by a new criterion. This new criterion should enable all the institutions which satisfy the new criterion to have unrestricted lending programmes. This, together with the amendments suggested to the Co-operative Societies Act and Rules to remove the legal rigidities should enable the LDBs improve their lending programmes. The resultant increase in the volume of lending and diversification of loan operations, in our view, would go a long way in the overall strengthening of the LDBs to meet the new challenges.

Share Capital

7.24 The state-wise position of paid up share capital, reserves, total loans outstanding and overdues of SLDBs and PLDBs is indicated in tables 7 and 8. It will be seen that while the total owned funds of SLDBs and PLDBs are found adequate to enable them to raise sufficient resources on the basis of the maximum borrowing power fixed for these institutions, they would not be adequate for absorbing overdues either fully or in all cases. For instance, in respect of a few states, namely, Andhra Pradesh, Assam, Orissa, Rajasthan, Tamil Nadu, West Bengal and Tripura the SLDBs, and in Assam, Karnataka, Orissa, Rajasthan and West Bengal the PLDBs would not be able to absorb the overdues with the present level of their owned funds. Since the deficit in owned funds for absorption of overdues is substantial in many cases, it will be beyond their capacity to further raise their owned funds by way of additional share capital, or by augmenting reserves for want of adequate profitability. It will, therefore, be necessary in these cases for an external agency like state governments to contribute to the share capital of these institutions by way of additional share capital at least for a limited period

Table 7
Owned Funds of SLDs as on 30.6.1986

(Rs. crores)

State	Paid up Capital	Of which from State Govt.	Reserves	Total owned funds	Working capital	1/25 times owned funds	Total loans outstanding	Of which overdues	% of Overdues to demand	Deficit col.9-5
1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.
Andhra Pradesh	14.45	1.06	28.23	42.68	444.75	1067.00	348.29	74.72	58.6	- 32.04
Assam	0.88	0.64	0.01	0.89	7.87	22.25	5.69	1.09	63.4	- 0.20
Bihar	22.19	10.52	1.61	23.80	171.71	595.00	110.29	5.90	16.1	
Gujarat	10.86	0.43	27.37	38.23	138.51	955.75	104.78	20.99	58.3	
Haryana	9.02	0.70	11.22	20.24	263.67	506.00	196.16	3.71	13.6	
Himachal Pradesh	1.07	0.66	0.02	1.09	8.63	27.25	5.74	8.72	44.4	
Jammu & Kashmir	0.64	0.25	0.73	1.37	6.94	34.25	3.85	0.54	51.4	
Karnataka	12.57	4.45	13.92	26.49	281.12	662.25	226.04	22.23	48.6	
Kerala	6.22	1.41	10.70	16.92	206.92	423.00	161.36	2.74	13.3	
Madhya Pradesh	9.19	2.35	11.98	21.17	216.95	529.25	174.16	16.38	41.4	
Maharashtra	39.31	4.93	61.78	101.09	494.89	2527.25	356.28	39.05	55.2	
Orissa	4.56	1.67	4.51	9.07	93.88	226.75	72.38	14.92	66.5	- 5.85
Punjab	8.94	1.11	11.60	20.54	298.09	513.50	185.90	4.75	9.4	
Rajasthan	5.69	1.40	5.45	11.14	171.33	278.50	114.99	17.01	62.4	- 5.87
Tamil Nadu	7.06	1.70	47.60	54.66	212.24	1366.50	172.67	58.34	75.4	- 3.68
Uttar Pradesh	35.21	10.12	41.06	76.27	441.03	1906.75	332.33	27.11	23.7	
West Bengal	4.56	2.67	2.08	6.64	69.27	166.00	51.50	12.64	77.2	- 6.00
Tripura	0.23	0.13	0.03	0.26	2.28	6.50	1.40	0.32	76.4	- 0.06

Source : Data on Credit and Non-Credit Co-operatives - Important Items

Table 8

Owned funds of PLCBs as on 30.6.1986

(Rs. crores)

State	Paid up Capital	Of which from State Government	Reserves	Total owned funds	Working capital	1/25 of working capital	Overdues	% of over-dues to demand	Deficit Col. 8 - Col.5
1	2	3	4	5	6	7	8	9	10
Andhra Pradesh	36.17	2.67	6.00	42.17	300.50	12.02	25.42	48.8	-
Assam	0.40	0.04	0.01	0.41	4.09	0.16	0.70	N.A.	0.29
Haryana	17.42	2.46	1.45	18.87	237.49	9.50	14.26	30.2	-
Himachal Pradesh	0.31	0.19		0.31	1.87	0.07	0.11	40.7	-
Karnataka	17.09	2.70	3.85	20.94	209.05	8.36	23.37	56.1	2.43
Kerala	7.70	0.48	4.29	11.99	141.39	5.66	1.81	19.7	-
Madhya Pradesh	15.65	4.25	1.80	17.45	172.00	6.88	14.60	34.7	-
Orissa	6.74	1.59	0.69	7.43	59.82	3.99	7.68	39.1	0.25
Punjab	18.22	0.65	1.58	19.80	216.46	8.66	5.47	13.5	-
Rajasthan	11.34	1.06	4.85	16.19	134.17	5.37	17.61	60.2	1.42
Tamil Nadu	13.39	2.00	22.98	36.37	196.46	7.86	32.37	66.9	-
West Bengal	5.15	1.91	1.48	6.63	62.68	2.51	9.07	57.2	2.44

Source : Data on Credit and Non-Credit Co-operatives - Important Items

as a part of ISP. In this connection we observe that the eligibility norms fixed by NABARD for the PLDBs for share capital contribution from the state government stipulate that the banks' overdues to demand should not exceed 25 per cent as at the end of previous co-operative year for being eligible for the government share capital contribution. This stipulation has kept out a good number of PLDBs from receiving government share capital contribution even after the need gets established. We feel that NABARD should in the circumstances relax this stipulation so as to enable the PLDBs having overdues upto 40 per cent of demand eligible for such contribution. However, in the case of banks under a programme of ISP, the government share capital contribution to the required extent should be given irrespective of the level of overdues.

7.25 In the case of SLDBs which have been brought under a programme of ISP, the share capital contribution by the state government may be augmented up to the required extent by obtaining loans from the LTO Fund. For this purpose also the existing stipulation/norms of NABARD for becoming eligible for government share capital contribution should be suitably relaxed.

7.26 The SLDBs have by now generally built up owned funds to a level adequate to enable them to borrow sufficient funds except in a few cases as indicated in table 7. The PLDBs receive share capital from their individual members at a rate ranging from five per cent to ten per cent depending upon the amounts borrowed. The PLDBs have in turn to purchase shares of SLDB at a fixed ratio and this leaves a very small amount with the PLDBs for their business. The RBI had earlier fixed the proportion of share capital to be shared between the SLDBs and PLDBs in the ratio of 4:1. It was subsequently revised in 1974 to 3:2 so that more funds could remain with PLDBs. However, some of the SLDBs even now continue to collect share capital from PLDBs in the ratio of 4:1. In order not to reduce loanable funds, the SLDBs which have got adequate owned funds should not collect any additional share capital contribution in excess of the prescribed ratio of 3:2.

Resources Mobilisation

A Deposits

7.27 In June 1971 the Reserve Bank of India permitted the SLDBs to

raise fixed deposits subject to the following stipulations :

- i) The period for which fixed deposits may be accepted may not be less than one year and not exceed two years.
- ii) The bank pays interest at not more than 7 per cent per annum on deposits for one year and 7.5 per cent per annum on deposits for more than one year but up to two years.
- iii) The bank keeps at least 10 per cent of the total term deposits accepted and outstanding on any day in liquid form by way of (a) cash with itself, (b) current/deposit account with the state co-operative bank and/or (c) unencumbered securities of Central or state governments.
- iv) The deposits are not from :
 - (a) institutions and (b) loanees or their near relations within the period of the loan or before such disbursement.

In so permitting it was thought that the LDBs would be in a position to mobilise fixed deposits from rural areas which could be used by them inter alia as interim finance. However, most of the banks discontinued raising of deposits in this manner since the terms offered were not attractive enough to the savers who looked for terms competitive with small savings schemes of the Government and similar other schemes. The SLDBs are presently contemplating alternative schemes for mobilisation of resources which will carry tax concessions on the lines available for public sector bonds, National Savings Certificates etc. Since two year duration deposits would not be entitled for tax concessions, it is necessary that the scheme so formulated should be in the nature of a financial instrument on the lines of those certificates or bonds of public sector institutions which enjoy the tax concessions. The duration also will accordingly need to be for a period of five years or more. Since the resources are utilised for financing agricultural development, we see no reason why these tax concessions cannot be granted. The cost of funds raised are, however, bound to be high compared to the concessional rates at which resources are now available from NABARD by way of refinance or interim finance. But the tax concessions will help the LDBs add a new dimension to their image in the rural financial market.

B. Interim Finance

7.28 Under the law as at present, the debentures floated by SLDBs are required to be backed by effective mortgages. LDBs have, therefore, to first disburse loans so as to collect the mortgages before debentures could be floated. But for the purpose of issuing loans the SLDBs require funds. Customarily, funds so required are raised by way of interim finance which they usually arrange through the SCBs or commercial banks by availing themselves of overdraft facilities from SCBs or SBI and its subsidiaries or commercial banks at the prevailing market rates. Thus the rate of interest on interim finance charged might range anywhere from 10 per cent to 13.5 per cent, where the funds are raised from the state co-operative banks. But SBI and its subsidiaries charge a higher rate of interest of 14 per cent. SLDBs' lending rate being lower than these rates, the LDBs necessarily incur losses continuously on this account. However, the SCBs/SBI and other commercial banks providing interim finance at an uneconomic rate of interest as compared to the cost of raising deposits will not be feasible. NABARD also provides interim finance at a rate of interest of 8.5 per cent to 9 per cent but this is only to a limited extent. Further, there are several conditions attached to such refinance and is also linked to recovery performance of the SLDBs. Since it takes nearly three to four months for one cycle of debenture flotation, the additional interest paid by the SLDBs on interim finance is substantial in the case of such accommodation having been obtained from sources other than the NABARD and is an extra cost to the banks. While providing interim finance, NABARD also requires the banks to liquidate the interim finance within two months. The SLDBs find this very difficult to comply with, as a great deal of time is required to complete the necessary formalities including documentation. Further, the banks have to justify the need for funds every time a drawal is made from NABARD, which delays availability of funds for loaning. The LDB Federation had represented that NABARD should provide interim finance to LDBs at the same rate at which it provides refinance to the banks, and should also relax the conditions relating to the maximum period of such loans. We are of the view that NABARD should provide the necessary interim finance at the existing rates, viz., 8.5 per cent to 9 per cent to SLDBs. Although we agree that SLDBs should in their own interest reduce the time taken for debenture flotation, in view of the several legal and procedural formalities involved, NABARD should provide interim finance for three months instead of two months as at present.

C. Refinance from NABARD

7.29 NABARD is at present providing refinance to SLDBs by way of contributions to the special development debentures for financing schemes for agricultural development. Flotation of these special debentures involves elaborate paperwork such as seeking Registrar's advance approval, getting government's formal approval and contribution, preparation of trust deeds, etc. The debenture bonds are transferable and servicing of debentures involves detailed follow-up and house-keeping. This leads to delays and causes loss of interest to the SLDBs in view of the time lag between the issue of loans to and actual flotation of debentures on that basis. We have considered in this connection a suggestion that NABARD might provide refinance by way of term loans instead of by contributing to the special development debentures and are inclined to commend this proposal for adoption. But in the absence of provision in the Co-operative Societies Acts of some states and byelaws of some SLDBs for raising resources by way of term loans, early steps need be taken to make appropriate changes in the Act and Rules to enable the LDBs to raise resources in the form of loans from NABARD. When refinance is in the form of loans, the existing practice of first raising resources by way of interim finance, issuing loans and collecting mortgages and then floating debentures against the security of mortgages can be dispensed with. The refinance by way of loans in the event be granted by NABARD without the SLDBs having to collect mortgages first. This modification will do away or reduce the need for interim finance suitably. Mortgages will, however, have to be collected by the LDBs as and when the loans are issued to the borrowers and shall continue to form security for refinance. NABARD has already stipulated that the LDBs should repay special development debentures on an annual basis or as per the repayment schedule of the loans issued under the special schemes sanctioned by NABARD. Hence the terms of debentures have undergone a change as far as their redemption is concerned. We recommend that NABARD should agree for refinancing LDBs by way of loans repayable in annual/suitable instalments, in place of special debentures where a legal provision for raising resources by SLDBs in the form of term loans exists and pursue with the other states/LDBs to fall in line quickly. This will quicken the process of availment of refinance and reduce the loss of interest incurred by LDBs on interim finance.

D. Ordinary Debentures

7.30 Non-schematic lending for productive purposes cannot altogether

be dispensed with by LDBs even though emphasis is being continuously laid on reducing the quantum of such lending and increasing the loans under schematic lending. This is because preparation of schemes on an area basis may not always be possible as there might be purposes for which long-term loans are required by farmers which may not lend themselves to an area approach. There are also cases where the number of borrowers is too small and widely scattered to justify the formulation of any worthwhile scheme. As long as these loans are granted for approved purposes, the land development banks should be encouraged to give them on a limited scale. Further, there are purposes like construction of farm-houses, cattle sheds etc., for which NABARD does not provide refinance. Therefore, such loans are granted by LDBs as ordinary loans and these loans are funded by raising ordinary debentures. The proportion of such ordinary loans is, however, small in spite of strong justification for an increase. The percentage of ordinary debentures floated by SLDBs during 1986-87 to the total debentures floated by them was only 10.6. The total programme of ordinary debentures approved for the last five to six years has been around Rs.100 crores. However, the actual flotations were much less than the approved programme. During 1986-87 the ordinary debentures floated by SLDBs totalled only Rs.57 crores. The ordinary debentures carry interest rates at 10.5 per cent to 11 per cent. The loans under the programme are, however, issued mostly at 10 per cent. It is, therefore, now a loss making proposition.

7.31 A way out is the restoration of the practice followed in the past. It was customary for Life Insurance Corporation of India, the State Bank of India, and other commercial banks, Central and state governments to contribute to the ordinary debentures of SLDBs in certain proportions. The level of contribution by the various institutional agencies till 1980-81 was as under :

	Percentage to total
Life Insurance Corporation	40
State Bank of India and Commercial Banks	20
Central and state governments	10
Mutual support and self-help	30

The support given by LIC was later withdrawn, on the ground that the yield from these securities was not as attractive as the same on Government and

other public sector bonds. We would like to emphasize here that the debentures floated by LDBs cannot be treated merely as a profitable avenue of investment by the public sector institutions. It should be considered as an involvement in a priority sector activity by way of investment in agriculture and fulfilment of a social responsibility. Since, in absolute terms, the amounts which these institutions will be contributing in any one year to the ordinary debentures would be only a small proportion of their total investments, they should, in our view, be willing to invest in these debentures at a concessional rate of interest so as to leave a reasonable margin for the LDBs on their lendings. The Central Government has been making a small contribution to these debentures. We are also of the opinion that the Government of India should not only make a token contribution of say, five per cent in these debentures to demonstrate their interest/involvement in investment credit for agriculture but also direct LIC and other public sector institutions to contribute to such debentures at a concessional rate of interest. The General Insurance Corporation which is involved in the crop insurance scheme during the last few years has in fact even a stake in agricultural credit and, therefore, should also be asked to contribute 10 per cent of these debentures. The Reserve Bank of India was contributing to the ordinary debentures till the early 70's to the extent of the shortfall in the flotation or upto 20 per cent of the total amount floated. Since NABARD has taken over the role of refinancing rural credit from the Reserve Bank of India, NABARD may also be asked to contribute to the ordinary debentures to the extent of 10 per cent of these debentures. The contributions from out of the mutual support and self help from SLDBs may be fixed at 15 per cent since their capacity to grant support at concessional rate of interest is very limited. We, therefore, recommend that the ordinary debentures of SLDBs upto the extent of 10 per cent of the total lending programme in any year may be supported by institutional agencies and government as indicated below :

	Proportion of contribution
Life Insurance Corporation	30
General Insurance Corporation	10
State Bank of India and other Commercial Banks	25
NABARD	10
Government of India	5
State Government concerned	5
Mutual support and self help	15
	<u>100</u>

The debentures may carry a rate of interest of 8 per cent for 10 years maturity and 8.5 per cent for 15 years maturity.

7.32 In case any SLDB wishes to raise ordinary debentures in excess of 10 per cent of its lending programme, it may have to raise debentures at the market rate of interest, ruling at that time.

Loans

7.33 The purposewise classification of loans issued by LDBs during the last 10 years is given in table 9. It will be observed that there is a definite shift away from the traditional purposes such as redemption of debts, purchase of land, levelling and bunding, soil conservation etc. towards minor irrigation works, mechanization and further to purposes like horticulture, animal husbandry, fisheries, etc. A table showing the classification of loans granted by LDBs during the last 10 years for non-productive, not easily identifiable productive purposes and identifiable productive purposes is given in table 10.

Table 10
Purposewise Classification of Loans Issued (Rs. crores)

	For debt redemption and purchase of land	For levelling, bunding, soil conservation, fencing	For minor irrigation, water lifting devices, etc.	For purchase of machinery, implements	Diversified purposes
1975-76	5.47 (2.67)	19.82 (9.67)	124.79 (60.89)	42.08 (20.53)	7.48 (3.65)
1981-82	4.44 (1.20)	14.38 (3.89)	176.38 (47.72)	106.13 (28.71)	43.91 (11.81)
1985-86	6.64 (1.25)	30.25 (5.68)	255.25 (47.90)	91.53 (17.18)	121.34 (22.76)

(Figures in brackets show the percentage to total)

As the table clearly brings out, the proportion of loans issued for minor irrigation purposes has declined during the last 10 years, though however, it continues to be the single major purpose for which loans are granted by LDBs. These loans constituted 47.9 per cent of the total loans issued during 1985-86. The loans granted for purchase of machinery and implements have also shown a decline with the percentage of such loans to total which stood at 20.5 during

Table 9

Classification of Loans Issued by LDBs

Year	Total loans issued	For sinking of new wells and tanks	For boring, deepening and repairs to wells	For purchase and installation of pumpsets, electrification, persian wheels	For purchase of machinery and implements	For levelling, bunding, reclamation of land & fencing	For soil conservation	For construction of godowns and farm houses	For debt redemption	For purchase of land	For preparation of land for orchards and plantation	(Rs. crores)		
												Purchase of bullocks/carts/camel carts	For animal husbandry, poultry & fisheries	Others
1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13.	14.	15.
1975-76	204.93	44.77 (21.85)	18.37 (8.96)	61.65 (30.08)	42.08 (20.53)	19.56 (9.54)	0.26 (0.13)	4.92 (2.40)	3.20 (1.56)	2.27 (1.11)	2.56 (1.25)			5.28 (2.58)
1981-82	369.64*	52.67 (14.25)	42.22 (11.42)	81.49 (22.04)	106.13 (28.71)	12.58 (3.40)	1.80 (0.49)	9.29 (2.51)	2.17 (0.59)	2.27 (0.61)	13.82 (3.74)	7.87 (2.13)	12.64 (3.42)	23.75 (6.36)
1985-86+	532.83	101.58 (19.06)	12.41 (2.33)	141.26 (26.51)	91.53 (17.18)	26.03 (4.89)	4.22 (0.79)	18.34 (3.44)	3.94 (0.74)	2.72 (0.51)	42.99** (8.07)	13.18 (2.47)	43.93 (8.24)	19.65 [⊙] (3.68)

* Break up of Rs.0.91 crore in respect of Kerala not available Figures in bracket show percentage to total

** Includes Rs.334 crores for sericulture.

⊙ Includes Rs.2.90 crore for biogas plants.

+ Statistical tables relating to working of Co-op. LDBs by NCLDB Federation.
Statistical Statements relating to the Co-operative Movement in India. NABARD.

1975-76 coming down to 17.2 during 1985-86. This reduction is mainly due to the shift in the policy of NABARD in fixing a limit for refinancing loans for purchase of tractors, power tillers etc. and also in the reduction in the rate of refinance for such loans. The percentage of loans granted for levelling, bunding and reclamation of land has declined. Further, non-schematic loaning under this purpose is not encouraged because of its not easily identifiable nature, unless taken up by an implementing agency like a land development corporation. The proportion of loans granted under soil conservation although forming a small percentage had increased from 0.1 per cent to 0.8 per cent during the last 10 years. Emphasis is presently being put on soil conservation under dryland development programme and state governments have to take up more programmes under watershed development as a national policy for increasing the productivity of dry land. At present some of the state governments finance these programmes out of their budgetary resources. We would suggest that the banks show more interest in these programmes. Financing horticulture and plantation crops has shown a significant increase from 1.3 per cent to 8.1 per cent of the total loans issued during the last 10 years. This is an area where there is more scope for financing, especially in view of the better utilisation of the limited water resources in many parts of the country and the better returns available as compared to cultivation of food crops. Under the diversification of the loan portfolio, the LDBs have enlarged the volume of finance under animal husbandry, fisheries and for purchase of draught animals which were previously exclusively financed by the short-term credit structure. Loans for purposes like debt redemption and purchase of land etc. have been brought down to a very low level.

7.34 The state-wise position of purpose-wise classification of loans advanced during 1985-86 is shown in table 11. The table reveals the following trends :

- i) Minor irrigation continues to be the major purpose the LDBs have financed. In 11 out of 17 states the major purpose for which loans are granted by LDBs is minor irrigation works. The states where banks had financed for minor irrigation heavily are Bihar (84.6 per cent), Uttar Pradesh (83.1 per cent), Orissa (68.9 per cent), West Bengal, Madhya Pradesh, Rajasthan and Maharashtra (more than 50 per cent).

Table 11
Classification of loans issued by LDBs during 1985-86 Statewise

(Rs. crores)							
States	Total Loans issued	Minor Irrigation	Purchase of machinery & implements	Plantation and Horticulture	Diversified purposes	Levelling, bunding, soil conservation, barbed wire fencing and command area development.	Payment of old debts, purchase of land etc.
1.	2.	3.	4.	5.	6.	7.	8.
1. Andhra Pradesh	63.14	20.08(31.8)	10.04(15.9)	7.56(12.0)	11.25(17.8)	10.13(16.0)	--
2. Assam	1.50	0.56(37.3)	0.16(11.0)	0.09(6.0)	0.68(45.3)	--	--
3. Bihar	31.09	26.32(84.6)	3.15(10.1)	0.29(0.9)	1.05(3.4)	0.21(0.7)	0.07(0.2)
4. Gujarat	26.97	10.67(39.5)	6.72(24.9)	0.17(0.6)	1.17(19.2)	--	--
5. Haryana	52.16	9.24(17.7)	11.08(21.2)	2.34(4.5)	13.71(26.3)	1.22(2.3)	2.94 ^x (5.6)
6. Himachal Pradesh	1.53	0.10(6.5)	0.69(45.5)	0.26(16.9)	0.29(18.9)	0.17(11.1)	--
7. Jammu & Kashmir	1.65	0.01(0.6)	1.30(78.8)	0.12(7.1)	0.18(10.7)	0.04(2.4)	--
8. Karnataka	56.07	25.48(45.4)	9.44(16.8)	5.78(10.3)	12.22(21.8)	1.85(3.3)	--
9. Kerala	41.02	3.72(9.0)	1.68(4.1)	14.89(36.3)	7.15(17.4)	11.61 [†] (28.3)	0.04(0.1)
10. Madhya Pradesh	31.57	15.94(50.5)	12.24(38.8)	0.15(0.5)	1.49(4.7)	--	--
11. Maharashtra	57.22 ^o	31.13(54.4)	2.92(5.1)	3.31(5.8)	4.43(7.7)	0.07(0.1)	0.04(0.1)
12. Orissa	7.62	5.25 (68.9)	0.29(3.9)	0.45(5.8)	1.39(18.2)	--	--
13. Punjab	46.61	7.97(17.1)	13.15(28.2)	1.07(2.2)	16.98(36.4)	3.26(7.0)	3.31(7.1)
14. Rajasthan	18.94	11.08(58.5)	6.84(36.1)	0.44(2.3)	0.49(2.6)	--	--
15. Tamil Nadu	21.48	8.60(40.0)	7.89(36.7)	1.33(6.2)	3.14(14.6)	0.19(0.9)	0.33(1.5)
16. Uttar Pradesh	74.78	62.14(83.1)	7.35(9.8)	0.50(0.7)	3.24(4.3)	0.65(0.8)	--
17. West Bengal	8.53	4.81(56.4)	1.10(12.9)	0.85(9.9)	1.20(14.1)	0.57(6.6)	--

Note : The figures in bracket show the percentage to total.

^oRs. 11.69 crores advanced to State Electricity Board & Rs.3.62 crores to Warehousing Corporation not included in breakup.

+ Rs.5.39 crores for barbed wire fencing under schematic lending.

X Rs. 12.72 crores shown under others - Not taken (24.3%)

Source : Statistical tables relating to working of co-op. LDBs.

- ii) Purchase of machinery (tractors, power tillers etc.) constituted a major purpose financed by LDBs in Jammu & Kashmir (78.8 per cent), Himachal Pradesh (45.5 per cent), Madhya Pradesh, Rajasthan and Tamil Nadu (more than 36 per cent). Plantation and horticulture advances by LDBs have picked-up in Kerala (36.6 per cent), Himachal Pradesh (16.9 per cent), Andhra Pradesh (12 per cent). However, the banks in states like Jammu & Kashmir, Uttar Pradesh, Punjab Rajasthan, Madhya Pradesh, Gujarat and Bihar had very low percentage of advances under plantation and horticulture.
- iii) LDBs which have granted substantial proportion of loans for diversified purposes like purchase of milch cattle, poultry, piggery, fisheries, purchase of bullocks, bullock-carts, camel, camel-carts etc. were in states of Assam (45.3 per cent), Punjab (36.4 per cent), Haryana (26.3 per cent), and Kerala (28.3 per cent), while the banks in states of Bihar, Madhya Pradesh, Uttar Pradesh and Rajasthan have done very little in encouraging such diversified lending.

Housing Finance

7.35 Housing is one of the basic needs of human life. With the high and rapid growth of population in the last 50 years coupled with the shift of people from rural to urban/semi-urban areas, the housing problem has worsened all over the country including rural areas. However, because of the very long-term nature, the banks generally did not look with favour towards this activity. The states had their housing boards but they generally restricted their activities to urban areas only. The LIC is another financial institution which provides funds for financing housing schemes. Housing Development Finance Corporation (HDFC) was set up to provide refinance facilities for this purpose but considering the magnitude of the problem, all these efforts were falling considerably short of the actual requirements. During the last decade or so, the banks particularly commercial banks and urban co-operative banks are being goaded to take up financing this activity. But because of long-term nature of such finance as against short-term nature of their resources, as well as risks of defaults and the difficulties in enforcing security and demands of other priority sector lending, the banks have made available meagre resources for housing finance.

7.36 As a part of the strategy aimed at larger flow of resources for housing, measures are being taken to create a net-work of specialised housing finance institutions with a national housing bank at the apex level. The National Housing Bank has already been set up with an initial share capital of Rs.100 crores fully contributed by the Reserve Bank. The Reserve Bank also proposes to contribute to the National Housing Bank another Rs.50 crores to be earmarked exclusively for rural housing. The responsibilities of this Bank are to promote and develop specialised housing finance institutions, to mobilise resources for housing, to provide refinance facilities to housing finance institutions and scheduled banks, extend credit facilities for housing, in particular for the economically weaker sections of the society and co-ordinate in general the working of all the agencies connected with housing.

7.37 The Union Finance Minister, in his budget speech of 1988-89, made a policy statement extending the role of LDBs to cover the field of rural housing finance for farmers and suggested that the LDBs should mobilise resources for this purpose. So far there does not seem to be any follow up action by NABARD or the National Housing Bank in this behalf. No guidelines have been issued about the manner in which the LDBs can take up this activity and raise resources required for the same.

7.38 We agree that housing is an important activity not only in urban and semi-urban areas but also in rural areas which needs assistance from the banks with their expanded branch net-work. However, in the case of LDBs, it needs to be noted that they depend entirely on external resources for financing their activities. Unless, therefore, a source of refinance is provided to the LDBs, they would not be in a position to undertake this activity. It may, therefore, be necessary to link them up with the National Housing Bank.

7.39 The experience of a few SLDBs like the one in Maharashtra which had earlier ventured in the housing finance as well as the performance of the various housing boards set up by the states, in the recovery of loans has not been, by and large, very happy. The recovery performance of LDBs even in their traditional role of financing investment activities for productive purposes, is far from satisfactory. Housing loans, of course, stand on a somewhat different footing. The repaying capacity in the case of housing loans is adjudged from the criterion entirely different from that which applies in

the case of production loans. In their case it is the incremental income generated by the investment credit that is all that matters. But in the case of housing it is the total income of the family, the amount they spend currently as rental for the residential accommodation (which will be saved) will be the main consideration in deciding the viability of the housing loan. Further, the loans will not only be adequately secured but would also be secured by an appreciating asset although difficulties in enforcing the security in the case of default and realising the loans by sale of the assets cannot be ruled out.

7.40 We are, therefore, of the view that housing finance activity, especially rural housing finance, though socially very desirable, needs to be undertaken with full awareness of the risks involved. In the case of LDBs which have no resources of their own, we recommend that they may take up this activity on an agency basis. This will involve no risk on their borrowed resources being frozen in housing loan defaults. Since LDBs have reached rural areas of the country extensively and have overall competence to dispense long-term credit, they will be a proper agency for the National Housing Bank to use and extend credit for housing in particular for the economically weaker sections of the society which is one of its major objectives. The LDBs should be paid reasonable agency charges for this purpose. Necessary amendments to the Co-operative Societies Acts/Bye-laws of LDBs will also have to be made to enable LDBs to undertake the activity on an agency basis. The state governments should amend the Acts/Bye-laws suitably.

Overdues

7.41 The overdues of LDBs during the last 10 years from 1975-76 to 1985-86 and the percentage of overdues to demand are indicated below :

	(Rs. crores)					
<u>1975-76</u>	<u>1980-81</u>	<u>1981-82</u>	<u>1982-83</u>	<u>1983-84</u>	<u>1984-85</u>	<u>1985-86</u>
92	291	252	269	267	285	298
(34)	(46)	(40)	(44)	(36)	(40)	(39)

(Figures in brackets indicate percentage to demand)

The percentage of overdues to demand has remained for all banks taken together more or less static around 40. The LDBs in eight states out of 22, however, had total overdues exceeding 50 per cent of the demand and in another five

states the overdues ranged from 40 to 50 per cent. Classified purposewise, the overdues for minor irrigation and horticulture constituted 46.1 per cent and 44.9 per cent respectively of the demand for the year 1986-87 for which latest data are available while overdues under land development, farm mechanisation and biogas plants were lower at 27.6, 17.4 and 14.9 per cent respectively to the demand for that year. As we have observed elsewhere in this report, overdues are common to all types of lending institutions and the LDBs are no exception. What is, however, disquieting in the case of LDBs is that their overdues are larger than those of the PACSs even though their loans have been granted for productive investment purposes and are adequately secured by mortgage of lands. These loans represent investments in agriculture and generally result in creation of productive assets which should normally generate adequate incremental income to repay the loans. But this does not seem to be taking place. The phenomenon of high overdues, therefore, become more puzzling. To an extent, defective practices are at the root of the defaults, such as fixing of wrong repayment schedule without proper correlation with the cash flows of the project, inadequate unit cost, not ensuring the availability of working capital, not granting reschedulement/rehabilitation facilities in the case of infructuous investments like failed wells, ineffective supervision over the end-use of loans etc. These, however, do not explain the position fully. One of the many reasons for high overdues seems to be the lack of will among the borrowers to repay. A second likely reason seems to be the feeling that extreme measures like attachment and sale of security would not be taken even if there was a wilful default. The absence of a proper climate conducive to recovery is thus an important contributing factor for poor recovery. The whole question has been discussed separately in Chapter XV.

Lending Rates and Margins

7.42 Another major problem of land development banks is the viability of their lending operations in the context of growing cost of funds borrowed and lending rates fixed uniformly by the Reserve Bank of India. The LDBs raise their resources mainly by way of flotation of debentures. The special development debentures contributed by NABARD and the Central and state governments form about 85 to 90 per cent of the total debentures floated in a year. The rate of interest on special development debentures, lending rates to the ultimate borrowers and the margin available to the LDBs are indicated on the next page.

Purpose	(Per cent)		
	Rate of interest on Special development debentures	Rate of interest to the ultimate borrower	Gross margin
Minor irrigation and land development (for all categories of borrowers)	6.5	10	3.5
Diversified purposes			
a) Small, marginal farmers and other weaker sections	6.5	10	3.5
b) Other farmers	8	12	4.5

NABARD stipulates a minimum percentage of lending to the weaker sections to the extent of 60 per cent of the loans issued under schematic lending. Minor irrigation continues to be the major purpose financed by LDBs. Besides, LDBs have to meet the cost of additional interest on interim finance, the rate of interest of which ranges from 10 per cent to 14 per cent. Hence, the average margin available to LDBs is only about 3.5 per cent. This margin is slender taking into account the need for staff, follow up measures on the loans sanctioned and administrative expenses. Studies conducted by our Consultants have revealed that LDBs, on an average, lose about 0.65 per cent to one per cent at the PLDB level on their lending. Hence, even under schematic lending, LDBs are not able to make any profit because of the transaction cost being high as they have to service a very large number of small borrowers scattered over a number of villages.

7.43 Apart from schematic lending, the banks also finance normal loans to the extent of 10 to 15 per cent of the total resources raised by them. The resources for normal loans are raised by way of ordinary debentures where they earn no margin or even a negative margin because the rate of interest on ordinary debentures is 10.5 and 11 per cent for periods of 10 years and 15 years respectively. Since most of these loans are lent at 10 per cent rate of interest, the loss on account of such advances will not be less than 1.5 per cent to 2 per cent. Since the Government of India wants financial institutions to lend for agriculture at concessional rates of interest, either LDBs will have to be provided with resources at cheaper rates of interest so as to give them adequate margin for meeting the required transaction

cost or allow LDBs to charge a rate of interest on loans which will be economical. We have discussed the question at length in paragraphs 27 and 28 also. Our recommendations in this regard are given in Chapter XVIII on Interest Rates, Costs and Margins.

Security

7.44 In the case of long-term loans under the existing provisions of Co-operative Societies Act, land development banks are obliged to obtain mortgage of land as security for their loans as issue of debentures by LDBs is at present linked to mortgages obtained by them. The bye-laws of LDBs, therefore, provide for obtaining mortgage of land and other immovable properties of the borrower or government guarantee as security for issue of loans. The procedures for taking mortgage of land are complicated and time-consuming but in the present legal framework, security of land and mortgage of the same cannot be avoided. Although the Hazari Committee had recommended a new form of security i.e. a special charge known as "GEHAN" which could be effected by a mere declaration by the borrower and which could have all the characteristics of a mortgage without its time consuming formalities, it was found that the procedure was as time consuming as the one relating to mortgage because a charge on land cannot be created without establishing the ownership rights. In this context a suggestion is often made that LDBs may not insist on mortgage of land as security. It is argued that best security for loan is the asset created out of it. Hence to avoid delays in execution of mortgages and consequent sanction of loans, it is suggested that wherever possible, particularly in the case of loans for farm machinery etc., hypothecation of the moveable assets such as machinery may be accepted as security without insisting on mortgage of land. We have considered this suggestion. The difficulty in accepting as security, hypothecation of moveable assets in the case of long-term loans, however, is that the asset depreciates very fast. In case the repayments are not forthcoming according to the schedule, the security may not be adequate to cover the loan outstanding with interest. Security by way of mortgage of land has definite advantages particularly where investment credit is concerned. In fact the whole LDB structure has been evolved on the basis of mortgage banking. In view of this position we are not inclined to accept that the mortgage security may altogether be done away with in favour of hypothecation of assets at least in respect of land based activities. We are aware of the difficulties the financing institutions experience in the execution

of mortgages when the land records are not up-to-date or the rights in land are not well established etc. The remedy, therefore, lies in not doing away with this security of mortgage but taking speedy steps to remove the difficulties encountered by the borrowers in the execution of mortgages of land such as making the record of rights up-to-date and readily available. We, therefore, recommend that such steps may be taken by the state governments early. It is also suggested that the state governments might introduce the system of issuing revenue pass-books with statutory recognition which will eliminate the need for execution of various documents by the borrower and will enable the banks to sanction loans without delay. As regards non land based activities like cottage and small scale industries etc, we have recommended amendment of the Co-operative Societies Acts to include hypothecation of assets as security.

Management

7.45 In the case of most of the land development banks there is no definite policy in regard to recruitment, appointment, career planning and development for the staff. There are still banks which depend either entirely or substantially on the government staff even for the basic functions of identifying potential borrowers, sponsoring loan applications and formulation of schemes. In the case of most of the SLDBs, the chief executives are either officers belonging to the Indian Administrative Services or to the Co-operative Departments while some of them even at the middle level are found to be on deputation from the state government. In the absence of elected boards, a large number of LDBs have official management instead of professional management. The permission or prior approval of the Registrar of Co-operative Societies is required for new posts. This results in demoralisation of the banks' own staff. LDBs should have a policy for recruitment, appointment and promotion and training of the staff and for manpower development for meeting future needs. The primary objective should be to introduce professional management and also to ensure the functioning without day to day interference from the state government. We have already dwelt at length in an earlier chapter on the problem of the debilitating government control and interference in the management of co-operatives. The LDBs, like other co-operatives in the system, must develop and must be allowed to develop their own staff on proper professional lines.

Integration of the Short and Long-term Structures

7.46 Over nearly seven decades of their chequered history, the land development banks have been able to carve out a niche as a specialised institution in the co-operative sector, catering exclusively to the investment credit needs of the rural areas. Beginning purely as mortgage banks largely for redemption of past debts, these institutions have since transformed themselves into rural development banks, though they are not banks in strict legal term, inasmuch as they do not raise deposits from the public withdrawable by means of cheques or otherwise on demand for the purpose of their lendings.

7.47 The land development banks today finance not only agriculture and allied land based activities, but also several non-land based developmental projects like dairy, poultry, sheep rearing, fishery etc. The progress which these banks have made, their organisational weaknesses and our recommendations to remedy the deficiencies have already been discussed. But one major issue which in recent times has emerged as a constant irritant to the structure and, in the view of those who man these institutions, has become a threat to their separate identity and, therefore, also a major obstacle to future growth, namely, the ongoing debate on the integration of the structure with the short-term structure. Starting with the emphasis on the need for effective co-ordination between the two structures, the debate subsequently centered round full-fledged integration following the recommendation of the Hazari Committee on Integration (1976), with a dissenting note by one of its members for such an integration. The logic for integration as contained in the report is reproduced in the two extracts given below :

"The lending institutions exist or have come into being for the benefit of the ultimate borrower cultivator and the entire exercise of moulding, remoulding or restructuring them has to keep in focus the efficiency and capability of the credit delivery system to meet the needs of the beneficiaries. It is the ultimate man - the farmer who is to be provided with the wherewithal for his production and investment needs".....

"In the context of national agricultural policy, from the point of view of farmers' convenience, of taking a comprehensive view of the borrower's requirements, of closer supervision over end-use of credit, of improvements in the quality of loans advanced and of better financial discipline among the borrowers, of the cost advantages accruing through better deployment of funds, etc., the case for integration at all levels in the two wings of the co-operative credit structure is well established."

As is evident from these extracts, the thinking on integration by the committee has been influenced largely by the concern for ministering to the convenience of the farmers by providing "one contact point" for them. The concept of one contact point for short, medium and long-term credit itself, however, arose from the concept of the farmers' service co-operative society (FSS) which along with the scheme for financing of PACSs by commercial banks and ARDC's routing of long-term credit through these societies in the mid-seventies, had emerged as the sheet anchor of future policy in reorganising the co-operative credit structure so that there was one institution at the base level to provide the farmer with both credit - whether short, medium or long-term - and other allied services such as provision of inputs, extension services etc. in an integrated manner. The comparative position of FSSs, and PACSs in several states reveals that although the membership, owned funds and loans outstanding showed comparatively better position in FSSs as compared to PACSs, mainly because of their larger size, in respect of mobilisation of deposits and recovery of dues there was no significant difference between the two. The multipurpose functions envisaged in the FSSs were also absent in most of the PACSs. Overall, their performance has not been very encouraging. In fact one of the terms of reference required the committee, inter alia, to examine the organisation and staffing pattern at the base level which is expected to deal with farmers so that it may be able to integrate the different types of credit and other services like supplies of agricultural inputs, marketing of agricultural products, technical guidance etc. also. It is thus evident that the objectives aimed at was not merely integration of short, medium and long-term credit, but also of supplies of agricultural inputs, marketing of agricultural produce, technical guidance and related services. But in effect the committee limited their concern to the integration of credit structure and did not consider such integration as a part of an overall package of integration.

7.48 It also needs to be added that the terms of reference by which the committee was bound, subsumed a priori, integration of the two structures. In other words, the issue remitted for consideration of the committee was in fact merely the working out of the mechanics of integration including whether or not integration may be in one stroke or in phases. Thus while one of the terms of reference required the committee "to examine whether the integration may be brought about simultaneously at all levels of the two

wings of the co-operative credit structure or it may be done in a phased manner at the different levels" while another required the committee "to examine the structure of management and the staffing pattern at the intermediate and higher levels of the integrated wings of the two units of the co-operative credit structure so that they may be able to handle satisfactorily short-term, medium-term and long-term agricultural credit".

7.49 As regards integration merely of the two credit structures, the views of the high level committees, such as the All India Rural Credit Survey Committee, and the All India Rural Credit Review Committee, which had considered the question of a separate structure in long-term credit, had ruled out the possibility of unified structure for short, medium and long-term credit. The Seventh Indian Co-operative Congress held in 1976 also, discussed the question of integration of the two units of the co-operative credit structure, and had come to the conclusion that it was not necessary to effect such an integration at any level. The findings of the Study Groups of the Hazari Committee also do not bring out any data to show that lack of integration by itself or in other words, the existence of separate institutional streams for short and long-term credit have by themselves impeded the progress of the agricultural credit system. And yet, the committee came to the conclusion that from the point of view of farmers' convenience and taking a comprehensive view of borrowers' requirements, as well as of the advantage accruing through management and better deployment of funds, it was imperative that there was integration of the two wings of the co-operative credit structure at all levels. Nonetheless, the committee recognised that the process of integration should be suitably phased and that integration may be expected to begin with in clusters of districts where command area projects for area development schemes approved by ARDC were then in operation. The committee had also observed that the integration to be successful would call for reorganisation of PACSs since it was recognised that the PACSs in general as they were constituted and functioning would not be able to disburse long-term loans in a satisfactory manner and reorganisation of PACSs on the lines suggested by the Reserve Bank was a sine-qua-non for effecting integration at the primary level. Such reorganisation with appointment of full time paid secretaries trained in functions of long-term lending has not yet been accomplished even after 12 years of the submission of the report. Likewise the FSS's experiment has not taken off although a few societies came to be organised in some isolated

pockets. The scheme of financing of PACSs by commercial banks which was also expected to promote integration of the two credit streams has since been given up following the recommendation to this effect by a Working Group which went into the working of the scheme. It cannot, therefore, be said that conditions exist in which integration can now be attempted successfully.

7.50 Also, the state governments themselves held divergent views on the main issue of integration - some in favour and some against, while the SLDBs and their national federation totally opposed the integration proposal. The Planning Commission also suggested a cautious approach as it involved disturbing the existing structure. In view of the divergent views expressed by various parties concerned on the main recommendation of the Hazari Committee, viz., integration of the two wings of the co-operative credit structure, the recommendation was deferred when it came up for discussion at the Agricultural Credit Board of RBI. The suggestion that PACSs may act as agents of LDBs for disbursing long-term credit was, however, endorsed.

7.51 The issue of integration has been subsequently examined by the CRAFTCARD (1981) and the High Level Working Group on Land Development Banks (Rajgopal Committee, 1985), which recommended that the objective of meeting farmers' credit needs at one contact point could be better served by functional co-ordination and not by integration.

7.52 Thus as late as in 1985, the consensus among the various committees except the Hazari Committee was that integration was not the solution to the problem though the Seventh Plan paper no doubt mentioned that one of the objectives of policy for early action would be the integration of the two structures. While there is consensus about the need for effective co-ordination between the two structures, the overwhelming view of expert committee has been that the existing arrangements may not be disturbed without assured advantage.

Integration experiments

7.53 Four state governments, viz., Punjab, Madhya Pradesh, Rajasthan and Andhra Pradesh which favoured such an integration later formulated schemes for integration of the two wings of the co-operative credit structure although

the pattern was different as among the four proposals. The Government of Punjab proposed a scheme which envisaged not only integration of the short-term and long-term co-operative credit structure but also merger of all CCBs and PLDBs with the SCB/SLDB, thus creating a two tier composite credit structure. The Government of Rajasthan had similarly prepared a scheme proposing the conversion of the three tier co-operative credit structure into a two tier one and establishment of the branches of the reorganised State Co-operative Development Bank at the level of Panchayat Samitis. The scheme proposed by Madhya Pradesh Government broadly envisaged action on the lines of the majority view of the Hazari Committee. The Government of Andhra Pradesh proposed an altogether different pattern, viz., (a) reorganisation of PACSs to make them co-terminus with Mandals, (b) integration at all levels of the credit structure and (c) restructuring of the marketing co-operatives in the State.

7.54 The proposal from Punjab, Madhya Pradesh and Rajasthan were considered by the Agricultural Credit Board of Reserve Bank of India (ACB). While no view was taken on Punjab proposal, pending further examination of some of its aspects, the Agricultural Credit Board was not in favour of the proposals from Madhya Pradesh and Rajasthan. The concerned state governments were advised to proceed cautiously, as in the then existing financial position of the two structures, integration might have resulted in choking the flow of both short-term and long-term credit. However, if despite the Board's advice, state governments wanted to go ahead, they were advised to take certain minimum safeguards and to this end, provide certain degree of financial assistance to the emerging structure so that the weaknesses of the merging units were not inherited by the integrated structure. The more important among them being as under :

- a) Provision of necessary funds by the state governments on redeemable basis at the disposal of the CCBs and PACSs to enable them to absorb the overdues in excess of owned funds.
- b) Outright grants by the state governments to cover deficits in the bad and doubtful debts reserves so that a smooth flow of credit could be ensured.
- c) Availability of adequately trained personnel to man the restructured institutions at all levels.

- d) Provision of suitable managerial subsidies; and
- e) The need to ensure that democratic character and set up of the co-operative credit institutions were not jeopardised.

7.55 The governments of Punjab, Madhya Pradesh and Rajasthan, however, developed second thoughts on their proposals and decided not to pursue the matter further. But Government of Andhra Pradesh in the last couple of years vigorously pursued the proposal.

7.56 The main concern underlying RBI/NABARD's view on the integration proposals has been that integration of two weak structures, as then obtaining in Punjab, Madhya Pradesh, Rajasthan when the state governments proposed the scheme as in Andhra Pradesh later was likely to result in the integrated structure inheriting the weaknesses of the merging units and clogging the flow of credit, whereas the Seventh Plan envisaged substantial increase in the flow of credit which pre-supposed existence of strong and effective channels of the credit delivery system. Strengthening of the integrated structure entailed massive doses of financial assistance to wipe out the bad debts, losses, etc. of the merging units which, it was thought, the state government might find it difficult to provide.

7.57 The Andhra Pradesh proposal was, however, further considered in June 1985, by the Cabinet Secretariat which suggested that integration might be attempted on a pilot basis in a small area and constituted a working group for working out the modalities of the pilot project. The working group endorsed the Andhra Pradesh proposal for implementation in a phased manner to start with at the level of PACS. It simultaneously recommended financial assistance from the state government (quantum of which was to be settled between state government and NABARD) to ensure financial soundness of the emerging structure. Subsequently, as advised by Government of India, RBI/NABARD approved the integration of short-term and long-term structure and Government of Andhra Pradesh reorganised the primary credit structure and integrated PLDBs with CCBs at the intermediate level, in March 1986. Integration of the SLDBs with SCB is to take place at a later date. It is, however, too early to judge the success or failure of the experiment.

Schematic loaning of State Co-operative Banks

7.58 An emerging phenomenon to be reckoned with, in the scenario of term lending by co-operatives, is the increasing involvement of the short-term credit structure in schematic lending. The state co-operative banks (SCBs) in several states such as Maharashtra, Gujarat, Kerala, Karnataka, Rajasthan, Orissa, Madhya Pradesh, Tamil Nadu and Uttar Pradesh, with refinancing facilities from NABARD and its forerunner, have been providing finance for long-term purposes, even in the absence of any structural integration. Such purposes included minor irrigation, land development, farm mechanisation, plantation, allied agricultural activities like poultry, fisheries, dairy development, gobar gas plants etc. As against refinance of Rs. 25 crores drawn by them from ARDC/NABARD during 1981-82, their drawals increased to Rs.41 crores in 1983-84 and further to Rs.65 crores in 1986-87, though the proportion of their drawals to the total disbursements by NABARD in the last year were modest at five per cent. However, a few SCBs had made rapid strides in long-term lending. In the years 1981-82 and 1982-83 the long-term lendings of the Orissa State Co-operative Bank had exceeded those of the Orissa SLDB. Similarly, in 1986-87 the long-term lending of the Tamil Nadu SCB had exceeded that of the Tamil Nadu SCLD Bank. It has been a major achievement that as many as 15 SCBs have already embarked on schematic lending involving term loans.

Integration - whether or not

7.59 The argument in favour of integration is mainly based on the advantage in having a single contact point providing all the credit requirements. This it is argued would, apart from obviating the need to approach different agencies for different types of credit, enable the credit agency to take an integrated view of borrowers' total credit requirements, ensure that the total credit is kept within the borrower's repaying capacity and also ensure better supervision over the performance of the borrower. Since the security offered by the borrower is the same, the present system makes it difficult to apportion the security among the two structures.

7.60 As against this, the arguments in favour of maintaining the existing pattern are firstly, the provision of long-term investment credit for agriculture is of a specialised nature, and needs expertise and special skills and the LDBs have, over the years acquired this expertise and technical competence for

the purpose. Secondly, the short-term credit structure and the long-term credit structure have not grown uniformly in all the states. Thirdly, while the short-term credit structure is largely a three-tier one, the long-term credit structure is a two-tier one where it is federal and unitary in the remaining states. The base level institution in short-term credit structure, viz., the PACS is even today ill-equipped to handle investment credit. In spite of several attempts to reorganize the primary societies on a viable basis during the last 30 years, a large number of societies does not have even a full-time paid secretary, leave alone other staff required for appraisal of loan proposals and/or completing other legal formalities for obtaining mortgage deeds etc. In the absence of this essential requirement recognised by the Hazari Committee as a precondition for integration, the integration of the two structures is more likely to jeopardise the flow of investment credit to the agricultural sector. The objective needless to say is to offer better services to the agriculturists and this can be done only by a strong and efficient structure. Judging by the present status of the two structures which suffer from serious weaknesses, there is reasonable apprehension that the emerging integrated structure may not be strong or efficient enough to provide the required services. The flow of credit in the process, it is feared, is likely to be disrupted which is a risk the country cannot afford to take at the present juncture. The co-operative credit structure with its two separate wings is only a division of labour which ensures specialisation and better efficiency in operations.

7.61 Normally in considering integration of structures the policy is for the weak institution to be merged with the strong institution, so that the new institution removes the weaknesses and is able to serve the clientele in a better way. In the present case, it is at best an attempt at bringing together two weak structures into a unified credit structure in the co-operative sector. It would, therefore, be open to question whether such a unified structure will prove better in the matter of effective coverage, expansion of business and recovery of the loans.

7.62 We thus find that the opinion, not only among the co-operators but also among the experts, is sharply divided on the issue but certain broad conclusions emerge. They are :

- i) The PACSs as they are functioning at present cannot, by and large, be expected to undertake long-term lending effectively and efficiently. The condition postulated by Hazari Committee regarding their reorganisation on a viable basis with a trained secretary is yet to be fulfilled.
- ii) Integration may not bring in any saving of expenditure because there will not be any reduction of staff. On the contrary, since uniformity will have to be introduced, the lower salaries etc. of staff in one of the structures will have to be raised to match those of the other.
- iii) 'Single window' concept is a desirable one. It, however, needs to be recognised that there could be limitations to this, in view of the present status of the two structures and their working, particularly the manner in which they raise resources.
- iv) There is no positive evidence to support that integration will lead to a stronger, efficient and profitable co-operative structure capable of providing credit of all types to agriculturists.

We further find that in spite of the opposition in certain quarters, experiments were thought of by four states but only Andhra Pradesh has gone ahead in favour of integration, but it is too early to judge its results. The efforts made to ensure effective co-ordination between the two structures have yet to bear fruit but need to be pursued. It is noted that the SCBs have undertaken long-term lending by way of schematic loans with NABARD refinance but the SLDBs have yet to make a beginning in providing short-term loans even though they are assured of refinance facilities by NABARD. The scene, therefore, although confused at present, leads us to envisage that the distinction between the two structures is more likely to decline as time passes. At the same time we cannot ignore the possible adverse effects on the co-operative credit structure. One cannot also ignore the present unsatisfactory position of both the short and long-term structures and the risk involved in disturbing the flow of credit if two such structures are merged. In the light of these considerations, we recommend that :

- i) the short-term and long-term credit structures of co-operatives may be allowed to function separately where they so exist. No

integration of the two structures is considered necessary because (a) in our view the merging structure will not be a strong one (b) considering that the PACSs are not strong enough or well equipped to undertake the long-term credit business, immediate integration is likely to create more problems than it seeks to solve and (c) the imperative need to maintain and in fact even increase the flow of short-term as well as investment credit for the current as well as the next two Five Year Plans and (d) both the structures in most of the states are financially and organisationally weak and require strengthening to enable them to play their role effectively.

- ii) There is a need for the two structures to develop specialisation in their respective fields in the face of new challenges and the changing face of the agricultural sector of the economy.
- iii) Although we do not favour immediate integration, we are not against the concept of "single window" facility for the borrowers through co-operatives. Well managed and viable PACSs should therefore, be allowed to grant long-term loans where necessary.
- iv) There is need to have an effective co-ordination between the two agencies to complement the efforts of each other. This could be brought about at the district/block level through the 'service area approach' being adopted for all the credit agencies in the districts.

7.63 We thus believe that the integration of the two structures at the present juncture is not feasible. However, where the necessary conditions exist and adequate financial and other support comes from the concerned state government, it may be undertaken. It is our considered view that if forced, it may create more problems than it is expected to resolve. The urgent need today is, therefore, to strengthen on the one hand, PACSs organisationally and managerially and we have made several recommendations elsewhere to achieve this, and on the other, to strengthen particularly the LDB structure. Renewed efforts are also called for to ensure effective co-ordination between the two structures.

Overall Assessment of the Long-term Structure

7.64 With the advent of planning in the country in 1951, the LDBs were

assigned a positive role in the context of raising investment in agricultural sector for increasing production. The LDBs have, as pointed out in para 4 (Table 1) earlier, acquitted themselves well in investment lending for agriculture.

7.65 During the period of about 60 years, the banks have undergone various changes. Starting with pure mortgage banking in 1929, they have now become agricultural and rural development banks catering not only to the investment needs of agriculture and allied activities but also in some cases the credit needs of rural artisans, rural cottage industries and small enterprises in rural areas.

7.66 Their growth has also not been uniform in all parts of the country. While some states like Andhra Pradesh, Punjab, Maharashtra, etc. have done much better, other states like Assam, Bihar, Himachal Pradesh etc. have lagged far behind. The structure is also not uniform in the country. In some states it is unitary; in other states it is federal and in two states it is mixed. Since there is no evidence to prove that one or the other is better in performance, we have made no recommendation in altering the structure as it exists in the states.

7.67 Like the short-term co-operative credit structure, this structure is also facing some problems that have so far defied solutions. The most important and critical problem is the high level of overdues. The percentage of overdues to annual demand of PLDBs increased from 28.1 in 1975-76 to 44.1 in 1985-86. Only 32.3 per cent of the total number of PLDBs/branches of SLDBs during 1985-86 have unrestricted lending eligibility (overdues upto 25 per cent of demand) and 23.7 per cent of the primary units have a highly restricted lending eligibility from NABARD during the same year (overdues above 65 per cent of demand). The second problem consequential to high overdues is the non-viability of a large number of base level units. Thirty per cent of the total number of PLDBs/branches of SLDBs were deemed not viable as on 30.6.1986. High overdues leading to restricted lending eligibility, inability of non-viable and weak banks to improve the lending performance and consequent deterioration of the profitability, high cost of raising debentures and lower margins available following the administered lending

rates are the factors responsible for this unsatisfactory position. To obviate the difficulties, we have made certain suggestions in this report elsewhere in regard to tackling the problem of overdues, provision of higher margins to PLDBs and the adoption of viability criteria in the place of present EC for being able to obtain adequate refinance for lending from NABARD.

7.68 Another problem the banks have been facing for a long period is the uneconomical cost of interim finance for issuing loans before debentures are floated. At present the banks pay the market rate to commercial banks and SCBs for this finance. This has acquired currently added significance because of the low margins available to SLDBs. We have recommended NABARD to provide adequate interim finance at a concessional rate to reduce the interest burden on SLDBs. Since the introduction of administered rates of interest, the scattered loans financed through raising ordinary debentures have become uneconomical for banks as the cost of funds is more than the lending rates fixed for the ultimate borrowers. As a solution to this problem and in view of the importance of such lending, we have recommended elsewhere institutional support for this programme at somewhat concessional rate.

7.69 Even with the recommended interest margins in chapter XVIII the land development banks to work as viable institutions will have to make every effort to increase their volume of business with such diversification of activities as may be feasible. The replacement of the eligibility criteria by the viability criteria followed by a programme of institutional strengthening would help the institutions to play their role more effectively and on a viable basis.

CHAPTER VIII

BRIDGING THE SYSTEMIC GAP IN CO-OPERATIVE CREDIT: THE NATIONAL CO-OPERATIVE BANK OF INDIA

The co-operative banking system in India, other than the long-term credit structure, is as we have brought out earlier, organised in three tiers in most states. While the primary level credit co-operatives are the main shareholders of the District Central Co-operative Banks, all the DCCBs in the state are the shareholders of the State Apex Co-operative Bank (SCB) which is the third and top tier of the co-operative banking system in a state. In the long-term credit structure, however, it has generally been a two tier pattern in view of the special nature of their resource mobilisation and credit functions. But in common with the short-term structure the long-term structure is also by and large federal in nature and at its basis are the Primary Land Development Banks (PLDBs) at the local level and the State Land Development Bank (SLDB) at the state level which is the top tier whose shareholders are the PLDBs.

8.02 The co-operative system also includes a number of co-operative organisations which offer specialised services. These are the functional societies such as the primary marketing societies, primary consumer societies, primary small scale industrial co-operatives and primary handloom production and marketing societies etc. These structures have also followed the same federal multi-tier pattern with the state marketing federations, state consumer federation and so on at the state level.

8.03 Co-operative systems have evolved in unison with organisation of government that constitutes the national polity and its administrative structures. In the Indian polity there is at the national level a union of states with the Central Government and an elected national parliament, and in each state a state government, again with an elected legislature. The administrative structure in states is broken down into districts and the taluka and the village below. In some states there are people's representative bodies at the district and taluka level and in all cases the panchayats at the village level, although their functional effectiveness varies from state to state. Structurally, the co-operative system in the country has also developed on these lines, but as Co-operation remained

a state subject, verticality in co-operative systems had for long stopped with state apexes.

8.04 However, as the national economy became more and more integrated, the need for co-operative systems which are basically self-managed organisations of people coming together with common economic interests, to derive the benefits from participation in the integrated national economy and the wider market it provided, began to be felt. Over the years, therefore, the specialised functional co-operatives of different states have come to organise their own national systems with the state apex organisations federating into a national apex in each case. Each of the functional co-operatives has, therefore, its national level organisation and together these sectors have become part of a national co-operative system in dealing with their respective state apexes. The National Co-operative Marketing Federation, National Consumer Co-operative Federation etc. are examples which signify this trend. The adoption of the Multi-unit Co-operative Societies Act even much earlier, to provide for national co-operative organisations is itself a recognition of this fact.

8.05 The credit structure, though the oldest among the co-operative structures in the country, has, however, yet to build a national system with an apex bank at the national level. In the absence of such an apex bank for the credit co-operatives and the consequent systemic gap at the national level, the co-operative credit structure has not been able to optimise its services to the rest of the co-operative structures. As a result, the national systems in the other sectors and the larger co-operative enterprises such as the Indian Farmers Fertiliser Co-operative, Krishak Bharati Co-operative and the like which have countrywide spread, are compelled to rely on the commercial banking systems for credit support. Their surpluses also ultimately go to swell the deposits of the commercial banking system instead of the co-operatives. The co-operative banking system thus becomes a two way loser. On the one hand, it loses out a large chunk of deposits to the commercial banks and on the other, it again loses out to the commercial banks its legitimate opportunities of investments in commercially worthwhile co-operative enterprises.

8.06 We are visualising, that the co-operative system, whether in the area of marketing, distribution or production will witness dynamic growth in the

years to come. Apart from the credit support that may be necessary for these areas, we are envisaging a more dynamic role for the co-operative credit system itself than it has witnessed ever before even in the limited sphere of investment and production credit needs in the agricultural sector. In the context of this enlarged role for the co-operative credit system, it seems to us inconceivable that for a country of India's size and complexities, there is no national level organisation for the co-operative credit system. We would consider that the co-operative banking system developing into a national system with an apex bank for the co-operative credit structure for the country as a whole would be crucial to the development of a cohesive and integrated co-operative credit system which in the long-term would itself help development of an integrated credit system in the co-operative sector and provide to the state, district and even primary level co-operatives the much needed leadership at the national level and be their effective spokesman at all policy formulation forums of bankers.

8.07 If the co-operative credit system leaves a void at the national level, the system in the long-term cannot be either strong or resilient enough and it is likely that as the co-operative business in the areas of production, distribution, marketing etc. grows, the credit system might fall by the wayside because in the absence of a national level co-operative bank not only the credit needs of the national level co-operative federations but also of the larger co-operative enterprises would continue to be met by the commercial banks instead of by the co-operative credit system. Further, the co-operative credit system will be denied a large area of the relatively more viable and profitable business including that in the field of exports, within the co-operative sector itself.

8.08 One reason why a national system has eluded the co-operative credit system has been its dependence on refinance from the RBI earlier and NABARD now. But refinance is only one part. More important are, as we have emphasised repeatedly in this report, deposit mobilisation by co-operatives at all levels and balancing of resources within the system and leadership functions of the higher tiers in the structure. These functions can be discharged in the co-operative sector by the higher tiers only if the latter are a part of the system itself and they are owned and managed by those tiers, be they the secondary tiers with reference to the primaries, the state apexes with reference to the secondary

tiers or the national apex with reference to the state apexes. No external organisation can be a substitute for this even if such agencies provide refinance.

8.09 There are as of now, as the discussion in the preceding chapters on the co-operative credit structures has shown, two apexes in each state, one for short-term and another for long-term, these together adding to 50 state apexes (31 SCBs and 19 SLDBs). In the absence of a national system, each of these 50 apexes stands on its own, or in a manner of speaking, hangs loosely whereas these need to be bound together into one national system.

8.10 The issue in other words is whether the state system should or should not join into one cohesive national system and if the answer is in the affirmative, the National Co-operative Bank will only be a natural and logical consequence. The question, therefore, is not just the creation of another bank at the national level, but one of closing a systemic gap which exists in the system and provide for a natural union of the state apexes into a national system. A visual presentation of the existing structural position and of the proposed structure is given below in Chart I and Chart II respectively.

CHART I

The Existing Structure

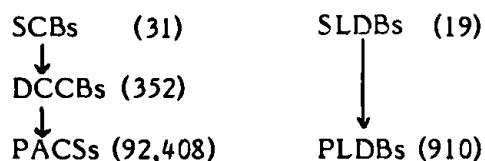
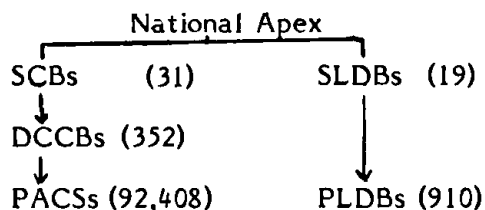


CHART II

The proposed structure



8.11 As the charts show, under the existing structure, the two types of apexes hang loosely without a head while the proposed structure with a national apex

makes for a total system from the primary level to the national level. One argument could, however, be that in the existing structure as well, there is co-ordination at the top, earlier through the Agricultural Credit Department (ACD) of RBI and now through the NABARD. But this co-ordination firstly is associated with the refinance that the NABARD provides and discharging of the responsibilities incidental to the provision of refinance. These ancillary functions are primarily designed to ensuring the safety of the refinances provided. In any event NABARD is (or earlier the ACD in RBI was) not an apex of the system itself inasmuch as they are organisations external to the system - neither owned nor managed by the co-operative banking system.

8.12 What the co-operative banking sector needs, therefore, is its own national apex which will impart systemic strength to the apexes as the DCCBs do in respect of PACSs in a district and the state apex does in respect of the DCCBs in a state. It is this principle of federalism in organisation that has characterised the multi-tier structure in co-operatives and which holds the key to the systemic strength of co-operative organisations. Implicit in this is the principle of democratic collectivism which is universally recognised as fundamental to the co-operative systems. It is again these principles of universalism in its membership for all those who share a common economic interest which they seek to promote and democratic control in the governance of these co-operatives that makes a co-operative distinct from all other types of organisational structures. Implicit in this is also the principle of federalism in the organisation of the higher tiers in the co-operatives and recognition of the universal law that in union there is strength and the inherent capacity to gather more and more strength as the sub-systems grow. The national apex bank as proposed is, therefore, intended to meet a structural or, in other words, a system need in the expectation that such an apex will, over a time, impart greater strength to the structure and that the system will thereby be able to operate in a cohesive, co-ordinated and mutually supportive and reinforcing manner. During our visits to some of the countries abroad we have seen that even in more developed economies, such as the Netherlands and West Germany in Europe and Japan and Korea in the East, a major factor which has contributed to the phenomenal growth of the co-operative credit system in these countries has been their strong national level apex banks.

8.13 We are not conceiving a national level bank for co-operatives as just yet another banking institution. Nor is it the intention that this National Apex would be adding yet another tier in the co-operative hierarchy for the purpose of routing of refinance from NABARD to the state systems. We are quite clearly of the view that refinance function would continue to be with the NABARD, or in other words, the present arrangement in this regard will remain undisturbed. As we see it, it is a systemic gap in the co-operative credit system that is sought to be filled by the national level bank, the establishment of which we recommend in this chapter.

8.14 The National Apex as we have proposed, assumes conditions of adequacy of resources and profitable operations. These aspects are dealt with separately later in this chapter. To start with, however, it could along with its responsibilities as a national balancing centre for state apexes, by acting as a receptacle of their surplus funds and as a transfer machinery for the movement of these resources on a national scale, also function as an effective spokesman of the co-operative banking system in the bankers' forums at the national level, sharing with the rest of the banking system its right to be heard and listened to. As it grows in strength, it could expand its functions to :

- a) Provide overall leadership to the system in banking operations;
- b) Prepare the credit programme for the loanable resources of the system at the national level, which could be broken down into state level and then to district and block levels under the umbrella of the sub-apexes. This does not imply that the planning is a top-down process - it has to be a combination with bottom-up planning;
- c) Issue, if necessary, bonds or debentures to generate resources;
- d) Borrow, if necessary, abroad (such as from the World Bank);
- e) Engage in operations deemed to be profitable and supportive of the operations of the system such as clearing operations; export financing, import financing, fund transfers; loaning to national non-credit co-operative federations, trust functions, operate in call and short money market, investment banking etc.;
- f) Develop policy directives for the system and perform co-ordinative and integrative authority over the system;

- g) Develop training capability programme for the system;
- h) Provide downstream assistance in terms of accounting systems, procedures etc.; and
- i) Develop institutional reinforcement programmes for the members of the system.

8.15 We would also consider that the National Co-operative Bank of India should also function as a national data clearing centre for the co-operative credit system. In pursuance to this function, it may take up the publications relating to co-operative credit system and in particular resume the two publications, one, the 'Statistical Statements relating to Co-operative Movement', annually and the other 'The Review of Co-operative Movement in India', which used to be brought out earlier by the RBI in their ACD, the first being an annual publication and the second, a biennial publication. These two publications had been recognised as two basic authoritative documents by the policy makers in the Reserve Bank, Government of India and the state governments as well as researchers. It was also considered useful reference material by the co-operatives outside India as well. It was expected that the NABARD would continue to bring out these publications. However, the position as of now is that the last Statistical Statements relating to Co-operative Movement in India published was for the year 1982-83 and that on the 'Review of Co-operative Movement' for the period 1980-82. The two federations of SCBs and SLDBs presently compile and bring out certain data regarding co-operative credit movement annually. However, both from the standpoint of resources and the greater liaison with co-operatives, the National Co-operative Bank will be better placed to obtain, compile and present the data than the two national level federations.

8.16 The question of establishing a National Co-operative Bank had come up for consideration for the first time following the recommendations to establish such a bank by the Committee on Co-operation (1965) of which Shri Ram Niwas Mirdha was the Chairman. In their view, the National Bank was to be an apex bank at the national level for the co-operative credit structure of all states. The role envisaged for this bank by the Committee, however, was primarily the routing of refinance provided by the Reserve Bank and such other finance as provided by the Central Government to the co-operatives through this national institution.

8.17 The proposal was considered at various levels and the view taken was that in the existing circumstances then, and in the absence of a clear picture about the capacity of a National Co-operative Bank to mobilise sufficient financial resources or of any firm assurance on that behalf by the Government, the time was not ripe for considering the question of organising an institution of this type. The Rural Credit Review Committee (1969) subsequently dealt with this proposal. The Committee felt that no apex co-operative bank had surplus resources to spare and the need for a balancing centre at the national level did not exist. Further, in the view of the Committee, such an institution, if it has to be a channel for routing of refinance from RBI would only add one more tier to the set-up and increase the cost of credit to the ultimate borrower. As regards co-ordination and the need for discharging the function as a spokesman of the co-operative banking system at the national level, it was thought that the All-India State Co-operative Banks' Federation could as well serve this purpose.

8.18 However, the proposal was again revived in 1978 by the All India Conference of Central Co-operative Banks convened by the National Federation of State Co-operative Banks. This conference urged the Government to establish a National Bank for Agriculture and Co-operatives. In the following year, the Eighth Indian Co-operative Congress directed the National Co-operative Union of India to take necessary steps jointly with the National Federations of State Co-operative Banks and Land Development Banks to establish a National Co-operative Bank. Against this background the question came up again for consideration by the CRAFTCARD (1981). The CRAFTCARD did not favour the idea of establishing such a National Bank, on the grounds among others, that :

- (a) With the adoption of multi-agency approach to the problems of rural credit, the refinancing, co-ordinating and development functions at the national level had to encompass all the credit institutions in the field;
- (b) The RBI's national agricultural credit funds were not meant for the exclusive use of co-operative credit institutions;
- (c) In the above context, Reserve Bank's funds would have to pass through all these systems in a balanced way, according to the exigencies of time and requirements;
- (d) If the National Co-operative Bank were to borrow from the RBI/NABARD

to lend to SCBs/SLDBs, it would be an additional tier adding to the cost of retailing agricultural and rural credit;

- (e) Only a few apex banks seemed to have real surpluses and these were also only for short periods and hence the need for a national balancing centre did not exist;
- (f) The state apex banks might not agree to a National Bank handling their money. What the apex banks really want is lending outside the state on their own.

8.19 The basic objections of both the Rural Credit Review Committee and the CRAFTICARD have been that a National Co-operative Bank would be adding one more tier making credit to the ultimate borrower more costly if Reserve Bank's national funds or refinance from NABARD were to be routed through the National Bank, and secondly the surpluses of the apex banks were not sizeable enough to warrant a national balancing centre. We have considered these as well as the other reservations of the two committees in rejecting the proposal. Firstly, the argument that the National Co-operative Bank would add another tier making credit costly to the ultimate borrower is not relevant in the context of the scheme for National Co-operative Bank as we envisage. We are not envisaging that the proposed National Co-operative Bank as a channel for routing the NABARD or Government or RBI funds at all. As we see it, the refinancing function and the routing of Government funds through the NABARD will continue to be that of NABARD as before, and these would not be routed through the National Bank. As regards the surplus funds, we do not share the view with CRAFTICARD that the position would remain the same for all times to come as it was when they considered the issue. Even as it is, considerable surpluses have emerged in the co-operative banking system. In fact the Task Force set up by the Reserve Bank of India on the Deployment of Resources for Co-operative Banks (July 1988) concurred with the NABARD's assessment that such surpluses in the system were of the order of Rs.450 crores of which Rs.200 crores were considered long-term resources as available for deployment in non-SAO advances. We have already recommended certain measures for the enlargement of deposits and other resources of the co-operative banks. With the sizeable growth, thus, in deposits on the one hand and the expansion of the co-operative credit system on the other, we believe that the co-operative banks in various states would be in a position

to generate even more surpluses than at present as estimated by the RBI Task Force.

8.20 The CRAFTICARD did not favour the setting up of a separate national bank for co-operatives also on the ground that the state co-operative banks may not agree to such a National Bank handling their surpluses. But this is clearly an untenable stand in view of the unanimous recommendation of the All India Conference of the State Co-operative Banks and the Central Co-operative Banks that there should be established a National Co-operative Bank as a National Apex Bank for the co-operative credit system. This was since endorsed by the Eighth Indian Co-operative Congress. Even as of now such of those state co-operative banks which look for investments outside the state for financing co-operative enterprises themselves have to look up to or join one or the other consortium of commercial banks. If on the other hand a National Co-operative Bank which will be a federal body of the co-operative banking system on its own can manage the investment of such surplus funds as are managed today by one or more consortia of commercial banks and more so in financing co-operative ventures themselves, the state co-operative banks could only welcome such a development. As regards the other reservations which the CRAFTICARD had, it may be said that it is precisely for the reason that with the adoption of a multi-agency approach and opening up of the Reserve Bank's national funds to other banking systems and the NABARD having to balance the competing demands of the rest of the banking systems with the co-operative banking system and hence their having to adopt a position of neutrality, that we believe there is a case today for a National Bank for the co-operative system. The bank will be a body owned and operated by the co-operative credit system as distinct from NABARD which would be an umbrella bank for all the streams of credit structures. The other reservation which the Rural Credit Review Committee and the CRAFTICARD had about the National Co-operative Bank was with reference to the duality in control and inspections, in case a National Co-operative Bank were to be established. However, in the scheme as we envisage, there is not likely to be either duality or conflict of roles; firstly the functions the CRAFTICARD envisaged for the NABARD which are spelt out in their recommendations and the role which we envisage for the National Co-operative Bank are mutually exclusive. In particular, the functions devolving on the NABARD are in the nature of a co-ordinating and refinancing body for the agricultural and rural credit

system as a whole, whether such credit is provided by the commercial banks or the co-operative banks, whereas the National Co-operative Bank of India (NCBI) which we visualise would exclusively be a bank owned and operated by the co-operative banking system for certain specified functions in respect of co-operative banks only. We do not envisage the transfer of inspection function of the NABARD over the co-operative banks to the National Co-operative Bank. In fact the NCBI will itself be subject to statutory inspection by the Reserve Bank or under its delegated authority by the NABARD. The role, as we envisage, of the National Co-operative Bank is implicit in the nature of responsibilities such a bank would have to be entrusted with and it is obvious that this in no way conflicts or overlaps with the role of the NABARD. The proposed bank, on the other hand, will be of great assistance to NABARD in its vital role of institution building in the co-operative sector. The National Bank will also provide the necessary links through the network of co-operative units in the country, thus enabling NABARD to play its role more effectively in the field in co-ordination with this bank as the spokesman of co-operative banking system at the national level.

8.21 Another apprehension sometimes found articulated is that the resources required for setting up a national co-operative bank could be substantial, and that the co-operative credit system which is already experiencing financial constraints will be put to further strain. In the role envisaged for the proposed National Bank and the resource-structure we have suggested, the bank's resources are expected to come from the resources the co-operative system is already investing outside its fold. In other words, the National Bank will only be a repository of such of the surplus funds of the co-operative system which look for investment outside of the system. As for the contribution to the share capital of the National bank, the returns on it will be both in terms of dividend and the services which the National Bank will provide to the system which would own the Bank as well as some of the intangible advantages it will have in having a national system. Another area where the proposed bank could play an important role will be the providing of nationwide remittance facilities for co-operatives. The present facilities offered by RBI/SBI schemes are often found inadequate.

8.22 We, however, observe that the Rural Credit Review Committee, did recognise the need at the national level for a body for functioning as a spokesman

of the co-operative banking system and for the purpose of co-ordination, but it believed that the All India State Co-operative Banks' Federation can serve the purpose. Experience, has, however, shown that the two national federations of the co-operative credit system, viz., the National Federation of State Co-operative Banks and the National Federation of Land Development Banks have not been able to function either as effective spokesmen of the co-operative banking system or discharge the responsibilities of co-ordination. This has been largely because neither of the two federations has any operational responsibilities to perform. For this reason, they have not been able to provide effective leadership to the state co-operative banks and the tiers below them. As a result, in the forum, where banking policies are discussed and formulated by the Reserve Bank or the Government of India, the co-operative banking system has remained totally unrepresented though many of the policies have a direct bearing on the functioning of the co-operative banks as well. As a matter of fact, representatives of both the interests, short-term and long-term structures have themselves pleaded for the establishment of a National Co-operative Bank.

8.23 Subscribing to the idea in full measure and underpinning the need for the establishment of a national system for the co-operative banking sector, as proposed, one of the members presented a paper (given at Appendix IV) which spelt out his own views on the organisational structure of the emerging national bank. As stated in the paper the success of the Bank in his view should not be left to chance; in other words its success should be a certainty. To this end it was further necessary to invest it with adequate financial strength with Government almost fully subscribing to its equity base as well as providing other financial resources. Only such an institution, he felt, would be able to 'downstream' funds to the base level structure and 'prime' the lower tiers; in other words, with a national apex there should be sizeable flow of funds from top down. The paper proposes two models to choose from. The first model envisages (a) the organisation apparently of a new national bank to meet the nominal corporate requirements and (b) the transfer to it (the corporate shell) of all the financial, material and human resources including the physical facilities as well as, the systems, procedures, functions etc. of NABARD as might be deemed necessary. This could however imply the bifurcation of NABARD's functions and resources to provide for the functions relating to co-operatives and corresponding

share of resources going to the new bank while the rest of the functions and resources remaining with NABARD. In consequence, the residuary NABARD will be an agricultural credit apex only for commercial banks including the RRBs. The second model, on the other hand, seeks a complete transformation of the existing NABARD into the national apex co-operative credit bank, through appropriate changes in the law. While the author of the paper strongly believed that either of the two models, if adopted, would result in the creation of an instant apex that can straightaway function as the fountainhead of strength and leadership to the co-operatives which in turn will help strengthen the co-operative credit system down to the primary level, the emerging consensus was that it would be inappropriate to moot a proposal involving either the division of NABARD which is what is involved if the first model is adopted or the conversion of NABARD into a national apex co-operative bank which is what is entailed in adopting the second model. However, the NABARD as envisaged is to be at the apex of the entire agricultural credit system and not merely of one or the other sector. Secondly, the systemic gap or void at the national level in the co-operative banking system for bridging which the NCBI as a national system for the co-operative banking structure owned and managed by the co-operative sub-apexes has been proposed, would still remain. Further, the CRAFTCARD in pursuance of whose recommendations the NABARD was established, envisaged that it had to be an apex agency responsible for the refinancing, co-ordination and development functions relating to the agricultural credit system as a whole at the national level encompassing all the credit institutions and not the co-operatives or the commercial banks, either wholly or mainly. It was in the light of this consideration that the long term operations fund of RBI was transferred to the NABARD with the further proviso that future accretions to the fund should also vest in NABARD. It was equally clearly envisaged that this corpus and the further accretions to it through appropriations from out of the profits of the Reserve Bank which today constitute NABARD's strong resource base was meant for providing the requisite financial strength to the apex of the rural credit systems as a whole and not for an apex co-operative credit bank only. Against this background it would not be realistic to assume that either the Government of India or the Reserve Bank would agree to the use of the capital provided to the NABARD together with long term operations fund transferred to it by the RBI might be used by an apex agency mainly of the co-operative credit structure. Neither is it the intention that there should be any dilution

of the responsibilities of the NABARD eroding even its existing clout with its commercial banking clientele.

8.24 The rationale for the proposed National Co-operative Bank of India lies in creating a democratic national system exclusively of the co-operative banking system and it should acquire its strength through the union of the state apexes and other larger co-operatives. Its role would primarily be to provide leadership in the area of banking operations to the state apexes and would largely operate as a balancing centre at the national level for co-operative banking system. In other words, it would function by and large as a consortium of the co-operative banking system besides mobilising deposits at the all India level which the state systems are not in a position to do. The NCBI's role in relation to the state apex and the levels below, will more essentially be in establishing effective liaisoning on behalf of the sub-apexes and managing of whatever surpluses the state systems are unable to utilise within their states in addition to representing the co-operative banking system at the bankers' forums etc. at the national level. Consistent with the principles of federalism and democracy which characterise the co-operative organisations at all levels and our thrust on the need to adopt a bottom-up building shorn of Government participation whether in the equity or management, what is aimed at, is the creation of a national system which will be a federation of state apexes both short and long term, owned and managed by the federating units. Consistently again with the various other recommendations made by us in the preceding chapters on the co-operative structure, this national system is also expected to be structured and organised on democratic lines and to function on its own momentum distancing itself from government patronage with the concomitant government control and interference as well as props including financial support from it. The NCBI will accordingly, not depend on the government for its capital base or other resources. It is also not envisaged that the National Co-operative Bank of India should be an agency for routing of Reserve Bank or government funds to the state apexes and through them to the various tiers of the co-operative system below.

8.25 It should be added here that the NABARD was intended also as an exercise in decentralisation of Reserve Bank's functions relating to refinancing the credit system whether co-operative or commercial banks in the sphere of rural and agricultural credit. It is for this reason that the RBI's traditional role in providing

short-term refinance for the co-operatives was transferred to the NABARD alongwith term finance for the co-operatives which was being already provided by the erstwhile ARDC, the predecessor of NABARD. Similarly, as for commercial banks, the NABARD took over the function of providing refinance in respect of term finance from the ARDC, the latter having merged in the NABARD on its formation. In fact refinance in respect of term finance extended by NABARD to commercial banks including RRBs in the year 1987-88 was of the order of Rs.951 crores as against Rs.531 crores to co-operative system. NABARD's assistance to the commercial banking system for their term finance requirements can, by all reckoning be expected to increase to much higher levels in future. Against this background, any suggestion for conversion of NABARD into the national apex co-operative credit bank, would be untenable.

8.26 In sum, the emerging conclusion is that at the national level the bank such as the one proposed, among others, to bridging the existing systemic gap in the co-operative banking system in the country, has to be a National Co-operative Bank shorn of any participation either in its equity or otherwise by the Government. We are concerned about preserving both democratic and federal character of the system and its total freedom from Government control.

Resources of the National Apex Bank

Equity Share Capital

8.27 Initially the Bank's authorised and issued share capital may be fixed at Rs.50 crores and Rs.25 crores respectively. The face value of each share may be Rs.1,000 to be paid in three instalments as under :

First)	50 per cent on allotment
Call)	
Second)	25 per cent after three years
Call)	from allotment
Third)	25 per cent after five years
Call)	from allotment

It should be a bank fully-owned by the co-operative system. Seventy five per cent of the paid up capital at any point of time should be subscribed by the state co-operative banks, state land development banks and urban co-operative banks whose operations cover either one whole state or more than one state and the balance 25 per cent by the national level co-operative organisations.

The law may provide also that in the event of a shortfall of the allocated quota to each of the constituents as may be prescribed, the same may initially be subscribed by the Reserve Bank of India or the NABARD. As and when the concerned constituent member subscribes additional share capital, the subscription by the Reserve Bank/NABARD initially made on its behalf will be retired to the extent of the additional subscription till the constituent member subscribes to his quota fully so that it is an apex owned wholly by the co-operative system.

8.28 The investment in the shares of the National Co-operative Bank of eligible co-operative banks should be treated on par with those in the shares of the higher tier institutions, such as investments of central co-operative banks in the shares of SCBs etc., for purposes of the Banking Regulation Act. Similarly in the case of other co-operative institutions eligible for membership in the National Co-operative Bank of India, their investments in the shares of NCBI should also be treated in the same manner and it should not become necessary for these institutions to separately seek permission as may be required in the normal course under any law or rules governing such investments.

Repository of unused Resources of the Co-operative System

8.29 One of the functions of the National Co-operative Bank as already stated would be to act as a balancing centre for the surplus funds of the state co-operative banks including the state land development banks which look for avenues of investment outside their respective states. It has sometimes been argued, and as was argued by CRAFTICARD also to which we have already referred earlier, that only a few state apexes have such surpluses and that even these surpluses are only seasonal. Firstly, by their very nature, surpluses with any banking system are subject to fluctuations but taking the country as a whole, certain surpluses could always be expected to be available to the National Bank from the state co-operative banks and district co-operative banks through the SCBs in larger or smaller measure at any point of time. As already alluded to, Reserve Bank's Task Force which went into this question as late as in July 1988, estimated such surpluses at Rs.450 crores then, of which Rs.200 crores are long-term resources. Even conceding that a part of the surplus is seasonal, a substantial amount is long-term.

8.30 We also propose that the state co-operative banks should deposit to

the extent of 50 per cent of the SLR with the National Bank and it should be possible to treat this investment against SLR just as it is so in the case of deposits of central co-operative banks with the state co-operative banks with suitable modifications to the Banking Regulation Act. Investments of the lower tier in the higher tier being reckoned for purposes of SLR is a principle which has been accepted even while amending the Banking Regulation Act to bring within its orbit the co-operative banking system. We have proposed the NCBI as a national level organisation for the SCBs and hence it is only logical to extend the existing facility of reckoning the investments of the lower tiers with the higher tier for SLR purposes. With this the resources of the co-operative sector will partly remain within the system. Investment of SLR other than in government/trustee securities as stipulated by the Banking Regulation Act, is permissible only in the case of co-operative banks to the extent they invest in the higher tier banking institutions. In view of this, any apprehension that SCBs investing their SLR upto 50 per cent in the NCBI as proposed will amount to weaning away of such investments from commercial banks is misplaced. Our proposal does not, therefore, affect the commercial banks in any manner. Since the total deposits of the SCBs are presently of the order of Rs.4,000 crores, this should enable the NCBI to collect deposits of atleast Rs.500 crores. A suitable amendment to Section 24 of the BR Act may be made. The National Bank will pay on such deposits a rate of interest which will not be less than the one earned by the SCBs on their investments in government securities to avoid any loss of income to them following this change. Another advantage in the SCBs investing the SLR with NCBI is that the co-operative credit system will be able to have larger resources available within itself for business. This is illustrated below. The SCBs have to invest 25 per cent of the demand and time liabilities as SLR which is about 1,000 crores now. If 50 per cent of this amount is invested in NCBI, the latter has to invest 25 per cent of this amount in government securities i.e. only an amount of Rs.125 crores and Rs.375 crores will be released for business operations within the system.

8.31 But it could be argued that diversion of investment of SLR of SCBs from government securities to NCBI will affect the borrowing programme of the government. The position, however, is that as against the SLR requirements of SCBs at Rs.1,000 crores, it is proposed to invest only Rs.500 crores in NCBI. Since NCBI will invest Rs.125 crores in Government etc. securities to comply with

its SLR, the impact on Government borrowing programme will be only Rs.375 crores. This amount is very small as compared to the total market and other borrowings of the Central and state governments, which amounted to Rs.1,20,000 crores as on 31st March 1988 and may have increased further to Rs.1,40,000 crores by now. Hence, the diversion of 50 per cent of the SLR of SCBs forming about 0.30 per cent only will not have any perceptible impact on government borrowing programme. We would also like to mention that till recently NABARD was investing its surplus resources entirely in government securities and an amount of Rs.1,190.67 crores was invested in government securities as on 30th June 1988. Reserve Bank had extended the facility to purchase these securities at par whenever NABARD wanted to sell their securities for the purpose of providing refinance. The Reserve Bank has, however, recently permitted NABARD to invest these amounts in bill market scheme and NABARD has already invested in such instruments Rs.385.34 crores as on 31st March 1989.

8.32 Under the Co-operative Societies Acts and Rules in various states, a co-operative bank is required to invest, its Reserve Fund, Building Fund not invested in premises and Bad and Doubtful Debts Reserve outside its own business, in the manner specified in the Act. It is proposed that such reserves and funds of SCBs and other national level co-operative institutions be invested atleast partly with the National Co-operative Bank. We have however no precise data regarding the exact amount of these funds but all the reserves and other funds of the SCBs as at the end of June 1988 were around Rs.500 crores. It is proposed that 50 per cent of this amount be kept in term deposits with the NCBI to cover the funds to be invested outside the business. On a rough estimate, this should bring in deposits of Rs.250 crores to the NCBI from SCBs only. Under the statutory provisions a co-operative organisation can invest the reserves in the higher financing institution or in government/trustee securities. Apart from complying with the statutory provisions of the Act the proposal as recommended would ensure that available funds in the co-operative sector are mobilised for the purpose of financing co-operative institutions and the investing institution would get a return which is equivalent to what they are otherwise receiving on their investments in government securities etc.

8.33 The SCBs, SLDBs, urban banks and other national and state level co-operative institutions which are at present keeping their surplus resources with

the commercial banks will maintain these with the proposed NCBI. These surplus resources in the case of SCBs will exclude the funds being invested in the consortium arrangements with commercial banks. Assuming such permanent or semi-permanent surpluses at Rs.250 crores, the proposed bank will have deposits of over Rs.1,000 crores.

8.34 We expect the National Co-operative Bank to be able to mobilise deposits from the national level co-operative organisations and other public corporations and other bodies as listed by the Task Force, besides the several non-equity based co-operative federations at the national level established for discharging promotional and consultancy functions. There are, as of now eight such federations.

8.35 There are then the co-operative enterprises, such as the larger fertilizer co-operatives producing and distributing fertilizers and the national level marketing organisations like the NAFED and National Co-operative Consumers' Federation (NCCF) engaged in export and import business, all of which need suitable banking facilities which today are extended by the nationalised commercial banks. These national level institutions have also their surpluses and they require credit support as well. It is our hope that the new National Co-operative Bank which we envisage will not only be a balancing centre for the state co-operative banks enabling them to invest their surpluses in the co-operative system in other states where there are no surpluses, but also emerge as the principal banker to the national level co-operative organisations and the larger co-operative enterprises.

The Proposed Structure

8.36 The Bank will be named as we have already mentioned, the National Co-operative Bank of India (NCBI) and will function as the national apex institution for all co-operatives. Its main functions will be :

- (i) to act as a balancing centre for state level co-operative institutions;
- (ii) to accept deposits of all types from members and non-members except individuals;
- (iii) to make loans and advances;
- (iv) to act as an apex co-operative bank at the national level and provide

leadership in all matters of co-operative interests, including developmental and promotional activities;

- (v) to evolve and administer an efficient national system of training exclusively for the co-operative banking personnel.

The Bank to be incorporated under an Act of Parliament

8.37 Since the National Co-operative Bank, as we propose, would be a bank and will be functioning as such, it may be established under a special law to be enacted by the Parliament. This is desirable since banking is a Central subject. We do not believe that this will in any way conflict with the position that Co-operation is a state subject under the Constitution, since it is already permissible to register such a bank under the Multi-Unit Co-operative Societies Act and be licensed under the Banking Regulation Act to carry out banking functions. We have, however, thought it appropriate to have a special legislation for the purpose since what we envisage is not just a co-operative society at the national level but an apex bank to serve the co-operative banking system at the national level. As we have discussed earlier, it will have clientele, albeit, limited, outside the co-operative banking system also.

Management of the Bank

8.38 We now come to the question of the management of the Bank. The National Bank should have an elected board. As in the case of subscription to the share capital, the representation for each of the groups of constituent units may also be determined and prescribed in the Act. As we see it, the bank will then have a Board of Directors elected from three electoral colleges. The first will consist of SCBs and SLDBs who will jointly elect 18 directors, the eligible urban banks will jointly elect two directors and five Directors will be elected by the electoral colleges consisting of other co-operative institutions jointly. It may be provided that the bank can co-opt two more directors - one of them being an eminent professional banker and the other an expert in management. The Board will elect a Chairman either from its members or invite any outside person of eminence in the field of banking, economics or management. In the event the Chairman is not from among the members of the Board, on his election the Chairman will become an ex-officio director. A Managing Director who will be a professional banker, to be appointed by the Board, will be the Chief Executive Officer of the Bank. With a view to ensuring the professional

competence of the incumbent for the post of Managing Director, it may be provided that the appointment be made with the approval of RBI. The bank will appoint other staff necessary for running its business efficiently. We are envisaging the proposed bank to be manned by highly professionalised bankers.

8.39 As already referred to, the National Bank will have the same status as that of any scheduled bank and it would be eligible to such concessions and facilities only as are available to a scheduled co-operative bank in terms of provisions of RBI Act/B.R. Act.

Business Potential of the Bank

The Bank to do all Banking Business

8.40 The Bank being a scheduled bank established under an Act of Parliament would be eligible for all facilities in respect of borrowings, remittances, etc. from the Reserve Bank which are available to co-operative scheduled banks. Apart from the share capital, the bank will accept deposits of all types, from the co-operatives as well as other institutions in private and public sector. It shall not, however, accept deposits from individuals. We do not envisage that the National Bank may be barred from dealing with non-co-operative organisations, though its primary responsibility will be that of functioning as a National Bank for co-operatives. So as to be able to provide adequate support to its constituents including support for exports to the national and state level marketing organisations, the National Bank, should also be enabled to deal in foreign exchange.

8.41 We also envisage that the bank will conduct the various other types of banking business including deposit banking, bills business, opening letters of credit, issuing bank guarantees and operations on inter-bank call money market, apart from lending to clientele institutions for purposes such as working capital requirements, block capital requirements etc.

Foreign Exchange Business

8.42 The bank will also be authorised to deal in foreign exchange. It is necessary that the proposed NCBI be given a licence to deal in foreign exchange. There are several institutions in co-operative field presently engaged in either exports or imports of goods, products and inputs, for example Maharashtra Co-operative Marketing Federation exports cotton under the State Government's

Scheme of monopoly procurement of cotton and Amul exports milk products. The Bank should also be authorised not only to deal with the co-operative sector but also private and public sector business.

8.43 Among the various types of foreign exchange business which an authorised dealer deals with, the NCBI may initially take up the trade related transactions. Presently India's total international trade transactions consisting of exports and imports are of the order of Rs.40,000 crores and are further expected to grow to a much larger level during the next decade. It would not be unreasonable to expect that the NCBI will have a small share of this total pool. In other words, the Bank may be able to handle trade related transactions of foreign exchange of the value of Rs.500 crores and raise it in due course to a level of Rs.1,000 crores. Of course, it will take some time for the Bank to build up the necessary infrastructure facilities and appoint trained personnel for this business on par with other banks in the field. We envisage that there is enough potential for the bank in this area and the earnings of this foreign exchange business may be of the order of Rs.5 crores to Rs.10 crores annually within a reasonable period of time.

Deployment of Resources and Viability

8.44 The bank will be required to maintain 3 per cent of its outside liabilities as Cash Reserve in terms of Section 42 of the RBI Act. In terms of Section 24 of the Banking Regulation Act, it will have to maintain 25 per cent of its liabilities in eligible assets indicated under the Section (these assets include government and trustee securities and balances with Reserve Bank of India and other notified banks). Thus about 30 per cent of deposits will be immobilised. The balance of resources, viz., 70 per cent of the deposits i.e., about Rs.700 crores will, however, be available for lending. Its lending will be primarily to SCBs, SLDBs and institutions such as IFFCO, KRIBHCO, NAFED, NCCF, National Tribal Development Corporation, CAMPCO as well as any other state level co-operative banks or institutions where necessary. The credit limits sanctioned to four of these institutions, viz, IFFCO, KRIBHCO, NAFED and NCCF during the last three years and the balances held in current account with the banks are given in the following table :

Table
Working Capital Limits Sanctioned to
National Level Co-operative Institutions

	<u>1986-87</u>	<u>1987-88</u>	<u>1988-89</u>
(Rs. crores)			
<u>Through Commercial banks</u>			
IFFCO	131.66	131.66	163.80
KRIBHCO	78.00	79.00	75.05
NAFED	9.00	15.00	26.00
NCCF	35.90	11.70	19.30
	<u>254.56</u>	<u>237.36</u>	<u>284.15</u>
<u>Through Co-operative banks</u>			
IFFCO	75.34	75.34	109.20
KRIBHCO	29.00	33.00	31.45
NAFED	6.00	6.00	9.00
NCCF	2.00	2.00	2.50
	<u>112.34</u>	<u>116.34</u>	<u>152.15</u>
<u>Balances in current account with banks</u>			
IFFCO	13.44	61.30	19.09
KRIBHCO	2.06	13.03	15.28
NAFED	3.38	0.96	2.66
NCCF	0.09	0.10	N.A.
	<u>18.97</u>	<u>75.39</u>	<u>37.03</u>

There is, therefore, enough potential for this Bank to build up its business over the years to a much higher level, considering that NCBI will be financing not only these four institutions but many others at the national level. Though the Bank will finance the co-operatives by way of a priority charge on its resources, there will be no bar to finance other institutions, companies etc. if necessary. It could finance non-members also.

8.45 As for the prospects of viability, we feel that since most of the deposits

collected by the NCBI will be term deposits, the financial cost of raising these deposits including the call/short term deposits will be around 10.5 to 11 per cent. As against this, 30 per cent invested in CRR and SLR requirements i.e. Rs.300 crores may fetch in about the same return. In other words, there will be no margin on 30 per cent of the banks resources. On the remaining 70 per cent resources i.e. Rs.700 crores which do not include the resources of SCBs/ DCCBs to be routed through the NCBI instead of through the commercial banks' consortium, should be able to keep a margin of 2 to 2.5 per cent at least since the loans will be granted for purposes such as working capital requirements and block capital requirements for which the lending rate will be 13.5 to 14 per cent at least. This margin should enable the bank to earn an annual net income of Rs.14 crores to Rs.17.50 crores. Besides these, the bank will also earn income from its other operations such as foreign exchange transactions etc. which cannot be estimated at this stage. Presuming the total net surplus income is of the order of Rs.20 crores, it should not be difficult for the bank to meet its establishment and other operating expenses and leave sufficient balance to pay a reasonable dividend on its share capital. It needs to be noted in this connection that looking to the nature of work and the business it will handle, the bank could do with a relatively smaller complement of staff as compared to a bank of the same size.

Creation of a Co-operative Development Fund

8.46 We would also recommend that apart from creating the normal reserves, the NCBI should establish a Development Fund by appropriations from profits. Co-operative federations, the larger co-operative enterprises, and the state apexes both in the short and long-term structure should also contribute to this fund. This fund may be utilised for assisting the SCBs and SLDBs to train the secretaries/managers of primaries and taking up research projects of relevance to the development of co-operative banking system.

Conclusion

8.47 We have made a number of recommendations in the earlier chapters on the need for both functional integration in the organisational structure of the co-operative banking system and better organisational ties as among the different tiers so that each tier functions as a part of a total system. We have in this

context also emphasised the role of every higher tier in the structure and its responsibility with reference to the one below it in the latter's development. Such ties have to be more than mere ownership of the higher tier by the lower tier or provision of refinance by the higher tier to the lower. The more these ties are developed and they permeate the entire system up to the national level, the more effective the system itself would be. It is in this context as well that a national apex bank is necessary so that those kind of functional inter-relationship and organisational ties run through the entire system from the primary to the national level.

8.48 A national system with the proposed National Co-operative Bank at the top and its horizontal relationship with the other national apexes of the functional co-operatives, as a receptacle of their surplus funds and provider of credit support to them, in our view, would help build the required degree of mutualism and federalism which are the essence of any co-operative system. The National Co-operative Bank would also be in a position to more effectively orchestrate the vertical and horizontal relationships among the different tiers in each segment and as between the different segments in the co-operative banking system as a whole in the country.

8.49 It is also our belief that with the establishment of the proposed National Bank, the co-operative credit system will attain new heights and grow in stature.

CHAPTER IX

NATIONAL BANK FOR AGRICULTURE AND RURAL DEVELOPMENT - ROLE, ORGANISATION & MANAGEMENT

Setting up of NABARD

Established under the National Bank for Agriculture and Rural Development Act (1981), the National Bank for Agriculture and Rural Development (NABARD) commenced functioning from 12th July 1982. This followed the recommendations contained in the Interim Report submitted in November 1979 by the Committee to Review the Arrangements for Institutional Credit for Agriculture and Rural Development (CRAFICARD) which had been set up by Reserve Bank of India in March 1979 under the Chairmanship of Shri B. Sivaraman, former member of Planning Commission.

9.002 The terms of reference required the Committee to review in the first instance, the structure and operations of the Agricultural Refinance and Development Corporation (ARDC) in the light of the growing need for term loans for agriculture and allied purposes relevant to Integrated Rural Development (IRD). On a review of the working of ARDC and other national level institutions concerned with the disbursement of credit for rural development programmes, then existing, the CRAFTICARD came to the conclusion that a new arrangement was called for at the national level for achieving the desired focus and thrust towards integration of credit activities in the context of the strategy for Integrated Rural Development. Against the background of the massive credit needs of rural development over the next decade and the need to uplift the weaker sections in the rural areas within a given time horizon the arrangement called for, in the view of the CRAFTICARD, a separate institutional set-up. The ARDC had according to the CRAFTICARD more or less failed to ensure that the ultimate borrowers secured the necessary supporting short-term credit for carrying out the production activity on the level envisaged. ARDC's assistance to the non-land based activities had not reached any significant level as compared to the need for promotion of such activities in the context of IRD nor did the statute empower the ARDC to support activities which were not connected with agriculture. Further, the development role assigned to the ARDC was inadequate to take due care of institution building, training and research. The RBI, on the other hand,

had onerous responsibilities to discharge in respect of its many basic functions of central banking in monetary and credit regulations and was not therefore in a position to devote undivided attention to the operational details of the emerging complex credit problems of IRD. In the past, whenever any of the special responsibilities the RBI undertook acquired dimensions of a magnitude warranting special attention, the answer was to hive off that function and entrust it to a separate institution with suitable links with the RBI for attending to the separated function. Institutions like UTI, IDBI and even ARDC had come out of RBI in this way. The question before the CRAFTICARD, therefore, was whether it was the opportune time to create an institution exclusively devoted to the diverse aspects of rural credit. This was particularly important since the All India Rural Credit Review Committee (1969), had rejected the proposal to take away agricultural credit function from RBI and instead, recommended the establishment, within the RBI, of a statutory Agricultural Credit Board to be entrusted with the task of formulation, review and modification of the Bank's policy in the sphere of rural credit. The Agricultural Credit Board (ACB) was no doubt constituted in 1970 but sans statutory status. With the adoption of the multi-agency approach to rural credit delivery, the introduction of Lead Bank Scheme and the emergence of RRBs, rural credit functions looked after by RBI's Agricultural Credit Department acquired new dimensions and CRAFTICARD felt that the time had come for the decentralisation of the functions of the RBI in the sphere of rural credit. The Committee's recommendation for the creation of a national level institution through the merger of the ARDC and the Agricultural Credit Department and Rural Planning and Credit Cell of RBI so as to give undivided attention and forceful direction to IRD flowed from the above conclusion. The Committee, however, felt that it would be necessary for the new institution to maintain organic links with the RBI so that its continued guidance and financial assistance was available to it.

9.003 RBI, thus, continued to be vested with the responsibility for the overall national rural credit policy and for issuing directives on rural credit. NABARD accordingly operates within this policy framework. Apart from providing refinance assistance to NABARD, RBI transferred to it the NAC (LTO) and (Stabilization) funds aggregating Rs.1390 crores and also entrusted to it the task of statutory inspections of co-operative banks and RRBs. RBI also agreed to contribute in the initial years certain amounts to these funds from its

profits annually to enable NABARD to augment its resources free of cost. It is with such strong support from RBI that NABARD commenced its operations. In a way, the issues discussed and the recommendations made by CRAFTICARD for an integrated approach to rural development were not new ones. These issues have indeed been the central focus of several earlier committees. Persistence of these issues only underline how intractable the problems of bringing about a truly integrated rural development are. Has NABARD during the last six or seven years, with its present mandate, organisational structure, powers and financial resources contributed more effectively towards the solution of these problems in the rural financial sector in India? If not, what were the causes for its failure? The rest of this chapter examines these issues and offers suggestions so that NABARD can emerge during the next 10-12 years, as a strong development bank for India's growing agricultural and rural sector.

Role and Organisational Structure of NABARD

9.004 The NABARD was envisaged as the centre piece of the rural credit system, as also the provider of supplemental funding to rural credit institutions such as Commercial Banks, Co-operatives and RRBs. The preamble to the Act which established NABARD in 1982 states its role thus -

" providing credit for the promotion of agriculture, small scale industries, cottage and village industries, handicrafts and other rural crafts and other allied economic activities in rural areas with a view to promoting integrated rural development and securing prosperity of rural areas, and for matters connected therewith or incidental thereto. "

9.005 The Act accordingly gave the NABARD a very broad and flexible mandate with following functions.

- i) Refinance (ST, MT & LT) to the co-operatives and RRBs, including for co-operative marketing and distribution;
- ii) Refinance to commercial banks against term lending for agriculture and rural development;
- iii) Direct lending singly or through consortium arrangements in special cases;
- iv) Developmental policy, planning and operational matters relating to

credit for agriculture, allied activities, rural artisans and industries and other rural development;

- v) Training, research and consultancy relating to credit for agriculture and rural development;
- vi) Co-ordination and monitoring of all agricultural and rural lending activities with a view to tying them up with extension and planned development activities in the rural sector;
- vii) To be available for advice and guidance to State Governments, Federations of Co-operatives etc. in regard to the co-operative movement in close collaboration with the RBI and Central Government.

9.006 In brief, the NABARD's role comprised three main functions :

- (a) To provide refinance to lending institutions in rural areas.
- (b) To bring about or promote institutional development.
- (c) Evaluation, monitoring and inspections of client banks.

9.007 The NABARD's performance in each of these three functions and other allied areas is reviewed in the later part of this Chapter in greater detail. While passing any judgement on its success or failure in any area, it has first to be noted that, the NABARD, in the seven years of its life has extended substantial refinance to client banks, taken steps to diversify its activities increasingly into non-farm sector and lent support to IRDP and other special production programmes. It, however, appears to us that as time passed, the refinance function attracted more and more attention and resources. Though it is not anybody's case that the other two functions were altogether neglected, these by and large received a lower priority and resources. It needs no emphasis to say that the objective of providing refinance and its effectiveness at the ground level can be well served only if the credit agencies through which the finance flows are healthy, strong and viable. The developmental role is no less important, than the refinance role itself. It is, therefore, necessary for NABARD to take more vigorous, innovative and forward looking initiatives and inspire similar attitudes in its client institutions, other apex bodies, state governments and down to the block and village levels. If NABARD has to fulfil its leadership role, it has necessarily to expand its activities much beyond the refinancing of loans

for agricultural projects. NABARD should become the primary source of inspiration of conceptual guidance, of information and research in all matters relating to credit for rural development and should be so perceived by its client institutions and other organisations. We have in this context made specific recommendations and expect that NABARD will be able to play its due role in this area.

9.008 In particular, we would like to emphasise two aspects of the NABARD's role in future.

(a) One of the weak areas in NABARD's role, in our view, pertains to the promotion of viable co-operatives. Apart from providing substantial refinance support to the co-operative sector, NABARD has not made much dent in revamping the system as such. We are aware of the intricate nature of the problems in the strengthening of the co-operatives and have made several recommendations in this regard in other Chapters. We could, however, see the need for strong directing hand from NABARD with necessary support from RBI and a thrust on proactive promotional role to revitalise the co-operative system.

(d) As we have mentioned earlier, the relative share of agricultural sector in the economy in the coming years would decline progressively. As the non-farm business and agro processing activities are likely to be the more dynamic sectors in the rural areas in the coming years, we feel that NABARD should give much greater attention to these activities than what it has done so far. It is in this sector that NABARD should evolve more and more innovative projects. In fact one of the failures of the erstwhile arrangements for rural credit had been their insufficient attention to this emerging sector which was supposed to be corrected by NABARD. Thus although we do not envisage any change in the NABARD's statute, we feel that there is a pressing need for a new thrust to promote and fund truly integrated rural development schemes through a major redirection of its current operations which are mainly concentrated on refinancing of standard schemes submitted to it by the client banks to avail of NABARD's concessional finance to boost their operations with a view to fulfilling the targets of rural lending and the various sub-sectors thereunder.

Organisation

9.009 NABARD was formed as already referred to through a merger of ARDC and ACD and RPCC in RBI in 1982. Since then the organisational structure of NABARD has undergone considerable change. These changes have however been haphazard and did not reckon the need to group activities logically and to provide for effective co-ordination of related activities within the structure. The current organisational structure of NABARD is given in Chart I. Although the system as presently operating has its positive aspects, its major drawback is its excessive fragmentation of key activities within 15 Head Office departments. In other words, NABARD functions are an amalgam of activities inherited from its parent organisations rather than those of a unified new apex institution. Further, despite the on-going plans to relocate operations to state level, Regional Office responsibilities have still not been sufficiently broadened to enable NABARD to tailor its programmes effectively to meet the local needs in different regions and of client banks and their borrowers, and develop as a lead contributor to policy formulation and planning for agriculture and rural development at the state level. These and other deficiencies in the organisational structure have been examined by the Consultants V in detail. The recommendation of the Consultants and our own proposals are dealt with later.

Review of NABARD's Operations - Refinance

9.010 In the next three sections we propose to review the performance of NABARD during the past six years or so. For greater clarity, performance of NABARD has been classified under three broad functional heads i.e. refinance, institutional development and inspections. NABARD provides assistance by way of refinance or otherwise, at concessional rates of interests, to client banks, viz., CBs, SLDBs, SCBs and RRBs. While refinance for term investment credit is available to all the client banks, short-term credit for production and marketing and medium-term credit for investment and for conversion of short-term loans are confined to SCBs and RRBs. The aggregate disbursements of all types of loans made during the last six years are given in table 1. The disbursements referred to in Col. 3 of table 1 include long-term loans to state governments granted by NABARD for contribution to the share capital of co-operative credit institutons which ranged from Rs.95 crores to Rs.169 crores; the cumulative total for the 6 year period ended 1987-88 being Rs.718 crores.

Table 1

Total Volume of Refinance Disbursed 1982-83 to 1987-88

(Rs. crores)				
Year (July-June)	Total Disbursements (ST/MT/LT)	ST/MT Disbursements	Long-Term Disbursements	
			Amount	No. of Schemes Sanctioned*
1	2	3	4	5
1982-83	3,911	3,208	703	4,957
1983-84	3,882	2,990	892	4,961
1984-85	3,410	2,349	1,061	5,601
1985-86	3,788	2,596	1,192	7,964
1986-87	4,282	2,948	1,334	10,099
1987-88	5,402	3,920	1,482	9,995

Source : NABARD Annual Reports

* Excludes IRDP

9.011 NABARD's refinance functions can conveniently be divided for purposes of analysis, into two broad categories- long-term investment finance and short-term production and marketing finance. Since its inception, the long-term (investment) credit disbursed through client banks has recorded a steadily rising trend as may be seen from table 2.

Table 2

Long-Term Refinance Disbursements

(Rs. crores)					
Year (July-June)	SCBs	RRBs	SLDBs	CBs	Total
1982-83	45	61	235	362	703
1983-84	41	87	314	450	892
1984-85	37	140	314	570	1061
1985-86	36	158	337	661	1192
1986-87	65	208	433	628	1334
1987-88	64	216	467	735	1482

Agency-wise, the Commercial Banks and the SLDBs are the major institutions dispensing investment credit. The share of the former has been progressively

increasing as compared with the SLDBs which are bogged down with the problem of overdues and shrinking eligibility for refinance. Commercial banks accounted for half the refinance in 1987-88 while SLDBs, a little less than one third. The SCBs are essentially short-term lending institutions while the RRBs' lendings are confined to a given target group. Consequently, the share of these two agencies in NABARD's schematic refinance remains small, if not insignificant.

9.012 Since its inception, NABARD's strategy has been to provide refinance support for activities aimed at improving the productive capacity of the economy taking into account the natural resources of different regions and the available technological opportunities. Obviously, its initial attention, had been focussed on the upgradation of the productivity of the nation's most important but scarce resource, viz., land. The country is fast reaching the limits of the expansion of net area under cultivation. Emphasis, therefore, was placed on increasing agricultural output mainly through the use of investments for minor irrigation, largely ground water, shaping land for using water, mechanisation of farming operations and the diversification of land use to horticulture and other tree crops. The availability of ground water almost throughout the country and the introduction of high yielding seed technology and other modern farming methods had enlarged the scope for such investments. The purpose-wise break up of NABARD's refinance (indicating major purposes) disbursed during the last 6 years is given in table 3. As can be seen from table 3, over 50 per cent of the NABARD's refinance support has gone for land-based investments.

9.013 In consonance with the policy followed by the erstwhile ARDC, the NABARD has accorded the highest priority to minor irrigation projects since its inception by creating additional potential on the one hand and better management of available resources on the other. The strategy has been to promote financing of irrigation over large areas based on evaluation of ground water potential. Drip/sprinkler irrigation, efficient pumping and distribution systems have been encouraged with a view to ensuring better water management. Similarly, in the context of inadequate power in many states, the NABARD jointly with REC provides refinance assistance to SEBs which is specially intended to strengthen the electricity distribution network in rural areas for energisation of pumpsets.

Table 3

Long-Term Refinance - Purposewise Disbursement by NABARD

(Rs. crores)

Year (July-June)	M.I.	L.D.	IRDP	F.M.	AH/ Fisheries	Plantation Horticulture & Forestry	Others	Total
1982-83	244 (35)	21 (3)	185 (26)	147 (21)	-	31 (4)	75 (11)	703 (100)
1983-84	312 (35)	29 (3)	233 (26)	204 (23)	-	43 (5)	71 (8)	892 (100)
1984-85	335 (32)	43 (4)	354 (33)	170 (16)	-	49 (4)	110 (11)	1061 (100)
1985-86	385 (32)	27 (2)	376 (32)	200 (17)	13 (2)	73 (6)	118 (10)	1192 (100)
1986-87	460 (35)	26 (2)	379 (28)	192 (14)	18 (2)	77 (6)	182 (13)	1334 (100)
1987-88	473 (32)	25 (2)	448 (30)	200 (13)	20 (1)	94 (6)	222 (14)	1482 (100)

MI : Minor Irrigation
 FM : Farm Mechanisation
 LD : Land Development
 AH : Animal Husbandary including poultry, dairy, etc.

(Figures in bracket represent percentage to total)
 Source : NABARD Annual Reports

9.014 NABARD has also evolved a strategy for financing rainfed areas, on a pilot basis, in compact watersheds with a credit package in the form of 'cyclical credit' to suit the fluctuating productivity of such lands and thereby introducing a measure of stability. A typical cycle may cover a period of 5 to 7 years. While production credit is assured for seasonal operations during the entire cycle period, higher repayments will be required to be made in good years and lower or no repayments in bad years. If experience shows that the dues cannot be cleared fully, some compensatory arrangements will have to be made. If credit is to achieve a breakthrough in rainfed areas adopting the latest technology, it seems inescapable for the banks to modify their lending policies on these lines.

9.015 An important sector which is engaging NABARD's attention and

resources increasingly, is the non-farm sector. In view of its high income and employment generating potential, the NABARD has taken a series of steps to promote larger credit flow to this sector. The NABARD provides cent per cent refinance to client banks and has also exempted client banks from the eligibility criteria for the purpose of refinance. The NABARD's schemes include composite loans to rural artisans and small entrepreneurs, integrated loans to small and tiny units in the modern sector, grants to voluntary and other promotional agencies in setting up training-cum-production centres for upgrading the skills of and adoption of appropriate technology by potential small entrepreneurs, seeking self-employment with the help of institutional credit and refinance for infrastructural development, apart from those covering agro-based industrial and processing activities. Although these schemes are, as yet, to pick up in any big way, a beginning could be said to have been made in these areas.

9.016 NABARD's new thrust areas include besides rainfed farming and non-farm sector, social forestry and wasteland and development also. NABARD is extending refinance support and technical guidance for the afforestation programmes comprising farm forestry, commercial nurseries for seedlings, suitable for wasteland development, raising of trees on community lands under the 'tree-patta' schemes and captive plantation by user industries. Detailed guidelines have been issued by NABARD to facilitate formulation of farm forestry and wasteland development projects. The disbursements under these projects have been small so far though they increased from Rs.3.57 crores in 1982-83 to Rs.19 crores in 1987-88.

9.017 The NABARD has endeavoured to earmark a sizeable proportion of refinance for the benefit of weaker sections like small and marginal farmers, agricultural labourers and other rural poor. At least 60 per cent of the credit in land-based investments like minor irrigation and plantation/horticulture is earmarked for small farmers. This is in addition to the massive support to the poverty-alleviation programme of IRDP which has taken up about 30 per cent of the NABARD's refinance. This is next only to minor irrigation.

9.018 Region-wise, on an average, about 2 per cent of NABARD's refinance has gone to States in the North-Eastern Region, 15 per cent each to Eastern Region and Western Region, 19 per cent to Northern Region, 21 per cent

to Central Region and 28 per cent to States in the Southern Region. The NABARD has tried to support special schemes in States with low credit absorption capacity, such as the Special Foodgrains Production Programme (SFPP) in the Eastern States and by relaxing the credit eligibility norms for banks in the North-Eastern States. The recommendations of the Sen Committee¹ on Eastern States set up by the RBI are under implementation since July 1986.

9.019 The NABARD's refinance for short-term production and marketing is confined to the SCBs and RRBs for which purpose these banks are sanctioned annual credit limits from out of the General Line of credit of RBI. The most important type of refinance is for seasonal agricultural operations or what is popularly known as crop loans issued by the co-operative credit system. Over the years, the co-operative banks have been meeting a good proportion of the crop loan needs from out of their own resources and the RBI/NABARD supplemented their efforts with a line of credit in areas where the need was high. During the last two/three years, however, NABARD has had to meet an increasing share of crop loans disbursed at the base level by PACSs (table 4).

Table 4

Crop Loans disbursed by Co-operatives and NABARD's support

(Rs. crores)			
Year (July-June)	Crop loans disbursed	NABARD's support	Percentage of NABARD's refinance (col. 3 to 2)
1	2	3	4
1982-83	1908	858	45
1983-84	2158	803	37
1984-85	2323	868	37
1985-86	2747	873	32
1986-87	2620	936	36
1987-88	2900*	1307	45

* Estimated

The increase in crop loan refinance has mainly been on account of the large requirements of credit which the co-operative system has been called upon

1 Committee on Productivity of Agriculture in Eastern States.

to provide for certain special programmes such as the National Oilseeds Development Programme (NODP), SFPP, etc. launched by GOI and NABARD during the last two years viz. 1986-87 and 1987-88. The steep rise in crop loans disbursed as well as refinance provided in 1987-88 is on account of massive support extended to co-operatives by NABARD and RBI in the wake of unprecedented natural calamity that occurred in that year and also for launching of the programmes as mentioned below aimed at stepping up of foodgrains production. Although NABARD's support forms about 45 per cent of the 'crop loans disbursed in the aggregate at the field level, it should be noted that as compared to the outstandings at this level, NABARD's refinance is not more than 25 per cent, since the overdues forming part of the outstandings are absorbed by the co-operative credit system itself.

9.020 In the context of National Oilseeds Development Programme (NODP), Special Foodgrains Production Programme (SFPP), and other special schemes such as SRPP launched by GOI, NABARD sanctioned special/additional credit limits to the banks on a liberal basis to implement these programmes. Thus, separate limits were sanctioned to CCBs in the NODP districts from the year 1986-87 irrespective of their levels of overdues (CCBs with overdues above 60 per cent of the demand are not normally eligible for NABARD's credit limit). This facility has been extended to the OTP districts (246) as well. Credit limits for NODP had increased from Rs.41 crores in 1986-87 to Rs.192 crores in 1987-88 for 113 CCBs; Rs.11 crores were also sanctioned to 26 RRBs in the programme areas. In regard to SFPP under implementation in 169 districts, enhanced credit limits were sanctioned to the CCBs taking into account the additional requirements for inputs, etc. under the programme. The NABARD also provided for the first time, interim accommodation for such of these CCBs which were unable to avail of the limits for want of Non-Overdue Cover (NODC). Small farmer defaulters upto 20 per cent of their crop loan eligibility, were allowed to be financed in the SFPP areas. The limits sanctioned during 1988-89 for 151 CCBs and 64 RRBs in SFPP districts aggregated Rs.1,322 crores as against Rs.1004 crores in the previous year.

9.021 For enabling the PACSs to meet credit needs for the new and non-defaulting members even in cases where the CCBs were not eligible for limits from NABARD, it was decided in 1982-83 to sanction to the SCBs on behalf of eligible CCBs, additional limits, so that the SCBs could cater to the needs of

ineligible banks. Experience has, however, shown that this facility had not been able to ensure fresh finance to the members of PACSs who have repaid their previous dues. In some cases non-defaulting members of PACSs in the areas of even eligible CCBs were thus not being issued fresh loans. The NABARD has since introduced a scheme in consultation with RBI, wherein the CCBs have been enabled to take care of the needs of non-defaulting members fully. Under this scheme, effective from Rabi 1987-88, CCBs which are not able to draw refinance from NABARD for want of sufficient non-overdue cover (NODC) are eligible to draw refinance solely for the purpose of issuing fresh finance to the members of PACSs who have repaid their previous dues. The banks however, have to make good the deficits in NODC within a period of 3 months. The CCBs can draw upon the limits upto the amount of crop loans recovered by the PACSs from their members or the amount of fresh advances proposed to be made to the members who have repaid their dues. This is a major step forward taken by NABARD in enabling co-operative banks to hold out an assurance that those who are regular in repayment will not be denied fresh credit for carrying on their seasonal agricultural operations. This is also likely to go a long way in creating a favourable climate for repayment.

9.022 Provision of conversion facilities to the borrowers of crop loans affected by natural calamities from out of the N.R.C. (Stabilisation) Fund transferred to it by RBI is another important refinance function of NABARD. The National Fund which stood at Rs.365 crores in June 82, was augmented to Rs.703 crores by June 88 by contributions from RBI and NABARD out of their respective profits. The assistance from the fund which was Rs.91 crores in 1982-83 increased to Rs.287 crores in 1987-88.

9.023 Following the reduction in the ultimate lending rates on crop loans effective 1 March 1988, announced in the 1988-89 Budget and taking into account the implications of revised interest rate structure on the profitability of SCBs and CCBs, in consultation with RBI, NABARD evolved a formula for compensating the SCBs and DCCBs for the losses by facilitating cross-subsidization. In the case of co-operative banks this was to be made good partly by a reduction in the refinance rates from NABARD/RBI and partly by opening of other avenues of investment which would fetch them higher returns. RBI was earlier charging a rate of interest of 6 per cent on the general line of credit for crop loans and the same was passed on by NABARD to SCBs at 7 per cent retaining

a margin of 1 per cent. On account of the reduction in the ultimate lending rate on short-term agricultural loans effective 1st March 1988, the RBI itself reduced its rate of interest to 3 - 5 per cent. The NABARD agreed to charge the same rates on its refinance to SCBs, thus foregoing its own margin of 1 per cent from 1.3.1988. The rates on refinance from NABARD to SCBs would, according to new arrangement, depend on the extent of CCB's own involvement in crop loans on whose behalf SCBs draw refinance. The co-operative banks will get the benefit of lower interest rate on refinance if their borrowings from NABARD/RBI are lower and vice versa. Thus, an in-built incentive has been provided for in the revised refinance scheme for co-operative banks to involve a larger portion of their lendable resources in crop loans, if they are to get the benefit of refinance at the lower rate of interest. Nearly 90 per cent of the CCBs availing of credit limits from NABARD have reportedly become eligible for the lowest refinance rate of 3 per cent. However, despite this reduction in refinance rate, the co-operative banks were found likely to suffer losses in view of the heavy investment of some SCBs/CCBs in crop loans at concessional/reduced rate of interest. Consequently, the National Bank has also opened up higher yielding new avenues to co-operatives such as participation in (a) food credit consortia (b) consortia arrangements for production, processing and marketing in the co-operative and public sector undertakings and (c) participation in the bills rediscounting market. The restrictions in regard to investment of the seasonal surpluses of SCBs/CCBs in call and short-term deposits in money market have also been relaxed by NABARD. With the above measures, co-operative banks are expected to secure, on an average, a return of 13-1/2 per cent, which is expected to adequately compensate them for the losses in agricultural sector. Though these changes are welcome, their impact on profitability of co-operatives is yet to be assessed. The position has, in the meantime, changed for the worse in view of the further cut in the interest rate upto 2 per cent on advances between Rs.15,000 and Rs.25,000 to ultimate borrowers. The NABARD would need to review the entire position again and ensure to the co-operatives adequate margins as suggested in the Chapter "Interest Rates, Costs and Margins". Further, the adhoc arrangements as now envisaged cannot be a substitute for a rational interest rate structure. In the case of commercial banks loss of income on lendings for crop loans was to be absorbed by the system itself through the higher incomes earned in other sectors/services.

9.024 The new thrusts needed in NABARD's refinance functions as identified by the Consultants for Study V are to

- a) re-emphasise area based schematic lending; modify and increase the flexibility of investment guidelines to stimulate this approach; and encourage comprehensive integrated lending of short, medium and long-term loans for both farm and non-farm activities;
- b) take steps, in conjunction with RBI, to strengthen district and credit planning within the Lead Bank Scheme, actively help banks to plan and prepare credit schemes and achieve better co-ordination between banks and district and other local authorities;
- c) maintain better linkages with other institutions in respect of national credit planning and scheme formulation.

We agree with these and hope that the various recommendations made in this Chapter and elsewhere in this report would help redirect the refinancing activities of the NABARD on these lines.

9.025 The Consultants have also stated that lack of co-ordination amongst various activities, together with the absence of monitoring and evaluation of the effect of NABARD's refinance activity upon the credit system, means that the refinance operating cycle is not working effectively. Regional Offices are not adequately involved in planning schemes to be refinanced to meet local needs. In their view, NABARD's refinance operations are characterised by top-down policy and planning. While individual constituent activities are quite effective, there is no co-ordinated approach that :

- a) ensures that borrowers have access to adequate amounts of credit;
- b) encourages banks to identify total rural credit potential within a single scheme or area; and
- c) links annual and perspective planning to district credit plan.

Based on an analysis of the refinancing activities of NABARD, the Consultants have identified certain weaknesses, the more important ones being :

- i) Investment guidelines, model financing plans and unit costs are being utilised in a rigid fashion and they do not take account of varying local conditions and credit requirements;
- ii) there is no effective integration of farm and non-farm credit planning, nor of short, medium and long-term refinance;

- iii) District Credit Planning (DCP) is not integrated with perspective planning and is not identifying the real potential for lending in the districts;
- iv) NABARD needs both to strengthen DCP activities related to IRDP and measure the effects of IRDP in order to make a more effective contribution to the programmes;
- v) eligibility criteria do not achieve their goal of improved loan recovery by banks; and
- vi) responsibilities of Regional Offices are too limited, notably in the areas of development of investment guidelines and performance monitoring of refinance.

9.026 The Consultants have, however, noted that NABARD has already begun to take certain steps towards reversing this trend. These include :

- a) delegation of Head Office authority to Regional Offices to sanction the majority of applications for refinance;
- b) development of methodologies to enhance the quality of district credit plans.
- c) deployment of District Development Officer (DDO) at district level to increase interaction with client banks; and
- d) development of state and region specific model financing plans to provide appropriate guidance to banks in schemes preparation.

9.027 But this process needs to be applied to all aspects of the operating cycle in order that refinance satisfy borrowers' requirements at the local level. We have noted with satisfaction that NABARD has started preparing what is called potential-linked credit plans for the districts in various states. This exercise is being done in full co-ordination with the bankers and state government functionaries in the district. In this way, the district credit plan is expected to help preparation of realistic micro plans ensuring production credit support for investment, integrating farm and non-farm sector activities and also the relative backward and forward linkages. Eventually, it is hoped that the village credit plans under the Service Area Approach (SAA) will be dovetailed into the potential-linked district credit plans (such plans have

already been prepared for a few districts in different states) and thus integrating the macro and micro credit planning for the credit delivery system. The adoption of the potentially linked district credit planning will help hasten the process of upgrading the Service Area Approach to the suggested Development Area Approach in Chapter X of our Report. Both RBI and NABARD have to actively co-ordinate and interact amongst themselves and with other agencies concerned. In this connection we would also endorse the views of Consultants III that NABARD's R & D Fund should be used in financing in-depth studies of selected sectors and regions in order to formulate comprehensive IRD-type schemes. It is our hope that by this process the achievement of the goals of IRD could be expedited.

9.028 NABARD has already started, it is learnt, to decentralise powers to the regional offices. The regional offices have now powers for sanctioning refinance assistance upto Rs.150 lakhs for Minor Irrigation and Rs.100 lakhs in respect of other government sponsored/area-based schemes. As of now, about 90 per cent of the schemes are sanctioned at the Regional Office (RO) level itself by and large within a time frame of about 45 days. It is only the rest of the schemes with larger outlay or innovative schemes that are referred to the head office. Of course, close monitoring of the ROs would be necessary in order to ensure that the delegated powers are being, in fact exercised.

9.029 The NABARD should build up the capacity of its client banks so that the latter can satisfy themselves about the financial and technical viability of the schemes, on the basis of guidelines furnished by NABARD. This will help NABARD to improve its own scheme scrutiny and sanctioning process. In selected states, viz., Andhra Pradesh, Madhya Pradesh, Rajasthan and Uttar Pradesh, the banks have been authorised to sanction and disburse loans upto Rs.25 lakhs in such schemes as Minor Irrigation, Dairy Development, Plantation and Horticulture. They can seek refinance thereafter almost on an automatic basis. However, unlike the case with commercial banks, the SLDBs and SCBs are not well equipped for the task. Their Technical Monitoring and Evaluation (TME) Cells have to be substantially strengthened and NABARD's R&D Fund assistance for the purpose should be enhanced if these banks were to efficiently appraise and monitor the schemes. Another experiment relates to what is called the Technical Appraisal Group (TAG), under implementation in Karnataka for

pooling the technical expertise of banks in the state for appraisal and sanction of schemes. The idea is that such schemes appraised by TAG would not need detailed appraisal by NABARD and be expeditiously refinanced.

9.030 As suggested by the Consultants V, disbursements of refinance should be at places convenient to the client banks. NABARD is already disbursing the loans at the RO level in respect of SCBs and RRBs. So also repayments are received at RO level, inclusive of those from SLDBs. We understand that NABARD is taking steps for disbursements to SLDBs at the state level. This may be expedited. Smaller/Regional Commercial Banks may also need similar facilities. All these measures would help to remove the deficiencies identified by Consultants V in the refinancing system of the NABARD.

Direct Lending by NABARD

9.031 Section 30 of the NABARD Act, 1981 provides for NABARD making loans and advances otherwise than by way of refinance to any institution approved by the Central Government on such terms as considered appropriate. CRAFTICARD, in their Report had referred to the fact that the ARDC had this provision since 1975 and had suggested that this provision could be applied in areas where the institutional network was weak, by directly funding public development corporations. Thus direct lending implies that NABARD could finance rural credit schemes of development institutions taken up on their own for on-lending. Direct lending if resorted to under certain special circumstances in the wider interests of regional or sectoral development, is not likely to affect the business of the client banks. Nor in our view could this detract NABARD from its efforts in strengthening credit institutions.

9.032 The arrangements we have recommended in Chapter XI for the setting up of Development Corporations for Eastern and Northern-Eastern States are aimed at filling up the existing infrastructural and in some cases institutional inadequacies. The Corporations may have to borrow for their own programmes for on-lending. We recommend that NABARD may, under Section 30 of the NABARD Act, provide direct finance to these Corporations on a project to project basis, to start with. Based on experience, the financing may either be continued or transferred to client banks, and if transferred and refinance flows through banks, the Corporations can continue their promotional and developmental role.

Recent initiatives by NABARD

9.033 In 1982-83, NABARD introduced a scheme for the development of selected PACSs, somewhat on the lines recommended by the CRAFTICARD for their further upgradation into truly multi-purpose societies. Over 5,000 societies in different states were selected but the scheme was not adequately followed up. The SCBs in the concerned states were obviously not playing their leadership role expected of them in implementing this scheme. The NABARD came up with a 15 Point Programme for specifically covering 30 PACSs in each of its pilot project districts for strengthening the credit delivery system. Financial assistance from NABARD covers the full cost of additional secretary of PACSs, LAMPSs and 50 per cent of the cost of counters, safes, etc. besides liberal share capital contribution. The grant made so far amounts to Rs.10 lakhs. However, the Pilot Project is an experimental one and its cost-effectiveness is yet to be fully assessed.

9.034 As for 'weak' CCBs, their number remained for long constant at 170 or thereabout ever since the programme was launched by RBI in 1971. Experience has shown that the CCBs under the programme only temporarily improved their financial position and quite a few CCBs which are taken out of the 'weak' list soon slid back. In the absence of any specific incentives for the CCBs or financial support either from the State Governments or the concerned SCBs, the CCBs were neither enthused nor well equipped to carry out the detailed examination of the large number of overdue accounts envisaged under the scheme. The ACD (RBI) Scheme of Rehabilitation of 'weak' CCBs was supplemented by a 12 point time-bound action-oriented programme by NABARD in 1987 under which substantial grant is available towards the managerial and supervisory cost of the CCBs subject to a matching assistance by the State Governments. The special feature of the scheme is that the National Bank will open a line of credit for the 'ineligible' CCBs for three years, during which period the concerned CCB and the State Government have to implement the action programme. Excepting for identification of about 60 weak units, this scheme also remained a non-starter mainly because of the inability of State Governments to meet their part of the financial commitments.

9.035 In regard to the LDBs, as in the case of short-term credit institutions, NABARD has been implementing the schemes like reorganising primary units

on a viable basis, improvements in organisation and management etc. Recently, NABARD itself introduced a 10 Point Action Programme covering all 'weak' PLDBs having overdues exceeding 60 per cent of the demand. While about 14 weak units were identified in 8 states and financial assistance of about Rs.14 crores were extended, LDBs in other states are as yet to respond to the programme.

Review of NABARD's Operations - Institutional Development

9.036 The emphasis of AIRCSC 1954 was on progressive institutionalisation of rural credit. But such institutionalisation would be fruitful only when the lending channels acquire a measure of strength. As we have mentioned elsewhere, what we see to-day is a phenomenon where several factors such as target approach to lending, poor recovery, administered lending rates etc., have gradually eroded the strength of rural credit institutions. We are aware that these factors present in the rural credit environment of the country exogenous to NABARD are contracting its efforts to strengthen its client institutions and have suggested remedial measures elsewhere in this report. Here we propose to review the NABARD's role in institutional development and the changes we envisage in this regard.

9.037 Each of the four types of lending institutions; CB, SLDB, SCB and RRB is subject to varying degrees of control by GOI, State Governments, RBI and NABARD. Further, branches and primary units responsible for rural credit delivery, report to their controlling offices.

9.038 As regards NABARD, its statute is explicit in that it enables NABARD to disburse and recover refinance and inspect SCB/DCCB/SLDB/RRB. Section 38 of NABARD Act requires the NABARD to undertake the responsibility for institutional development. NABARD's lever of refinance should be effectively used as an instrument to enforce institutional development. We are aware that this is a delicate instrument and its deft use with a view to ensuring results, is a function of the leadership capability of a national apex system. It is for the development of this capability which NABARD at the apex of the rural credit system has to work up to. It is worth recalling in this connection that the ACD of RBI had specifically evolved policies over the years whose objective was to build overall co-operative structure at all levels,

with particular reference to the co-operative credit system. A major reason advanced for the creation of NABARD was that ARDC was unable to expand its developmental role towards institution building. As NABARD assumed the functions of these two organisations, it also inherited their policies and NABARD has accepted its responsibility for institution building. Development of the rural credit system, involving as it does such activities as business planning, identification and implementation of new lending opportunities and manpower development, cannot be achieved solely through regulation. The NABARD, statutorily as the apex institution for rural credit, is well placed to develop a positive climate for institutional development on a collaborative basis with the support of GOI, RBI and State Governments.

9.039 As at present the NABARD's activities in institutional development are primarily reactive rather with the exception of Volunteer Vikas Vahini (VVV) which has been taken up on a limited scale, all activities have been more or less a continuation of those which were being pursued by the parent organisations. NABARD is seen devoting more of its energies to the refinance function. This bias needs to be corrected because, unless the institutional network is sound, the flow of credit may, in the long-term, be maintained only by relaxing discipline to such a degree that there is no effective regulation of the system. Overall, NABARD should undertake more effective leadership role in institutional development that was envisaged at its inception, particularly with regard to ACD's emphasis upon co-operative development.

9.040 Reviewing this, Consultant V have made the following recommendations:

- a) A clearly defined policy for NABARD's institutional development functions be established with quantifiable objectives and targets for achievement;
- b) the process of integrating all activities and programmes within the organisation structure be completed and the roles and responsibilities of Head Office and Regional Offices for institutional development be defined so as to increase the involvement of Regional Offices;
- c) links between NABARD and other organisations be strengthened so that institution building activities meet local requirements;

- d) existing rehabilitation programmes be restructured and broadened towards a "Comprehensive Business Health Development Programme", which emphasises business viability through the growth of credit activities, resources mobilisation, sound management and enhanced credit delivery, supervision and recovery systems; and
- e) NABARD's client bank training activities be redefined to become one facet of its integrated institutional development function providing professional advice to the bank's training institutes.

9.041 We are in broad agreement with this approach and have observed in Chapter XII, that NABARD should be responsible for overall policy and monitoring of institutional development. We have also spelt out the role of NABARD in ISP and the various components of the programme. The role of NABARD as envisaged by us is one of policy planning and review, besides extension of necessary financial assistance particularly in the form of grants, among other things. These expenditures could be met by NABARD out of its R & D Fund. It may, however, be mentioned that unlike the RBI vis-a-vis commercial banks, NABARD has little say in the management of co-operative banks. A greater degree of professional management has to be brought about in the co-operatives and it should be NABARD's responsibility to ensure this. The following recommendations of the consultants merit re-emphasis :

- i) At least one senior officer of NABARD should be nominated by the State Government on the Boards of each of the SLDBs and SCBs for guiding and monitoring the implementation of ISP and other developmental programmes and lending operations on the right lines.
- ii) The appointment of Chief Executives of SCBs/SLDBs should be made subject to prior approval of NABARD. Similarly, the removal of chief executives should be done with the concurrence of NABARD. The NABARD in collaboration with RBI and GOI should take up the matter with State Governments.

Review of NABARD's Operations - Inspections

9.042 Under Section 35 of the Banking Regulation Act, 1949 as amended by the NABARD Act of 1981, NABARD is empowered to conduct periodic statutory

inspections of SCBs, DCCBs and RRBs. The inspections conducted by NABARD are a statutory obligation under Banking Regulation Act and serve to ensure mainly the following :

- (i) that the affairs of the bank are not conducted to the detriment of depositors,
- (ii) that the provisions under Banking Regulation Act relating to liquidity requirements, real and exchangeable value of paid-up capital and reserves, filing of returns, etc. are complied with,
- (iii) that the bank follows sound systems, procedures relating to loans and advances and management of funds and,
- (iv) that the directives issued by RBI from time to time are followed.

In addition, NABARD also undertakes voluntary inspections of SLDBs, Co-operative Apex Marketing Federations and Apex Handloom Weavers Societies to which it provides refinance, in order to review the overall financial health of these institutions.

9.043 The basic purpose of inspection is to maintain the banking system on sound footing in conformity with banking laws and regulations. The main objectives of inspections are to ensure that banks protect the interests of their depositors, pay their claims as and when they accrue, conduct their business on approved lines, regulate the flow of credit to borrowers and comply with the various statutory provisions of BR Act. Although RBI regulations thus specify the basic requirements of an inspection, bank inspectors are empowered to examine any aspect of a banks' operations, managerial competence and specify any actions deemed necessary to protect depositors' interests. Inspections are expected to cover not only financial matters but also operations, management and the potential for development of the banks' business.

9.044 As on 30th June 1987, NABARD is required to inspect a total of 605 SCBs, CCBs, RRBs, SLDBs and other co-operative institutions. Although the lending institutions are obliged to comply with the findings of NABARD inspections, the powers of enforcement of inspection findings by NABARD are limited. According to the Consultants V, some of the limitations are as indicated below :

- a) NABARD has no powers to grant or withdraw licences. It only makes recommendations to RBI in respect of licences for the banks inspected,
- b) restriction or withdrawal of refinance is likely to weaken banks rather than improve them,
- c) among co-operative lending institutions, it is only their banking and financial operations that are subject to RBI/NABARD control. Organisation and management are subject to the Co-operative Societies Acts and Rules of the respective states and the powers are exercised by Registrars of Co-operative Societies of the States.

Thus, according to the Consultants V, the NABARD has to depend mainly on its own persuasiveness for ensuring enforcement of its inspection recommendations which invariably contain developmental aspects also. In extreme cases, it has to seek action through the RBI or Registrar of Co-operative Societies.

9.045 While NABARD inspections by and large fulfil the statutory requirements, they are not, according to the Consultants V, effective and the following deficiencies have been pointed out :-

- a) inspection reports typically highlight defects (about which the banks management are well aware), without providing any analysis of their causes and detailed recommendations and proposals for their solution,
- b) follow-up action by NABARD is limited largely to desk monitoring of compliance reports,
- c) NABARD is not using the inspection findings to monitor banks' performance except in a general way. The only extensive use of inspection reports by NABARD is in assessing banks' eligibility for short-term credit limits,
- d) regulatory powers other than directives are not used to control banks whose performance is poor.

The main weaknesses identified by the Consultants are :

- a) Inspections do not always succeed in causing banks to regulate their affairs in accordance with statutory provisions.

- b) Little real use is made of inspection reports by the banks, NABARD or other agencies.
- c) There are very limited links between inspection and other NABARD functions, notably institutional development and inspections do not make any positive contribution to the institution building process.
- d) Information about banks that is collected during inspections is not used as data source by NABARD to review its refinance and institutional development policies and programmes.
- e) Demands for inspection staff disrupt the other work of Regional Offices.

9.046 The consultants have observed in general that the inspection function is not integrated with NABARD's other two main functions viz. refinancing and institutional development, and that inspection findings are not being effectively enforced. Accordingly, the Consultants V recommended that :

- a) NABARD should redefine the purpose and objectives of its inspections so that the function is integrated with other functions and can be used as a tool to :-
 - i) fulfil NABARD's various functions and improve the performance of the banks.
 - ii) endeavour to enforce findings, where appropriate, and as a last resort, where banks fail to improve, through withdrawal of refinance and other sanctions through RBI.
- b) The scope and content of inspection reports should be improved so as to provide the analysis and recommendations that will :
 - i) assist banks to take corrective action to improve performance; and
 - ii) provide useful information for monitoring and evaluation of NABARD's refinance and institutional development policies and programmes;
- c) All inspections should be undertaken by Regional Offices with consequent increase in manpower at Regional Offices and a reduction at Head Office.

9.047 For improving the process of inspections and make them more meaningful to client banks and other concerned agencies the following specific proposals have been made by the Consultants :-

- a) the submission of pre-inspection statements may be discontinued.
- b) inspection teams should not give banks, advance warning of precisely when they intend to inspect the bank, other than a general intimation at the beginning of the year. The team should arrive unannounced and begin work,
- c) branch and primary unit visits should be similarly organised and the inspection team should not announce, in advance which centres they intend to visit. In addition, teams should also visit actual borrowers at random, not only to verify records but also to seek their views and attitudes to the bank,
- d) the inspection team should, if appropriate, put forward and assist the bank's management to implement any immediate remedies that have been identified during the course of the inspection,
- e) the Chief Inspecting Officer should meet and discuss the findings with the apex banks for CCBs' inspections and State Government Officers (notably RCS) for inspections of other Co-operative institutions at the end of every inspection,
- f) within one month of the issue of an inspection report the senior management of the bank should discuss with the Chief Inspecting Officer and others concerned with inspections, the findings and recommendations of the report and agree upon the time table for the action to be taken. The RCS and apex bank should also participate in this meeting. This should be followed by a detailed action plan to be drawn up by the bank and copy sent to NABARD and others concerned,
- g) the Chief Inspecting Officer should visit the bank concerned every three months following receipt of quarterly compliance reports, to review progress of compliance and consider any additional action needed to be taken. These visits could be more frequent where banks are not complying with the findings or have serious defects,
- h) the banks' senior management should have meetings with NABARD

staff and those of the other institutions every 6 months following an inspection and conduct comprehensive review of the compliance, decide any action needed to achieve targets and revise and up-date the action plan for compliance,

- i) the content of reports should be the same for each operational areas inspected and should summarise the situation, analyse any problems, propose solutions and state who is responsible for taking action,
- j) inspection reports should also contain as few financial and statistical statements as possible, other than those required by the regulations. These should, in any case, be in annexes. This especially applies to those statements which have been obtained from the bank itself as they add to the burden of report preparation and typing.
- k) the full inspection report should go out from NABARD to :-
 - i) the bank/institution inspected,
 - ii) the apex bank,
 - iii) RCS at state and district level in the case of SCB, DCCB, SLDB and other co-operative societies, and
 - iv) RBI in the case of banks coming under the purview of the B.R. Act.

9.048 This procedure should be automatic even if these institutions are not required to take action on the findings. It is vital that they are kept fully and formally informed as to inspection findings, particularly if subsequently either they or NABARD would need to intervene in the bank's affairs.

- l) as regards the amount of time in mandays laid down by NABARD for inspections, it is felt that it is sometimes inadequate for teams to fulfil the full role and scope of inspection operations envisaged. The duration of an inspection will have to be decided considering the workload involved in each case and may be left to the Chief of the Regional Office.
- m) In the matter of continuity of inspection teams, it is suggested that staff assigned to inspections should remain in post for not less than three and preferably five years. Each inspection team should be allocated specific banks in a specific geographical area to inspect on a continuous basis. No more than half of any team should be

replaced at one time. New Chief Inspecting Officers should be supported during the first inspection cycle by another officer who has experience in inspections and is fully familiar with the bank being inspected. As a control mechanism, NABARD's Internal Audit, Inspection and Vigilance Departments should review inspection operations regularly and make spot checks at the banks in order to ascertain whether any malpractices are developing.

9.049 We broadly endorse, these recommendations of the Consultants V, including the 'surprise' element in the inspection of co-operative banks. We have, however, some reservations on the feasibility as well as desirability of the recommendations made at (k) and (m) above from the administrative point of view. We would expect that when our recommendation for the merger of RRBs is accepted and given effect to, NABARD will be relieved of the inspection work to that extent and be in a better position to concentrate and improve upon the quality and content of inspection of co-operative banks. Although we are in agreement with the broad approach of Consultants V regarding inspections by NABARD, we would leave it to NABARD/RBI to take a view on specific operational issues recognising the existing constraints relating to staff related matters.

Organisational Structure of NABARD - Needed Changes

9.050 The Consultants V had specifically reviewed the effectiveness of NABARD's organisation structure in the light of the MSD report of May 1988, which sets out detailed organisation structure and revised manning levels. According to the Consultants, despite the on-going plans to relocate operations to state level, R.O. responsibilities are still not sufficiently broadened to enable the NABARD to tailor its programmes effectively to meet the local needs of client banks and their borrowers, and develop as a major and leading contributor to state level policy formulation and planning for agriculture and rural development. The MSD report of May 1988 is devoted principally to Head Office organisation structure and activities and in many areas does not enhance the operational autonomy of the R.O. The need has therefore arisen for revising the present organisation structure at both Head Office and Regional Office level.

9.051 The revised functional organisation design proposed for NABARD's H.O. by the Consultants V is given on Chart II and the relationship between H.O. and R.O. as well as the basic organisation structure proposed for a R.O. is depicted on Chart III at the end of the Chapter. With the clearcut division of responsibilities between H.O. and R.O., the autonomy and decision making authority of the R.O.'s are expected to be ensured. There are four senior positions to head the Policy and Planning, Operations, Information & Evaluation and Services in the H.O. The Consultants have suggested that the Head of Policy & Planning should deputise the M.D. in the latter's absence, while in the R.O., the Head of Operations, who is the co-ordinator of the state level activities of refinance, institutional development and inspection should similarly deputise the officer-in-charge whenever he is absent. A department for district development is provided for at the R.O. level to fit in the NABARD's proposed scheme of appointing Designated District Officers (DDO). These officers would represent NABARD at the District Level and make NABARD's operations responsive to local needs and conditions. Though located at the R.O., the DDO is expected to spend at least half of every working month in the respective district. They are the link between R.Os and districts.

9.052 It is expected that the strengthening of the top level structures of the NABARD would enable senior management to concentrate upon matters of broad policy and direction, including liaison with GOI and other national level institutions with a view to ensuring that national policies and plans are favourable for a healthy rural credit system. The greater authority and autonomy for the R.O. should enable senior regional staff to influence state and district policies and develop specific programmes that support the rural credit infrastructure.

9.053 We would commend for adoption the models suggested by the Consultants with such modifications as NABARD may consider appropriate. We understand that NABARD's management has already initiated action somewhat on these lines based on its MSD report and following detailed discussions with its senior officers and R.O. in-charges.

9.054 According to the Consultants V, NABARD's legal mandate appears to suffer from the following weaknesses :-

- (a) the apparently identical powers vested in the Board and Managing Director;
- (b) the lack of definition of the relative roles and functions of the Chairman and Managing Director;
- (c) inadequate definition of the powers and functions of the Executive Committee; and
- (d) inadequate definition of the role, function and relationship of the Advisory Council to NABARD.

They have therefore suggested that NABARD regulations (Section 60 of the Act) should be modified suitably to remedy these weaknesses.

9.055 The Executive Committee, as the Consultants have stated, should be delegated adequate authority to direct the affairs of NABARD, with the Board retaining only those powers consistent with establishing and reviewing NABARD's broad policies. The Committee should be of manageable size. Apart from the Chairman who is a Deputy Governor of RBI, the remaining four non-executive directors of the Executive Committee may comprise :

- (a) a GOI nominee say, Principal Secretary of the Union Ministry of Agriculture;
- (b) one member with expertise in rural banking;
- (c) one senior expert in agriculture and rural development; and
- (d) one member representing State Governments.

The Consultants have added that in case the Chairman ceases to be a Deputy Governor of RBI, the composition of the Committee may be altered to include an RBI member, if necessary by increasing the size by one additional member.

9.056 It is not correct to say as the Consultants V have done, that the powers of the Board and the MD are identical. Section 7(1) of NABARD Act is very clear and specific that the general superintendance, direction and management of the affairs and business of the Bank vest with the Board. Although, the MD, in terms of sub-section (3), is vested with similar powers, being the Chief Executive for carrying on the day-to-day operations, his powers are subject to the overriding powers of the Board and the Regulations framed under the Act as qualified in the sub-section itself. We note that

in the case of all decisions taken by the Board, it is the MD who is the competent authority and in fact is duly authorised to take action. As for the roles and functions of Chairman and MD, it is pertinent to recall what the CRAFTICARD had intended. In order to maintain NABARD's organic links with RBI, CRAFTICARD recommended that a Deputy Governor of RBI should be the Chairman of the NABARD (unlike the case with other National level institutions say IDBI which has a full-time Chairman who is also the MD). It is for this reason that the law as enacted by Parliament rightly provides vide sub-section 5 of Section 5 of the NABARD Act, for the MD following such directions as the Chairman may give. In our view, it is not necessary to define their respective roles in the Statute. These are better established by convention rather than statutory regulations.

9.057 The Executive Committee (EC) was constituted during 1987-88 under Section 13(1) of NABARD Act read with Regulation 3(1) of the General Regulations 1984. Four directors besides MD and Chairman are its members. The EC can discharge such functions as may be prescribed or delegated to it by the Board. Thus, it is entirely for the Board to delegate such of the powers as it deems fit to the EC. As of now, the Board has delegated all its powers subject to the provisions of the Regulations 1984 and excepting for those powers specifically reserved by the Act itself for the Board to exercise. This in our view is in order.

9.058 As regards the Advisory Council, the Consultants have suggested that it should provide a broader range of top level specialised advice and knowledge to the Board. The Council's membership should be based on acknowledged competence and status in a particular interest group. The membership may be drawn from universities, research institutes, client banks, government departments and apex institutions. While endorsing this recommendation, we would suggest that the Advisory Council like ACB, should be a compact body of experts not exceeding 12 in all. The present Advisory Council of NABARD set up in January 1987 is rather an unwieldy body, consisting of as many as 33 members. In nominating persons for membership, the areas of expertise and specialisation mentioned in sub-section (1) of Section 13 of NABARD Act should be kept in view.

9.059 The Consultants V have indicated that NABARD may consider creation of local Advisory Councils or Boards at State level as subsidiary units of the Advisory Council. This would be in tune with their proposal to decentralise decision making to R.Os in the areas of policy and planning for refinance and institutional development. State/Regional level matters involving policy and planning should, in our view, receive the attention of NABARD's Board and top management. We would therefore, commend, the continuance of the present practice of NABARD Board discussing sector-wise, State status papers on problems of individual states and giving policy directions. Such meetings are held in the respective headquarters. Detailed discussions are held with the state representatives at the highest level. This is in addition to the periodical discussions held by Chairman/MD on problems of development with individual states which provides the appropriate forum for resolving local problems.

9.060 It would be preferable according to the Consultants, to replace the existing management committee which meets every week, with a top management team, conceived as a permanent working group, comprising a relatively small number of senior managers. The top management team may be restricted to the MD and the four Heads of Policy & Planning, Operations, Information & Evaluation and Services. It should be convened as and when required on a relatively informal basis, to assist the MD in the following activities :

- a) review and initiate strategic changes in implementing NABARD policies for operations, finance and human resources;
- b) develop NABARD's corporate plans and budgets;
- c) set standards of service towards client banks in all operational matters; and
- d) promote organisation change and management development.

9.061 It has been suggested by the Consultants that in order to support the MD and top management team in carrying out their responsibilities, a corporate services unit be established in NABARD. The unit should report to the MD and may have the responsibilities of corporate planning, legal services and secretarial and liaison support to the Board, Committee and top management team. The unit may incorporate the present Corporate Secretariat and inde-

pendent Legal Division which should be separate and not part of administrative services. In the view of the Committee, these are matters on which NABARD's Board may take appropriate action. It is understood that NABARD has since reconstituted its management committee consisting of the Chairman/MD and all the Chief General Managers. This committee which meets once a fortnight, assists the Chairman and MD broadly in the areas referred to above by the Consultants, besides a review of the working and problems of the ROs.

9.062 Delegation of authority to regional levels is still to be defined fully. More importantly, according to the Consultants V, delegation has not addressed the question of the policies which guide operational and services activities. The concept of regional autonomy whereby ROs can develop specific policies and strategies that address the diverse agro-climatic, economic and social variations found in each state and meet the needs of client banks and their borrowers within broadly defined regional goals and objectives for NABARD is also to be considered. Decision-making in these areas at present remains centralised at top management and Board levels. Consequently important decisions affecting a single state are often inappropriate and rigid for others. Decisions are subject to delay as recommendations are gradually passed up the management hierarchy. The system in vogue does not enable NABARD to be adequately responsive to local conditions at the state level. Decisions have to be taken as close as possible where the activity takes place. Decision-making powers should be located at a level where all relevant information is readily available. Only in exceptional cases should decision-making be by the Committees. While national policies, overall strategies and standards should be approved by the top management team, the MD, Executive Committee or the Board, specific sector strategies and programme, annual plans and budgets should be approved by senior managers at HO and RO. Day-to-day operational decisions should be made by heads of departments and divisions. Decisions which affect the resourcing of plans, specifically personnel and financial expenditure should involve those line managers where resources are affected. NABARD has to set precise authority limits realistically. NABARD has already accepted the concept of 'regionalisation' for making its operations more effective in furthering rural development at state and district level. Revised authority limits for the sanction of refinance have been defined giving more decision making powers to ROs-in-charge.

9.063 The Consultants V have reported that though NABARD has inherited and utilised manuals from its parent organisations (ARDC & ACD), it has begun to develop its own manuals which is a step in the right direction. Apart from the requirement for the new recruits, operating manuals to be developed by NABARD can assist it to establish its own corporate identity. We agree that there is need for a prioritised programme for development of operating manuals together with standardised, high quality manuals. The responsibility for preparing the manuals with MSD which would identify and prioritise the need for manuals and allocate internal resources or designate outside consultants for their preparation. The manuals should be maintained in loose leaf form to facilitate future revisions. MSD should be responsible for revising the manuals based on requests from the appropriate user departments. MSD should also undertake an updating exercise once every two years to incorporate relevant and necessary changes to manual.

9.064 The Consultants V have underlined the need for NABARD developing functional expertise among its officer cadres. According to them although the existing economic, technical and legal cadres may be retained as they are, the general cadre of staff may be separated into functional cadres of banking, human resources, finance and administration. It has also been suggested that the existing specialist cadres of security, secretarial and national language may be absorbed into the administration cadre and a single senior management cadre should be established for top posts with a new cadre to be established for computer services. The Consultants V have also made recommendations on recruitment, promotions and transfer policies etc. We, however, feel that it may be left to NABARD to tackle these issues. As regards promotions, the Committee is of the view that the existing practice in NABARD which takes into consideration both merit and seniority for promotions is in order and may continue. In this context, the Committee feels that NABARD may follow the example of RBI in regard to exchange of staff between RBI and commercial banks for a specific period. NABARD can consider introducing the system of exchanging its staff in certain cadres with client banks particularly SCBs and SLDBs for a short duration for gaining experience and expertise in specific areas for mutual benefit and manpower development.

9.065 An organisation's culture can be defined as a system of shared values, beliefs and attitudes which are manifested in the behaviour of managers,

officers and groups of employees. Consultants V feel that there is need within NABARD for a change in the present organisational culture which represents the prevalent culture of the public sector in India and is inappropriate for NABARD's developmental role. The regulatory role which is predominant now has to give way to that of development and service. NABARD should have a high profile corporate identity with effective regionalisation and decentralisation. There is need for increased employee motivation. The culture change should embrace acceptance of responsibility, authority and accountability. A more open and participative style of management is needed in NABARD, apart from introduction of the concept of team building. In their view, these changes can improve the image of NABARD and can lead NABARD to establish its own specific identity as an apex institution for agricultural and rural development. After all, NABARD is a bank as well as a development agency and was expected to emerge as the leader in the growth and strengthening of the rural credit system in India. An appropriate manpower development and training can bring about a change in the attitude of employees who will project NABARD's identity. We see and endorse the need for a change in NABARD's image and identity which can be brought about only through better employee motivation and performance. Against this background the NABARD may consider the various suggestions of Consultants V in regard to delegation of authority, preparation of operating manuals, induction of change in the organisational culture and manpower development and take appropriate action. We expect that these recommendations will be taken due note of, for the overall review of Organisation Structure on manpower assessment which the NABARD has recently undertaken, following the recommendations made in the study report of Tata Consultancy Services on Organisation, Design and Development of NABARD.

Information and Evaluation

(i) **Organisation of information and evaluation**

9.066 As the apex institution for rural credit, NABARD is required to collect and analyse information not only for its own use, but also for providing the information to GOI, client and other institutions for facilitating co-ordinating policies and programmes at all levels. On a review of NABARD's current management information, monitoring and evaluation activities and computerisation programme, with a view to fulfilling the above, the Consultants V feel that there is a need for creating a new Information & Evaluation Depart-

ment for co-ordinating and controlling NABARD's information gathering, processing and reporting activities.

9.067 The main tasks of the departments are to :-

- a) provide information on the performance and effects of NABARD programmes and activities to the top management, Regional Offices, client institutions, GOI and other institutions;
- b) collect relevant information from and provide it to institutions external to NABARD, where this information will enable NABARD and other institutions to more fully assess the effect of NABARD's activities and
- c) improve current information storage, analysis and reporting activities for NABARD internal functions such as accounting, administration and for institutional development, refinancing and inspections.

9.068 The functioning of this Department according to the Consultants V would enable NABARD's management and other institutions to have access to the information on the performance of NABARD in refinance, institutional development, inspection as well as its own finance and administration activities.

(ii) Monitoring and Evaluation

9.069 Monitoring measures the progress towards predetermined targets and identifies reasons for poor performance, while evaluation is the analysis of all monitoring and other relevant information to take account of all factors affecting performance in order that the reasons for the degree of achievement can be determined. Monitoring and evaluation plays a vital role in measuring both the performance of NABARD's programmes and effectiveness of its strategies for the development of the credit system.

9.070 For the purpose of their study, the Consultants V have defined monitoring and evaluation as the collection, evaluation and interpretation of information covering NABARD's three key functions of refinance, institutional development and inspection. As such, it would encompass a significant proportion of NABARD's management information requirements. The Management Information System (MIS) is the reporting system through which top management receives regular reports, which summarise the progress of these operational

functions and all service functions (in particular personnel and accounting) in standardised format to facilitate decision making.

9.071 Taking into account the inherent weaknesses in the existing system, there is need according to the Consultants V, to exercise a major overhaul in the way information is collected, collated, analysed, evaluated and used. Current monitoring, evaluation and follow-up procedures primarily serve to ensure that NABARD guidelines are being adhered to.

9.072 In order that monitoring and evaluation activities become an integral part of NABARD's operations, the following measures have been recommended by the Consultants :

- a) monitoring and evaluation activities be co-ordinated and managed as a separate entity within the organisation which will have the prime responsibility of collecting, co-ordinating, evaluating and distributing information from, amongst others, DOM studies, ex-post evaluation, inspections, operational monitoring and institutional development activities;
- b) the design of ex-post evaluation be reviewed to reinforce their value in planning and in disseminating the results of NABARD's programmes. The decision should include :
 - (i) an assessment of external factors affecting performance;
 - (ii) the utilisation of operational monitoring informations;
 - (iii) utilisation of information from the other institutions involved in projects and programmes;
 - (iv) the evaluation of success or failure and the reasons for success or failure, whether the outcome is a result of NABARD's activities, other institutions or external factors;
- c) programmes are developed to encourage institutions both to develop their own monitoring and evaluation capabilities and to recognise the value of monitoring and evaluation to the development of their own operations;
- d) the role of DOM studies be reviewed in the light of the need for the monitoring and evaluation of NABARD's activities rather than the monitoring of adherence to NABARD's guidelines;

- e) NABARD should develop clearly defined programmes to promote, publish and disseminate examples of successful credit operations among credit institutions.
- f) Regional Offices should concentrate on operational monitoring and evaluation with Head Office concentrating on the monitoring and evaluation of the effects of refinancing and institutional development activities on client institutions, and
- g) the content and quality of monitoring and evaluation studies be reassessed in order to ensure that their findings are of relevance to users, for example, sector evaluators.

9.073 For the desk monitoring of the progress in the implementation of these schemes NABARD has introduced returns in the prescribed forms for reporting details of the various stages of implementation of the schemes, in terms of disbursements, phasing, physical units etc. It has been observed by us during our visits that the banks are sluggish in submitting the prescribed returns and there are inordinate delays, for instance, the quarterly returns in many cases, are sent by the banks to NABARD after a lapse of one or two years, or not sent at all. In the absence of such data, it may not be possible for NABARD to monitor the schemes closely and systematically. NABARD's R.Os. should impress upon the client banks to submit the returns in time. It may also be observed that while the flow of information is somewhat regular in the case of SLDBs, Commercial Banks find it difficult to comply the needed information which is to be obtained from their large network of branches all over the country and submit the same in time. It is worth considering, whether the RBI could obtain this information from the commercial Banks as part of Basic Statistical Returns, and pass on the same to NABARD. It is understood that both RBI and NABARD are exploring the feasibility in this regard. While we would suggest an expeditious decision, we would also suggest that the formats of the various prescribed forms could also be simplified so that banks are enabled to collect, compile and furnish the same in time to RBI/NABARD.

(iii) Management Information Systems (MIS)

9.074 Management information is data which have been processed and presented in a form to enable management to take effective decisions. NABARD's

management needs information on delivery of credit, effect of credit and institutional performance throughout the credit delivery system. In practical terms this means that information has to be collected from over a lakh credit outlets and such information will often reach NABARD only after passing through several tiers of the credit infrastructure.

9.075 The present MIS in NABARD does not measure upto the needs of the senior management and requires to be streamlined. The following measures have been suggested by the Consultants V to improve MIS:

- (a) a review, evaluation and redefinition of the real information needs of NABARD's most senior managers be required along with planning and design of an appropriate MIS to meet those needs. The MIS should reflect NABARD's organisation structure, should recognise NABARD's defined role and functions and should incorporate general principles of good management, whilst also recognising the difficulties of extraction of requisite information both from within NABARD and from the client banks;
- (b) requirements and responsibilities for management information co-ordination be specified and appropriate organisation structure and resources determined;
- (c) the duplication and redundancy of information flows resulting from lack of management information co-ordination be eliminated. Special projects are required to :
 - (i) create a full inventory of all returns to, from and within NABARD and
 - (ii) review the need for and relevance of each return and its frequency keeping only what is genuinely required;
- (d) NABARD should take a lead role in improving management information within the rural credit system. This includes reviewing client difficulties in providing requisite management information and identifying short and long-term measures to improve management information;
- (e) a standards committee should be formed, chaired by NABARD, to ease the introduction of computerisation, improve collation of management information and implementation, and control the introduction of standards for agricultural credit management information;

- (f) NABARD should prepare a MIS manual and distribute it to client institutions and provide appropriate training seminars for client banks, and
- (g) NABARD should compile statistical returns relating to the co-operative movement in India and publish them regularly on an annual basis.

(iv) Computerisation Strategy

9.076 NABARD can provide computerised support to activities which are repetitive, involving non-judgemental work and in processing of quantitative information. It has undertaken a number of steps towards large scale computerisation throughout the organisation. Computer Services Division (CSD) which is a wing of EAPD is responsible for all data processing activities at HO. This Division is also responsible for the introduction of computerisation throughout NABARD. According to Consultants V, the computer hardware that NABARD has selected is well suited to the applications that are being developed and provide a sound foundation for future development .

9.077 The computerisation strategy for NABARD should be based on the need to provide support to the activities that NABARD should carry out to achieve its principal objectives of :-

- (a) regionalisation of the operations of the main function of refinance, institutional development and inspection;
- (b) conducting more effective monitoring and evaluation of both the progress and effects of the functions at Head Office and at Regional Offices; and
- (c) provision of more timely, relevant and accurate information to management to assist them in decision making.

9.078 NABARD must analyse and identify specific activities that are particularly suited to computerisation such as

- (a) preparation for inspections,
- (b) production of inspection reports,
- (c) appraisal of applications for refinance.

Other activities like assessing the sources of refinance or planning institutional strengthening programmes require more qualitative analysis and are less suited

for early computerisation. NABARD can computerise the collection of data through the use of data base being established by GOI. Notable among these is DISNIC under the control of the National Informatics Centre. Under this plan, information is intended to be collected and stored on computers in each district and aggregated at state and national levels. A range of data is intended to be collected and made available including some agroclimatic data.

9.079 For overseeing and directing the planned programme of computerisation in NABARD the Consultants V have suggested that three steering groups may be constituted :

- (a) NABARD Computerisation Steering Group with MD as the Chairman and all departmental heads as members.
- (b) Operations and Planning Steering Group with the Head of Operations or Policy and Planning as the Chairman and selected divisional managers from departments and of Information & Evaluation as members.
- (c) Finance, Accounts and Personnel Steering Group with Head of Services as the Chairman and managers of Finance & Accounts and Personnel and the Head of Information and Evaluation as members.

9.080 In the initial stages each group should meet monthly and when the implementation path is firmly established such meetings can become quarterly. The involvement of senior management should ensure that appropriate focus is placed on the critical role computerisation will play in NABARD, meeting its strategic objectives in this sphere.

9.081 NABARD may, according to the Consultants V, require external assistance in the area of training, development of applications, establishment of new methods and standards, and preparation of detailed plans. NABARD may use an external consultant to assist it in the preparation of more detailed implementation, in advising on the methods to be used and in quality assurance of the plans.

9.082 NABARD may consider these recommendations of Consultants V relating to Information and Evaluations (details of which are contained in Chapters XXIII, XXIV, XXV, XXVI and XXVII of Consultants V Report) and initiate action. The Committee has noted that NABARD is already making steady

progress in developing computer-based MIS with the help of Indian Consultants.

Training of NABARD and Client Banks' Staff

(i) Training of NABARD's Staff

9.083 The observations made by the Consultants V in the training arrangements currently in vogue may be summed up as follows :

- (a) There is no clear statement of policy as a result of which training programmes have developed in an ad hoc manner.
- (b) Training has come to be equated with formal off-job courses which are mostly theoretical in approach. Training has not much relevance to making up deficiencies in job performance.
- (c) Identification of training need is restricted to the annual performance appraisal. The needs are mostly linked to available courses rather than the demands of both the organisation and specific jobs.
- (d) The current officer training programmes are oriented towards the general service rather than specific job performance problems and inadequacies.
- (e) The importance of developing professional cadre of trainers is not recognised.
- (f) Overseas training tends to react to the availability of donor funded scholarships rather than demonstrated training needs.
- (g) There is no systematic training programme for Group B employees (clerical and administrative staff) to whom officer level vacancies are open.

9.084 As for different types of training, the Consultants V have suggested :

- (i) Induction training programmes for new recruits.
- (ii) Job specification training, wherever necessary, for developing the knowledge, skills and attitudes required for the posts.
- (iii) At the time of promotion, to suit the requirement of high-graded post.
- (iv) For skilful performance - Expertise in rural banking etc.

9.085 Steps to be taken for developing training programmes as suggested above are :

- i) Training programmes should be based upon the identified priority and needs of NABARD employees.
- ii) Training should be imparted through a variety of methods and the selection of appropriate methods should be the responsibility of the Training and Manpower Development Division. These may include in particular :-
 - a) on-the-job training supervised by internal employees, who are nominated for reasons of their particular expertise and training competence; and
 - b) off-the-job training provided at the NABARD Staff College;
- iii) Overseas training should be open to nominations from all officer grades and places allocated on the basis of training need rather than seniority.
- iv) NABARD's annual training plan and budget, to include programmes from all sources, should be examined and approved by the Training Advisory Committee.

9.086 Evaluation of effect of training from time to time deserves attention. The contents of all training courses should continue to be validated with the association of the participants immediately after the completion of the course by way of confidential questionnaire to provide appropriate feed back to trainers on course delivery. The questionnaire should be approved by the Training and Manpower Development Division which should also develop appropriate methodology for judging the impact of training subsequently at the field level.

9.087 NABARD may consider these suggestions made by the Consultants V in their Report and take appropriate action. We endorse the recommendations of the Consultants that NABARD should

- i) undertake a detailed analysis of training needs at all levels within the organisation
- ii) develop a co-ordinated approach to the management of training,
- iii) improve the design and delivery of training programme, and
- iv) establish a core of professional trainers.

9.088 The Consultants have proposed that the management of training of NABARD's own staff should be separated from that for client-banks. This seems to be appropriate since training for NABARD's own staff is a service activity for it alone to be pursued in keeping with its goals and objectives, while client-bank training is an operational activity for the banks. However, the need for co-ordination between the NABARD staff college in Lucknow established in 1986 and client-bank training institutes should be recognised. Client-bank training is a key programme for the effectiveness of NABARD's role in institutional development and needs special attention.

ii) NABARD's role in imparting training to client banks

9.089 At present NABARD's role in imparting training to client banks takes the following forms :-

- i) Deliver training, primarily through BIRD, and
- ii) Monitor the number of courses and participants at the JLTC of the SLDBs, through the Training Division and RO Training Cells. (Details of the existing training arrangements supported by NABARD are dealt in Chapter XIII.

9.090 For imparting training to client banks in the proper manner, the needs of these banks which are responsible for training their own staff have to be assessed. Client banks expect NABARD to support their own training capacities. The Consultants V have in particular identified the need for NABARD's support in curriculum development and training of trainers.

9.091 NABARD has been given a clear mandate in training for client banks. It remains to interpret this mandate in terms of precise objectives and activities which meet the needs of the client banks for training support. NABARD's specific objectives for client bank training have been specified by the Consultants V so as to provide a professional training advisory service to assist and guide client banks in making training more effective, deliver specific training programmes where client banks lack the necessary resources, develop the capabilities of the internal training institutions of the client banks, and monitor and evaluate the overall effectiveness of client bank training for rural credit.

9.092 According to the Consultants V, NABARD's main responsibilities should be to carry out the following professional training support activities, namely to :-

- a) develop curricula for use in client banks' training institutions including both training material and selection of methods.
- b) identify organisational training needs of individual client banks and assist in developing methodologies for the analysis of functions and individual training needs.
- c) assist in selecting and developing the faculty of client bank training institutions.
- d) assist the client banks in evaluating the effects of their training programmes and thereby monitor and evaluate the overall effectiveness of client bank staff training for rural credit.

9.093 These activities should be carried out in a participative manner to ensure that NABARD's assistance can ultimately be replicated by the banks using their own resources. In course of time, NABARD should continuously assess its activities as an apex institution for client bank training as the training capabilities of client banks improve. NABARD may also undertake to impart training in the form of workshops and seminars on rural credit for the benefit of senior officials of client banks and government agencies. While NABARD should step in to fill the gap wherever the training institutions of commercial banks are under-developed, the direct training by NABARD could be gradually phased out as the commercial banks develop their own training capacities and capabilities. NABARD then, apart from its other activities and responsibilities in this area, can become an institution for training the trainers.

9.094 We have also examined if there is any overlap in the activities of BIRD and RBI's CAB, which also runs courses in agriculture and rural banking but find that there is a difference between BIRD and CAB, in as much as the composition of clientele with CAB concentrating on commercial bank officers, RBI Officers and senior staff of co-operative banks, and BIRD's focus on RRB officials. As pointed out in Chapter XIII, BIRD will henceforth be freed of its responsibility to train RRB officials, and hence we have recom-

mended that it should concentrate on high level research in rural credit. The Consultants V, have, however, suggested merger of BIRD and CAB. But CAB which has continued to remain with RBI as a result of a policy decision taken jointly by the RBI and NABARD has since acquired a recognised international dimension to its work. CAB also conducts higher level workshops and seminars for senior banking and public sector officers. The existence of both BIRD and CAB as separate entities is in our view, well justified on the grounds of the magnitude of the training task in rural banking which cannot be met by BIRD or CAB singly. Considering the specific roles played by these two training institutions, we do not consider merger of these two to be appropriate. There is an advantage in retaining the international image built up by CAB undisturbed. There could, however, be closer co-ordination between BIRD and CAB with their respective areas of functioning broadly demarcated so as to avoid an overlap in their activities.

9.095 As suggested by Consultants V, NABARD may consider setting up the client bank training division within the Institutional Development Department in the Head Office which should be responsible for policy formulation and national planning for client bank training. There is no need, however, for a separate and specialised unit for client bank training at the ROs.

9.096 In the light of foregoing, NABARD may initiate appropriate action on the recommendations of the Consultants V.

Other Issues

(i) Research and Development Fund (R & D)

9.097 R & D fund was established under Section 44 of the NABARD Act to undertake studies and applied research on agriculture and rural development topics in order to develop innovative approaches and scheme adequately justified on technical and economic grounds. The R & D Fund is also expected to strengthen the efforts of NABARD's client banks in preparation, appraisal, monitoring and evaluation of projects to be financed either wholly or partly through NABARD.

9.098 NABARD has drawn up and published "General Principles and Guidelines" for the use of the R & D Fund covering institutions eligible for grant, assistance, procedures for submission and approval of proposals and the various

activities which can be covered by the proposal.

9.099 A diverse range of proposals are received by the R & D Fund. These are reviewed and approved according to the Consultants III, without any apparent link to clearly defined strategy, objectives or priorities. While the R & D Fund approved 40 proposals involving financial assistance of Rs.231 lakhs since its inception, the cumulative disbursements upto June 1987 were only Rs.168.44 lakhs. With an accumulated balance of Rs.25 crores, just the annual interest earning of R & D Fund could exceed the cumulative disbursements. Some of the key activities financed through R & D Fund include conferences, seminars and workshops; strengthening of Technical, Monitoring and Evaluation (TME) Cells in client banks; research studies and projects.

9.100 The Consultants III have recommended that the R & D Fund should be used much more imaginatively and aggressively to identify, evaluate, develop and promote new and practical initiatives in rural development. A number of recommendations in this regard have been made in their report.

9.101 A detailed strategic action plan may be developed for the use of the R & D Fund for identified priorities which should include :

- i) Financing indepth studies of selected sectors (e.g. non-farm) and selected regions (e.g. North-Eastern India) in order to formulate comprehensive IRD type programmes;
- ii) training of executives and staff of client banks in standardised/improved accounting systems and practices;
- iii) assistance through consultancy services to develop and implement comprehensive Institutional Reinforcement Programmes; (renamed as ISP by us)
- iv) assistance to client banks to strengthen their monitoring, evaluation and inspection systems and procedures; and
- v) financing, supervision, co-ordination and implementation of a long term computer strategy for the agricultural credit sector.

9.102 We agree with the views expressed by the Consultants III on the strategy and priorities for the use of R&D Fund. The NABARD should extend liberal

assistance from the fund on a priority basis to client banks particularly the co-operative banks viz. SCBs, CCBs and SLDBs in strengthening their monitoring, evaluation and inspection systems and procedures. Assistance for institutional development is one of the important purposes envisaged for the R & D Fund. Funding the formulation and monitoring of IRD type schemes should also receive similar priority. We have made recommendations in the relative chapters about R & D assistance for the proposed Primary Co-operative Development Fund to be set up at the SCB level, for supporting the institutional Strengthening Programme (ISP) etc. NABARD may accordingly modify its guidelines to facilitate assistance in the manner envisaged by the Consultants/ this Committee.

(ii) Implications of other recommendations on NABARD

9.103 As we have noted in the first section, the NABARD operates within certain policy constraints which pertain to the overall rural financial systems over which it does not have direct influence. We have made several recommendations for the removal of these constraints and to strengthen the institutional credit system in the country. These when implemented will make a marked favourable impact on the NABARD's capacity to operate more efficiently and effectively.

9.104 We have recommended merger of RRBs with their sponsor banks. Consequently, NABARD's current efforts - both manpower and financial resources - extending for this system of rural lending will no longer be necessary in future. We feel that the resources so freed could be meaningfully utilised by NABARD to support other promotional activities, particularly relating to co-operatives.

9.105 Thus, the thrust of our report has been on the creation of viable institutional structure for rural credit. With the implementation of various recommendations we have made in this chapter and elsewhere, we hope that the NABARD will emerge as a true leader of the credit system comprising of commercial banks and co-operatives - a strong and viable national development bank true to the spirit with which it was conceived by the then policy makers.

Resources and Profitability

(i) Projections for refinance from NABARD

9.106 In the chapter on 'Supply of Agricultural Credit - Estimate of Resources', it has been said that in 1994-95 and 1999-2000 the credit systems will have in the aggregate a deficit of Rs.5,487 and Rs.21,426 crores vis-a-vis the estimated demand for credit with 5 per cent increase in the output costs. The credit systems i.e. co-operatives as well as the commercial banks will naturally look up to NABARD for refinance for making good the deficit. However, the draft on NABARD resources will not be limited to these amounts only. It will be higher for the following reasons :

- (i) The LDBs which have no resources of their own depend totally on NABARD for resources for their term lending operations.
- (ii) NABARD refinance is available to both the credit systems in the case of term lending irrespective of whether the credit institutions have a deficit of resources or not. The commercial banks avail of its refinance more for reducing the cost of resources than for raising the resources as such.
- (iii) NABARD refinance is available to co-operatives and RRBs for financing a part of their crop loans also.

In other words, the figures showing the deficit in supply of resources in Chapter XXIII and the projections of lendings by NABARD discussed here will not exactly tally. The lending programme of NABARD, in fact, is for an amount larger than the deficit for the reasons explained above at Rs.15,079 crores and Rs.26,389 crores for 1994-95 and 1999-2000 respectively.

Crop Loans

9.107 In the Chapter on 'Demand for Credit - Projections', the demand for crop loans for both commercial and co-operative banks by the end of 2000 A.D. has been estimated at Rs.53,534 crores. The share of commercial banks and co-operatives therein has been estimated at 50 per cent each i.e. Rs.26,767 crores. Since the commercial banks will have adequate resources, it is not envisaged that they would seek refinance from NABARD for their involvement in crop loans. At present also the NABARD does not grant refinance to commercial banks for their involvement in crop loans. We do not consider any change necessary in this policy. As regards the co-operatives which are even at present getting refinance from the NABARD subject to

certain conditions being fulfilled will continue to depend on NABARD for a part of their requirements. We have noticed that over the years the dependence of co-operatives on refinance from NABARD is gradually declining although during the three years 1986-87, 1987-88 and 1988-89 the refinance provided has sharply increased. The increase was due to, as explained earlier in Chapter VI, specific special programmes entrusted to co-operatives. As at the end 1985-86 the dependence was only to the extent of about 25 per cent of the loans outstanding at the primary agricultural credit society level. In view of the measures suggested elsewhere in this report, as well as the initiative taken by NABARD to make involvement in agricultural loans remunerative, we are of the opinion that by 2000 AD the co-operatives in many States will be self-reliant, though in certain underdeveloped areas/states they may continue to depend on NABARD refinance. Overall, we feel, the dependence may not be more than 10 per cent of the outstandings at the aggregate level i.e. Rs.26,767 crores. On the basis of this assumption, the NABARD may have to provide refinance to the co-operatives to the extent of Rs.2677 crores as against Rs.1308 crores provided in 1985-86. This would be done by NABARD as at present by obtaining the funds from the general line of credit available from the Reserve Bank of India. We further recommend that RBI should continue to provide this general line of credit to NABARD as hitherto.

Investment Credit

9.108 NABARD had aimed at an average growth rate of refinance of 12 per cent per annum during the VII Plan. Its refinance support increased from Rs.703 crores during the the year of its inception i.e. 1982-83 to Rs.1482 crores in 1987-88. Considering the enlarged role assigned to NABARD in agricultural sector as well as in the non-farm sector, NABARD will have to provide refinance support in an increasing manner during the next 10-12 years.

9.109 We have in Chapter XXII detailed the demand for credit in different sub-sectors of agriculture and allied systems. As we see, the demand for developmental activities in the non-farm sector will increase fast through a sub-sectoral shift that the Indian Agricultural system will experience during the next decade. NABARD has therefore to step up its growth rate in traditional and emerging new sectors by launching new innovative schemes which hold promise of growth, particularly in non-farm sector. It is this sector

which will emerge as a more demanding sector on NABARD for resources - financial and technical:

9.110 NABARD may have to continue its involvement in Minor Irrigation and IRDP as the major components of its programme. Though some areas in a few states are beginning to reach saturation levels of ground-water extraction, there are vast areas in most states where such development has a long way to go. Also, pumpsets installed to lift water are about 55 per cent of the total number of wells. Minor irrigation will, therefore, continue to absorb its historical share of total credit. Farm mechanisation, mainly tractors, has been due to a deliberate policy to restrict refinance is taking a declining share of refinance. This policy has to be continued although the demand, by all accounts, is far higher than what NABARD has been able to allocate to this sector. Refinance for IRDP has been around one-third of the banks' entitlement. A major reason for this short-drawal is the difficulty experienced by the commercial banks in gathering information regarding disbursements to establish branch eligibility for further refinance. Banks are bound to streamline their procedures in course of time and seek larger quantum of refinance, as they stand to gain from NABARD's low-interest refinance. Higher growth rates therefore in the VIII Plan for land-based activities falling under these three traditional categories have to be planned. NABARD's role envisages a significant step-up effort in most other traditional sectors allied to agriculture and exploration of new areas, such as financing farmers for the conveyance of water from Government outlets in major and medium irrigation projects, watershed-based dryland farming in rainfed districts, farm forestry and waste land development schemes to fill the growing gap in the fuel-wood requirements of rural areas and raw material needs of user industries and non-farm rural activities linked with marketing outlets.

9.111 We have estimated the demand for term credit as Rs.14,954 crores, Rs.29,450 crores and Rs.57,339 crores at the end of 1989-90, 1994-95 and 1999-2000 respectively. The shares of commercial banks and co-operatives will be as under :

	1989-90	1994-95	(Rs. crores) 1999-2000
Commercial banks (65 per cent)	<u>9,720</u>	<u>19,143</u>	<u>37,270</u>
Co-operatives (35 per cent)	<u>5,234</u>	<u>10,307</u>	<u>20,069</u>
Total	<u>14,954</u>	<u>29,450</u>	<u>57,339</u>

9.112 The above figures represent the term loans outstanding at the ultimate borrowers' level. Generally, NABARD sanctions refinance to the extent of 75 to 90 per cent of schematic lending by banks. Apart from the margin thus to be provided at 10 to 25 per cent by banks, the lendings not covered by specific schemes are not refinanced by NABARD. Thirdly, overdues at the borrowers' level are absorbed by the banking systems. The net result of all these factors will be that not more than 50 per cent of the outstanding loans will have to be refinanced by the NABARD. At the end of 1985-86, NABARD refinance formed 41 per cent of the term loans outstanding at the borrowers' level. On this basis the draft on NABARD for refinance of term loans in the context of projections made by us above will be as under

Projected NABARD Refinance outstanding in the years	(Rs. crores)		
	<u>1989-90</u>	<u>1994-95</u>	<u>1999-2000</u>
	7,477	14,725	29,669

The position of resources of NABARD that will have to be raised to refinance these estimates are discussed below.

9.113 As against these estimates, NABARD has itself made some estimates regarding its refinance support during the VIII Plan with a view to supporting a higher demand of credit in the traditional areas as well as in the emerging new thrust areas. The financial projections of NABARD are given in brief below.

Demand for resources	(Rs. crores)	
	<u>1988-90 (2 years)</u>	<u>1990-91 - 1994-95 (VIII Plan)</u>
Loans and advances to be issued	3904	18,531
Repayments	<u>350</u> 4254	<u>750</u> 19,281
<u>Supply of Resources</u>		
Recoveries of loans	2147	10,283
Contribution from RBI to NRC (LTO) fund	660	1,650
Contribution to NRC (LTO) fund by NABARD out of its profits	675	2,568
Borrowings from GOI	<u>208</u> 3,690	<u>-</u> 14,501
Deficit	564	4,780

9.114 There is no indication as to how this deficit will be filled in but it will have to be filled in either by borrowing from market or Government of India or in the alternative slow down on refinance schemes a bit. Further, it may be noted that the above estimates represent "flows" of funds and not "stock". Our estimates in this report have been on the basis of 'stock' i.e. loans outstanding. There is, therefore, some difference between the two sets of estimates as the total term loans issued during a period and the loans outstanding at the end of the period could not be the same. Our own estimates not only for the VIII Plan but also for the IX Plan are as under.

	(Rs. crores)		
	<u>1989-90</u>	<u>At the end of</u> <u>1994-95</u>	<u>1999-2000</u>
Refinance from NABARD	6,831	15,079 (+ 8,248)	26,389 (+ 11,310)

Our annual projections and the basis on which they are made are furnished in table 5.

9.115 The above projections show an increase in lendings of Rs.8,248 crores by 1994-95 over the level in 1989-90 and additional Rs.11,310 crores during the next five years ending 1999-2000. To meet these estimated lendings the principal sources of funds to NABARD as suggested by the Consultants III are :

- a) Continuing contributions from RBI profits to LTO and Stabilisation Funds.
- b) Market borrowings.
- c) Counterpart funds from World Bank/IDA as and when available.
- d) NABARD's own profits.
- e) GOI/RBI additional contributions to NABARD's LTO Fund.

Our own proposals on the future resources of NABARD are given in the following paragraphs. As would be seen, we are in general agreement with the Consultants' proposals except the suggestion regarding additional contribution to NRC Funds by RBI/Government of India. Recognising the limitations on the part of RBI/GOI to provide free resources on such a large scale, we have proposed to substitute it with borrowings from GOI/RBI at a concessional rate of 5.5 per cent.

Table 5

Term lending for agriculture - Projections of NABARD Refinance

(Rs. crores)

Outstanding on 30th June	1984-85	1985-86	1986-87	1987-88	1988-89	1989-90	1990-91	1991-92	1992-93	1993-94	1994-95	2000
1.	2.	3.	4.	5.	6.	7.	8.	9.	10.	11.	12.	13
A. <u>NABARD Refinance</u>												
1. CBs	1,807	2,181	2,421	2,688	3,825	4,440	5,157	5,991	6,999	8,247	9,801	17,152
2. Co-operatives	1,526	1,719	2,040	2,386	2,059	2,391	2,777	3,226	3,769	4,441	5,278	9,237
3. Total	<u>3,333</u>	<u>3,900</u>	<u>4,461</u>	<u>5,074</u>	<u>5,884</u>	<u>6,831</u>	<u>7,934</u>	<u>9,217</u>	<u>10,768</u>	<u>12,688</u>	<u>15,079</u>	<u>26,389</u>
B. <u>Total Term Lending</u>												
4. CBs	5,136	5,649	6,213	6,834	7,517	9,720	11,178	12,854	14,781	16,998	19,143	37,270
5. Co-operatives	ø 3,531	3,884	4,272	4,699	5,168	5,234	6,018	6,917	7,955	9,152	10,307	20,069
6. Total	<u>8,667</u>	<u>9,533</u>	<u>10,485</u>	<u>11,533</u>	<u>12,685</u>	<u>14,954</u>	<u>17,196</u>	<u>19,771</u>	<u>22,736</u>	<u>26,150</u>	<u>29,450</u>	<u>57,339</u>
Percentage 4 to 1	35.18	38.60	38.96	39.33	50.88	45.68	46.13	46.61	47.35	48.75	51.20	46.02
5 to 2	43.21	44.25	47.75	50.77	39.84	45.68	46.14	46.64	47.37	48.52	51.21	46.03
6 to 3	38.45	40.91	42.54	43.99	46.38	45.68	46.14	46.62	47.38	48.52	51.20	46.02

Note to table 5.

A)

- a) Figures of outstanding for the period from 1984-85 to 1987-88 are actuals taken from NABARD Annual Reports. (A - 2 to 5)
- b) Figures of outstanding from year 1988-89 to 1994-95 have been arrived at after adding and subtracting commitments and resources respectively taking the figures of 1987-88 as a base, indicated in table 5 of this Chapter in the proportion of 65:35.
- c) Figures of outstanding for the year 2000 have been arrived at after taking into account annual growth rate @ 15 per cent per annum from 1994-95.

B)

- a) Figures shown under Col. 2 of B are actuals taken from Currency & Finance Report - 1984-85.
- b) Figures of term lending for the period 1985-86 to 1988-89 have been arrived at after assuming 10 per cent growth rate. Figures for term-lending for subsequent period are taken from tables 17 and 22 of Chapter XXIII.

9.116 We are confident that NABARD can raise the required resources somewhat on the following basis. They represent increased outstandings under each head.

	<u>1994-95</u>	(Rs. crores) <u>1999-2000</u>
1. RBI contribution at Rs.400 crores p.a. in VIII Plan and Rs.450 crores p.a. in IX Plan	2,000	2,250
2. NABARD's profits	2,600	4,000
3. Market borrowings	800	1,300
4. Borrowings from RBI or GOI at 5.5 per cent	2,248	2,760
5. Counterpart funds of IBRD/IDA	600	1,000
	<u>8,248</u>	<u>11,310</u>

9.117 There could be some problems in raising resources under items 3, 4 and 5 and to that extent there will remain a deficit uncovered. We, however, strongly recommend to RBI and Government of India to support the activities of NABARD adequately. The impact of funding the resources in this manner is discussed later under heading "profitability".

9.118 The funding of additional resources required to finance the projected lending programme during the VIII and IX Plan are given above in para 9.116. The assumptions on which the funding has been suggested are as under :

- (1) Even recognizing certain constraints RBI will contribute Rs.400 crores per year during the VIII Plan and Rs.450 crores per year in the IX Plan period. This indicates an increase of Rs.50 crores during the VIII and IX Plans over the level during the preceding Plan period.
- (2) Market borrowings are assumed at 10 per cent of the total funding amount.
- (3) The overall short-fall in the resources will be raised by NABARD by way of concessional borrowings from RBI/GOI at 5.5 per

cent interest. If these assumptions are compared with the assumptions of Consultants (III) for model No.2 it will be seen that they are, more or less, alike. In fact, the assumptions made by us are slightly more favourable to NABARD to maintain its profitability. For example, the Consultants have suggested that the short-fall would be made good by GOI by loans at 6.5 per cent, we are suggesting the interest rate at 5.5 per cent which is the break-even point as per the Consultants. Secondly, the RBI contribution to NRC funds has been assumed at Rs.375 crores by the Consultants during the entire 10 year period, while we have assumed it at a slightly higher level, which will fetch additional cost free resources of Rs.500 crores to NABARD over the 10 year period. The model No.2 indicates that the profits of the NABARD will be Rs.615 crores in 1994-95 and Rs.831 crores in 1999-2000. We have, in fact, assumed a marginally lower level of profits though on the basis of assumptions made by us which are more favourable to the NABARD's profitability, the profits may be, in fact, slightly higher. We may, therefore, mention that if the resources required are funded in the manner suggested by us in para 9.126, the profitability of NABARD will not be adversely affected.

- (4) Under the above assumptions NABARD's profits during the VIII Plan and IX Plan are estimated at an average of Rs.520 crores and Rs.800 crores respectively per year.

Profitability

9.119 In the scheme of things envisaged by CRAFTICARD, NABARD was to start off with substantial resources at its disposal to meet the challenges of agricultural and rural credit. NABARD was endowed with, at its birth itself, in addition to the share capital of Rs.100 crores, the assets and liabilities of ARDC and also the NAC Funds of the RBI to the extent of Rs.1390 crores. These transferred Funds, being cost-free resources and though not share capital per se, can be considered on par with equity. Reckoned this way, the NABARD enjoyed a very favourable debt-equity ratio which has been continuously improved upon by transferred profits of the RBI as well as NABARD's own to the NRC Funds, besides the building up of substantial

reserves again out of NABARD's profits.

9.120 In addition to its equity funds, NABARD has drawn on various lines of debt funding. The three major sources are RBI, which provides all of its ST requirements, GOI which is on-lending WB/IDA funds on a counter-part basis and Open Market borrowings in the form of debentures. The latter two forms of borrowings supplement its equity in its investment credit operations.

9.121 The Consultants III have reviewed the balance sheets of NABARD for the years 1982-83 to 1986-87 and observed that as a result of the transferred National funds in the very first year NABARD which started with a favourable Debt-Equity Ratio of 1.35 : 1 has been able to improve upon the same every year leading to a even more favourable ratio of 0.81 : 1 in 1986-87. With such high equity, NABARD has been able to operate very profitably and as a result, as rightly observed by the Consultants III, its own profits have become one of its most important sources of funds. Higher equity funding is of even greater importance in the context of, as pointed out by the Consultants III, the basic imbalances in its interest rate structure. In the year 1986-87, again as observed by the Consultants III, 46 per cent of NABARD's schematic disbursements for MT & LT was at 6-1/2 per cent besides almost 86 per cent for diversified purposes to the small farmers also at the same rate of 6-1/2 per cent, while about 70 per cent of the short term disbursements to the SCBs was at 7 per cent or lower. Thus, if one reckons the overhead cost of lending, most of NABARD's loans funded by debt is loss making. In other words, NABARD owes its profitability solely to the high equity component of its resources base. Stated differently, when NABARD expands its operations in future, based on debt, its profitability will decline and even result in losses depending upon the rate at which its favourable equity position is eroded.

9.122 Obviously any growth if substantially funded by borrowings in the present interest rate structure would not only erode NABARD's profitability but also as a consequence adversely affect its capacity to ploughback substantial amounts to its lendable resources. The Consultants III have examined the implications of the NABARD's growth in the context of the present

interest rate structure for borrowings as well as lendings and have presented 3 models of its operations in their report (see attached tables 6, 7 and 8).

9.123 The major assumptions on which Consultants III have worked out the three models are as follows :

Model 1 : An annual growth rate of 14 per cent and resources met from RBI and GOI at levels similar to historic ones and the shortfall in funding is met from market borrowings. (Table 6)

Model 2 : With the same annual growth as at Model 1, market borrowings restricted to growth of 10 per cent annually and the shortfall made up by GOI loans at 6-1/2 per cent. (Table 7)

Model 3 : No significant increase in available funds and market borrowings allowed to grow only by 10 per cent annually. (Table 8)

9.124 The following comments have been made by the Consultants on the models. Firstly, as expected, funding the lending expansion from borrowings erodes NABARD's profitability. In Model 1 profits begin to decline in 1994 and NABARD makes its first operating loss in the year 2000; even with concessional borrowings from GOI allocations (Model 2), NABARD will eventually go into losses paying interest at a rate of 6-1/2 per cent. It will also be noted that the quantum of such budget allocations has to be considerable and has to increase each year. The scenario in Model 3 ensures profitability for NABARD but at the cost of a reduced growth rate growth progressively declining from the annual rate of 14 per cent in 1988-89 to just over 8 per cent by 1999-2000. The Consultants have come to the conclusion that either NABARD must grow at a rate low enough or most of that growth has to be funded from profits and equity injections from RBI and GOI or further free or very low cost funds will need to be found. In the context of the projections made by us earlier for NABARD's lendings for 1994-95 and 1999-2000, we feel that model No.2 will be more appropriate for considering NABARD's profitability

9.125 There is no alternative source, according to the Consultants III, in the present interest rate environment, to GOI and/or RBI, and they have recommended the adoption of a formula based method of calculating additional

equity contributions to be made annually, when necessary by RBI or, as an allocation of the Central Government budget. The formula would be based on the average cost of funds to be raised by NABARD in each year to meet anticipated demands where the average cost of these funds (including profits) will exceed NABARD's break even point (this is approximately 5-1/2 per cent), RBI/GOI will be called upon to make an additional contribution to the LTO Fund of sufficient amount to reduce the average cost of funds to be raised in the year to no more than the break-even point. As an illustration, based on the growth and interest rates used in Model 1, the quantum and timing of these equity contributions has been worked out by Consultants III as follows :

<u>Year</u>	(Rs. crores)
	<u>Equity contribution</u>
1988 - 89) to) 1992-93	Nil
1993-94	30
1994-95	145
1995-96	285
1996-97	480
1997-98	680
1998-99	905
1999-2000	1145

If growth rates exceed these levels, or borrowings carry higher rate, correspondingly such equity contributions will have to be enhanced under this formula. They have recommended that the NABARD's share capital may immediately be raised by Rs.200 crores (50:50) by contribution of Rs.100 crores each by RBI & GOI) and the needed budget provision for the same may be made. We note in this connection that NABARD has already moved the GOI for share capital contribution as well as for soft loans/grants out of budgetary resources for meeting NABARD's lending programme for the year 1989-90. We would only urge expeditious consideration by both GOI and RBI for stepping up the resources of NABARD in the form of soft loans and contributions to share capital and LTO Fund as indicated by us earlier in para 9.119.

9.126 The impact of the changes in crop loan interest rates announced in the Budget of 29 February 1988 (as also on 28 February 1989) had not

been included in the models but the Consultants have observed that if as a result it is necessary to further reduce NABARD's margins, the effect will be to accelerate the timing of the additional share capital/LTO contributions, and to increase the amounts that will have to be contributed. NABARD has since forgone its margin of 1 per cent in the General Line of Credit from RBI. This has no doubt an adverse impact on NABARD. Firstly, there would be a reduction in interest receivable and secondly, there would be a further gap in funding need to be filled through additional borrowings resulting in increased interest payable. This would reduce NABARD's profits according to the Consultants, to the area of about Rs.10 crores in 1988-89, and in 1994-95 by Rs.27 crores. The consultants have, however, not reckoned the loss of income to NABARD on the conversion loans granted out of its National Stabilization Fund. Since such loans carry the same rate of interest as crop loans, the interest loss is between 2 to 4 per cent on the loans granted out of Stabilization Fund. This again reinforces the Consultant's conclusion that reduction in margins and business expansion through borrowed funds will rapidly erode NABARD's profitability and hence merits serious consideration for expanding NABARD's equity base (share capital) and/or larger contributions by GOI/RBI to the LTO Fund, if the reasonable growth rate in schematic lending, as projected above is to be facilitated.

Concluding Observations

9.127 The NABARD was established in 1982 to give a new thrust and direction to the rural credit delivery system in the country so that the emerging credit needs of integrated rural development could be met satisfactorily. The bank has now run through a span of seven years during which it has made significant progress in giving refinance for the development of agricultural credit projects through the three credit systems of commercial banks, regional rural banks and co-operatives the volume of refinance substantially increasing year after year. The thrust in this area has however, to be accompanied simultaneously by strengthening the credit system without which the refinance will have failed to achieve its desired objective of increasing agricultural production, and raising the level of rural economy. As the foregoing review would show, the NABARD has not been able to fully live up to the high expectations of the then policy makers for several reasons. Although it could achieve quantitative expansion in refinancing the client banks,

it has not yet become the real driving force of the rural credit system, as was envisaged. We feel that there are certain areas in which the NABARD has to take fresh initiatives if it is to emerge as a strong development bank for rural regeneration.

9.128 Firstly, the NABARD should concentrate more on the building up of the co-operative credit delivery system, viz., the rehabilitation of the DCCBs and the healthy functioning of PACSs as deposit-attracting and self-financing business units, for which we have made several recommendations elsewhere in this report. Many of the commercial banks' branches also operating in rural areas need to be strengthened to enable them to absorb and monitor credit more effectively. This we consider is the most important area of responsibility of the NABARD without which the cycle of credit flow and recovery would not be complete and the system blossom forth as a self-reliant and self-sustaining mechanism. Secondly, the NABARD should improve its functional capabilities in project identification, preparation, appraisal and monitoring and ensure that its client banks are equipped to perform these functions more effectively. In particular, the NABARD and client banks should improve their project monitoring activities such as obtaining the prescribed returns, and ensure proper use of credit and recovery of loans to enable the ultimate borrowers to realise the full potential from the sanctioned projects. The weakness in monitoring is due to lack of control over the credit agencies, even the commercial banks. The NABARD can acquire and develop the necessary clout over these institutions initially with the help of and co-ordination with the Reserve Bank which as the central bank of the country and the licencing authority has a better grip over the client banks, mandatory and even otherwise. In course of time, however, NABARD will have to evolve its own image to enforce the required discipline in this area as well as in other areas where the Reserve Bank has found it necessary to issue directions. Thirdly, the NABARD should be able to forge a better linkage between its inspection function and development function. In other words, the findings of inspections should be better utilised to strengthen the client institutions. Inspections will have little meaning unless, following the implementation of their findings, the client bank or branch improves its organisational and operational capabilities and emerges as a dynamic service link between the lender and the beneficiary. Fourthly, NABARD

should pay greater attention in extending refinance and developing the non-farm sector in areas like waste lands, afforestation programmes, financing the artisan class and agro-processing industries. Fifthly, NABARD has not only to ensure that its own staff is fully trained in the several aspects and areas of project programming but should share the responsibility with the Reserve Bank in ensuring and co-ordinating the training of the personnel of client banks, (with appropriate refresher courses), so oriented as to primarily meet its own needs also. Sixthly, the bank should extend its network to the district level with the appointment of an officer in each district who should associate himself with district credit planning and assist the client banks in programming the rehabilitation of weaker units, particularly the co-operatives. Finally, NABARD will have to play its part in open market borrowing also, despite several difficulties which it may face in raising resources through sale of bonds, as it may have in future to face a resource crunch if it were to depend for the purpose wholly on outside agencies, which might affect its projected programmes.

9.129 We feel that NABARD has a long way to go in fulfilling its mandatory objectives and responsibilities. We are confident, however, that basically a financially strong institution like NABARD should be able to cover considerable ground in the next decade or so with the active participation of the Reserve Bank and the assistance of the newly proposed National Co-operative Bank. The former viz. the Reserve Bank should impart to the NABARD its strength in the formulation and implementation of all broad policy issues and the latter viz. the National Co-operative Bank should assist it in reaching the base level units of the co-operatives whose confidence it would enjoy better, in reinforcing their structure and building their strength through a comprehensive health programme.

Table 6
Financial position - Model I

	<u>1990</u>	<u>1995</u> (Rs. crores)	<u>2000</u>
BALANCE SHEET			
Loans	8770	16887	32514
Investments	1400	1650	2000
Other assets	482	929	1788
	<u>10652</u>	<u>19466</u>	<u>36302</u>
Capital	100	100	100
Reserves*	2212	4489	5435
LTO and Stabilisation Funds**	3960	5760	7635
	<u>6272</u>	<u>10349</u>	<u>13170</u>
Borrowings - GOI	2166	2916	3666
RBI	1181	1656	2323
Debentures	855	4265	16540
Deposits	77	109	149
Other liabilities	101	171	454
	<u>10652</u>	<u>19466</u>	<u>36302</u>
SOURCES AND APPLICATIONS OF FUNDS			
Profits*	413	433	(96)
LTO and Stabilisation Funds**	325	375	375
Borrowings - GOI	150	150	150
RBI	77	108	152
Debentures	235	1140	3620
Deposits	5	7	9
Other liabilities	5	25	77
	<u>1210</u>	<u>2238</u>	<u>4287</u>
Advances	1078	2074	3993
Investments	73	50	75
Other assets	59	114	219
	<u>1210</u>	<u>2238</u>	<u>4287</u>
INCOME AND EXPENDITURE			
Interest receivable	771	1327	2381
Interest payable	298	759	2200
Overhead expenses	57	118	244
	<u>355</u>	<u>877</u>	<u>2444</u>
New profit before R+D expense	416	450	(63)
R+D expense	2.5	17	33
Net profit	413	433	(96)

* inclusive of transfer to LTO and Stabilisation Funds from NABARD's own profits.
** RBI Contributions only.

Table 7

Financial Position - Model 2

	<u>1990</u>	<u>1995</u>	<u>2000</u>
	(Rs. crores)		
BALANCE SHEET			
Loans	8770	16887	32514
Investments	1400	1650	2000
Other assets	482	929	1788
	<u>10652</u>	<u>19466</u>	<u>36302</u>
	=====	=====	=====
Capital	100	100	100
Reserves*	2220	4911	8642
LTO and Stabilisation Funds **	<u>3960</u>	<u>5760</u>	<u>7635</u>
	6280	10771	16377
Borrowings - GOI	2336	5660	15300
RBI	1181	1656	2323
Debentures	680	1100	1765
Deposits	77	109	149
Other liabilities	<u>98</u>	<u>170</u>	<u>388</u>
	<u>10652</u>	<u>19466</u>	<u>36302</u>
	=====	=====	=====
SOURCES AND APPLICATIONS OF FUNDS			
Profits*	421	615	831
LTO and Stabilisation Funds**	325	375	375
Borrowings - GOI	320	1010	2700
RBI	77	108	152
Debentures	60	100	160
Deposits	5	7	9
Other liabilities	<u>2</u>	<u>23</u>	<u>60</u>
	<u>1210</u>	<u>2238</u>	<u>4287</u>
	=====	=====	=====
Advances	1078	2074	3993
Investments	73	50	75
Other assets	<u>59</u>	<u>114</u>	<u>219</u>
	<u>1210</u>	<u>2238</u>	<u>4287</u>
	=====	=====	=====
INCOME AND EXPENDITURE			
Interest receivable	<u>771</u>	<u>1327</u>	<u>2381</u>
Interest payable	290	577	1273
Overhead Expenses	57	118	244
	<u>347</u>	<u>695</u>	<u>1517</u>
Net Profit before R + D expense	424	632	864
R+D expense	<u>2.5</u>	<u>17</u>	<u>33</u>
Net profit	<u>421</u>	<u>615</u>	<u>831</u>
	=====	=====	=====

* Inclusive of transfers to LTO and Stabilisation Funds from NABARD's own

** Profits.
RBI Contributions only.

Table 8

Financial Position - Model 3

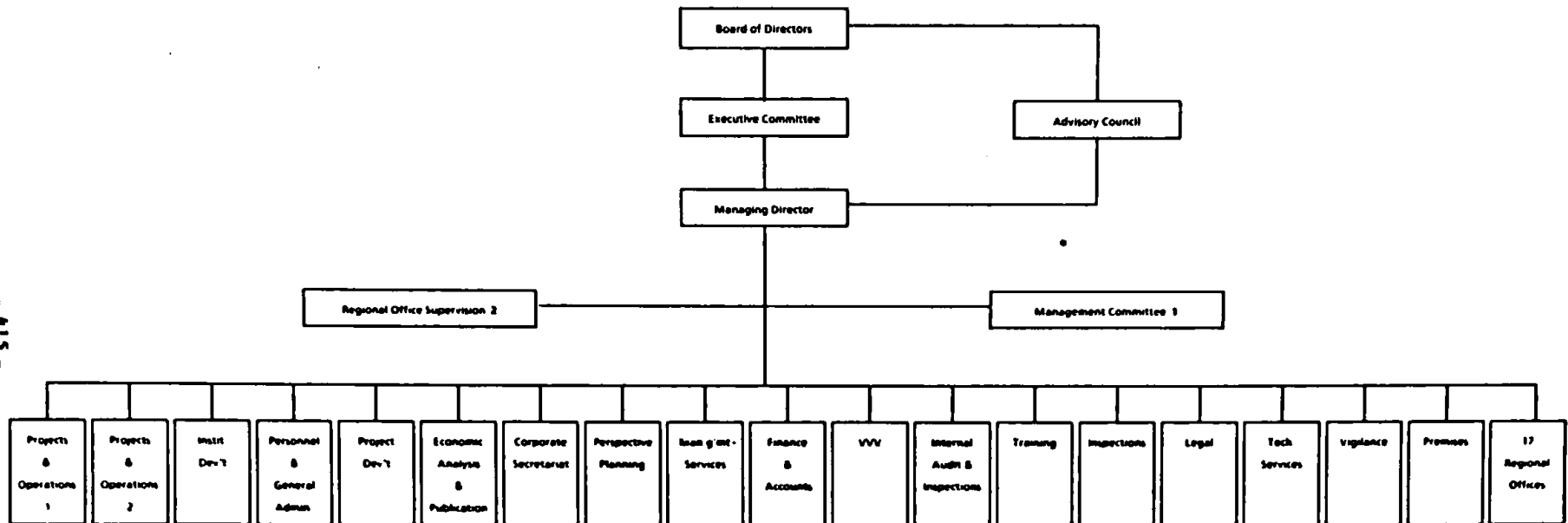
	<u>1990</u>	<u>1995</u>	<u>2000</u>
	(Rs. crores)		
BALANCE SHEET			
Loans	8620	14290	21660
Investments	1400	1650	1900
Other Assets	470	785	1190
	<u>10490</u>	<u>16725</u>	<u>24750</u>
Capital	100	100	100
Reserves*	2228	4968	8954
LTO and Stabilisation Funds**	3960	5760	7635
	6288	10828	16689
Borrowings - GOI	2166	2916	3666
RBI	1181	1656	2323
Debentures	680	1100	1765
Deposits	77	109	149
Other liabilities	98	116	158
	<u>10490</u>	<u>16725</u>	<u>24750</u>
	=====	=====	=====
SOURCES AND APPLICATIONS OF FUNDS			
Profits *	428	637	915
LTO and Stabilisation Funds**	325	375	375
Borrowings - GOI	150	150	150
RBI	77	108	152
Debentures	60	100	160
Deposits	5	7	9
Other liabilities	3	8	9
	<u>1048</u>	<u>1385</u>	<u>1770</u>
	=====	=====	=====
Advances	928	1265	1630
Investments	73	50	50
Other assets	47	70	90
	<u>1048</u>	<u>1385</u>	<u>1770</u>
	=====	=====	=====
INCOME AND EXPENDITURE			
Interest receivable	1763	1162	1673
Interest payable	280	411	575
Overhead expenses	53	100	162
	333	511	737
Net Profit before R+D expenses	430	651	936
R + D expense	2.5	14	21
Net profit	428	637	915
	=====	=====	=====

* inclusive of transfers to LTO and Stabilisation Funds from NABARD's own profits.

** RBI contributions only.

Chart - I

Organisation chart of NABARD Head Office (as at 15 January 1988)



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Notes: 1 All heads of department and independent division (24 members)
2 Chief General Managers

Chart - II

Recommended functional organisation structure for NABARD Head Office

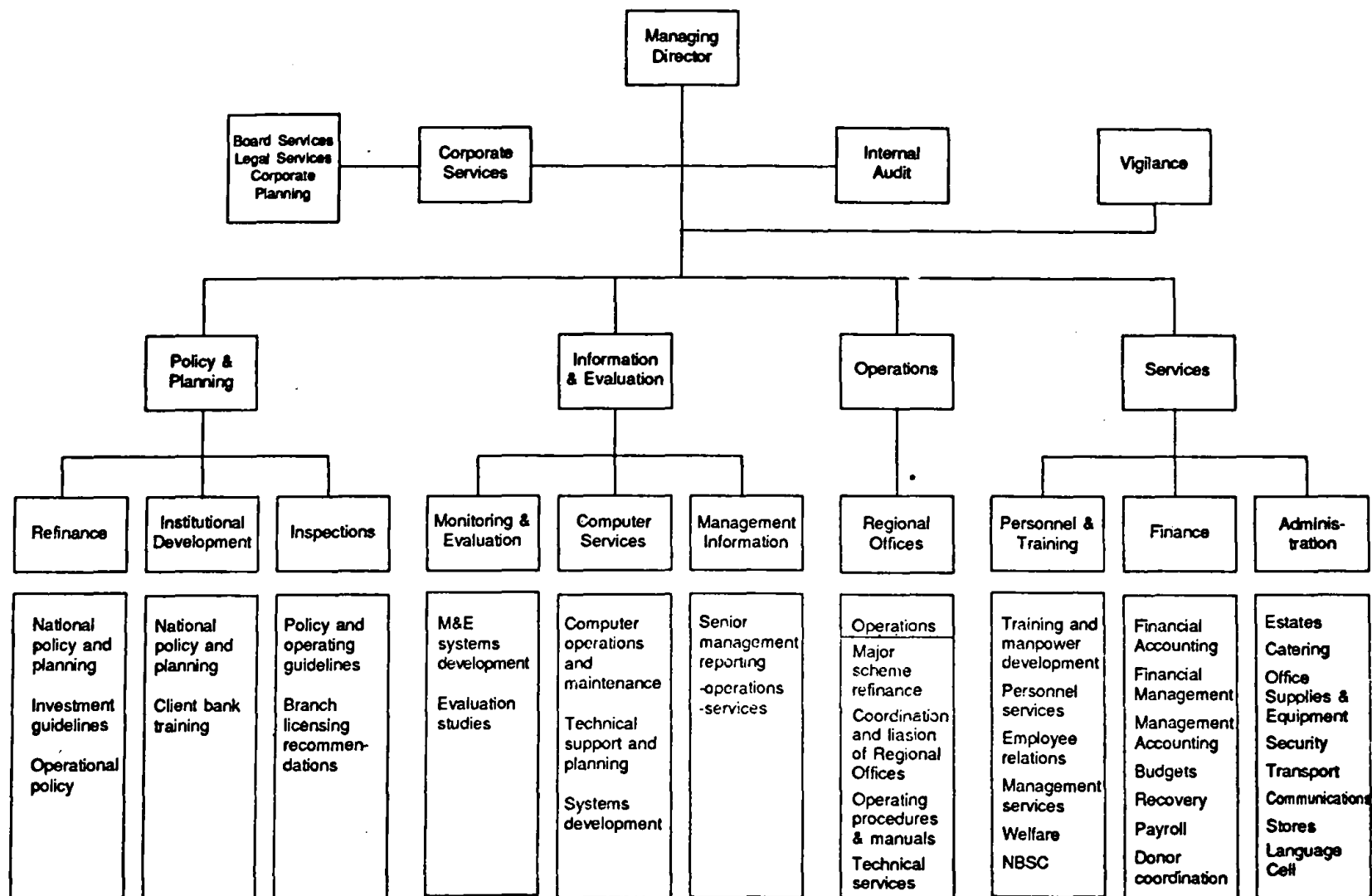
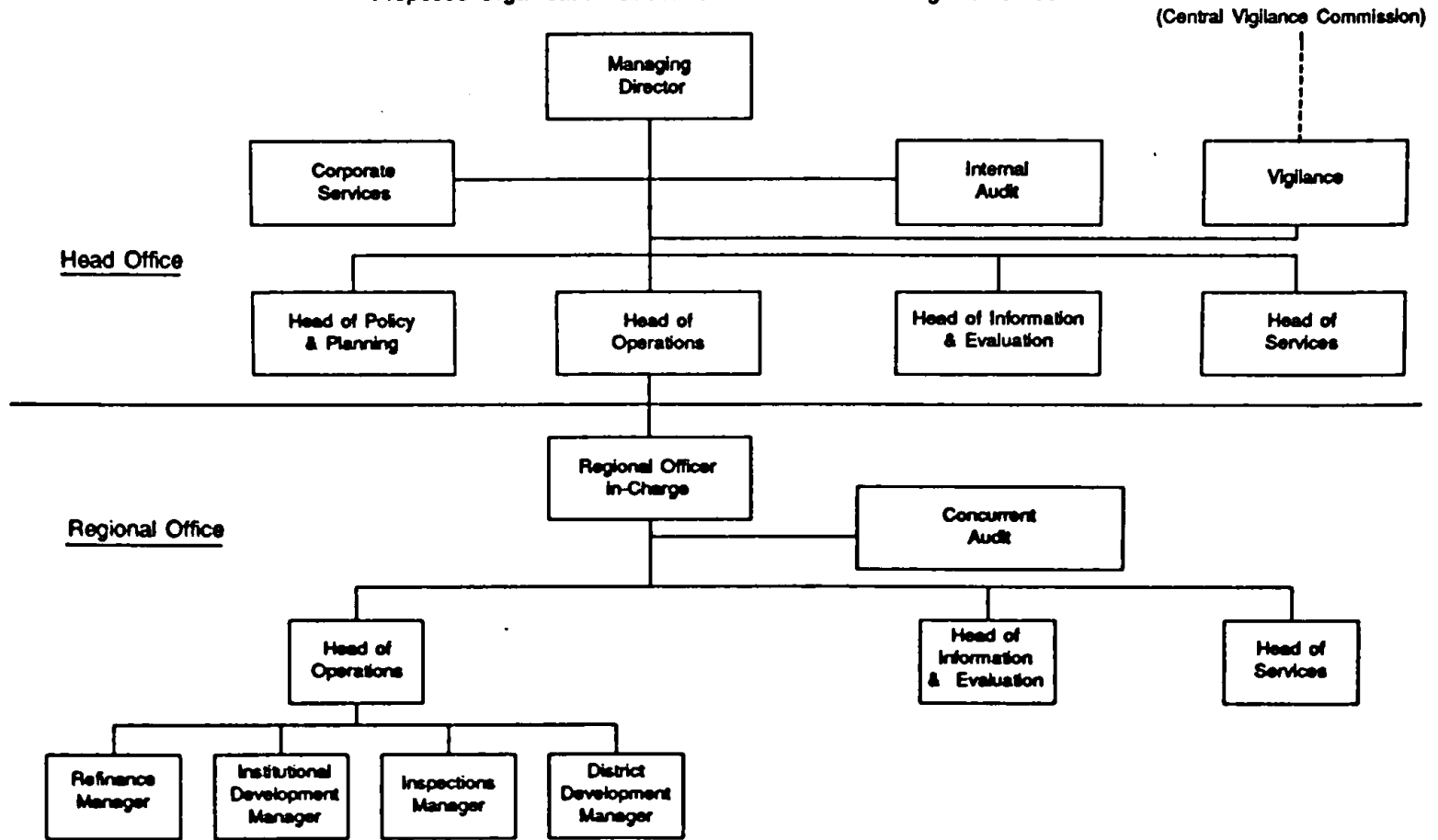


Chart - III
Proposed Organisation Structure-Head Office and Regional Office



Note : No grades or designations are implied by the position in organisation structure.

PART III

STRENGTHENING OF AGRICULTURAL CREDIT SYSTEM

- X DEVELOPMENT PLANS AND CREDIT PLANNING
 - XI REGIONAL IMBALANCES : SOME CORRECTIVE MEASURES
 - XII PROGRAMME FOR INSTITUTIONAL STRENGTHENING
 - XIII STAFF TRAINING AND MANPOWER DEVELOPMENT
 - XIV ACCOUNTING SYSTEMS AND POLICIES, COMPUTERISATION
AND MANAGEMENT INFORMATION SYSTEMS
-

CHAPTER X

DEVELOPMENT PLANS AND CREDIT PLANNING

In a credit system which is becoming increasingly sophisticated, its present weaknesses notwithstanding, and is attempting to bring about qualitative improvements in its lending operations, credit planning assumes crucial importance. Such credit planning has to be undertaken not merely at the apex level or even intermediate levels like the regional offices of the credit institutions but more importantly at the grass root level as well, viz., bank branches and co-operative institutions. But credit planning and the blue prints evolved for such planning from time to time seem to have so far made no serious dent at the level of actual formulation and implementation of credit plans.

10.02 Some of the deficiencies noticed in the existing district credit plans brought out by our Consultants I, II & III are as below :

i) The quality of statistics required for credit planning at the grass-root level is far from satisfactory. Little reliable data are available about production, marketing, equipment, income-estimates, transportation, village and cottage industries - most of the sectors for which credit plans are to be formulated. The quality of statistics affects the quality of the credit plans. Unless the concerned Government Departments and banks realise the value of accurate statistics for planning and set about compiling reliable time series, the credit plan estimates based on these statistics cannot but be tentative. (Consultants II)

ii) The DCPs/AAPs still do not appear to be broken down by categories in sufficient detail. They are an aggregation of credit plans and projections based on the banks' perception of their borrowers' credit needs. In the absence of better targetting by purpose, monitoring under the lead bank scheme can only be a comparison between actual approval/disbursements and the DCP/AAP projection. Results of lending, as distinct from mere disbursements, are not monitored or evaluated. (Consultants III)

iii) Another problem is the unwieldy size of the DLCCs and SLBCs, which makes meaningful discussion practically impossible. To solve this problem,

some core working groups were formed at the district and state levels to thrash out key issues and to prepare a tighter agenda and background papers before the meetings. Detailed notes of meetings are often not kept although they are essential to inform participating banks of agreements reached and implementation required. The large number of participants in these forums make any indepth discussion and coverage of issues difficult. (Consultants III)

iv) AAPs/DCPs are not being dovetailed with district development plans as these were not made available to the lead banks. The AAPs/DCPs were formulated on the basis of broad estimates received from different developmental agencies and were thus not prepared on the basis of development schemes as such. (Consultants I)

v) Disaggregating of AAPs into the branch specific action plans is not yet being done with the result that AAPs are still not becoming fully operational documents integrated into the business plan of the banks. (Consultants I)

vi) On the whole, AAPs are, of late, formulated in an arithmetical manner. Hardly any new economic schemes are added in the AAP. Further, the sectoral achievements are lopsided. Under IRDP there is too much stress on performance under the service sub-sector rather than on agriculture and industry. The AAPs still remain more or less a statistical exercise in so far as there is imbalance observed in achievements in the different sub-sectors on account of conscious efforts of investments in specified sectors. It is observed that the overall percentage achievements under the AAPs are mainly because of over fulfilment of services sub-sector targets. Other sectors, more particularly agriculture, do not receive the attention they deserve. (Consultants I)

vii) The provision of infrastructural facilities including supply of inputs, power, transport, marketing and extension service, so necessary to ensure the successful implementation of development programmes are very poor. (Consultants I)

viii) Co-ordination among rural credit agencies and also between banks and development agencies is weak. The extent of co-operation and assistance received by banks from the official development agencies in the implementation of programmes at the micro level is inadequate. (Consultants I)

ix) The unsystematic lending under government sponsored programme assessing the demand for various activities and services has led to under utilisation of assets and lower than anticipated income from various investments. On account of these factors, the impact of the lead bank scheme on the overall growth of the district economies has been rather modest. Most beneficiaries could not realise the full benefit of bank credit because of the weak backward and forward linkage. (Consultants I)

10.03 Credit planning is important in terms of :

- i) foreseeing and forecasting credit demand, and indeed the creation of credit demand;
- ii) providing resources to meet the demand through the mobilisation of deposits and other resources as well as refinance;
- iii) avoidance of waste and the deflection of surplus funds of one sub-sector to another and of one region to another;
- iv) effective formulation of schemes and projects including infrastructure construction, and effective lending and successful recovery of loans.

10.04 In this Chapter, however, an attempt is made only to suggest the broad outlines of credit planning at various levels in terms of a methodology and we would suggest that further details in pursuit of this methodology and its implementation would have to be provided by the various banking institutions and the administrative machinery of governments in conjunction with each other, under the guidance of RBI.

10.05 The key point to note is that a District Credit Plan (DCP) must emerge from the District Development Plan (DDP) and a Block Credit Plan (BCP) from the Block Development Plan (BDP). Credit Planning is ineffective if it is not backward linked with a development plan in physical terms and if it is not forward linked, via credit disbursing agencies, with the credit using agents - the farmers, the village professionals and artisans, the rural industrialists and the infrastructure builders, both governmental and private.

10.06 We have examined the state of district planning in the country in some detail and we find that while some exercises have been undertaken and some are in the process of evolution in the Planning Commission and

other official bodies, no clear blue print with a methodology of district planning has so far emerged.

Decentralized Planning

10.07 It has often been argued that rural development planning must not be imposed from the top but should be evolved from the bottom at the grass root levels. This is an excellent idea and may well become feasible in due course. But in the current state of data and information at the village and the block levels, it is most appropriate to begin development planning at the district level and let the district plan be split into block plans and village plans, meanwhile commissioning the accumulation and analysis of data at the grass root levels. When such base level information and data get collected on a regular basis, the ground will have been prepared to commence grass root level planning and to let it work upwards to the state and regional levels. Until then development planning at the district level is the most feasible and workable. The district development plan can of course be administered downwards to the block and the village levels, even as the district credit plan which evolves, from the district development plan, can be so administered at the lower levels.

10.08 In the heyday of community development strategy during the 1950s, an attempt was made to assess the felt needs of the people at the village level in terms of the items which they desired at the village level during a five-year period. Through questionnaires and other means people would then specify their requirements for minor irrigation projects, dams, village approach roads, clinics, schools and other felt needs. But these were merely needs and had no relation with the availability of resources to fulfil these needs. When all the needs for a given village, for the aggregate of villages in a block and the aggregate of blocks in a district were totalled up, they would add up to something phenomenally large which could not be accommodated within the available resources. The felt needs had to be so heavily pruned that the resulting allocations towards these needs bore no relation quantitatively to what was originally asked for. After this experience it was felt necessary to start realistically with the assessment of resources available at the state level both from state and Central sources and then allocate these resources on certain norms of population endowments, potential, project costs etc.

to different districts and blocks. That is where, basically, development planning stands at present.

10.09 After the experience of seven Five-Year Plans and considering the need to bring planning closer to the people, it should now be possible to shift crucial decision-making in a decentralised fashion from the state to the district level. This is feasible because currently economic and social data do exist at the district level. The districts have Statistical Officers as well as departmental functionaries and subject matter specialists and it is possible to upgrade quickly the statistical system at this level without much loss of time. Decision making in terms of development planning can be decentralised further in the years to come, but only as the statistical and information systems are commissioned to collect and analyse block level and village level data.

District Development Plan

10.10 In this country, a development plan has essentially meant a projection, in time-chunks of five years, of (a) the levels of different activities i.e. targets, that could be achieved at the end of the period and (b) the investment required to support and generate the targeted level of activities. Our development plans are thus targets of outputs and targets of investments in different sectors and sub-sectors of the economy. This targeting of outputs and investment is currently done at the national and the state levels and the state targets are then broken up into sub-targets for districts and blocks, etc. Once it is decided to decentralise planning and shift its focal point to the district level, a district development plan would be seen as a projection (targets) of various economic activities in the district over a five-year period, and a similar target for investment activity during that five-year plan.

10.11 Using the best techniques of projection available to us, it should be possible to begin with an assessment of the present level of each economic activity and project each activity to the target date. But unlike the National Plan or the state plans which have so far concerned themselves only with planning of output and investment by the Central and the state governments and public enterprises, leaving private sector planning only to broad guidelines and indications, the district plan of current vintage would have to concern itself with the targeting output and investment both for public and private

functionaries. If a district plan, and a block plan which emanates from it, does not target for private farm output and investment, especially when all farming is in private hands and if it does not indicate targets for the activities run by rural artisans, professionals and small industrialists, it is not worth having. Targeting of such activities will be based on an assessment of endowments in the district, and will include changes in land utilisation, cropping pattern, irrigation, rural industrialization, electrification, infrastructural developments, technology improvements as well as institutional developments.

10.12 Based on existing levels of activity and endowment potential, when production targets, with the aforementioned changes, are estimated, these production targets become the first part of a district development plan. Then with the knowledge of the additional investment required in each line of activity per unit of additional output (the marginal capital-output ratio), the production targets can be converted into investment targets i.e. additional capital required over the five-year period for each activity in order to generate the required additional output. One does not have to have estimates of these capital-output ratios afresh in each district for a given activity. In a whole region of structural similarity where the input-output relations and the capital-output relations are approximately alike, the same ratios will do and the knowledge of these co-efficients already exists both with governmental authorities and financial institutions. We can thus obtain both the production targets and the investment targets for each activity at the district level as far as private production operations are concerned, be these of farmers or of rural artisans and professionals or of rural and small industrialists. However, in order to obtain the targets of private production activity as well as private investment activity like bunding, drainage, well-sinking, electrification, provision of tools, designs, transport equipment etc., a good deal of governmental investment would be necessary. This will consist of infrastructural investment in earthen dams, other minor irrigation facilities, local power plants, animal breeding centres, market structures, roads and other transport facilities and, indeed, structures for services of health, medicine, literacy, schooling and vocational training etc. While governmental authorities at the district level would have to plan the governmental infrastructure for the district activity from the government's own resources, we are concerned here with the infrastructure construction by private operators as well as input availabilities also for private operators like farmers, artisans and rural industrialists which

will be financed through credit from banking institutions i.e. commercial bank branches, co-operative societies and co-operative land development banks.

District Credit Plan

10.13 Once a district development plan in real terms is available, it has to be converted into a district credit plan. The bankers as well as governmental authorities know by now the credit requirements per unit of output in different sub-sectors of the rural economy. Scales of finance have already been worked out in different organisations even though they may not have been worked out too efficiently and can be revised. Using the input requirements for targeted outputs and the requirements of farm labour, private transportation, storage and marketing etc., targets of output and physical investment can be converted into credit targets and the summation of these credit targets at the district level is the District Credit Plan.

10.14 While converting the district development plan into a district credit plan, the availability of resources which the banking system can effectively mobilise through deposits and refinance has to be realistically assessed. If the available resources are not sufficient to meet all the identified bankable projects based on the district development plan, it may be necessary to accord priority to certain projects and type of projects to be included in the credit plan within a given time frame. Thus, a meaningful conversion of a district development plan into a district credit plan would have to take into account the availability of

- i) projects that are financially viable and bankable,
- ii) resources within the banking system to meet the credit needs of identified projects, and
- iii) resources that the government can mobilise to create the necessary infrastructure for successful implementation of these projects.

We would stress here also the desirability of the state governments preparing the district development plans without which the district credit plans cannot be formulated on a realistic basis.

The Mechanism for District Development Plans and District Credit Plan

10.15 The objectives of a District Development Plan are to obtain a set of physical targets of output and investment for different activities over

the stipulated period and to pursue the achievement or implementation of these physical targets. The objective of a credit plan is to convert these physical targets of output and investment in each activity into their credit equivalents, and to pursue their achievement and implementation.

10.16 Experience has shown that economic development planning is a technical exercise but to become meaningful and effective it has to have an economic content, an administrative/organizational content, a social content and an input of popular wishes and aspirations. Without these a development plan is lifeless or virtually dead before it is born.

10.17 These considerations require that the district development plan which already has a stipulated allocation of spendable resources to be received from the State Plan, be designed in full co-operation and interaction in socio-politico-economic-administrative group. This may consist of the Chief Executive Officer of the district (the Collector or the District Magistrate), the subject-level specialists or departmental functionaries at the district level, the Statistical Officer, the popular representatives such as the Chairmen of Panchayat Samitis in the district, the representatives of the other banks working in the district and the Chairman/President of the district co-operative central bank. Some other functionaries can be added suitably. Using the blue print of the state five-year developmental plan broken up into small plans for the district and within the limits of the financial allocation made by the state and the Centre, this group, to be called the District Planning Committee, under the chairmanship of the chief executive officer of the government (District Magistrate/Collector) will prepare the district development plan. In due course, through the sharing of experience of different districts and watching the angularities and faults emerging in time, the methodology and techniques of plan making would be improved. Popular representatives as well as other functionaries will go through a process of education in district planning and will begin to make better plans later, if not in the beginning.

10.18 When it comes to the conversion of the physical development plan of the district into a credit plan, the District Credit Planning Committee will take over the physical plan along with the magnitude of financial allocation and convert it into a credit plan for different activities or sub-sectors. It is important that such credit planning is done not only for APS but also for

AIS and AMPS. This District Credit Planning Committee may consist of the Chief Executive Officer of the district, the subject specialists i.e. the departmental functionaries, the Chairman of the District Panchayat Samiti, the lead bank officer, the representatives of other banks functioning in the district, the Chairman of the district co-operative central bank and some other functionaries suitably added.

10.19 The function of this credit planning committee will be to develop a linkage between the physical development plan and the credit plan to work out credit targets for each sub-sector, to split the credit allocations for each sub-sector into schemes and projects especially those which cut across different blocks within the district, and to decide which part of investment activity required in the district plan will be undertaken by the government, with its own resources, for infrastructural construction (like irrigation, roads, power generation facilities, health clinics, hospitals, colleges, technical schools, training centres, animal breeding centres, market structures, public storage constructions, etc.) and which activity will be placed in the private sector within the district.

10.20 Once the district credit plan is available separately in terms of investment targets for the government and the credit targets for private investment as well as production activity in different sub-sectors, the credit plan will be split by this District Credit Planning Committee into separate sub-totals for each block.

Block Level Planning

10.21 In the next stage, the block planning committee will take over the block part of the district development plan as well as the block part of the district credit plan, along with the activity targets for production and investment credit in different sub-sectors of the block economy.

10.22 The block planning committee may consist of the block development officer as chairman, together with the block Sarpanch and the popular representatives of the block panchayat organisations, the chairmen of all the co-operative societies working in the block, the heads of the land development bank branches working in the block and indeed the managers of the lead bank and all other branches of commercial banks working in the block as well as some other relevant functionaries.

10.23 This block planning committee, which must also have its smaller version for day-to-day operations, under some such name as the block credit management committee, will be concerned with identifying and devising schemes and projects within the block and setting indicative targets for credit provision in different sub-sectors of the block economy both for schematic lending and for crop and term loans.

10.24 From this point onwards the branches of commercial banks and the PACSs and LDB branches in the block will take over the block credit plan and begin to implement it. They will give credit to prospective borrowers in different sub-sectors as the borrowers approach these financial institutions. But they will also go out of their parlours through their field staff and contact potential economic functionaries in the block and canvass good projects, schemes, term loans and crop loans. They would have to involve the population in the implementation of the block credit plan.

10.25 It needs to be borne in mind that the credit targets at the block and the district level for each sub-sector are only indicative targets. If the planning has been good and realistic, the loans requested by the borrowers will approximate to the targets in each sub-sector. But should good projects, schemes and demands for term and crop loans emerge over and above the target for a sub-sector, it should not be the intention of the block credit plan or the district credit plan to put a straight-jacket on these projects. Internal adjustments, both plus and minus, are very much in order so long as the totality of the credit plan is not exceeded at the block or the district level beyond the stipulated margin. Such elasticity is absolutely essential as the spirit of district planning and block planning is not to restrain the activity but to encourage and expand it. Revision of targets in half-yearly and annual meetings as well as in five-yearly discussion should also be possible.

Role of Lead Bank

10.26 With the institution of District Development Planning and District Credit Planning, the Lead Bank of the District acquires a key role at the district level. In addition to its present responsibilities, a new dimension is added to the working of the Lead Bank and the Lead Bank Officer becomes a key functionary at the district level together with the Chairman of the District Central Co-operative Bank and would have special responsibilities :

- i) to serve as a key member of the District Planning Committee in evolving the District Development Plan;
- ii) to serve as a key member of the District Credit Planning Committee and assist in the formulation of the District Credit Plan;
- iii) to collect financial data and credit information from all the banks functioning in the district and make these available to the District Planning Committee and District Credit Planning Committee even as information and data for the co-operative banking system would be provided by the Chairman of the District Central Co-operative Bank and the Land Development Banks;
- iv) once the District Credit Plan is made and allotted to different blocks in the district, to serve as Chairman of the District Banking Committee and co-ordinate and supervise the implementation of the block plan and allot the credit allocation given to the commercial banking sector among the different commercial banks functioning in the different blocks;
- v) together with the Chairman of the District Central Co-operative Bank and the District Land Development Bank, to co-ordinate the credit allocation in the commercial banking and the co-operative banking sectors;
- vi) to monitor the implementation of the District Credit Plan and the Block Credit Plan as operated by various commercial banks within the district; and
- vii) to evaluate from time to time the ground level changes that are taking place in the economy and the economic activity of the district and the blocks, essentially as a consequence of credit disbursement and to pass this information to the District Credit Planning Committee and the District Development Planning Committee.

With the added functions and responsibilities, the Lead Bank Officer at the district level would, as we see it, emerge as the kingpin in the District Credit Planning exercise.

Role of RBI and NABARD

10.27 We have discussed the concept of LBS in Chapter III on "Commercial Banks and Rural Credit". The main focus of LBS has been on District Credit Planning. The overall directions and guidelines in this regard have been the

responsibility of RBI. In our view, RBI should continue to be in charge of Rural Credit Planning at different levels under the new DAA suggested by us. However, we see a need for more active collaboration of NABARD in credit planning exercises at different levels i.e. district, state and national. At the district level a designated officer of NABARD should associate himself with the various machineries created for credit planning at that level, since NABARD has a crucial role to play in the formulation and implementation of projects. Such active collaboration among LB, RBI and NABARD will help in reconciling resources estimates in assessing institutional capabilities and performance in rural credit operations, and in converting the estimates given by banks and governments into realistic schemes.

From Service Area Approach to Development Area Approach

10.28 We are in broad agreement with the service area scheme recently evolved by the Reserve Bank of India with a view to strengthening the rural lending operations of the commercial banks. The essential feature of the scheme is that every village in the country will be allotted to one commercial bank or another and will be serviced effectively by a branch of that Bank. But in our view it seems necessary to somewhat widen the scope of the scheme. As we see it, the scheme should encompass a re-ordering of the branch network of commercial banks, inclusion of the co-operative banking system as a partner in the scheme, and keep in view the total development of the command area. In other words, the service area approach should be graduated to 'development area approach' and in the process bring about also a rationalisation of the branches of the various commercial banks, so as to avoid wastage of resources and effort.

10.29 In the post-1969 period of bank nationalisation, the commercial banks have made a tremendous inroad in the rural-agricultural sector and a most impressive achievement has been registered in terms of establishing branches in far-fetched areas and extending institutional credit to farmers and non-farmers who could not have dreamt of being recipients of agricultural credit at reasonable rates of interest and wholesome conditions of credit. This was in marked contrast to the prevailing usurious rates of interest in the non-institutional sector and the most onerous and extortionist conditions of credit which accompanied these rates in the non-institutional sector. As we have noticed, as on December 1986 there were 53,397 branches of commer-

cial banks (including RRBs) in the country, of which 29,766 or 56 per cent were in the rural-agricultural sector. The credit disbursed by commercial banks to priority sector as on March 1988 amounted to Rs.28,463 crores, compared to Rs.441 crores in June 1969. In consequence of this phenomenal extension of institutional credit disbursement at reasonable interest rates, the non-institutional interest rates have come down substantially even though they are still high, and by far the larger proportion of credit is being obtained by farmers and non-farmers in rural areas from the commercial and the co-operative banking systems as well as the RRBs. Even in terms of serving the weaker sections of the community, the record of commercial banks is most commendable. As on March 1988 Rs.7,310 crores of credit i.e. 11.8 per cent of total credit given by the commercial banking system went to this category.

10.30 With all these achievements, the commercial banking activity today still leaves a great deal to be desired and attention has now to shift from the quantitative to the qualitative aspects of banking. This requires giving a new dimension to deposit mobilisation, a new concept of service and development lending and new functions and methods for loan recovery in order to minimise overdues and bad debts. On the whole, the recycling of credit is in bad shape today in all systems of banking in the country including the commercial banks. This recycling which consists essentially of resources mobilisation, effective lending and successful recovery, has to be re-established on a higher growth path. The service area scheme which purports to take care of many of these concerns, will cater substantially to these objectives by allotting each village to a specific commercial bank branch and by introducing the concept of efficient service in the agricultural-rural sectors. But we find that many other structural improvements have yet to be made and a new approach, as we shall presently spell out, requires to be adopted. These structural changes together with the new developmental approach can well be captioned as Development Area Approach to Banking and hence we stress that the future approach to agricultural rural banking inclusive of the service area improvement should be designated as Development Area Approach. This is really necessary before the service area scheme can come into its own. If the service area strategy is to deliver the goods and serve effectively, then, even as each village is allotted to a commercial bank branch, a block would have to be allotted to one commercial bank instead of many. A block is an area of approximately 100 villages on an average and is currently served by several branches of

several commercial banks. In numerous blocks the presence of several commercial banks often with a sparse and isolated presence of merely one or two branches is a disturbing commentary on the somewhat irrational expansion of commercial banking in the country. It was right that many banks which were previously burrowing regionally should extend their services in other regions and in fact become national banks in many cases. It was also right perhaps that several banks should have their branches in many districts in the country. But it was not right that several banks should have a very small number of branches in many blocks of the country. It was a misunderstanding of the idea of a multi-agency system and in fact a great detraction from the efficacy of multi-agency system that one bank should have four branches, another two branches and yet another one branch in a given block.

10.31 The essence of the multi-agency system is that every borrower and depositor should have a choice of institutions to approach and that the credit institutions themselves should have a competitive rather than a monopoly situation in which to operate. These conditions are adequately met if it is provided that the borrowers and depositors of every village have access to a co-operative as well as a commercial bank branch and furthermore that they have access to another branch of the same commercial bank within or just outside the block and, for that matter to another commercial bank at the district centre, or, indeed to any commercial bank branch anywhere. It was certainly not required that every block in the country should have several branches of several commercial banks functioning simultaneously. Such an extensive multiplicity detracts from the effectiveness of the multi-agency system as it denies scale economies, cost efficiencies, effective field operation and supervision, as we shall presently see. As all nationalised commercial banks in the country have the same structure of deposit interest rates and lending interest rates and are subject to the same rules, procedures, directives and guidelines from the Reserve Bank and NABARD, competition among the commercial banks is a rather restrictive concept in this country. It is, of course, true that different attitudes to rural lending emanating from the head office and zonal offices of different commercial banks might prevail. Besides, some personality factors and individual behavioural attitudes on the part of bank branch staff might make for differential treatment to customers. But these factors can be taken care of, not necessarily by setting up another branch of another commercial bank in the block but by providing access to

customers to a co-operative bank as well as a commercial bank branch, by providing a machinery for the redress of grievances through easy access to the managers and the supervisory staff within the block, providing access to another branch of the same bank within or outside the block and indeed through removing the restrictions on access to a branch of another bank outside the block or anywhere within the district.

10.32 The trouble with the multiplicity of branches of different banks in the same block is that if one bank has four branches in a block, another has two branches and yet another has one branch in a block, the cost of supervision becomes quite enormous. Supervisory staff may come from the district or regional offices, spend a little time in the area of a branch or a few branches and may not visit the branch again for a considerable length of time, because of the time and cost involved in frequently visiting distant scattered branches. In fact it has been observed that the transport costs of bank officers constitute a substantial proportion of the operational costs. Staff time and such high overheads involved in these long distance visits have acted as constraints on more frequent branch visits, thereby generally slackening the supervisory system. If, instead, a block were to have several branches of a single commercial bank, this will constitute a critical mass of branches in which some supervisory and field staff could be permanently located. They would be attending to their supervisory and field work in these, say, eight or ten branches continuously and would not be involving the bank in inordinate T.A. and D.A. Supervision and guidance will become continuous and effective with a substantial cost saving. In other words, scale economies would be obtained and more service would be rendered at less cost per unit of service.

10.33 It is a well known phenomenon continuously bedevilling the role of commercial banks that the managers and the staff substantially recruited from urban centres do not wish to be posted in the rural branches and an important factor in this reluctance is the absence of social amenities like schooling for the children, health clinics and hospitals and an absence of interaction with peers and colleagues. Life in rural areas very often tends to be drab and inconvenient. On the other hand, if the commercial bank had 8 or 10 branches and thus had a substantial presence in that area, a collectivity of its branches will be a catalytic factor in the establishment of educational institutions, provision of clinics and health centres at some central points

in the block or at the block headquarters. This will also result in the emergence of private establishments for health and education and indeed in the provision of social interaction among the staff, thus making rural life more attractive, and less onerous. Hence there are substantial pecuniary and social advantages in letting branches of the bank with the largest presence in the block function within that block, and making the few branches of other banks gradually move out of that block to the other blocks allotted to them where they have the largest presence already. We see this homogenization of a block through the operation of several branches of a single commercial bank as a major advantage to the bank as well as to the customers and we regard this as an important attribute of an effective service area or development area scheme. We strongly recommend that even as each village would be allotted to one commercial bank branch, each block should be allotted to one commercial bank. We propose that every block should be allotted to that commercial bank which already has the largest presence through its many branches and that the other banks with smaller presence in a given block should be allotted other blocks where they have the largest presence. Banks may be asked to move out from these blocks where they do not have a large presence and which, therefore, have not been allotted to them.

10.34 We do not wish to make it immediately mandatory on the commercial banks with a small presence to move out of the block. However, gradually, in a finite length of time, say three years, banks should be provided guidelines to shift from blocks of small presence to blocks of predominant presence allotted to them. Some incentives towards these movements could also be thought of, but it is obvious that the banks themselves will see the point of shifting from areas of high cost operations and low efficiency to those of low cost and high efficiency, where they would have a critical mass of branches and would be able to operate more efficiently.

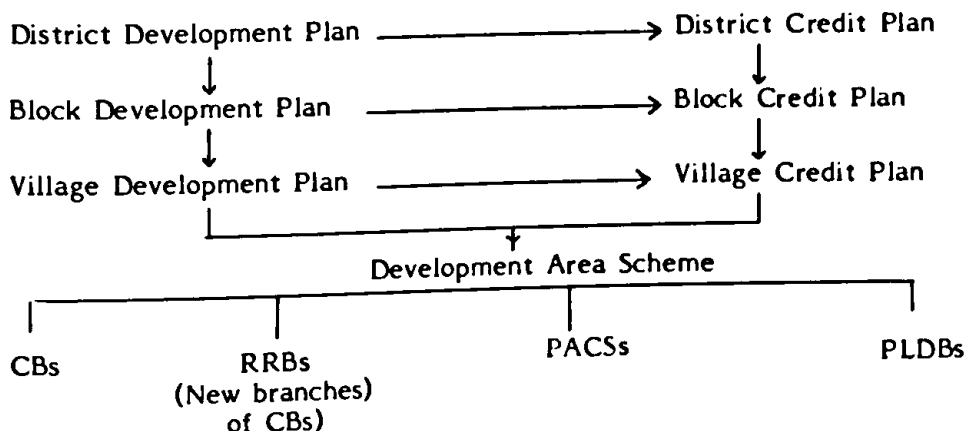
Dovetailing of the Service Area Approach with Development Planning

10.35 An effective service area scheme including both commercial banks and co-operatives is necessary but not a sufficient condition for viable banking operations. It is necessary because it will, in the first place, undo the neglect of certain areas in the last twenty years either because the banks and the co-operatives did not find it profitable to serve there or because of an emphasis primarily on the widening of credit rather than a deepening of it. In the second

place it will impart scale economies, cost effectiveness, homogeneity of operations and social cohesion. The necessary condition would, however, have to be buttressed (i) in terms of an adoption of decentralised district development planning, decentralized district credit planning, block development and credit planning, co-ordination between commercial banking and co-operative banking system within the developmental credit plans at district as well as the block level. And indeed it would have to be buttressed, (ii) through an adoption of development banking approach in place of a mere commercial banking approach.

10.36 In such a developmental approach, emphasis shifts on the one hand to effective savings mobilization through new techniques of financial intermediation and on the other to effective lending, with the banker going out of his parlour to canvass new schemes and projects, tying credits with inputs, inputs with outputs, outputs with repayments and repayments with new lending. The banker thus enlarges the credit continuously but he can do this only by becoming the friend, philosopher and guide of the client at every stage. Again, in a developmental approach, a banker is judged not so much by how much he lent, how well he kept the accounts and how thoroughly he followed the rules and procedures, but by how much he succeeded in changing the economy of the customer and the socio-economic face of the region. In such a development banking an audit becomes not an audit of accounts but an audit of development performance.

10.37 The development planning dovetailing the service area approach, thus envisages both vertical and horizontal linkages at all levels, viz., the district, the block and the village. The emerging linkages are presented in the following diagram.



CHAPTER XI

REGIONAL IMBALANCES - SOME CORRECTIVE MEASURES

The need to reduce regional imbalances has been repeatedly stressed in the successive plans as an important plank in India's development strategy. Nevertheless with development in the diverse fields of production, imbalances have only accentuated more and more rather than mutated. Thus, though there has been substantial development in agriculture in the country in the last two to three decades as a result of introduction of new strategies, the fruits of development have not accrued evenly to different regions. Several factors are responsible for this phenomenon of regional imbalances. There are wide disparities, as between regions, in natural endowments like area under cultivation, agro-climatic conditions, rainfall and irrigation facilities, basic infrastructural facilities, linkages and supporting services which are essential pre-requisites to the production process, leading to variations in agricultural investments by individual cultivators and their transition to new production technology. Consequently, in the regions which lag in the development, the credit absorption capacity has been seriously impaired, culminating in imbalances in the supply of credit as well. An analysis of the factors responsible for the emergence of these regional imbalances and measures contemplated for mitigating them are discussed in this chapter.

Imbalances in Agricultural Development

11.02 Ever since the planning era began in 1951, efforts are being made to bring about agricultural development and to improve agricultural production under various development programmes. Apart from general efforts at land reforms and tenurial security to actual cultivators, land reclamation and development, development of irrigation potential, use of sophisticated inputs and implements, diversification of agriculture, etc. all over the country, various specific programmes such as Intensive Agricultural District Programme (1959) and Intensive Agricultural Area Programme and more recently Special Rice Production Programme, National Oilseeds/Pulses Development Projects have been implemented from time to time for intensive development of important crops. The seed revolution brought about by evolving new strains of cereal crops led to New Agricultural Strategy in 1966-67. All these factors brought about substantial development of Indian agriculture lending to self sufficiency in food-grains.

11.03 However, the development of agriculture has been uneven as between different regions/states. While some parts of the country witnessed a phenomenal transformation in the last two decades and the growth that accompanied it, in some other areas there has been a tremendous lag. Some parts of the country made substantial progress through adoption of improved technology and application of better inputs, whereas other parts have not attracted much of the new technology and investments and hence their potential has remained untapped. For instance, the Eastern region though richly endowed with ground water potential has not attracted much investment while the North-Eastern region is yet to be brought into the main stream of investment and growth.

11.04 First and foremost, there is diversity in the endowment in the natural resources as between different regions. Of the total reporting area of 304.1 m.ha in 1982-83, 141.8 m.ha (46.6 per cent) represented the net sown area. As between different regions, the proportion of net sown area to total geographical area showed sharp variations, ranging from 56.3 per cent in Western region, 49 per cent in Central region, 48.3 per cent in Northern region, 47.1 per cent in Eastern region, 45.5 per cent in Southern region to only 16.2 per cent in the North-Eastern region. Thus there is wide variation region-wise in the distribution of arable land in the country.

11.05 Distribution of land holdings is also skewed due to pressure of increasing population on land. The total number of holdings increased from 49.8 million in 1961-62 to 89.4 million in 1980-81. The average size of operational holdings fell from 2.7 hectares in 1961-62 to 1.8 hectares in 1981-82. In 1980-81 the marginal holdings (below one hectare in size) constituted 56.6 per cent of total number of land holdings with 12.1 per cent share in total operational area. The ratio of marginal holdings to the total holdings in 1980-81 varied from nine per cent in Nagaland to 89 per cent in Kerala. It was higher than the All India average in Assam (59 per cent), Bihar (76 per cent), Jammu and Kashmir (70 per cent), Tamil Nadu (70 per cent), Uttar Pradesh (71 per cent), West Bengal (70 per cent) and Tripura (69 per cent).

11.06 With a view to bringing more area under intensive cultivation and multiple cropping, development of irrigation facilities has been a major plank of agricultural development programmes under the successive plans. The irrigation development programmes have led to an increase in the gross irrigated

area from 23.2 m.ha in 1951 to 52 m.ha in 1982-83 i.e. the share of gross irrigated area to gross cropped area has gone up from 17.4 per cent in 1951-52 to 30.1 per cent in 1982-83. However, region-wise there were large variations in the irrigated area. Central region ranked first with its share of net irrigated area of 31 per cent followed by Northern region (24 per cent), Southern region (19 per cent), Eastern region (13 per cent), Western region (10 per cent) and North-Eastern region (2 per cent). The percentage of irrigated area to the net sown area was more than 50 in 1982-83 in states of Punjab, Haryana and Uttar Pradesh while it was less than all India average of 28 per cent in 16 states and five Union Territories. Region-wise, the percentage of irrigated area to the net sown area was 33 in Northern and Central regions, 27 in Southern and Eastern regions, 22 in North-Eastern region and 14 in the Western region.

Infrastructure and Supporting Services

11.07 Apart from natural resources and irrigation facilities, essential to the development of agriculture are the basic infrastructure, the linkages-backward and forward - and the supporting services. In areas where basic infrastructure has developed and linkages such as arrangements for supply of physical assets/ agricultural inputs, storage, processing, transportation and marketing of produce in the terminal markets, extension and other services are available, the agricultural development could be left to the initiative of the individual farmers. In areas having relatively assured rainfall and fairly high irrigation potential, the progressive farmers are always on the look out for remunerative crops and better methods of cultivation. Public investments could be confined largely, if not mainly, to the areas of agricultural research and extension, efforts for dissemination of information regarding new crops and new farming technology.

11.08 In the less developed areas like Eastern region and North-Eastern region the problem is entirely different. In the Eastern region, farmers' choice and decision making in the production process are greatly constrained by factors which are beyond their control. There are problems pertaining to land tenure, absentee landlordism and actual cultivation either by landless labourers or tenants-at-will or bargadars persists. The agricultural development potential in these areas is quite high as also the irrigation potential but very often the actual tiller, bereft of rights in the land has little incentive or initiative in the development of land. In the Himalayan region characterised by the mountainous terrain and shortage of arable land, the severe winter,

confining agricultural operations to a few months in a year, problems of transportation, etc. make the practice of agriculture considerably difficult. In the North-Eastern region, besides these, there are other problems such as community ownership of land, shifting cultivation, absence of cadastral survey of land which pose difficulties for the credit institutions in granting loans for developmental purposes. Besides, the rural settlements are dispersed and transport and communication difficult in the distant and far flung areas making movement of men and materials minimal. Farmers seldom have adequate access to sophisticated inputs and other supporting services or outlets for their marketable surplus produce.

11.09 The case studies undertaken by our consultants, revealed lack of adequate facilities in these regions for input supplies and related services for marketing of agricultural produce as also agro-processing for providing to the farmers the maximum value out of rural products such as agricultural produce, dairy products, fruits, etc. It was also observed that adequate attention was not being paid for developing the supporting delivery systems. Unless these secondary and tertiary sectors based on agriculture are developed and farmers are able to get reasonable value for their products, commercialisation of agriculture in these areas would be a distant dream.

Adoption of New Technology

11.10 Due to constraints of natural resources, irrigation facilities, defective land tenure system, inadequacy of infrastructure and supporting services experienced in the under-developed Eastern and North-Eastern regions the percolation of technological innovations in agriculture to these regions has been slow and inadequate in comparison with the other relatively developed regions. The farming activity in these regions has to contend with low productivity and low profitability.

11.11 The above factors culminated in the sharply diverse picture of productivity of major foodgrains as between different regions/states. During the triennium ended 1985-86 the all India average yield of rice stood at 1481 Kgs. per ha. The relative productivity of rice was highest in Southern region (1952 Kgs.), followed by Northern region (1887 Kgs.), Western region (1439 Kgs.), whereas the average was very low in North-Eastern region (1176 Kgs.) and in the Eastern region (1169 Kgs.). Between states the diversity was more sharp;

in Assam average yield of rice per hectare was 1097 Kgs., in Bihar 1060 Kgs., and in Orissa 1112 Kgs. compared to 3112 Kgs. in Punjab, 2576 Kgs. in Haryana, 2143 Kgs. in Jammu & Kashmir, 2181 Kgs. in Tamil Nadu and 2098 Kgs. in Andhra Pradesh. Similarly, during the triennium ending 1985-86 as against all India average yield of wheat at 1915 Kgs. per hectare, the average yield in Northern region was 1993 Kgs., followed by 1844 Kgs. in Eastern region and 1135 Kgs. in the North-Eastern region. In the case of coarse cereals, the average yield per hectare was 1267 Kgs. in Southern zone as compared to 1086 Kgs. in Eastern zone, 1068 Kgs. in Northern zone and 930 kgs. in the North-Eastern zone.

11.12 With the constraints of natural endowments, public investments in infrastructure and supporting services could play a key role in accelerating the growth of agriculture. But even the pattern of public expenditure reveals that investments in agriculture and irrigation per agricultural worker have been uneven between different regions/states. During* the period 1969 to 1985, expenditure on agriculture, irrigation and rural electrification per agricultural worker was the lowest in Bihar (Rs.1645) followed by West Bengal (Rs.1730) and Orissa (Rs.1998); in contrast, it was around Rs.3980 in Gujarat, Rs.2166 in Rajasthan, Rs.2708 in Maharashtra, Rs.2164 in Karnataka, Rs.4000 in Kerala, Rs.4433 in Punjab and Rs.5887 in Haryana. As a result of these diversities, notwithstanding some progress made in certain sectors benefitting from state governments development programmes, some regions/states particularly the Eastern and North-Eastern regions continue to be characterised by low agricultural efficiency, slow growth rate in crop productivity and farm incomes.

11.13 In areas where conditions congenial to the agricultural development persisted, farmer took initiative in making investments in agriculture i.e. for irrigating, mechanising his farm and improving its productivity and switching over to intensive cultivation or commercial cropping through use of sophisticated inputs and allied services. This threw up substantial demand for credit - both investment and working capital - and in the process increased the credit absorption capacity of agriculture in the area. Conversely, in the under-developed regions like Eastern and North-Eastern regions caught up in the vicious

* Source : Committee on Agricultural Productivity in Eastern India (1984)

circle of traditional production technology, low demand for agricultural inputs/investments, low productivity, low incomes and low levels of savings have not been able to generate adequate demand for credit. The low credit absorption capacity of agriculture has been the major characteristic of the under developed regions. The imbalances in agricultural development as reflected in the supply of agricultural credit are discussed below.

Variations in Supply of Credit

11.14 There has been a substantial increase in the aggregate supply of credit to agriculture and allied activities by all credit agencies (commercial banks, co-operatives and RRBs) from Rs.4,884 crores at the end of June 1975 to Rs.16,409 crores at the end of June 1986 but the supply of credit has been uneven in various regions/states as may be seen from table 1 showing loan outstandings by all agricultural credit agencies at the end of June 1986. As the table shows, credit provided by the concerned institutional agencies directly for agriculture and allied activities was concentrated in a few states. Five states, viz., Andhra Pradesh, Maharashtra, Uttar Pradesh, Tamil Nadu and Karnataka together accounted for 50 per cent of the credit provided by all credit agencies whereas other 11 states, viz., Assam, Orissa, West Bengal, Sikkim, Jammu and Kashmir, Himachal Pradesh, Mizoram, Nagaland, Manipur, Tripura, Arunachal Pradesh and all Union Territories together had a share of only 11.5 per cent of the credit.

11.15 An analysis of the performance of different types of credit agencies shows more or less the same picture. Thus, of the credit provided by PACSs in the co-operative credit structure, five states, viz., Maharashtra, Uttar Pradesh, Tamil Nadu, Gujarat and Kerala together accounted for 55 per cent of the total credit whereas the share of the 11 states (named earlier) and all Union Territories was only eight per cent. Similarly, in the case of commercial banks, six states, viz., Andhra Pradesh, Uttar Pradesh, Tamil Nadu, Maharashtra, Karnataka and Gujarat together had a share of 58.4 per cent of the credit, whereas the share of the said 11 states/Union Territories in the credit was only 14.5 per cent. As regards RRBs four states, viz., Andhra Pradesh, Bihar, Karnataka and Uttar Pradesh received 55 per cent credit provided by them and the share of the said 11 states/Union Territories (except Orissa which received 8.3 per cent of RRB credit) was only 10.3 per cent.

Table 1

State-wise Distribution of Outstanding Institutional Credit as on June 1986

(Rs. crores)

Sr. No.	State	CBs	RRBs	PACs	PLDBs	Total
1	2	3	4	5	6	7
1.	Andhra Pradesh	800 (11.6)	158 (12.0)	277 (6.4)	366 (13.7)	1601 (10.5)
2.	Assam	140 (2.0)	23 (1.8)	9 (0.2)	8 (0.3)	180 (1.2)
3.	Bihar	359 (5.2)	165 (12.6)	63 (1.4)	110 (4.1)	697 (4.6)
4.	Gujarat	475 (6.9)	15 (1.1)	371 (8.6)	112 (4.2)	973 (6.4)
5.	Haryana	240 (3.5)	36 (2.7)	198 (4.6)	196 (7.4)	670 (4.4)
6.	Himachal Pradesh	146 (2.1)	11 (0.8)	27 (0.6)	6 (0.2)	190 (1.2)
7.	Jammu & Kashmir	66 (1.0)	12 (0.9)	6 (0.1)	5 (0.2)	89 (0.6)
8.	Karnataka	636 (9.2)	157 (11.9)	239 (5.5)	226 (8.5)	1258 (8.3)
9.	Kerala	196 (2.8)	40 (3.0)	523 (12.1)	161 (6.1)	920 (6.0)
10.	Madhya Pradesh	372 (5.4)	103 (7.0)	317 (7.3)	174 (6.5)	966 (6.3)
11.	Maharashtra	549 (7.9)	34 (2.6)	670 (15.5)	356 (13.4)	1609 (10.6)
12.	Orissa	215 (3.1)	109 (8.3)	165 (3.8)	74 (2.8)	563 (3.7)
13.	Punjab	418 (6.0)	7 (6.5)	243 (5.6)	198 (7.4)	866 (5.7)
14.	Rajasthan	292 (4.2)	85 (6.4)	265 (6.1)	115 (4.3)	757 (5.0)
15.	Tamil Nadu	664 (9.6)	26 (2.0)	382 (8.8)	173 (6.5)	1245 (8.2)
16.	Uttar Pradesh	917 (13.2)	248 (18.8)	427 (9.9)	332 (12.5)	1924 (12.6)
17.	West Bengal	271 (3.9)	69 (5.3)	126 (2.9)	49 (1.8)	515 (3.4)
18.	Others	163 (2.4)	20 (1.5)	18 (0.4)	4 (0.1)	205 (1.3)
	All India	6919 (100.0)	1318 (100.0)	4326 (100.0)	2665 (100.0)	15228 (100.0)

Note : 1. Data for commercial banks and RRBs relate to rural branches.
2. Figures in paranthesis indicate percentage to respective totals.

11.16 To a large extent the divergence in the credit supply could be ascribed to large variations in the gross cropped areas in the various regions/states but not entirely. When account is taken of the credit supply (loans outstanding both short-term and term loans) per hectare of the gross cropped area, it also brings out large variations in credit from state to state and also as between different regions, as will be seen from table 2.

Table 2

Loans Outstanding per Hectare of Gross Cropped Area on 30.6.86

State	Commercial Banks Rs.	RRBs Rs.	Co-operatives (PACSS + LDBs) Rs.
Haryana	606.3	50.7	694.6
Himachal Pradesh	344.3	53.3	341.3
Punjab	912.4	8.3	631.9
Rajasthan	214.9	40.5	200.9
Assam	186.2	35.3	47.0
Manipur	162.5	10.8	201.6
Tripura	315.1	261.7	159.6
Bihar	319.8	97.9	168.5
Orissa	217.0	78.0	249.3
West Bengal	446.8	54.8	223.8
Madhya Pradesh	195.6	32.6	217.0
Uttar Pradesh	357.7	65.4	302.8
Gujarat	541.2	13.6	463.3
Maharashtra	385.6	15.4	485.7
Andhra Pradesh	785.1	113.7	480.5
Karnataka	638.2	118.1	404.9
Kerala	1,290.3	182.1	2,391.5
Tamil Nadu	1,273.0	19.0	799.4
Jammu & Kashmir	191.8	73.9	108.3
Meghalaya	338.4	55.9	111.7*
Nagaland	448.2	7.6	60.5*
Sikkim	128.1	NA	22.5*

* Pertains to PACSS only.

11.17 As details in table 2 show, credit is concentrated in a few states like Kerala, Tamil Nadu, Punjab, Haryana, Andhra Pradesh, Karnataka and Gujarat, viewed in terms of loan outstandings per hectare of gross cropped area also. The per hectare loans advanced and outstanding by all credit agencies were highest at Rs.3,864 in Kerala, followed by Rs.2,091 in Tamil Nadu, Rs.1,552 in Punjab, Rs.1,379 in Andhra Pradesh, Rs.1,351 in Haryana, Rs.1,161 in Karnataka and Rs.1,018 in Gujarat. This is the group of states where per hectare advances not only of co-operatives (i.e. ST and LT) but also those of commercial banks were the highest, though commercial banks were originally intended to supplement the efforts of co-operatives i.e. more or less bridge the gaps in the credit supply by co-operatives. The credit has tended to concentrate in certain states irrespective of whether the institutional agency was the co-operatives or the commercial banks. On the other hand, Assam, Bihar, Sikkim, Manipur, Jammu & Kashmir, Tripura and Meghalaya comprised another group of states where the per hectare advances were low. The performance of RRBs had to some extent, helped reduce the regional/state-wise imbalance such as for instance, in Tripura where their per hectare advances (Rs.262) were the highest as against Punjab (Rs.8), Tamil Nadu (Rs.19) and Gujarat (Rs.13) where they were quite on the low side. However, the overall picture of supply of credit, as it emerges from the foregoing data, shows considerable imbalance in the supply of credit, the states in Southern, Northern and Western regions having considerably better credit supply while on the other hand most of the states/Union Territories in the North-Eastern region receiving lowest share of institutional credit followed by some states in the Eastern region.

11.18 Such wide variations in the supply of credit, state-wise, could to a certain extent be attributed to the aberrations in the functioning and performance of the credit agencies, besides the more fundamental factors which are in fact beyond the control of the institutional credit agencies. In any event the institutional weaknesses have also partly contributed to the problem. A broad analysis of the performance of the different types of credit agencies given below, brings out the extent to which credit agencies have contributed to these imbalances.

Co-operatives

11.19 In the case of co-operatives, while the geographical coverage is almost

complete (almost all villages being serviced by PACSs at the grass root level) in the well developed states, it is not so in the backward states. In Jammu & Kashmir for instance, only 68 per cent of the villages were covered by PACSs, at the end of 1981-82 for which data are available while in Nagaland the coverage was only 42 per cent. In West Bengal, the coverage of villages was 80 per cent and in Assam many villages are yet to be covered by PACSs. In many cases most of the villages came under co-operative fold, but the number of villages a society was required to serve was too large to be effective. For instance, the average number of villages covered by a society was as large as 25 in Meghalaya, 17 in Orissa, 12 in Tripura, 10 in Bihar and nine in Assam whereas the all India average number of villages per society was only six.

11.20 There were wide disparities in the proportion of cultivators actually served by PACSs. The percentage of borrowing membership of PACSs, to cultivator households was as high as 61.6 in Punjab, 43.6 in Haryana and 35.9 in Andhra Pradesh whereas it was much below the all India average of 23.4 in Orissa (19.3), Tripura (7.6), West Bengal (11.1), Jammu & Kashmir (6) and Meghalaya (5.5).

Commercial Banks

11.21 The region-wise network and business of the branches of all scheduled commercial banks as on 30.6.1986 is shown below :

Table 3
Data on Business of Commercial Bank Branches - Regionwise

Region	Offices		Deposits		Advances		CD ratio
	Number	% to total	Amount	% to total	Amount	% to total	
Northern	6,590	16.3	19,840	21.9	11,512	19.6	58.0
North-Eastern	969	2.4	1,505	1.7	715	1.2	47.5
Eastern	6,129	15.2	14,367	15.8	6,920	11.8	48.0
Central	6,861	17.0	11,980	13.2	5,900	10.0	49.0
Western	7,499	18.5	23,984	26.4	18,468	31.4	77.0
Southern	12,388	30.6	19,054	21.0	15,336	26.0	80.0
Total	40,438	100.0	90,730	100.0	58,851	100.0	64.8

The growth of commercial banks since nationalisation and their geographical coverage have been phenomenal. At the time of nationalisation the average population per branch office (APPBO) was as high as 65,000 (according to 1961 census). The position has improved considerably since then and the APPBO at the end of December 1986 worked out to 13,000 (as per 1981 census) taking into account RRB branches also. Considering only the rural and semi-urban areas, the states of Assam(22,000), Bihar (17,000), Maharashtra (16,000), Manipur (25,000), Orissa (16,000), Sikkim (17,000), Tripura (17,000), Uttar Pradesh (17,000) and West Bengal (21,000) are yet to reach the national level average of 13,000. Thus, there is a sharp variation as between regions with higher concentration of offices, deposits and credit in Southern region, Central region and Western region. The Eastern region closely follows North-Eastern region but is comparatively better served than the latter.

11.22 This shows that the geographical coverage by the branch network of commercial banks/RRBs was relatively sparse in some of the states in the Eastern and North-Eastern region like West Bengal, Bihar, Assam, Manipur Tripura, Sikkim and Orissa. Consequently their range of operations in this region both in terms of deposit mobilisation and loans and advances was also low. However, it is not the resource mobilisation which constitutes the major constraint in the flow of credit; on the contrary, data on the credit deposit ratio reveals that commercial banks were often unable to deploy even the quantum of resources which could be raised in the Eastern and North-Eastern regions, their credit deposit ratio being 47.5 for North-Eastern region and 48 for the Eastern region. These ratios were very low compared with those in other regions i.e. for instance Southern region with a ratio of 80 and Western region 77 where part of the resources raised in the Eastern and North-Eastern regions appear to have been diverted. The CD ratio, however, does not give a complete picture; it only depicts the position of commercial banks' direct advances vis-a-vis their deposits, in these states. This apart, commercial banks have been investing in debentures of land development banks, bonds of electricity boards, etc. and when these investments are taken into account, their total resource deployment in these states would be higher than that revealed by the CD ratios. But then CBs have been making such investments in other states also; so that the regional disparities will persist more or less to the same extent even when such investments are taken into account.

Regional Rural Banks

11.23 As regards RRBs, set up mainly to bridge the spatial and quantum gaps in credit availability they had coverage of all the districts in the Eastern and North-Eastern regions. At the end of 1986, RRBs had achieved a credit deposit ratio of 95* for the Eastern region (ranging from 176 in Orissa to 79 in Bihar) and 86 for North-Eastern region, though there were wide variations as between states in the North-Eastern region. While the credit deposit ratio in Manipur and Tripura was substantially high at 122 and 114 respectively, it was only 22 for Arunachal Pradesh and 43 for Meghalaya. Similarly, Himachal Pradesh and Jammu and Kashmir also had a very low CD ratio at 47 and 49 respectively.

Incidence of Overdues

11.24 One of the reasons for the poor credit supply in the Eastern, North-Eastern and Himalayan regions is the comparatively high level of overdues in all the three credit systems, viz., commercial banks, RRBs and co-operatives. Thus, for instance, the percentage of overdues to demand for 1985-86 in respect of commercial banks' direct lending to agriculture was as high as 79 in Manipur, 69 in Jammu and Kashmir, 67 in Tripura, 65 in Assam, 58 in West Bengal, Nagaland and Bihar as against all India average of 43. In RRBs the percentage was very high at 78 in Nagaland, 71 in Tripura, 61 in West Bengal, 60 in Orissa, and 59 in Bihar. Similarly, in co-operatives, the percentage at the PACSs level was nearly cent per cent of demand in Tripura, 91 in Meghalaya and Assam, 95 in Manipur, 66 in Orissa, 57 in Bihar as against all India average of 41. In the long-term co-operative credit structure, overdues were substantially high at 74 per cent of demand in Tripura, 60 per cent in Assam and 51 per cent in West Bengal as compared to all India level of 38.8 per cent.

11.25 The high incidence of overdues particularly in the Eastern and North-Eastern regions had virtually choked the fresh lendings to a large number of borrowers, who had become defaulters. Further, the credit agencies like RRBs and co-operatives which mainly depended on refinance from higher financing agencies had often to face resource constraint due to their ineligibility

* RRBs depend on borrowings from sponsor banks & NABARD to a large extent with the result that their total credit in relation to their deposits (CD ratio) is substantially high.

for adequate refinance on account of high level of overdues thus depriving even the new and non-defaulting members of credit supply.

11.26 It is evident that in these areas, RRBs as also co-operatives and commercial banks have not been able to push up loans and advances; the reasons for this appear to be not so much in the performance and efforts, or lack of them on the part of the credit agencies, as in the business of agriculture itself which also shows wide disparities in the growth and development as between different regions/states. A major factor responsible for this is the low growth rate in the demand for credit from the agriculturists in these regions. As a measure for pushing up the supply of credit in these regions, NABARD has increased its refinance facilities to the credit institutions by relaxing the usual norms and disciplines. In the case of term-loan refinance, for instance, NABARD laid down a more liberal set of eligibility criteria for the North-Eastern region by relaxing the recovery percentage by 5 to 20 per cent points in the case of some slabs, as a result of which refinance facilities from NABARD under schematic loan disbursements increased fourfold from Rs.808 lakhs in 1982-83 to Rs.3386 lakhs in 1987-88. In the case of short-term (crop production) credit also the criterion of overdues has been relaxed in the case of 'weak' co-operative banks and in some cases credit limits sanctioned to banks irrespective of level of their overdues. The aggregate limits for short-term (crop) production purposes sanctioned to co-operative banks in the Eastern and North-Eastern regions increased from Rs.10,020 lakhs in 1983-84 to Rs. 16,703 lakhs in 1986-87 and utilisation thereunder from Rs.7,808 lakhs to Rs.12,035 lakhs. Consequently, the aggregate disbursements by co-operative banks under production credit in the Eastern and North-Eastern regions increased from Rs.16,891 lakhs in 1983-84 to Rs.18,688 lakhs in 1986-87. However, as seen earlier, these measures fell far short in mitigating the regional imbalances in credit supply as such. Apart from the low credit absorbing capacity of these regions, a contributory factor has been the inadequacy of linkages - backward and forward - supporting systems and services, especially the infrastructural facilities necessary to make credit effective in these states and union territories. If these wide regional imbalances in credit supply, witnessed in the Eastern/North-Eastern regions are to be mitigated, they would call for a radically different and innovative approach to lending requiring the lending institutions to assume a role which may go beyond their conventional role.

Problems of Eastern and North-Eastern Regions

11.27 If the Eastern region has settled for a low level of productivity more than any other reason, it is because the prevailing inadequate level of organisational, promotional arrangements and supporting services impose high risk and heavy managerial responsibility upon the farm operators far beyond the capacity and the capital resources of the farmers most of whom are small/marginal farmers. The present system is inflexible and provides little scope for manoeuvrability to the farm operators of this region. The poor input delivery system, low level of research and technical support and inadequate marketing facilities have made them reluctant to intensify agriculture and diversify the cropping pattern.

11.28 The under-developed and difficult areas such as the Eastern region and the North-Eastern region thus need a radically different approach. In all these areas, the basic problem that one has to examine is how far can agricultural development be financed by individual investment efforts of the farmers with the help of institutional credit. For example, the expenditure on land development is often so high that the post-development incremental incomes may not enable the farmer to repay the loans raised for financing the development within a reasonable period of time. If the expenditure involved in development of the terrain, terracing and bunding of land, equipping it with the irrigation/drainage facilities, in not easily accessible areas is too high for the individual beneficiaries to afford, this expenditure needs to be taken off the shoulders of the poor farmer. In such cases there is a clear need for funding a part or whole of the investment out of public funds. In such circumstances, the scope for institutional credit, in these areas, for projects which are prima-facie creditworthy (i.e. where there is reasonable assurance to individual loanees of incremental income of a magnitude sufficient to facilitate repayment of credit) would be very limited. Development of agriculture in these regions would be possible largely through programmes/schemes financed, partly or wholly, through public funding or would depend largely on infrastructural support, to be funded through the public exchequer.

Agricultural and Rural Development Corporations

11.29 Under the present system, NABARD as well as other credit institutions expect formulation of schemes/programmes of lending which NABARD approves and refinances. This approach of financing individual investments with

institutional credit, has succeeded in the well developed areas, where banks equipped with technical expertise and infrastructural support have been able to formulate schemes of agricultural development though this approach has not proved useful with all banks and certainly not in all regions/states. The under-developed and backward areas where the imminent need is for the development of backward and forward linkages and supporting services as a pre-requisite for investments in agriculture, call for a type of projects/programmes, and a nature of funding substantially different from those in the developed regions/states. Even bank lendings in these areas, at their present stage of development may have to be more in the form of indirect lending for building up such linkages and basic infrastructure facilitating storage, transportation, distribution, arrangements for ensuring inputs supplies and for the marketing and agro-processing etc., than by way of direct finance to agriculture for creating assets or for agricultural operations. For bringing about a meaningful departure from the existing system of agricultural lending, which these areas call for, we feel the need for a suitable agency which could assume squarely this responsibility. We would in this context recommend the establishment of Agricultural and Rural Development Corporation (ARDC) in each of the three Eastern region states, viz., Bihar, Orissa and West Bengal and one for all the North-Eastern region states. Since the problems of the North-Eastern region are qualitatively different, a separate corporation for that region is considered desirable. Each such corporation may be jointly sponsored by the Central and state governments.

11.30 Each corporation would be jointly owned by the Central/state governments; the quantum of equity required by a corporation may differ in each case depending on the nature and scope of its activities e.g. the set up of the corporation for the North-Eastern region, covering several states would be more complex and, therefore, the composition of its funding would differ from that of other corporations in the Eastern states. The objective underlying the constitution of the corporations being preparation of schemes for agricultural/rural development and for building up linkages to be funded partly or fully through the public exchequer, the funding of bulk of the corporations' activities would have to be from the budgetary resources of governments though the corporations should have access to market borrowings, through floatation of bonds/debentures, as also to the bank credit, to the extent they would be able to take up the activities that could either be financed through

individual investment efforts of the beneficiaries or would otherwise be commercially viable. Similarly, the provisions as also the funding of the administrative machinery for the corporations will be the sole responsibility of the respective state government.

11.31 The main task of these corporations would be to adopt a bolder strategy for increasing the tempo of agricultural lending. To this end, each corporation would initiate action to take up in its area, area-wise potentiality studies, formulate location-specific projects for accelerating activities which will lead to transformation of agriculture in these backward areas, arrange for funding of these projects, through public exchequer where and to the extent individual investments are not feasible and also arranging for consortium lending, and establishing close and collaborative contacts with development bodies like government corporations. Apart from the projects for investments in agriculture to improve the productivity of the land holdings, the proposed corporations would primarily engage themselves in formulating projects for building up necessary linkages - forward and backward - such as arrangements for supply of physical assets and inputs in agriculture and allied activities, their storage and transportation, processing etc. of agricultural produce and marketing in the terminal markets and other supporting services. As regards implementation of the projects, while some projects will be implemented by the corporations themselves, it is not contemplated that the corporations should take up each and every activity involved in building up of the linkages; some projects may, therefore, be implemented either by private entrepreneurs or by co-operative organisations of farmers/rural producers and where such enterprise is lacking, which is possible in the concerned undeveloped Eastern North-Eastern regions, by other state corporations. The task of the proposed Agricultural and Rural Development Corporations will be confined more to identifying the bottlenecks/gaps in the linkages and the supporting services impeding the development of agriculture and removing them by formulating projects for bridging up such gaps. Similarly, it is not our intention that the proposed corporations should engage themselves in building up the rural infrastructure such as construction of roads, provision of electricity, communications, etc. since it is basically the responsibility of the state governments which they discharge through their different departments. It is not contemplated that these functions already being performed by the various departments of the state governments be taken over by the proposed corporations, as it would

amount to mere duplication of the existing arrangements. However, even in matters relating to the infrastructure arrangements, it would be the responsibility of the proposed corporations to identify vital infrastructural gaps which may be obstructing the promotion of agriculture and allied activities, pursue their redressal with the concerned departments of government to ensure that lack of adequate infrastructure does not become a stumbling block in the progress of the agricultural sector.

11.32 As regards funding of the projects prepared by the corporations, to the extent they are not sustainable through investments by individual beneficiaries, they would have to be funded, partly or wholly through the public exchequer. In cases, where individual investments by farmers are possible, the projects would be supported by institutional credit with refinance facilities from NABARD. Where the projects formulated by the corporation are of an area-based or commodity-based multi-disciplinary type including infrastructural development, that part of the project eligible for institutional credit could even be financed by the corporation itself and in such cases the corporation should be eligible for financial assistance directly from NABARD. NABARD can provide such finance directly under Section 30 of the NABARD Act. Further, for the task of formulating such projects, the corporations need to be equipped with competent technical and financial experts. They have to set up TME Cells for the purpose which may be eligible for financial assistance from NABARD out of its R & D Fund.

11.33 It must, however, be conceded that the proposed corporations could succeed only to the extent the concerned state governments assume a far greater degree of responsibility in developing appropriate development policies such as changes in land tenure system, prepare ground for sustained agricultural development, evolve mechanism and machinery, where necessary, by establishing government corporations for undertaking key infrastructural activities, determine roles of different government agencies in this sphere and co-ordinate the activities of these agencies and credit institutions with the initiatives of the individual farmers. We are envisaging this role for the proposed Development corporations largely as a catalyst for development, taking initiative in the matter, enlisting co-operation and mobilising support - financial, administrative and manpower - of the different agencies - government and others - and involving themselves fully in the task of agricultural transformation in these less developed states.

CHAPTER XII

PROGRAMME FOR INSTITUTIONAL STRENGTHENING

In separate chapters in Part II of this report, we have reviewed the performance of the different components of the agricultural credit system, identified the areas of their weaknesses and suggested measures for overcoming them with a view to strengthening the agricultural credit delivery system. An important aspect which has a direct bearing on the lending operations of the different components of the credit system is the refinance facilities available from NABARD. Entitlement of refinance from NABARD for schematic lending is presently governed by the 'Eligibility Criteria', which determine different levels of refinance with reference to the recovery performance of the lending institutions. It is to the issues concerning eligibility criteria, their impact on the lending operations of the credit agencies, their effectiveness in improving the recovery performance, etc. that we address ourselves in Section I of this chapter. Section II deals with the "Institutional Strengthening Programme" which we are recommending as a substitute for the existing rehabilitation programmes earlier introduced by RBI/NABARD for reviving the working of the "weak" co-operative banks.

Section - I Eligibility Criteria for Long-term Schematic Loaning

12.02 The refinance facilities from NABARD for schematic term loaning are governed by eligibility criteria (EC) envisaging different levels of refinance depending on the recovery percentage with reference to demand of the lending institutions. The details of EC currently applicable to the client banks, viz., commercial banks, RRBs, LDBs and SCBs/DCCBs are given below :

Eligibility Criteria for NABARD refinance

A. All Areas except North Eastern States

<u>Category</u>	<u>Annual Recovery Rate (percentage)</u>		<u>Refinance Facility</u>
	<u>From</u> 01/07/86	<u>From*</u> 01/07/88	
1	75 or above	75 or above	Unlimited

	From 01/07/86	From 01/07/88	
II	60 - 74	65 - 74	Highest amount lent in previous five years or average recovered in previous three years, whichever is greater.
III	36 - 59	41 - 64	Amount recovered in previous year or average of recoveries for past three years, whichever is greater.
IV	Upto 35	Upto 40	75 per cent of category III in first year. If bank/branch remains in this category and fails to show atleast seven percentage points improvement in recoveries, refi-financing would be 50 per cent and 25 per cent of category III in second and third years.

* Postponed from 01/01/88

B. North - Eastern States **

<u>Category</u>	<u>Annual Recovery Rate (percentage)</u> From 01/07/86	<u>Refinance Facility</u>
I	75 or above	Unlimited
II	60 - 74	Highest amount lent in previous five years or the amount recovered in the previous year or the average of recoveries in the previous three years, whichever is greater.
III	Upto 59	Amount recovered in previous year, or average amount recovered in previous three years, whichever is greater.

** N.E. States and Union Territories are Arunachal Pradesh, Assam, Manipur, Meghalaya, Mizoram, Nagaland, Tripura and Sikkim.

Source : NABARD circulars dated 18/03/86 and 31/03/86

12.03 The objective underlying the eligibility criteria was to restrict, in the case of banks/branches having high level of overdues, the level of refinance

and consequently fresh lending so that the credit agency would concentrate its efforts not so much on fresh lending but more on the recovery of dues where its performance called for much improvement. The overall trend of recoveries in the last decade (1975-76 to 1985-86), has been generally towards progressive deterioration except for some short spells of better recoveries largely attributable to favourable weather conditions and resultant good crops. The increasing trend in overdues is attributable to different causes such as socio-political environment which has vitiated the climate of recovery, absence of backward/forward linkages and infrastructural facilities, frequent crop failures, defective loan policies and defective procedures, declining profitability of agriculture, etc. and it is difficult to establish any definite relationship between the operation of the discipline of eligibility criteria on the one hand and the level of the overdues on the other. An examination of the impact of eligibility criteria on different types of credit institutions, viz., LDBs, RRBs and commercial banks made by our consultants on the basis of the available data shows that the impact on LDBs is quite different from that on other credit agencies, viz., commercial banks, RRBs and SCBs/DCCBs which have alternative resource base. In the case of LDBs, largely funded by NABARD, restricted eligibility for refinance directly curtails their ability for fresh lending thereby eventually reducing their total loan business and profitability. The impact of eligibility criteria on the RRBs, commercial banks, SCBs/DCCBs is different; as these institutions have access to resources, other than refinance from NABARD, mainly their deposit resources, they are in a position to continue fresh term lending for agriculture even when their eligibility for NABARD refinance gets restricted. In their case, the impact is in terms of interest rates and margins available to them since NABARD refinance is cheaper as compared to deposit resources.

Land Development Banks

12.04 The LDBs raise their resources primarily through the special development debentures and are mainly dependent on NABARD refinance, their ordinary debentures floated for non-schematic lending being both insignificant and unprofitable or only marginally profitable. The withdrawal of unrestricted refinance from NABARD, through application of eligibility criteria, in respect of LDBs having recovery of less than 75 per cent, stagnates their fresh loaning, leading to stagnation or even fall in their incomes while their operational costs continue

to mount. Table 1 gives data over a period of three years in respect of advances of eight PLDBs/branches of SLDBs, four of which had the lowest slab and four having highest slab of eligibility.

Table 1
Comparison of PLDB's Advances

	Year	Percentage of overdues to demand	Advances during the year (Rs.lakhs)	Percentage of increase (+)/ decrease (-) in advances	
	(1)	(2)	(3)	(4)	
A. <u>Restricted PLDBs/ SLDB branches</u>					
Vaghodia (Branch) (Gujarat)	84/85	76	6.30		-
	85/86	66	5.30	(-)	15.0
	86/87	75	4.55	(-)	16.5
Rohru (Branch) (Arunachal Pradesh)	84/85	68	2.30		-
	85/86	88	3.20	(+)	39.1
	86/87	69	1.64	(-)	48.8
Rayagada (Orissa)	84/85	72	2.31		-
	85/86	69	2.77	(+)	19.9
	86/87	64	2.03	(-)	26.7
Jalpaiguri (West Bengal)	84/85	83	10.30		-
	85/86	64	10.58	(+)	2.7
	86/87	77	4.56	(-)	56.9
B. <u>Unrestricted PLDBs/ SLDB branches</u>					
Amritsar (Punjab)	82/83	9	65.02		-
	83/84	10	85.48	(+)	31.5
	84/85	6	88.99	(+)	4.1
Balachaur (Punjab)	82/83	5	62.11		-
	83/84	4	71.80	(+)	15.5
	84/85	4	65.03	(-)	9.4
Malanand (Karnataka)	82/83	15	116.72		-
	83/84	12	131.14	(+)	12.4
	84/85	18	148.85	(+)	13.5
Palghat (Kerala)	82/83	17	84.94		-
	83/84	14	185.62	(+)	118.5
	84/85	18	222.74	(+)	20.0

12.05 Although the sample is small, two points seem to emerge fairly clearly. Firstly, there is a general decline in the advances of the banks having restricted eligibility though there are variations in the trend in some years, while the advances of the banks having unrestricted eligibility have shown a steady growth pattern. Secondly, the fresh loaning of banks having restricted eligibility is very significantly lower than that of the banks having unrestricted eligibility, so low, in fact, as to render the institutions dormant or near dormant.

12.06 Further, there appears to be a relationship between lower levels of refinance and profitability of LDBs. Restricted refinance stagnates fresh loaning and consequently the total loan business with the result that income earning capacity of the bank gets impaired whereas the bank has to continue maintaining the establishment and bear the increasing establishment costs. This leads to progressive reduction in profitability and even losses where the income falls short of current expenses.

12.07 The table below shows certain key financial variables of one of the three PLDBs (viz. Rayagada) in the lowest slab of EC :

Table 2
Financial Analysis - Rayagada PLDB

	(Rs. lakhs)					
	1982	1983	1984	1985	1986	1987
Advances	21.7	20.5	19.2	20.0	21.1	21.5
Borrowings from SLDB	24.2	22.7	22.4	24.7	26.5	28.7
Net worth	(5.5)	(8.1)	(10.9)	(14.1)	(16.7)	(17.9)
Net Loss	(2.0)	(2.6)	(2.8)	(3.2)	(2.7)*	(1.1)*
Overhead expenses	1.1	1.1	1.2	1.2	1.4	1.5
Percentage of :						
a) Borrowings to Advances	112	111	117	123	126	133
b) Overhead Expenses to Advances	5.1	5.4	6.3	6.0	6.6	7.0

*Upto 1985, the reported losses include provisions made for bad and doubtful debts; in 1986 and 1987, no provisions were made. The apparent improvement in result arises from this.

This bank's owned funds had been eroded by accumulated losses, throughout the period under review. It has continued in business and has been drawing refinance from NABARD through SLDB. Its level of business is less than 30 per cent of the minimum level at Rs.70 to 75 lakhs recommended for viability of PLDBs and there appear to be no prospects for the bank ever reaching the level of business to attain viability. In fact, its advances have declined. Throughout the period, the bank has incurred losses which have been funded in part by refinance. Overhead expenses are high in relation to income and are increasing. Thus, the impact of EC seems to be that in the short run these criteria may not necessarily affect the LDBs' profitability, but in the long run these banks may slowly wither away.

Regional Rural Banks

12.08 As regards RRBs, their cost of funds, for short-term and medium-term non-schematic loaning on an average works out to seven per cent which is also the average rate on deposits as worked out in the Kelkar Committee report. The average cost of deposits will, however, vary from bank to bank and from time to time depending on the composition of deposits and also on whether the bank offers the permitted extra interest at 0.5 per cent above the directive rates on savings and some term deposit accounts. In the case of schematic term finance, however, there is a cost advantage in favour of refinance which is available from NABARD only at 6.5 per cent. Thus, any restriction on the availability of refinance for schematic lendings and their funding from deposit resources would lead to lowering the profitability of RRBs. Further, the transaction costs of refinance will be lower than those of servicing deposits and hence obviously additional profitability can be gained from resorting to refinance as it will reduce the transaction cost per unit of overall resources.

Commercial Banks

12.09 Information available from RBI (Department of Banking Operations & Development) indicates that the current average cost of deposits for commercial banks is around 7.5 per cent while long-term refinance is available from NABARD at 6.5 per cent to eight per cent, with greater portion at 6.5 per cent. There is thus, on an average, an interest rate advantage of slightly less

than one per cent in funding agricultural lending from refinance rather than from deposits and a consequent decrease in profitability for the average commercial bank which funds ineligible lending from its own resources.

12.10 Perhaps more important, however, is the impact of requirements of Statutory Liquidity Ratio (SLR) and Cash Reserve Ratio, (CRR) on one hand and priority sector lending on the other. Currently, commercial banks are required to place 38 per cent of their outside liabilities in eligible liquid assets and 15 per cent more with the Reserve Bank as cash reserve. Hence out of every Rs.100 raised as deposits, only Rs.47 can be deployed as advances. Refinance from NABARD is not classified as "outside liabilities" for SLR and CRR purposes, thus Rs.100 out of every Rs.100 borrowed from NABARD can be deployed as advances, helping the bank reach its priority lending targets for agriculture, and at the same time leaving more of its deposits available for deployment in higher yielding advances - important for cross subsidisation.

State Co-operative Banks/District Central Co-operative Banks

12.11 In the case of SCBs, the average cost of deposits of the Maharashtra State Co-operative Bank, as indicated by our consultants was 9.7 per cent as at the end of June 1986. The average deposit rates of other banks would vary according to the composition of their deposits. NABARD provides schematic finance at 6.5 per cent and eight per cent, though the bulk of refinance (which was for minor irrigation, land development and diversified lending under IRDP and to small farmers) was available to SCBs at 6.5 per cent. Thus, there was a definite advantage accruing to SCBs in funding schematic loans from NABARD refinance rather than through deployment of their own deposit resources for the purpose.

12.12 On the basis of the Study conducted by our consultants, we have come to the following conclusions :

- i) There are significant differences in the recovery performance of institutions in different parts of the country - a reflection of the regional diversity. However, the EC does not recognise this diversity, (with some exceptions as in the North-Eastern

region, EC being uniform for the country as a whole) nor does it appear to have any corrective influence on these imbalances.

- ii) The analysis shows that in many cases, significant recovery of old overdues is beyond the managerial and operational capabilities of the banks, particularly in the co-operative sector, where the absence of state government assistance to enforce recoveries from wilful defaulters worsens the climate of recovery. Although in some other cases, causes of overdues are internal, they are not resolvable by taking stringent recovery action but require long-term measures to enhance the institution's operational capabilities.
- iii) Recovery performance of some of the credit agencies in different EC categories gives no indication that EC has achieved its purpose, viz., enhancement in the recovery levels of the banks. On the contrary, the conclusion our consultants have arrived at, is that recoveries have deteriorated over the years in banks to which EC has been applied with restrictions on fresh lending. The above conclusion was endorsed by executives of the credit agencies interviewed by the consultants. Their view was that EC gave them little incentive for recovery and could even serve as a disincentive.

12.13 The main objective underlying the provision of refinance facilities from NABARD for schematic lending is to promote investments in agriculture, to induce the agriculturists to take up agricultural investments and also the credit agencies to lend increasingly to this sector in preference to others. We find that this basic objective is getting defeated in the process of implementation of the EC which at best is a negative financial discipline seeking to penalise the credit agencies whose recoveries fall short of the stipulated norms. The most undesirable aspect of EC is that under this discipline, overdues become the sole determinant of eligibility for lending and consequently the new and potential borrowers of the credit agencies are penalised for no fault of theirs. The discussion on overdues in Chapter XV shows that defaults are caused, among others, by factors outside the control of the credit agency and some areas have high incidence of overdues irrespective of the type of the

credit agency involved. In the ultimate analysis it seems to us that EC has done more harm than good both to the borrowers and the credit system without realising its objective of improving recoveries. While the objective of improving the recoveries is no doubt laudable, the problem needs to be attacked through more direct measures including sanctions against defaulters especially the wilful defaulters rather than choking the conduits of credit, which is self-defeating.

12.14 In so far as NABARD is concerned, the annual calculation of eligibility of constituents, is itself a formidable task. In order to calculate the eligibility of each bank/branch for refinance, NABARD requires :-

- i) The demand, collection and balance position as on 30th June each year under term loans for agriculture , and
- ii) Upto five years, information regarding each bank's/branch's volume of lending and recovery depending upon the criteria of eligibility.

NABARD has to determine individually the eligibility of over 1,500 PLDBs/SLDB branches, nearly 200 RRBs and as many as approximately 25,000 commercial bank branches and 375 SCBs/DCCBs that may be applying for schematic lending. Visits to NABARD regional offices undertaken by our consultants show that this work alone occupies a significant amount of staff time; in some cases several months as banks do not submit the required information on time. This staff time could be more fruitfully utilised in improving the monitoring of credit.

12.15 While recognizing the imperative need for discipline on refinance so as to ensure the health of the credit agencies and effective control over the flow of agricultural credit, the present eligibility criteria, as we have seen from the position explained earlier, have, in fact, become more a cumbersome and time consuming task for NABARD rather than effective in improving recoveries. The EC as prescribed at present, in our view, serve little purpose or value to the agricultural credit system. We, therefore, recommend the scrapping of the current system of eligibility criteria and its replacement by a new discipline to be known as "Viability Criterion" (VC) supported by a compre-

hensive Institutional Strengthening Programme. The term 'Viability' is used in this context to indicate the state of the solvency of a bank. This will in turn be measured in terms of the extent of erosion of the owned funds by its accumulated losses and bad and doubtful debts as estimated by auditors/ inspecting officers of RBI/NABARD.

12.16 The switchover to the "Viability Criterion" would mean that lending institution so long as it is solvent as adjudged by the criterion fixed therefor, would be eligible for full refinance from NABARD, subject, of course, to its satisfaction about the size and scope of the lending programme, etc. Conversely, an institution which does not satisfy the solvency criteria as defined would not be eligible for any refinance, (whatever its eligibility could have been under the slab system of the present Eligibility Criteria).

12.17 Our recommendation for dispensing with the current eligibility criteria, however, does not imply a complete abandonment of the financial disciplines related to the recovery performance of the lending institutions. The viability criterion itself, in our view, represents a financial discipline of a higher order as the inability of an institution to maintain its solvency status would imply a complete denial of refinance facilities from NABARD and this we feel, is bound to motivate the bank managements to achieve and keep up a satisfactory level of recoveries and a profitable mode of operations. Further, the implementation of the various recommendations we have made in Part IV of the report, for mitigating the causative factors responsible for overdues is expected to bring about substantial improvement in the level of recoveries. The perspective programme indicated in para 15.117 of Chapter XV also envisages that the lending agencies could be expected to accelerate their recoveries progressively and achieve, in the next three to four years, upto 80 per cent recoveries in respect of their current demand. Measures are to be taken simultaneously to recover the arrear dues also. We, therefore, recommend that as a pre-condition for unrestricted refinance facilities from NABARD, it would be incumbent on all the client banks to show, at the end of each year commencing from 1989-90, a progressive improvement in recoveries at least under current demand and to achieve by 30th June 1992 and maintain thereafter each year, 80 per cent recoveries in respect of their current demand. Failure

to comply with the aforesaid financial discipline would subject a client bank to such restrictions on refinance facilities as NABARD may feel fit to impose.

12.18 We are, however, conscious that a sudden application of the "viability" criterion would not be feasible or fair, so far as it relates to the 'non-viable' category of institutions which are not able to stand the solvency test. Immediate application of this criterion would result in an abrupt closure of refinance to all non-solvent banks, whatsoever their number. To obviate any such possible disruption in the flow of credit, we recommend that all the banks which do not measure upto the solvency norms be taken under an "Institutional Strengthening Programme (ISP)" aimed at enhancing their viability and provided with, as an integral part of the ISP package, refinance from NABARD on the lines agreed upon. This is suggested as an interim arrangement only. Further, as a pre-condition for refinance facilities from NABARD, the banks taken up under the Institutional Strengthening Programme would be required to show a progressive improvement in recoveries at least under current demand and achieve in the next two to three years and maintain thereafter each year, 80 per cent recoveries in respect of their current demand. Failure of any insolvent bank, under ISP, to comply with the above condition would attract the penalty of complete stoppage of refinance facilities from NABARD. Similarly, if the bank concerned fails to implement the Institutional Strengthening Programme or where despite undergoing the programme it remains non-viable, such institution would be deemed "a non-bankable risk" and, therefore, become ineligible for further refinance. NABARD would extend any further refinance to it, only where in the context of long-term economic development of a particular area, or a particular group of borrowers solely or largely being dependent on it, the state government (in the case of co-operatives), Government of India/state government / Sponsor Bank (in the case of RRBs so long as they continue to function) decide to support the credit agency through injection of adequate equity to absorb the losses and make it a solvent institution and hence eligible for refinance from NABARD.

12.19 While under our proposal all solvent credit institutions would become eligible for unrestricted refinance, we are conscious of the need to have an early warning system to identify the marginal cases of near non-solvent banks (i.e. those which are in danger of losing their solvency status in the near future)

and bringing them also under the Institutional Strengthening Programme. Pending the formulation of ISP, NABARD may provide refinance to the banks, so identified, on a suitable and practical basis, allowing a degree of flexibility to cover differing conditions of these institutions. When ISP has been formulated for an institution, refinancing should be done on the lines agreed upon under that programme. These aspects we have dealt with in the latter part of this chapter.

12.20 We also consider that NABARD as an apex refinancing agency at the national level has absolute right to regulate the flow of its refinance to client institutions in accordance with sound banking practices. As a part of this, NABARD should determine the amount of refinance to be provided when appraising a scheme. We are of the view that the process of scheme appraisal should include not only technical and financial assessment of the scheme itself but also assessment of the bank's capacity to manage the scheme effectively, in other words, the assessment of whether a bank can reasonably be expected to disburse adequate funds on time to its borrowers, guide and supervise loan utilisation, recover the loans and interest thereon in time and generate a positive return on its investment. Unless a scheme and the bank which finances it satisfy this test, the NABARD would not be called upon to refinance the scheme. This decision should be taken by NABARD at the time of scheme appraisal itself.

12.21 At this stage, we consider it necessary to clarify certain points. Firstly, we are recommending in the case of co-operative banks and RRBs, the complete scrapping of the current eligibility criteria governing the provisions of refinance for schematic term lending with reference to recovery levels and not a modification of this system. Secondly, the eligibility criteria will not include and we do not intend to do away with, measures intended to impose and maintain the existing credit disciplines such as norms governing refinance to SCBs/DCCBs for short-term (crop loans) limits, medium-term (for approved agricultural purposes) limits, borrowing capacity as a multiple of owned funds of co-operative banks, non-overdue cover and other disciplines, to which short-term/medium-term refinance facilities from NABARD are subject.

12.22 We are recommending for lending institutions other than commercial

bank branches, the substitution of the eligibility criteria by the viability criterion, among others, for the following reasons:

- i) The system is simple to operate and easy to understand;
- ii) The current anomaly of refinance to institutions which do not enjoy solvency status will be corrected;
- iii) The consciousness of having to work on a viable basis will inculcate a greater sense of responsibility in the managements of the credit institutions;
- iv) The pressure from NABARD to achieve satisfactory recoveries is not likely to be reduced. In fact the client banks will feel the pressure all the more since they will be expected to comply with the discipline indicated in para 12.17 or otherwise face the possibility of restricted refinance/total denial of refinance, sooner than later;
- v) The obligation of government to regularly contribute to the operating losses of banks if they are to continue to be eligible for NABARD refinance, may help to discourage government interference with the banks.

12.23 The Viability Criterion will apply to all client banks of NABARD except commercial banks. In the case of SLDBs and SCBs, however, viability criterion could apply only for the banks as a whole and not separately for each branch. As for RRBs, we have indicated elsewhere that non-viability is built into the system and, therefore, recommended that they should be merged with the sponsor banks. However, till the actual merger is effected, the viability criterion would apply equally to the RRBs and pending such merger, NABARD may provide refinance to RRBs on a suitable basis to be evolved.

12.24 The case of commercial banks as already pointed out, stands on an entirely different footing, their lending for agriculture forming only around 18 per cent of their loans portfolio. Moreover, the commercial banking sector is dominated by public sector banks which account for more than

90 per cent of the total business of all the commercial banks. Their resources being large and the range of their operations wide and vital to all the various sectors of the economy including trade, commerce and big industry, these banks are subject to close and continuous monitoring by the Government of India/Reserve Bank of India. These banks will not, therefore, be allowed to slide into a situation of non-solvency. Application of viability criterion to these banks would, therefore, virtually amount to making them eligible for unrestricted refinance on a permanent basis irrespective of the quality of their agricultural lending. We are, therefore, recommending a modified eligibility criterion in the case of the commercial bank branches.

12.25 As indicated earlier, the perspective programme of recovery envisages that the commercial banks' branches should accelerate their recoveries and progressively achieve, by 30th June 1992, upto 80 per cent recoveries under current demand. Keeping in view the above discipline, we would recommend in the case of branches of commercial banks the following eligibility criterion governing refinance facilities from NABARD:

<u>Annual Recovery Rate</u>	<u>Eligibility for Refinance</u>
1. Recovery at 80 per cent and above in relation to the current demand.	Unlimited refinance.
2. Recovery between 40 per cent and 80 per cent in relation to current demand	Eligibility subject to such restrictions as NABARD may like to impose.
For being eligible for refinance facilities under 1 and 2 above, the concerned branch should also show recovery of atleast 25 per cent in relation to its arrears demand. Failure to comply with this stipulation will attract such further restrictions as NABARD may like to impose.	
3. Recovery at less than 40 per cent in relation to current demand and 25 per cent in relation to arrears demand.	Ineligible for any refinance.

The above revised eligibility criterion will be applicable to the branches of commercial banks from the year 1992-93. Till then the branches of commercial banks may continue to be governed by the existing eligibility

criteria for the purpose of NABARD refinance for schematic lending. After the switch-over to the revised eligibility criterion with effect from the year 1992-93, those branches of commercial banks which fail to reach recovery of atleast 40 per cent of current demand and 25 per cent under arrears and, therefore, become ineligible for any refinance from NABARD, may be taken under the Institutional Strengthening Programme (ISP). Pending formulation of ISP and during the period the branches are engaged in implementation of the ISP, NABARD may provide them refinance as a part of ISP.

12.26 For applying the VC/Institutional Strengthening Programme to client institutions, NABARD may draw up a workable action plan in consultation with the appropriate forums of the client banks. The plan may, inter alia, envisage:

- i) Review of the financial position of client institutions, examination of the estimates of their bad and doubtful debts based on their inspection reports, audit reports, etc. to determine institutions which are technically insolvent;
- ii) Classification of all client banks by NABARD for the purpose of VC/Institutional Strengthening into those which are
 - a) solvent/viable and with good performance,
 - b) solvent but in the danger of losing solvency status (criterion for identification of such banks is indicated in the latter part of the chapter),
 - c) non-solvent ;
- iii) Listing of the banks to be brought under Institutional Strengthening Programme taking into account the available resources of the client banks, apex institutions, state governments, NABARD, etc

The plan/preparatory work should precede the full scale implementation of the recommended Viability Criterion/Institutional Strengthening Programme.

12.27 The ISP conceived by the Consultants, with focus mainly on co-operative banks, is given in Section II of this chapter. The same may apply

to branches of commercial banks with few major areas of departure indicated subsequently in paragraphs 12.60 and 12.61.

Section - II Institutional Strengthening Programme

12.28 A programme of rehabilitation of "weak" co-operative banks, as referred to earlier, has been under implementation since early seventies by RBI and later by NABARD, but this has not met with much success. For instance, as at the end of June 30, 1986, 173 DCCBs were under the programme, of which 58 had been under the programme for over 10 years and 43 between five and 10 years continuously. Further, several banks apparently revived under the programme were found to have relapsed, one or two years later, only to go back into rehabilitation. NABARD itself recognised that the programme has not been successful and has developed and launched new programmes, viz., the 10 point programme for LDBs in 1985 and the 12 point programme for DCCBs in 1987. Both these programmes are of recent origin and it is too early to comment on their success or otherwise. In the course of their visits to the client banks, our consultants have identified, inter-alia, the following reasons for the failure of the previous programmes:

- i) programme guidelines suggest only what banks should do rather than how to go about the process of rehabilitation. The only exception to this has been the SLDB programme;
- ii) while rightly concentrating upon loan recovery, the programmes do not provide for an expansion component and development of new opportunities for lending and other services once recoveries are improved, so that banks can become more viable business units;
- iii) lack of adequate initiative, involvement and effort on the part of 'weak' bank itself in implementing the programmes, in several cases;
- iv) lack of effective support by apex institutions and state governments;
- v) the management of weak units (often by government officials)

was given little outside guidance and assistance in planning and implementing the programmes, either by the apex banks or NABARD;

- vi) frequent management changes in the 'weak' units; and
- vii) inadequate direct supervision, monitoring and evaluation of progress by apex banks, co-ordinating committees and NABARD and subsequent follow up action to improve progress.

Additionally, the external environmental factors such as government directed lending programmes and loan melas, inadequate support from the state government, financially and administratively, and the increasing politicisation of the credit system have all had a significantly detrimental effect upon rehabilitation programmes.

12.29 Notwithstanding these factors, there is a clear need for strengthening the agricultural credit system and developing it into a strong and effective delivery system. NABARD as a national apex, has the overall responsibility for orienting the programmes towards comprehensive development of the weak banks/branches. We are, therefore, suggesting a detailed framework for a revised programme for strengthening such banks within the context of NABARD's institutional development policies so that rehabilitation can be focussed towards -

- i) comprehensive development of banks as commercial business units;
- ii) effective action to solve their basic problems especially recovery of overdues, and
- iii) expanded lending into new activity - areas to improve business viability.

12.30 At the outset, we wish to state that, while our proposals are intended to build a stronger institutional credit delivery system, they do not represent an instant panacea which will revive rapidly the fortunes of all those banks in need of special support. Many, perhaps the majority of these banks,

suffer from deep rooted problems such as poor quality loan portfolios, heavy burden of accumulated overdues, inadequate resources, poor management and the feeling that despite past rehabilitation efforts, no worthwhile improvement has taken place. There is no "quick fix" to these problems. Further, it has to be recognised that the agricultural credit institutions do not function in isolation; they are often a product of the environmental factors such as the stage of development of agriculture in the area, adequacy of the planning process, susceptibility of the area to the natural calamities, overall climate of recovery, external interferences in the functioning of the credit agency, etc. The strengthening of the identified institutions would need effectively addressing all these factors. We have dealt with these aspects in different chapters and have recommended measures for strengthening the credit delivery system, insulating it from outside interferences, improving the credit planning, rationalising the loan policies and procedures, mitigating the causative factors of overdues, introducing comprehensive crop insurance and credit guarantee cover, etc. Implementation of these measures would help creating a congenial environment for the effective functioning of the credit agencies. In the case of co-operative banks, the state governments have a crucial role to play in any programme of their strengthening as these institutions function under the state laws which vest the governments with all necessary powers and authority. Strengthening of these institutions will, therefore, take time and hard work by the banks themselves, their apex institutions, government and other agencies and NABARD.

A. Aim and Objectives

12.31 Designated as "Institutional Strengthening Programme"; its aim would be to provide the necessary assistance to those banks which are unable to sustain lending and other services among their customers so as to enable them to become viable and capable of self-sustained growth.

The detailed objectives of the programme would be -

- i) plan, implement, monitor and evaluate programmes that would enable and assist client banks to

- a) identify the causes of their problems and take comprehensive steps to solve them and prevent their recurrence;
 - b) identify opportunities and implement schemes to expand the range and quality of services, including non-credit services (as appropriate);
 - c) improve and enhance their management capability and the skills and experience of staff; and
 - d) become viable business, run on sound banking lines in conformity with the banking regulations ;
- ii) motivate, guide and assist apex level banks; SCBs and SLDBs in planning and implementing programmes for their primary units/branches;
 - iii) provide such technical and financial assistance (by way of grants or loans) as client banks may require to implement programmes;
 - iv) initiate action to enable banks, branches and primary units whose operations are unlikely to become viable, to be restructured, amalgamated or liquidated in such a way that the bank's overall operations are not weakened commercially, or the business is transferred to another bank;
 - v) take appropriate steps, in conjunction with GOI/RBI/state governments, to maintain institutional credit flows to customers where banks have failed to implement effective ISP and to withdraw all NABARD support including refinance from such banks in favour of their replacements; and
 - vi) mobilise the support of GOI and State Government agencies and other institutions at national, state and district level to provide appropriate support to banks undertaking ISP.

The Institutional Strengthening Programme has been conceived as a time bound action programme to be implemented and the identified bank made

adequately viable within a specific time span of say three to five years. If the concerned bank fails to implement the programme or where despite undergoing the programme, it fails to reach solvency status and remains non-viable, NABARD would stop further refinance facilities to it and formally advise in the case of co-operatives the concerned apex bank and the state government accordingly. NABARD would also consider, in consultation with RBI, the question of making alternative arrangements within the identified bank's service area to maintain the flow of credit to the borrowers in such cases.

B) Target Group

12.32 Since the institutional strengthening programme would be an integral part of the viability criterion replacing the present refinance discipline of the eligibility criteria, the insolvent banks (insolvency being complete erosion of owned funds) would automatically be taken under the programme of institutional strengthening. However, the main objective of the programme would be to prevent the banks from becoming insolvent and, therefore, apart from the banks which are non-solvent, the near non-solvent banks (i.e. those which are in danger of losing their solvency in the near future) would also form the target group of this programme. Identification of co-operative banks for being brought under the programme shall be done on the basis of the following criteria:

"Banks whose total owned funds are eroded by estimated bad and doubtful debts, accumulated losses and 50 per cent of the overdues over three years, excluding those considered as bad and doubtful"

The criterion signifying the complete erosion of owned funds by accumulated losses and estimated bad and doubtful debts would reveal banks which have already become non-solvent; whereas in cases where the owned funds of banks stand notionally eroded if 50 per cent of their overdues over 3 years are also taken into account, the criterion would serve as a danger signal indicating "marginally/near non-solvent" banks which should be taken under ISP if they are to be prevented from non-solvency.

C) Programme Components

12.33 The individual ISP schemes should include any or all of the following components :

- i) Overdue loans recovery programme which would involve measures such as legal and penal action against wilful defaulters implemented in conjunction with active state government support, limited rescheduling of repayments from non-wilful defaulters plus additional credit as needed, full write off of irrecoverable loans, incentive schemes for prompt repayment (provided interest rate margins are adequate) and the introduction of formal and informal borrower groups on the lines of the VVV programme;
- ii) deposit mobilisation schemes which might involve measures such as introduction of new types of deposit accounts, where feasible, depositor rewards and incentives, deposit promotions and deployment and use of deposit collectors and agents, all based upon a detailed analysis of potential in the bank's command area. (Again deposit mobilisation depends upon the cost of such funds relative to lending interest rates). The same approach could be adopted for other cost-effective banking services ;
- iii) maintenance of credit flows to borrowers who repay their loans;
- iv) identification of new lending opportunities, preparation of detailed bankable schemes and their funding and refinance under the close supervision of competent and experienced staff from the apex bank and NABARD.
- v) identification of new non-credit activities and preparation and implementation of viable schemes backed by appropriate funding and refinance and technical supervision as needed;

- vi) increased capitalisation of banks whose performance has improved and whose eroded capital base would hinder further development, by direct funding from existing shareholders with appropriate refinance facilities as required;
- vii) provision of essential additional infrastructure facilities and equipment to implement proposed new lending, deposit and other programmes, either by way of grants or long-term loans from the apex bank, NABARD or other institutions;
- viii) provision of management and technical support either by way of deputation or recruitment of additional staff, whose cost is subsidised for a defined period, to manage and implement the specific measures required;
- ix) intensive formal and on-job training to improve the quality of bank staff at all levels as needed, conducted by the apex bank's own training institute, with BIRD support as required; and
- x) review and analysis of all operating procedures and management systems and the development, implementation and testing of improved systems and procedures, together with appropriate training support. This would be carried out by the apex bank staff in conjunction with bank staff plus outside technical assistance as needed.

D) Agencies involved and their Roles and Responsibilities

12.34 The following agencies will play a vital role in the planning and implementation of the ISP.

- i) NABARD
- ii) State Apex Banks
- iii) DCCBs, PLDBs
- iv) State governments

12.35 NABARD as the apex bank for rural credit has overall responsibility in respect of banks involved in rural credit. However, it is unrealistic to expect NABARD alone to plan and execute the detailed and individually formulated programmes of institutional strengthening that are required for each and every bank within a reasonable time (of say three to five years). If NABARD were to attempt this it would result in many banks having to wait for several years for assistance. This would only weaken the banks' position still further and NABARD's approach may revert to the one of issuing general guidelines and overall monitoring of progress which has proved in past quite ineffective. NABARD's consistent approach, which we endorse, has been that banks should themselves be responsible for their own development programme and that the apexes should assume direct responsibility for affiliated units at district and primary levels. We, therefore, propose that the target group for institutional strengthening for which NABARD would be directly responsible would constitute only the SCBs and the SLDBs in need of this programme. The apex banks in turn i.e. SCBs and SLDBs would assume the direct responsibility for monitoring implementation of the programmes in respect of their affiliated units at district and primary levels.

12.36 The roles and responsibilities of all institutions and agencies directly involved in the programme of institutional strengthening are indicated below:

NABARD

12.37 We have defined the role and responsibility of NABARD head office as essentially those of overall policy planning and review. NABARD should identify the general needs of the weak banks at all levels, develop broad strategies and components of ISP and advise appropriate methodologies and operating guidelines for the programme. It would be the responsibility of NABARD to arrange for provision of adequate resources and comprehensive management support to the banks brought under the programme. For this purpose it will liaise with other national apexes, concerned state governments, etc. so that the programme strategies are integrated with other agency's institutional building activities. NABARD would provide to the

apex banks, only where necessary and to the extent appropriate, direct financial and manpower support from its own budgetary resources for implementing and planning of the ISP schemes at the apex bank level and train, guide the apex bank staff to undertake ISP schemes for lower tier units. NABARD would also develop strategies for monitoring and evaluation of the ISP schemes, develop systems and methodologies to collect, analyse, interpret and present information for assessing the performance of the ISP schemes of individual banks and programme as a whole, identifying the needs of the client banks, reviving ISP strategies and evaluating the overall impact of ISP on the credit delivery system.

12.38 We envisage that an ISP scheme would be developed for each individual identified bank depending on its needs within the overall programme framework. Each scheme would utilise any or all of the components and resources indicated in para 12.33. The Regional Offices of NABARD would have a crucial role to play in planning and implementation of the scheme for each bank. Initially, it would be the responsibility of the regional office to identify, on the basis of the stipulated criterion, individual banks whose performance warrants ISP. Regional Offices would guide the apex banks in planning and formulating the ISP schemes for each individual bank, approve the schemes and commit NABARD resources for their implementation. They would manage operations of NABARD's activities in the scheme implementation, monitor the progress of the ISP schemes, ensure that schemes are conducted in accordance with the guidelines and procedures and liaise with state governments to ensure their commitment and active support to the schemes. Regional Offices would bring about effective co-ordination of various agencies implementing schemes and involve themselves actively in the working of state and district level review committees. For monitoring and evaluating the schemes they should collect, analyse and channelise the relevant information on ISP to the Head Office of NABARD, as required.

Apex Banks

12.39 Apex banks would be primarily responsible for planning and implementing ISP for their own banks, where identified for the programme. They would also assume responsibility, with proper guidance from NABARD, for planning and formulating ISP schemes for individual DCCBs, PLDBs

identified for undergoing ISP, monitoring their implementation and assisting the affiliated banks in completing the schemes. In other words, each apex bank would be responsible for planning and implementation of ISP schemes at all levels, viz., apex, district and primary. They should arrange for logistic, manpower, financial and other resources and technical assistance both for their own ISP schemes and those of their affiliated banks. Where necessary, the apex banks may depute their own skilled staff to the affiliated banks to plan, implement and monitor their ISP schemes and in all such cases apex banks would invariably themselves bear all the establishment cost of the staff so deputed. They would obtain necessary support for the schemes from state governments, NABARD, national level institutions, etc. It would be the responsibility of the apex level to establish the state level and the district level review committees for co-ordinating the efforts of all institutions involved in ISP schemes within the state, act as convenor for these committees and provide secretariat assistance to them. For this purpose, each apex bank would establish an operational cell within the bank with clearly defined authority and responsibility to implement its own ISP and supervising the ISP schemes of affiliated banks/branches, and advise/assist its affiliated units for improving their progress. The apex level would also collect from its affiliated banks and supply to NABARD/government relevant information needed in the context of the ISP.

DCCBs and PLDBs

12.40 In the same manner as the apex banks, we envisage that the DCCBs and PLDBs would be primarily responsible for the implementation of their own ISP schemes. DCCBs would also undertake revitalisation of the primary agricultural credit societies which are in need of strengthening. On receipt of recommendation from NABARD that the DCCB/LDB is in need of ISP scheme, it is for the board of the bank to consider the recommendation and if it accepts the proposal, undertake the responsibility for the scheme. The board would also make a specific commitment regarding the efforts it would make for improving the equity, internal resources, etc. of the bank. We specifically suggest this because, in the past, many banks have shown tendencies to treat the earlier rehabilitation programme as something imposed from above and have failed to show adequate interest and involvement in implementing the programme. Each bank would establish within

the bank an operational cell with requisite authority and responsibility to implement the scheme. It would utilise the district level committee to mobilise local support for the scheme, co-ordinate the work of all agencies involved in the scheme, monitor the progress in conjunction with apex bank and NABARD and take action to improve the performance as advised by the co-ordination committees, apex bank and NABARD.

State Governments

12.41 State governments have a crucial role to play in the ISP schemes of co-operative banks. It is necessary that state government machinery is involved in ISP schemes as closely as possible because state policies do greatly influence such vital aspects of the credit system as the climate for recovery which would be an essential factor for the success of the scheme. State governments should also take initiative in implementing the programme, liaise with NABARD, apex banks in determining the financial, administrative and manpower needs of and providing requisite logistic support to the concerned banks as envisaged in the ISP schemes. State governments are expected to actively participate and play a leading role in the state and district level review committees. They will also provide policy support and direct, as a part of the ISP, timely implementation of the restructuring, liquidation and or amalgamation process of co-operative banks/societies where necessary and such other administrative support as for instance for recovery of overdues through legal measures.

12.42 It needs to be further stressed that Government assistance is a very crucial input for the success of the ISP schemes. It has been the experience in the past that, in many states, Government assistance, on an adequate scale, has not been forthcoming for such programmes and it is to this that the failure of the rehabilitation programmes was often attributed. It is our apprehension that the ISP schemes may meet with similar fate unless the state governments take upon themselves to ensure provision of adequate government assistance as envisaged in the ISP scheme for each bank.

E) Co-ordination

12.43 For the successful implementation of the ISP, it is of utmost impor-

tance to bring about effective co-ordination amongst various institutions at different levels - national, state and field level. Primarily, co-ordination would be between NABARD and the apex banks/their affiliated units; then between the credit structure on the one hand and state governments/their district administrative machinery on the other. Similarly, the activities of NABARD and state governments for strengthening the credit institutions will have to be co-ordinated with development efforts of Government of India and other national level institutions. The institutional framework for co-ordination would be mainly in the form of state level review committees and district level review committees. The state level committee will oversee ISP schemes of all banks in the state while the district level committee that of all banks/branches/societies in the district. As convener of committees, primarily it will be the responsibility of the apex bank to convene meetings of the committees, provide information to them and to see that institutions actually take action as per recommendations of the forum. NABARD would also take initiative to ensure proper functioning and maximum utilisation of these Committees. The framework, roles and responsibilities of these committees as envisaged by us are given below:

State Level Committee

12.44 i) Indicative Membership

Chief Executive/Officer-in-Charge of the apex banks (Chairman and provision of secretariat), RCS, state government departments of agriculture, rural development, institutional finance and others as needed, state officers of national institutions directly involved in ISP scheme, RBI, NABARD and chief executives of affiliated banks implementing ISP schemes.

- ii) Frequency of meetings
Every three months.
- iii) Role
Provide a forum to co-ordinate and monitor ISP schemes.
- iv) Responsibilities
 - a) approve ISP schemes and confirm the commitments of participating institutions,
 - b) guide the apex/sponsor bank in implementation of ISP schemes,
 - c) monitor and evaluate progress and impact of schemes and

- initiate action to improve performance as needed, and
- d) provide information for all institutions at state and national levels to assess their policies and programmes in respect of ISP.

District Level Committees'

12.45 The framework, role and responsibilities of the District Level Committee should be identical to those of the state level committee. The Committees headed by officials of apex banks should have membership comprising departmental officials at the district level, representatives of NABARD and affiliated banks implementing ISP schemes. Meetings should be so timed that information on the committees deliberations can be passed upwards and reviewed at the next state level committee meetings.

F) Methodology and Implementation Guidelines

12.46 Each ISP scheme will be tailored to the specific needs of each individual bank. The development and implementation of individual ISP programmes for banks should be conducted in six stages :

- Stage I - Identification
- Stage II - Analysis
- Stage III - Preparation of Programme
- Stage IV - Approval of Programme
- Stage V - Implementation
- State VI - Monitoring and Evaluation

The methodology of each stage is outlined below.

Stage I - Identification

12.47 NABARD would obtain relevant data and identify the banks which warrant institutional strengthening. On identification, NABARD should formally recommend the names of such banks to the apex bank suggesting that the apex bank may take up the institutional strengthening programmes for those banks. Should the apex bank not accept NABARD's recommendation, NABARD shall formally advise the apex bank, concerned state government, and RBI that -

- i) It would be constrained to withdraw forthwith all refinance facilities to the identified non-solvent banks and in the case of those which are approaching the loss of solvency status it will withdraw refinance facilities and institutional support in case the identified banks later become non-solvent.
- ii) NABARD would consider, in consultation with RBI, the question of providing alternative and/or additional arrangements within such identified bank's service area to maintain the flow of credit to the borrowers where necessary.

Stage II - Analysis

12.48 On acceptance of NABARD's recommendation, the apex bank should constitute a small 'Task Force' to make an initial analysis of the bank's working to assess whether it has the requisite potential to become a viable institution. If the initial report reveals that the bank is unlikely to be viable, RBI/NABARD should decide in consultation with the state government to liquidate, amalgamate or restructure the bank. In the case of failure on the part of the state government to initiate necessary measures, NABARD should again formally advise the apex bank/state government, of its intention to withdraw its support along the lines stated in para 12.47 above.

Stage III - Preparation of Programme

12.49 In the case of the potentially viable banks capable of undertaking ISP schemes, the apex bank should constitute a ISP Planning Team in consultation with NABARD. The Team should be headed by a senior officer of the apex bank and made up of apex bank staff supplemented by NABARD staff and in the case of ISP schemes for apex banks, if considered necessary, consultants funded by NABARD. The Planning Team should, in the case of each identified bank :

(a) identify the basic problems, (b) analyse causes of the problems, (c) prepare recommendations for the solution to the problems, (d) assess the resources required for the purpose, and (e) identify areas/opportunities for expansion of bank's activities and prepare a detailed scheme and action plan for the bank's ISP. For each component of the plan, the team should

develop detailed proposals covering (a) specific targets and time frame for their achievement, (b) resources required and (c) constraints and dependencies. Concurrently the apex bank should establish the co-ordination committees at district and state level.

Stage IV - Approval of Programme

12.50 The apex bank should send the programme to the district level/state level co-ordination committees. The co-ordination committees should formally adopt the programme and each institution involved should formally confirm its commitment to it at that stage. On adoption by the co-ordination committees, the programme should be sent to NABARD for approval.

Stage V - Implementation

12.51 The apex bank or district banks would be primarily responsible for implementing the ISP scheme in accordance with the plan and time table agreed upon. The apex bank should guide and support its affiliated bank throughout the implementation period. The apex bank/district bank should establish a special cell within the bank, for implementation on a day to day basis, staffed by senior officers, with adequate authority, operating funds, logistics and administrative support. The apex bank cell should co-ordinate the inputs of other institutions supporting the scheme, supervise affiliated banks undertaking ISP schemes and ensure that the co-ordination committees have full information for their effective functioning.

Stage VI - Monitoring and Evaluation

12.52 Monitoring and evaluation should be a continuous process to assess both progress and effects of ISP schemes. Monitoring and evaluation should review the progress of each scheme or group of schemes, if being implemented by a single apex bank, in terms of the implementation time-table, in regard to :

- i) achievement of targets envisaged in the programme;
- ii) staff recruited and trained;
- iii) systems and procedures developed;
- iv) expansion of bank's activities.

Information regarding the progress should be compiled by the bank and presented to the co-ordination committees for their review.

12.53 Qualitative and quantitative information should be collected continuously by apex bank staff and presented to the co-ordination committees for their review. The committees should evaluate the information in order to :

- i) assess the results of ISP schemes;
- ii) advise the bank to revise schemes as needed; and
- iii) provide information and the committee findings to all other institutions including NABARD.

The committees should evaluate performance and advise the bank/other institutions to take action to ensure that implementation time-table remain on schedule, where necessary.

12.54 Based upon the information generated, NABARD should assess the progress of :

- i) each scheme;
- ii) each group of schemes under a single apex bank;
- iii) all schemes within the area of a Regional Office; and
- iv) all schemes nationally (at Head Office).

At each level, NABARD should, as necessary :

- i) offer guidance and additional assistance to banks individually to promote scheme implementation ;
- ii) offer more general guidance to banks upon implementation and undertake new initiatives to cope with common problems;
- iii) review and revise operating guidelines and programme components.

G) Resource Requirements

12.55 The Planning Team preparing the individual ISP schemes will assess the financial and manpower resources required under the scheme. While it is not possible, at this stage, to quantify the overall resource require-

ments of the programme, in general terms, the likely resources needed for implementing ISP schemes would come under following categories :

- i) Manpower
- ii) Budgetary provisions
- iii) Refinance

The requisite resources should be forthcoming, in appropriate measures, from all agencies, viz., apex banks, state governments, NABARD (in the case of apex banks undergoing ISP) in addition to the identified bank implementing the ISP scheme.

Manpower

12.56 The quality of manpower required for ISP schemes should be high in terms of professional skills, experience and attitude. In cases where bank implementing the ISP itself does not have the required quality of manpower, NABARD should provide it upto the level of apex banks and apex banks to their affiliated DCCBs and PLDBs. The long-term strategy would be for the bank to strengthen its own manpower by recruiting well qualified and experienced persons at various levels particularly executive levels and providing adequate training to them.

Budget Provisions from Institutions

12.57 In the case of the banking sector, specific provisions would be called for in their operating budgets for deployment of separate staff for ISP schemes (in the case of NABARD and apex banks also in respect of staff that they may have to depute to apex/affiliated banks respectively). The provisions would comprise, their establishment expenses including travelling and daily allowances, expenditure on staff training of banks under ISP, technical assistance including costs associated with outside consultants, where deemed necessary, for preparation of ISP schemes, etc. State governments would also be required to make specific budget provisions regarding financial assistance in the form of additional equity participation, term loan assistance for maintenance of non-overdue cover, contingent liabilities arising out of guarantees to be extended to co-operative banks, etc.

12.58 Grants-in-aid may be an essential component of the ISP schemes to support weak banks to take up these schemes without straining their finances. While state governments would primarily be responsible for providing this type of assistance, NABARD (from its R & D fund) and apex banks (from their development funds) should be in a position to extend support, on an appropriate scale, for specific purposes like cost of additional supervision staff, cost of establishing ISP cells in banks, etc.

Refinance

12.59 It is envisaged that the non-solvent banks brought under ISP schemes would continue to be eligible for NABARD's schematic term loan finance. It is imperative that the DCCBs under the programme are provided refinance by way of short-term and medium-term credit limits and refinance for conversions, etc. irrespective of the level of their overdues and other norms of eligibility in the normal course. We would also expect NABARD to adopt a liberal approach in the case of banks implementing ISP schemes and provide them appropriate refinance facilities to enable them to diversify their loan portfolios and expand lending operations for reaching viable status, expeditiously. However, as indicated earlier in para 12.17 schematic term loan refinance would be subject to the concerned banks showing a progressive improvement in recoveries atleast under current demand and achieving, in the next two-three years 80 per cent recoveries in respect of their current demand. Failure of the concerned banks to comply with the above condition would attract the penalty of complete stoppage of refinance facilities from NABARD.

Commercial bank branches

12.60 As stated earlier, the above guidelines would apply equally to the ISP schemes for commercial banks' branches with suitable modifications having regard to differences in their structural and financial set-up, etc. Unlike the comprehensive nature of the ISP for co-operative banks which is intended to retrieve them from insolvency, the ISP for commercial banks would be relatively simple, aimed at improving their recovery position and consequently their eligibility for refinance from NABARD. Thus, in the case of commercial banks, the target group would comprise branches which fail to achieve the recovery upto 40 per cent of current demand and 25 per cent under arrear demand by 30th June 1992, or those failing to maintain

recoveries at this level in the subsequent years. The ISP would aim at providing assistance to identified target group of branches to enable them to attain a stipulated level of recoveries under agricultural lending and keeping a sustained flow of credit to the agricultural sector. The major objective of the ISP schemes would be

- a) to identify the causes of overdues, take steps to overcome them and prevent their recurrence,
- b) improve the quality of loan appraisal and supervision over credit, and
- c) improve and enhance their management capacity and skills of staff and for this purpose provide such technical and financial assistance as the identified branches would require for implementing the ISP schemes.

12.61 As in the case of co-operative banks, each ISP would, in this case also, be a time-bound action programme and, therefore, concerned bank in each case will have to ensure that the identified branches are able to improve their recoveries to the desired level, failing which it will be left to the discretion of NABARD whether and to what extent refinance facilities be extended to such branches. The planning, implementation, monitoring and evaluation of the programme will be the sole responsibility of the Head/ Zonal/Regional Office of the concerned bank and the programme would be exclusively funded by the bank itself. NABARD as the apex level institution for the banks involved in agricultural credit would provide general guidance in formulating ISP schemes and oversee the implementation thereof, besides providing to the branches implementing ISP schemes, refinance facilities towards term loaning on a requisite scale. Unlike co-operatives, Government will have no role in the ISP of commercial banks' branches. Similarly, there is no need for any co-ordination machinery except such machinery as the concerned bank may like to build up within itself for overseeing proper implementation of the programme.

CHAPTER XIII

STAFF TRAINING AND MANPOWER DEVELOPMENT

Concept of Training

In the Indian context, to the bankers as partners in the economic development process, every change is a challenge to be met and knowledge provides the strength to convert these challenges into opportunities. But to so do, knowledge needs to be transformed into skills and this is a function of training. Viewed in this context, training becomes an investment in "Knowledge Capital". This capital resource is subject to both amortisation and obsolescence. It needs to be continuously updated and expanded. Training is, therefore, a continuing process and has become an important function in the management of human resources.

13.02 With the growing diversification of activities in banks and greater involvement of the people in banking, banks are called upon to face newer challenges and innovations, necessitated not only by expanding area and volume of business, but also by the ever changing socio-economic and political environments. This calls for developing appropriate training programmes for the bank personnel, to adapt themselves to these continuously changing needs and to meet the demands of changed circumstances. This also calls for multiple skills to be developed by the bank personnel. Banking which is essentially a service industry, is becoming more and more complex, more so rural banking. A banker has to deal with and extend service to a variety of functions - loans, deposits, remittances, etc. and hence a variety of customers. For a rural banker, in particular to be effective, one has to have not only the knowledge of banking per se, banking laws and practices but also various other skills. For instance, he has to have the right approach, attitudes and a style of management which is conducive to the genius and ethos of rural areas. He should have the knowledge of banking. He should also have the ability to assess the economic potential of the area in terms of the activities which offer scope for developing bank's loaning business. Effective communication ability is another quality which a rural banker has to possess so that he could deal with the rural clientele and earn their confidence.

13.03 The key components of a proper training system for the rural banker should be

- (i) meeting the needs of the financial institutions;
- (ii) skill upgradation ; and
- (iii) development of the overall personality as a banker

Training as a process of management intervention in these areas has been well recognised, for training facilitates meeting the ever changing and challenging competitive environment in which the banking organisations and bankers have to function. One has also to recognize that man-power development, man-power planning and strategy planning are closely inter-related activities. Strategy planning and man-power planning provide an useful framework for carrying out training and man-power development exercises more meaningfully. Without these supporting exercises, training per se is prone to degenerate into an organisational ritual carried out for its own sake.

13.04 Man-power planning aims at anticipating the future needs and supplies of man-power and taking advance action by establishing strategies in the area of recruitment, training, transfers, promotions, management development and retirement. A good man-power planning system achieves these objectives by recruiting proper people, training them, providing proper placement, job rotation and promotion and career development opportunities. Training and man-power development ultimately aim at developing appropriate beliefs and values and transforming the organisational culture thereby.

13.05 One lesson which emerges from experience in agricultural banking is that policies have often marched ahead of organization and organization, ahead of personnel. The relative lack of adequately trained personnel has been a major constraint in both the deepening and widening of credit in pursuit of rural development. And at a time when the requirement for adequately motivated and trained man-power is growing substantially as a result of the increase in the volume and variety of banking services and progressive changes that are on the anvil in the working methods of banks.

13.06 The problems of commercial banks in the development of banking for rural lending are low motivation as well as gaps both in knowledge and skills. Above all, the low level of sympathy for the disadvantaged classes and

over-shadowing all these, the bureaucratic approach are the other causes. In the co-operatives and RRBs there are, in addition, problems of recruitment based not unoften, on patronage, caste and community considerations. Governmental agencies at the ground level are also not free from some of these deficiencies. It is against this background one has to review the existing training arrangements in banks in the country.

Existing Training Arrangements

i) **Commercial Banks**

13.07 The need for training was recognized and beginnings made in the banking industry as early as in the early fifties and these were organised broadly to meet the immediate organisational needs. Prior to this, the belief was that an employee would learn as he worked. The Report of Adarkar Committee (1968) constituted an important landmark in training in commercial banks. For the first time, it established the need for a link between training, manpower development and personnel policy. The committee had emphasised that training would acquire a meaning and purpose only when it was properly linked with recruitment, performance appraisal, placement, transfers, promotions, job rotation, career planning and succession planning. Professionalisation of the management and preparing bankers for their new role were the main objectives for training as seen by the Adarkar Committee. The committee also recommended the establishment of a national level training institute to monitor the functioning of training colleges and training centres of commercial banks.

13.08 Nationalisation of banks in the year 1969 gave further impetus to training. The National Institute of Bank Management (NIBM) established in 1969, held a number of seminars and conferences on training, man-power planning, personnel management and other related management issues. The Department of Banking, Ministry of Finance, Government of India subsequently constituted a Committee of Direction for training in public sector banks. This committee in turn appointed a number of working groups to study the problems of training and man-power development in commercial banks. NIBM also appointed a number of task forces for the same purpose. As a result of all these efforts, some basic infrastructure for training in commercial banking has been created. At the industry level, there are at present seven institutes viz. The National Institute of Bank Management (NIBM), the Bankers' Training College (BTC),

the College of Agricultural Banking (CAB), the North Eastern Institute of Bank Management (NEIBM), the Northern India Bank Staff Training College (NIBSTC), the Southern India Banks' Staff Training College (SIBSTC), and the Bankers' Institute for Rural Development (BIRD). Each of these institutes offers 40 to 100 programmes (conferences, workshops, seminars etc.) in a year on general banking as well as on rural banking. At the bank level, there are in all about 30 staff colleges and 150 training centres. Each public sector bank has a staff college (SBI has 4 staff colleges while some others also have more than one) and a number of training centres. The college is the apex institution at the bank level and is meant for training middle and senior level managers. The training centres on the other hand are meant for training workmen staff and in some cases training of junior officers. The number of such training colleges/centres has been continuously increasing. It increased from 209 in 1985 to 237 in 1987. In the various programmes conducted by these colleges/centres about 3.04 lakhs staff have been trained during 1987 as against 2.26 lakhs in 1985 and 2.66 lakhs in 1986.

ii) **Regional Rural Banks**

13.09 In the initial stages, the staff of the RRBs were provided by the sponsor banks. When fresh recruitment was made both at officer and clerical levels in RRBs, arrangements for training of officers were made at CAB, Pune. Subsequently a decision was taken to entrust the responsibilities of induction training of newly recruited officers of sponsor banks and to bring these officers to CAB only after a couple of years, for training in various functional courses. Accordingly, the sponsor banks organised short duration courses from one week to two weeks for officers of RRBs. The clerical staff of RRBs were expected to be trained while on the job and at the training centres of the sponsor banks. No systematic efforts were made to train RRB Chairmen prior to their posting. All the training and orientation in regard to RRBs, they had, was the briefing at the sponsor banks. These arrangements were obviously unsatisfactory and needed changes. Over the years NABARD came to take over the responsibility of training the RRB personnel. The structure of training of RRB personnel today comprises primarily of the Bankers' Institute for Rural Development (BIRD) at Lucknow and two other training centres, one at Bolpur and another at Mangalore both set up by NABARD. Training centres set up by sponsor

banks exclusively for training of RRB personnel and capacity reserved by them in their staff colleges and training centres also are available for RRB personnel.

iii) **Co-operatives**

13.10 The importance of training in co-operatives has been emphasised repeatedly, as early as in 1928 by the Royal Commission on Agriculture and in 1935, when the Darling Report proposed a comprehensive scheme for training of co-operative officials. The Co-operative Planning Committee (1947) examined the issue and pointed out the inadequacy of training facilities. The All-India Rural Credit Survey Committee (1954) recommended the integrated scheme of rural credit and a comprehensive scheme for training co-operative personnel as an integral part of the system. As a result, the Central Committee on Co-operative Training was constituted jointly by Government of India and RBI. In 1962, the responsibility for these training programmes was transferred from RBI to the Committee of Co-operative Training which was later constituted as National Council for Co-operative Training (NCCT). During the past fifty years, the co-operatives could build an impressive infrastructure for co-operative training. At the top there is NCCT as part of the National Co-operative Union of India (NCUI). The NCCT is responsible for formulating training policies and for organising and managing the training functions. The Vaikunth Mehta National Institute of Co-operative Management (VAMNICOM) is the apex training institution which offers a variety of training programmes for senior and top level executives of co-operative institutions. In a year, it conducts 50 to 60 programmes and trains about 1200 to 1500 participants. There are 17 colleges located mostly in state capitals to cater to the training needs of intermediate personnel. These colleges conduct about 350 to 375 programmes in a year. In addition there are 89 junior level training centres which are managed by state level co-operative unions. They conduct diploma courses in co-operation and various programmes for clerical staff of the co-operative departments, different co-operatives and organisations and secretaries of the PACSs. There are 14 junior level training centres of LDBs which train rural branch managers and clerical staff of SLDBs and PLDBs. NCDC has also entered the field of training and set up an apex training institute known as Training of Personnel in Co-operatives (TOPIC) at Delhi and training centres in various states. They cater to the training needs arising from the EEC Project for construction

of rural godowns. Some of the co-operative personnel, particularly the senior and middle level officers also get training in senior level training institutes like BIRD, CAB, etc.

iv) **National Bank for Agriculture and Rural Development**

13.11 In support of its institution building efforts, NABARD has been providing a variety of training to officers of other banks-commercial banks, RRBs, SCBs/DCCBs and SLDBs - as well as to its own staff. NABARD's central training institute is the Bankers Institute for Rural Development (BIRD) at Lucknow. BIRD has capacity to run two streams of training courses with 30 participants each. BIRD now concentrates its training activities on RRB officers. Besides BIRD, NABARD has established two Regional Training Centres (RTCs) at Bolpur and Mangalore, which provide training to officers of the RRBs in their respective regions.

13.12 NABARD has also been providing faculty and financial support to CAB, Pune. The basic objective of CAB run by RBI is to provide training for senior and middle level officials of co-operative banks, commercial banks and Government departments concerned with rural development programmes. The college is considered as the apex level institution for training in rural banking. CAB conducts a number of regular programmes as well as specialised training courses on various subjects like agricultural lending, project planning and appraisal, financing of SSI units etc. CAB trains about 2300 officials in a year.

13.13 NABARD has been providing financial and other support to the Junior-Level Training Centres (JLTCs) of SLDBs which cater to the training needs of technical officers, loan superintendents, field assistants and Junior-level staff of SLDBs. The annual course calendars of these JLTCs as well as course modules are approved by NABARD.

13.14 The World Bank's NABARD Credit I Project includes US \$6.5 million for staff training of NABARD and participating banks. The World Bank recommended that besides continuing existing training programmes, NABARD should implement and monitor an experimental training programme for select branch managers of about 10 SLDBs, 15 to 20 RRBs, and five commercial banks

for improving rural branch operations. Accordingly, NABARD launched a training programme on "Rural Branch Management and Credit Delivery" for rural branch managers of commercial banks, RRBs and LDBs, designed to show rural branch managers how to enhance the quality of lending, improve recovery and streamline branch administration.

13.15 Following are the important training programmes conducted or supported by NABARD :

i) **Rural Development Projects Course**

A programme of four weeks' duration which focuses on improving the capability of participants to identify, formulate, appraise, implement, monitor and evaluate various types of agricultural and rural development projects. Trainees are senior and middle level officers of commercial banks, LDBs, SCBs, RRBs and government, as well as of RBI and NABARD.

ii) **Training Programmes for Selected Technical Disciplines**

These are short duration courses in animal husbandry, fisheries, forestry, plantation and horticulture schemes, etc. conducted primarily for officers of client banks and NABARD staff.

iii) **Rural Branch Management and Credit Delivery**

The programme is aimed at upgrading the skills of rural branch managers and to improve the efficiency of their branch operations. The programmes emphasise subjects related to credit delivery, recycling of funds, and improved branch operations and has also been introduced in selected participating banks.

iv) **Training of Trainers Programmes**

This is designed to accelerate the training process and is meant for trainers from participating banks as well as from NABARD.

v) **T and V Programme**

Under the programme Mobile Job Trainers selected from experienced staff members of RRBs/sponsor banks visit selected branches of RRBs periodically to provide on-the-job training. This has several features in common with NCDC's training through "mobile guides".

vi) **Training for NABARD Staff**

The training courses conducted by NABARD for its own staff include mainly induction training for newly recruited or promoted officers, inspection oriented training courses for its inspecting officers, programmes for officers appointed as nominee directors on the boards of RRBs and executive development programmes for senior level staff.

13.16 Upto June 1987, 24,819 persons were trained by ARDC/NABARD in various senior and middle level courses for LDB, commercial bank, RRB, SCB, DCCB, State Government, RBI and NABARD officers. Given the numbers of LDB staff already trained and their likely recruitment in the near future, their training needs may have been substantially met. With this exception the output of trained personnel is still far below the evident needs.

Training for Rural Lending in Banks - An Assessment

13.17 We have observed several weaknesses both quantitative and qualitative in the present training arrangements particularly relating to rural banking. As already mentioned, the commercial banks could build over the years an impressive infrastructure for training their personnel, with an annual capacity of about three lakhs. With the current level of staff at about nine lakhs including RRB staff and possible recruitment in the near future, we feel that the infrastructure facilities in the commercial banking sector are by and large sufficient to meet the training needs of their personnel. However, the position is different in the case of co-operatives except LDBs. Their annual capacity for training is much less when compared with the total staff in the co-operative structure.

13.18 As far as the quality of training is concerned, the most glaring weakness has been the inadequate linkage between planning and training and near absence of strategic planning in many banks. As a result, training and man-power planning have not taken firm roots in most of the banks. In many major banks business planning is done on an annual basis. As a result, corporate appraisal is not adequately done in these banks. Qualitative training needs for the banks as a whole as well as the various target groups for training are not properly identified on a long term basis. Individual training needs are expected to be identified on the basis of performance appraisal reports and career path planning. In the absence of succession planning and career path planning,

individual training needs are not very effectively identified. The training activity has failed to focus sharply on the training needs of the banks as well as of the individual employees. Many important target groups which are in need of training are remaining untrained. Planning for training lacks a long-term perspective and in most banks it is done on an annual basis. The objective of training appears to be full utilisation of infrastructural facilities and reporting of impressive output of numbers of trainees. The entire approach is supply oriented rather than demand oriented.

13.19 When attention is on numbers, little care is exercised in selecting the trainees appropriate to the training programmes. Any one who is easily available or can be easily spared is sent to complete the targets and not necessarily for meeting the training needs of the banks or of the employees. By and large the training institutions also keep the eligibility criteria for selection of candidates vague. In this atmosphere, it is no wonder that trainees perceive training as a diversion from routine work rather than as an opportunity to equip themselves with better skills. Similarly post training placement is not given adequate attention. Consequently, there is practically no post training follow-up and gains if any from training are not fully transferred into job performance. Overall, training has failed to make the required impact. Training is loosely coupled with man-power planning and so is man-power planning with corporate planning.

13.20 Training is not perceived as an essential need by the operating managers and the image of training in the line organisation is not very high. Many of them see training as a sterile academic activity mostly as a consequence of the way in which training is given. This in turn, affects the motivation of trainees. The quality of classroom teaching, post training follow-up and on-the-job coaching leave much to be desired. Training practices which are in vogue today succeed only in imparting knowledge. The skill and attitude aspects do not receive adequate attention. Training is also not geared to increase the performance capability. Except in a few cases, little effort seems to have been made to produce new training materials and course designs.

13.21 Training and man-power development are also intended to transform the organisational culture so that the social objectives of banking can be

achieved. Ideally they should meet the man-power needs of the banks and career aspirations of the employees. The training system as presently obtaining in commercial banks has to go a long way to achieve this end. The story of training and man-power development in RRBs is not much different from what it is in commercial banking. Their smallness and compact size do not seem to have given them any advantage. The situation seems to be worse in RRBs. We have recommended elsewhere merger of RRBs with commercial banks. Consequently, the responsibility for training the present RRB officers would fall on the commercial banks.

13.22 Training in the co-operative sector has had an early start and work was done on a more or less planned basis. The objectives had been clearer right from the beginning. The RBI took considerable interest in the development of training in co-operatives. The Central Committee for Training in RBI had systematically developed within a short time a sectoral level training structure comprising a net work of institutions at various levels of hierarchy with clear lines of specialisation. Thus the co-operative sector had, generally speaking, the advantage of a well developed training structure. These advantages however have been out-weighed by certain deficiencies endemic to the co-operative sector. The quality of staff recruitment left much to be desired. Caste, kinship and class considerations played a dominant role in recruitment and consequently the staff in some co-operatives was not of the desired quality. In the absence of cadres, professionalism and scientific approach in personnel management was absent. Domination of vested interests had its impact on discipline and quality. These factors had also reduced the effectiveness of training in co-operatives.

13.23 As in the case of commercial banks, management of the training function in co-operatives also is characterised by a degree of casualness. Selection of trainees and their post-training placement is not being done with due care. Training is not seen as an organisational need. Training is not being used as a strategy for organisational development for accomplishing corporate objectives. The general atmosphere in banks is not favourable to training. The decision makers are not fully committed to training. The quality of institutional training and classroom teaching are below the required standards. The predominant teaching method is lecturing. The case method and other

participatory methods are used only in a limited way. Little effort is made to develop teaching material. Naturally in this atmosphere the trainees are not intrinsically motivated. On the whole, perception of training and its role are very narrow in the co-operative sector.

13.24 These weaknesses were more evident in the case of training of Secretaries of PACSs. The co-operative training institutes have so far not been specialised institutes for training of secretaries of PACSs in banking functions. These institutes are in general very small, with small sized staff strength and having to train employees of all kinds of co-operatives, with a variety of activities and needs. In consequence, the training in these institutes has tended to be very general and theoretical with little links with actual practice. It is certainly not adapted to the special needs of secretaries and other personnel of PACSs. Moreover, there is very little influence of the SCBs on the programmes intended for secretaries of PACSs. Hence there is an immediate need to create with the SCBs specialised institutes for training of secretaries of PACSs. The SCBs/DCCBs with active support from the State Government should address themselves to this task on a priority basis.

Recommendations

Qualitative Improvements in Training

13.25 As we have mentioned earlier, there is a need to improve the quality of training in most training institutes. Our suggestions in this regard are:

- i) The general banking aspects should be covered in basic induction training in banking and branch management. This would enable the course in rural banking to concentrate on specific rural banking issues.
- ii) While there should be less emphasis on general lectures, the theoretical aspects should be covered with reference to area-specific schemes completed or on-going. Some area-specific knowledge of socio-economic background, agricultural technology etc., should be given before discussing formulation of schemes. Schemewise, the sessions should cover technical background, formulation of schemes and discussions on concrete case studies.
- iii) The need for participative training has to be fully recognized and each session should be so designed as to provide scope for the parti-

cipation of trainees. Trainees should be encouraged to bring with them live problems relating to rural lending.

- iv) The field visits and exercises based on do-it-yourself approach have to be given more time.
- v) A brief written test may be introduced at the end of each course. This, apart from making the trainees alert and attentive, helps them know how much training they have imbibed
- vi) Behavioural aspects of rural branch management have to be discussed in greater detail. Communication-cum-relationship strategy for dealing with branch staff, controlling offices, borrowers, government officials, etc. has to be worked out based on practical experiences.
- vii) Case studies of good rural branches should be prepared to identify the factors contributing to their efficient functioning. Similarly there are number of schemes which have proved successful. Case studies of such successful schemes should be prepared and discussed in the training programmes.
- viii) There is a need for regional orientation of training courses so that branch managers could discuss the specific problems pertaining to their regions.
- ix) It is advisable to train the whole staff of a branch or at least many of them at the same time. This will minimise chances of resistance to new ideas in the branch later.

Training in Short-term Co-operative Credit Structure

A. Training of Secretaries

- 13.26
- i) Basic training in Co-operation (diploma course) can remain with Co-operative training institutes under supervision of State Co-operative Union (SCU).
 - ii) There is, however, an urgent need for specialised institutes to train secretaries of PACSs so that they can improve their functional capabilities.

- iii) These institutes must be a part of the SCB, which as the leader of the co-operative credit structure in the state should be responsible for the quality and the training of secretaries.
- iv) In every state with about 4,000 PACSs or more, there must be SCB's own institute of sufficient size in order to make it possible to train regularly the PACS' secretaries and staff of SCBs and DCCBs who have close contacts with PACSs.
- v) SCBs with less number of PACSs should join together to set up the training institute or co-operate with a bigger SCB.
- vi) These institutes should have some mobile trainers in order to follow-up the training imparted at the institute at the field level and to guide secretaries wherever necessary.
- vii) The training as we envisage, apart from improving the skills of the secretary in credit dispensation and mobilising savings, should also equip him to advise, guide and stimulate members to take up profitable activities in agriculture or other activities.
- viii) Subjects like psychology of rural people, psychology of group behaviour and the role women can play in developing the village, should be given emphasis.
- ix) The Faculty in these institutes should be staff members of the SCB so that it is possible to bring them temporarily back to operations after a few years of teaching. This is necessary in order to avoid the gap between training and practice.
- x) A Committee of SCB managers nominated by the National Federation of State Co-operative Banks (NAFSCOB) can work together with NABARD to develop the necessary course modules and training material which can be adopted in all the proposed training institutes for secretaries.
- xi) A regular check on the results and the effectiveness of the training efforts should be done by an independent institute.
- xii) All the general recommendations mentioned earlier in the chapter with regard to the quality of training are applicable to these institutes also.

B. Training of the Members of the Management Committees of PACSs

13.27 There is an urgent need to train members of the Management Committees of PACSs so as to avoid any gap in the perceptions of the management committee and the secretary. For successful functioning of PACSs both should have the same ideas and policy. We see a need for two levels of training for the members of the Management Committee. They are :

- i) A basic training programme in co-operation which has to remain with the SCU. In such programmes it is necessary to give preference to the Management Committee members of those PACSs, whose secretaries are going to be trained. It is also necessary to have proper co-ordination between SCB and SCU in this regard.
- ii) Second, besides the basic training suggested above, there is a constant need to update the knowledge of the Management Committee members on various developments in the co-operative credit and measures they have to initiate. In our opinion, these refresher programmes on co-operative credit should be handled by SCBs/DCCBs. In doing so, there will not only be a flow of information from SCB/DCCB to Management Committee members but also-and that is very important - a stream of information from grass root level to higher tiers in the credit organisation which can be of great use to the policy makers.

C. Training of Personnel of SCB and DCCBs

- 13.28
- i) Apart from the training of secretaries and Management Committee members, there is a need for training of personnel of SCB/DCCBs. The induction training and more elementary courses can be handled as stated earlier, by the training institutes of SCU.
 - ii) The training of middle and higher personnel can remain at the training colleges of the NCCT.

Management of Training Functions

13.29 Principals and Training Managers have the responsibility of managing the training functions. Analysis of training policies and strategies, generating policy alternatives, designing implementation strategies on the basis of policies already approved, organising the training functions, estimating training needs, preparing short-term and long-term training plans, selection and development

of faculty, linking training with manpower planning and corporate planning are some of the important tasks they have to perform. These functionaries should be trained in these areas so that they can tackle the problems of training effectively and make training purpose oriented in their institutions. Another general weakness in the existing system is the lack of information for the management of training. Required data for policy planning, strategy planning and policy analysis are not by and large generated. The data regarding un-trained staff, types of various training programmes, post-training placement, career path planning etc. should be readily available for formulation of effective training strategy. To ensure this, the personnel department of each bank has to operate closely with the training department/institute(s).

Training needs Survey

13.30 As of now, data are lacking in the area of training needs. It is, therefore, necessary that there is a comprehensive assessment of the training needs in different sectors. Such a survey has to take into account :

- i) the number and kinds of staff required at various levels, their educational and technical qualifications as also attitudes and motivation.
- ii) the availability of the staff having necessary capabilities and of others suitable for up-grading.
- iii) the specific types of training needed by the latter.
- iv) the dimensions of the new requirement and the quality of training sought.

Without such an overall assessment of the training needs it would be difficult to frame a common strategy or a set of priorities for training in rural lending. Such information as we could gather during the course of our visits to various training institutions, has quite clearly established that the existing gaps in training, particularly the qualitative aspect, are indeed vast, more so in the case of co-operatives. Since substantial increase in the financial allocation for training and manpower development is not possible by rural credit institutions, it is important that new cost saving and network expanding methods of training are devised. Some of the methods we have in mind are Correspondence Courses, Open University methods, T.V. and Video facility etc.

An Apex Agency for Training

13.31 The preparation and conduct of a survey as envisaged will require the responsibility to be handled by an agency which has both clout with all the institutional systems involved in resource mobilisation and credit delivery perception and appreciation of the problems. This apex agency should develop a comprehensive training strategy and a set of national priorities and standards. It should also simultaneously develop a plan to make optimum use of the facilities and other resources of the various training agencies and institutions. In regard to the choice of an appropriate agency several alternatives were considered and we have come to conclusion that this responsibility should rightly be assigned to the Reserve Bank of India, since in our view, the agency which could undertake such a stupendous task can only be the Central Bank of the country. We are aware that there is a Standing Coordination Committee to co-ordinate, monitor and guide training arrangements in commercial banks set up in the Reserve Bank of India with a Deputy Governor as the Chairman. The possibility of using this Committee for the task we have in mind, needs to be examined: The Reserve Bank of India should associate NABARD in view of the latter's position as the apex development bank for rural credit. It should be the responsibility of this apex agency i.e. Reserve Bank of India or its Committee, to set priorities and standards (including those for selection of trainees) for curriculum development as well as preparation of course materials and for monitoring in conformity with standards set for a comprehensive rural credit training programme. This agency will have to work in co-operation with other agencies concerned with rural credit and training to perform this function effectively so that training facilities and other resources built up so far could be used to maximum advantage.

Co-ordination among various training institutions

13.32 As earlier noted, the training programmes relating to rural lending are being conducted by several institutions. The programmes conducted by these institutions differ in coverage, substance and emphasis. Although there does exist some co-ordination among the institutions, generally each one goes its own way. We feel that there is a need for greater collaborative arrangements among these various training institutions dealing in rural banking. With the completion of the training survey as we have suggested and an apex agency for training which will oversee and guide the training system, this co-ordination can be brought about more effectively.

Role of BIRD

13.33 In view of our recommendation to merge RRBs with sponsor banks, the present thrust of training of RRB personnel by BIRD will no longer be necessary. In our view, BIRD should become an apex training institute like the NIBM with a core faculty which would be engaged in training senior executives and carry out high level research in rural credit. It will be a quasi-autonomous body having a close relationship with and strong financial support from NABARD. We also feel that the thrust of BIRD's future activities after the merger of RRBs, should be on practical training. BIRD so reorganized should concentrate more on training of trainers, production of training materials, senior level seminars on policy issues etc. Only some of the faculty members of BIRD need to be full-time and the remaining should be drafted from NABARD and commercial banks on a specific term basis. We feel that full-time faculty members without any links to operations may gradually become ineffective. In the changed context, we do not consider it necessary to have one year diploma course at BIRD as suggested by NABARD Study Group.

Training of Trainers and Hierarchy of Training

13.34 We are convinced that training of trainers is the most crucial aspect of upgradation of training arrangements. Upto now, the apex level institutions have devoted most of their attention to direct training of middle level officers. We feel that there is need for a shift in emphasis at the apex level, from direct training to training of trainers and production of training materials. NABARD should cease to carry out direct training activities except for some executive management development courses and concentrate on training the trainers, production of teaching materials and supervision of training. Direct training of their staff should be the responsibility of the apex co-operative banks and commercial banks, if necessary by organising in-house training programme.

Post Training Evaluation

13.35 As we have mentioned, one weak area in training system is evaluation. Firstly, it is necessary to evaluate the training programme itself after completion of each programme. It is necessary to ensure that after training, the placement of trainees is appropriate and relevant to the training received. It will also be necessary to evaluate the trainees on the job after the completion of training. We feel such a feed back is necessary to re-orient the training systems to make them more relevant to the demands of the job.

Computerisation of Training

13.36 We feel that the gradual introduction of computers into staff training is an ideal medium not only to increase the efficiency of training techniques but also to create computer awareness. Computers can be used by both students and the tutors. The use of computers to store information in magnetic form provides speedy flexible alternative to both training colleges and individual financial institutions. Overseas experience has shown that there is more frequent access rate to information sorted in this manner than in hard copy. We feel that NABARD should take up computerisation of training needs on a priority basis.

CHAPTER XIV

ACCOUNTING SYSTEMS AND POLICIES, COMPUTERISATION AND MANAGEMENT INFORMATION SYSTEMS

We had commissioned M/s. Price Waterhouse Asia Pacific, Hongkong for undertaking a study of the "Role of Apex Level in Agricultural Credit". The consultants were asked, inter alia, to examine the accounting systems and policies as well as computerisation and management information systems, with particular reference to agricultural lending in the banking system, including the co-operative banks. They undertook an in-depth study of the current systems in vogue and have recommended a number of measures to improve the systems. We had also simultaneously held discussions at various levels during our visits to institutions to have a first hand knowledge about the systems in vogue and against this background considered the recommendations of the consultants. We find ourselves in broad agreement with the findings of the study undertaken by the consultants as well as their recommendations for improving the current systems. This chapter accordingly deals with both the findings of the study and recommendations on which our general comments are based.

Accounting Systems & Policies

14.02 While we agree with the basic approach of the consultants in recommending adoption of the format of general ledger suggested by them, the Committee is of the view that it is not necessary that the general ledger itself should throw up all the information and analysis. The function of the general ledger is primarily to provide at one place, the update of bank's financial position, that is to say, the balance of assets and liabilities as well as the income and expenses under broad heads on a daily basis. Moreover, the maintenance of the suggested general ledger on a daily basis will be, in many cases, impossible as long as the accounting system is not computerised fully. If the subsidiary ledgers are suitably drawn up depending upon the type of information/analysis required and posted up-to-date, they will facilitate the compilation of information for statistical and MIS purposes. What is, therefore, required is to regroup the subsidiary ledgers and maintain them up-to-date to facilitate the flow of information required. Similarly the change of accounting procedure recommended in para 14.33 may be introduced after the implications of such a change are first looked into by a group of experts as suggested by us in chapter VI.

Computerisation

14.03 The need for computerisation in banking industry as a whole is recognised by all. RBI had appointed a Committee on mechanization in banks in 1983 which submitted its report in 1984. This report provides a blue print on mechanization and computerisation in banking industry during the period 1985 to 1989. We note that the recommendations of this Committee are in the process of implementation by banks and the progress made is being periodically monitored by RBI and the Government. After taking into account the progress achieved so far and the needs of the banking industry in the future to improve customer service and productivity, the RBI has constituted a Committee under the chairmanship of Dr. C Rangarajan, Deputy Governor to prepare a perspective plan for computerisation of banking services for the next five year period covering the years 1990 to 1994. The terms of reference of this Committee are :

- i) To draw up a perspective plan for computerisation of banks at the Branch, Regional/Zonal and Head Office levels for the five years from 1990 to 1994 and to recommend the strategy for its implementation.
- ii) To suggest modalities for implementing on-line banking, specially at the branch level.
- iii) To indicate the application area (like Electronic Funds Transfer, Electronic Mail, Message Switching, etc.) relating to the use of BANKNET and SWIFT.
- iv) To suggest guidelines for installation of Automated Teller Machines and other self service machines by banks.
- v) To assess the requirements of trained personnel and the need for training on computerisation and to recommend suitable arrangements therefor.
- vi) To suggest modalities for phased introduction of bilingualisation in computers used in banks.
- vii) To make any other recommendations which are incidental or related to the above terms of reference.

While this Committee will no doubt look into all aspects of the problem of computerisation in banking industry as a whole, we feel that the recommendations of our consultants which address mainly to the computerisation in rural banking units deserve due consideration by the Committee.

14.04 As we see, the acceleration of the process of computerisation is important to the commercial banks not only from the point of view of bringing about improved customer service but also from the point of view of reducing the transaction cost. Because of the very large number of branches spread all over the country and the need to compile and furnish information on various issues, considerable time has to be spent manually by the bank staff. As the whole banking system gets increasingly computerised, it will have a favourable impact on the reduction of transaction cost of the commercial banks' operations.

14.05 The consultants have observed that one of the alternative for using the computer services will be to utilise the facilities already established or proposed to be established at the district level by the NIC. We are of the view that if there is spare capacity available at the established computer facilities at district level by NIC, the banks should use the same for compiling information on their various banking operations of the branches in the district. It will be necessary for this purpose to prescribe certain returns to be obtained at the district level from all the branches of the banks in the district for feeding to the computer. We suggest that the Lead Bank of the district should have the responsibility to obtain this information to be fed to the computer. Our concern here mainly relates to regularly obtaining the data from the branches and establishing proper co-ordination of rural branches of the banks with the computer facilities of the Government at the district level. This area needs special attention and priority.

14.06 Once these arrangements are worked out and become effective with proper co-ordination with the Government agencies, it will be easier for the regional offices of the banks to regularly supply the required information to their head offices in respect of all rural branches. This way it will be possible to evolve a proper system of information collection and its submission to the authorities like the Reserve Bank of India or the Government for helping them in the policy formulation decisions. Both NABARD and the Reserve Bank should exercise their authority through directives issued, meetings held etc. to ensure

that the returns are submitted promptly and the concerned projects monitored effectively.

14.07 Subject to the above general observations, we recommend that the accounting systems and policy as well as the computerisation and management information systems recommended by the consultants may be adopted by the banks both commercial and co-operatives, as early as possible with such adjustments or modifications considered necessary in giving effect to these recommendations in Indian circumstances.

The Findings and Recommendations of Study Report on Accounting Systems and Policies

A Review of Current Systems

14.08 It has been observed that all the institutions maintain full accounting records inasmuch as each one maintains a whole set of double entry accounts, general ledger, 'subsidiary ledgers, cash book, journals and the various other registers required to be kept for accounting purposes such as, liquidity registers, bills register, share register etc. One drawback which has been observed, however, is that the banks generally do not follow the system of product costing or cost or profit centre accounting by type of lending, although the Indian Banks Association (IBA) has given general guidelines in this regard. Nevertheless it must be said, that given the administered nature of interest rates and the obligation to finance all new and non-defaulting borrowers, the gains on account of the product costing may not contribute much to a more effective control. On the other hand, the gains, if any, are likely to be outweighed by the cost as well as the complexity of administering such a system.

14.09 It has been observed that there is a general deficiency in the level of analysis of the lending portfolio within general ledgers, and that the format of the general ledgers in this regard is not well suited to the effective and efficient retrieval of financial information, either for management purposes or for furnishing returns required by higher level or regulatory authorities. At one extreme in the case of a PACS there is only one loan account in the general ledger which means that every time any information is required for either management purposes or for statistical returns, a laborious analysis has to be performed from every account in the loan ledger.

14.10 Although one might have expected the degree of sophistication in analysis to improve in higher level institutions, we find that this relationship does not always hold good; thus some DCCBs provide a greater degree of analysis than some of the state level apex banks.

14.11 It would be fair to say that in most cases the accounting function is primarily set up only for record keeping, and not as a source of financial management information. This leads to deficiencies in the information available for management. Generally an age-wise analysis of overdues is prepared only annually. It is necessary, in every institution, for the Demand, Collection and Balance Register (DCB) to be prepared by analysis of each and every loan ledger account every month. It is also seen that the design of the loan ledger currently in use in some cases is such that its analysis is rendered difficult; in one case the simple task of ascertaining the balance of the loan account required a calculation involving three steps. In institutions which typically have a large number of loan accounts at each branch, such as RRBs or commercial banks, preparation of the DCB can be a very lengthy process, and in some cases takes weeks. For this reason, although periodic updates of the DCB are relatively quicker, we find that RRBs only update it quarterly or even half yearly, to monitor collections against demand. In other institutions the number of loan accounts per branch or other outlet can be much smaller, for example, a DCCB branch may only deal with 20 or so PACSs; for this institution the maintenance of the DCB is not such a problem, and the register can be an effective means of monitoring recovery trends on a monthly basis.

14.12 Although very few of the state level apex banks have or are about to introduce computerisation of some applications, accounting at the field level, including in the commercial bank branches, is exclusively manual. Some of the co-operative banks have advised that they were considering computerisation but it was evident that in most cases this consideration had not gone very far.

Accounting Staff

14.13 The staff employed in accounting roles in the institutions are found generally well educated. In both, the state and district level banks, most staff have tertiary education, and this is so even at the PACS level in some cases.

It is, however, worth pointing out that there appear to be very few Chartered Accountants employed.

14.14 On the question of training, it may be said that in many institutions the accounting staff have attended some training courses; however, the courses normally appear to be either of a general nature with some, probably fairly basic accounting element in the curriculum or courses which are not relevant to accounting training needs, e.g., deposit mobilisation. In some institutions the accounting staff have undergone no training, relevant or otherwise. .

14.15 It is, therefore reasonable to say that there is a general lack of formal accounting training for staff, and that most staff "pick it up" as they go along. Given this, and a frequently non-accounting or commercial education, deficiencies in systems are more likely to be copied and perpetuated by on the job learning rather than corrected.

Recommended Accounting System

14.16 In the longer term, it is desirable for the accounting systems of the client institutions to be computerised, which can lead to a full integration of the financial and statistical information systems. At the same time, we recognise that full computerisation is still a long way off, and that, in the case of some primary institutions, may not be feasible within any meaningful time span. Hence a manual based accounting system, adoption of which can be rapidly implemented and which can be computerised as and when possible may be prepared. This system will be able to produce the output envisaged in our recommendations on financial information and to provide the financial data needed for both management's and apex's supervision of client banks' financial health; at the same time, it can assist in the preparation of the various returns now called for by regulatory and other authorities.

14.17 As discussed above, the current structure of accounting, does not generally lend itself readily to a financial information system. The proposed system will provide for portfolio analysis by type of lending, for separate identification of arrears of penal interest, interest and principal if required and automatic ageing of short-term lending overdues. All of this information will be available from the general ledger, without the need for analysis of subsidiary ledgers.

General Ledger

14.18 The adoption of a model general ledger is recommended, which will have separate accounts for different types of lending. It has been observed that whilst the level of analysis would depend on the availability of accounting staff in the institution, the deeper the level, the greater will be the degree of meaningful analysis that is immediately available from the general ledger. For example, an account heading might be minor irrigation; this would be a general ledger heading and could be further analysed into subledger headings such as e.g., small farmers, scheduled tribes, etc. For each heading the ledger will have separate arrears accounts which could be broken down further, if required, into principal, interest and penal interest. A framework of such a general ledger is given in Appendix VII of the Study Report.

14.19 In the case of short-term lending, separate accounts may be opened for each new season's lending; given that all these accounts in one ledger will fall due on the same day, identification of arrears is straightforward - any balance in the account after the due date is the balance of arrears.

14.20 Identification of dues on medium and long-term would be by way of a register incorporating repayment schedules. This register would form a standing journal and would be totalled and posted to the general ledger periodically. A proforma of register page is given in Appendix VII.2 of the Study Report.

14.21 Cash receipts will need to be periodically analysed by type of account including whether interest or principal etc. As final posting to the general ledger would be done after posting to the loan ledger (to give the analysis by principal etc.), it is envisaged that cash clearing accounts would be set up in the general ledger to initially control the ledger recording of cash; these accounts could also be given a numbering system to allocate them to their respective general and subledger heading. A detailed discussion of the methodology for analysis of cash receipts and maintenance of cash clearing accounts is presented in Appendix VII.3 of the Study Report. Proformas for analysis and posting are also included in this appendix.

14.22 The general ledger can thus give details, by required classification, of disbursements, collections, balance and overdues, divided into principal

and interest, if required. The ledger will also give total values for the DCB: demand is the sum of opening arrears plus debits to the arrears accounts in the period, collections can similarly be obtained from an analysis of the general ledger credit postings and balance is the account balance in each account.

Agewise Classification of Overdues

14.23 As mentioned above, separate accounts should be opened, for each year's short-term lending operations. The advantage of this is that there is then no need to age these accounts by analysis as the title of the account will indicate the age of any balance in it e.g., SAO 1986 would be one year overdues, SAO 1985 would be two years overdues etc.

14.24 Ageing of the overdues on medium and long-term lending is not as simply accomplished and still requires manual analysis from the loan ledger. The task may, however, be simplified and speeded up by designing the loan ledger records in a similar format to the general ledger accounts - i.e. with analysis into principal not due and overdue and overdue interest. The design of the loan ledger and a format for a ledger card may be seen in Appendix VII.4 of the Study Report.

14.25 Given that the general ledger will provide a figure for arrears, this will give enough of a monitoring capability to provide adequate supervision of arrears and recoveries without the need for frequent ageing of the medium and long-term overdues. This can be conducted periodically and whenever the performance on recoveries and overdues shows an adverse trend against budget.

Special Considerations for PACSs

14.26 Although, given the perceived level of education of client banks' accounting staff, the methodology proposed above is considered not too complex given suitable training. It is, however, possible that some PACSs would not find it easy to implement. At the same time there is at least as much a need for an accounting system to provide management information at PACS level as at higher levels, and the greatest need in the present circumstances is for up-to-date data on recoveries.

Training and Promotion

14.27 If the accounting system and the associated MIS are to be widely adopted, NABARD should prepare a manual based on the material in Chapters and Appendices VI and VII of the consultant's report. As the accounting system is inter-linked with the financial MIS, we consider there should be a single manual for the entire accounting and financial MIS procedures. This manual should, once completed be distributed to client institutions. Following distribution, training seminars should be run for the client banks. If NABARD does not have the resources either for preparation of the manual, or to conduct the seminars, expert consultants should be engaged for these purposes.

14.28 Because in some states the RCS determines what books of account are to be kept, and the format in which they are to be kept, it will be essential that he be involved in the promotion and training process fully.

Allocation of Repayments

14.29 It is a normally accepted accounting practice for banks and other financial institutions to account for repayments received by allocating these firstly to penal interest, secondly to ordinary interest, thirdly, to overdue principal and lastly, to principal not due. Although this is a sound and normal principle, an anomalous position develops where there are multiple tiers and overdues. This is clearly illustrated in the simple example which follows. In this example, the PACS has remitted the entire repayment to the DCCB, including its own interest margin; even so the balances of principal are mismatched, the DCCB expecting to recover more principal from the PACS than the latter can recover from the ultimate borrowers.

	Principal (Rs.)	Interest (Rs.)	Total (Rs.)
PACS			
10 ultimate borrowers each due to repay Rs. 100/- principal and Rs. 10/- interest.	1,000	100	1,100
5 borrowers only repay in full	<u>500</u>	<u>50</u>	<u>550</u>
Balance due	<u>500</u>	<u>50</u>	<u>550</u>
DCCB			
Due from PACS	1,000	80	1,080
Received from PACS	<u>470</u>	<u>80</u>	<u>550</u>
Balance due	<u>530</u>	<u>--</u>	<u>530</u>

14.30 This will arise in any instance where there is more than one tier in the delivery system and there are overdues sufficient to cause default by one institution to its refinancer.

14.31 This has two potentially significant areas of impact. The first is that the profitability of the lower level institution will be affected in those instances where that institution does not charge interest on outstanding interest, which is common in the short-term co-operative structure; in the example above, the PACS will be charging interest on Rs.500 but paying it on Rs.530. The second, which applies solely to the short-term structure, is that the eligibility of the DCCB (and of the SCB) will be adversely affected. This will occur because for refinance to DCCBs and SCBs for short and medium-term lending, NABARD takes into account only the demand, collection and balance of principal; in the example above therefore NABARD will recognise collections only of Rs.470 rather than the Rs.500 of principal recovered from ultimate borrowers.

14.32 This issue has been raised on many previous occasions and the resolution of the problem is complicated by the allocation of remittances being defined in the bye-laws of some societies or in the Co-operative Acts of some states.

14.33 It is considered undesirable that the multiple tier system should have this unintended distorting effect, and we recommend that remittances to higher level institutions should be allocated as between interest and principal in the same manner as at the ultimate borrower level. The same procedure may be followed between the State apex bank & DCCBs.

14.34 NABARD should bring its definition of demand, collection and balance for DCCBs and SCBs into line with that applied to the other institutions, and include both interest and principal.

Accounting of Bad & Doubtful Debts

14.35 The position on accounting for the provisions for bad and doubtful debts is highly confused. Some banks (probably most of the co-operatives) treat accretions of the provision, as an appropriation of profits, and disclose these as transfers to reserve after striking profit, whilst others treat this as a charge against profit and deduct the charge from interest income. The

balance sheet position seems to be more consistent in that all the co-operative banks disclose the account as a reserve.

14.36 The accounts of the co-operative banks are required to show the estimated amount of bad and doubtful debts; in many (possibly most) the quantum of the reserve bears no apparent relationship to that of the estimation.

14.37 There seems to be a generally held belief that provisions for bad debts cannot be made if there are no profits to create them from. The result of this confused thinking can be seen most clearly in the PLDBs; since these are frequently only marginally profitable, they set aside only very small amounts, if any, for bad debts although many have high overdues. This approach ignores two fundamentals - firstly that debts become irrecoverable whether the bank is making profits or not, and secondly that the balance sheet must show current assets at the lower of cost or net realisable value.

14.38 Apart from giving an unduly optimistic impression of a bank's financial position (not very helpful if it disguises the fact that the bank is nearly, or actually, insolvent and in need of urgent financial help) this policy has a direct bearing on the bank's eligibility for NABARD refinance. It should be noted that procedures for write off of bad debts are frequently unduly complex for co-operative banks - the permission of the RCS has to be sought in many, if not, all states.

14.39 We recommend that provisions should be made to fully cover anticipated bad debts; these provisions must be made whether there are profits or not and must be a charge against profit. The provision should be deducted from the asset in the balance sheet to show the estimated net realisable value of the asset. The provision should, therefore, equal the estimation of bad and doubtful debts.

14.40 Pending implementation of this recommendation, we recommend that, to establish the true picture of the institution's solvency to receive refinance under VC approach, it will be necessary to deduct from the owned funds (comprising paid-up share capital and reserves) the quantum of estimated bad debts and accumulated losses.

14.41 There is frequently no consensus on the quantum of bad debts at present, and we, therefore, suggest that NABARD use its own inspection estimates until adequate and consistent accounting policies have been developed and adopted. Since NABARD does not regularly inspect PLDBs, it should take up the matter with LDB Federation to decide the acceptable formula.

14.42 Changes to commonly accepted practices will not be quick to implement (for instance the accounting for the bad debt provision may be stipulated in Co-operative Acts); however, NABARD can require the recommended format changes be adopted in the financial MIS reports discussed later; this will permit a more informed and, therefore, effective review of a bank's financial performance.

Interest Receivable

14.43 It appears that the commercial banks and RRBs account for interest receivable on an accruals basis and capitalise overdue interest. However, although it appears that most of the co-operatives take up only interest received and interest accrued but not due on non-overdue loans, documentation available in NABARD suggests that there are a number of departures from this norm; this must lead to a lack of comparability between reported results for some co-operative banks.

14.44. The fact that none of the banks provide any accounting policy note to explain their procedure means that there is no way of deducting it from the accounts.

14.45 We note that RBI has already developed and circularised a recommended accounting policy on interest for co-operative banks. However, the policy is not always followed (due in some instances apparently to different requirements of local Co-operative Acts), and, therefore, NABARD should stipulate the use of the RBI policy in the financial reports received from co-operative banks (including LDBs) as discussed below.

Accounting Policies

14.46 While it is desirable for the standard accounting policies to be employed in the preparation of the banks' annual statutory accounts, this may not be

possible in all cases e.g. if accounting policies are laid down by state law; however, NABARD should stipulate (if necessary as a loan covenant) that the policies be adopted in the periodic financial reports it calls for. If this is not practicable then NABARD may require that supplementary information be provided with the financial reports. This supplementary information would enable NABARD to qualify differences due to differing accounting policies, so that it could restate the accounts on basis comparable to other banks.

Computerisation

Introduction

14.47 There is need to quicken the introduction of computer technology, to generate accurate and meaningful data on lending at the lower institutional level and to assess what type of data are required at higher levels to maintain overall control over agricultural credit. Computerisation is also necessary to improve the quality of services provided to the customers by banks.

14.48 The study conducted by the Consultants reveals an almost total lack of computerisation in the agricultural credit environment. Whilst the commercial banks have made some progress with computerisation, no use of computers was noticed in rural branches. In co-operatives also, computerisation is all but unknown.

Current Position -

Commercial Banks

14.49 The commercial banks as a group have developed computerised applications to serve their wide range of business needs of which agricultural credit is a part. In general, the application of computers to agricultural credit is for management information data collection needed for compilation of returns.

14.50 There has been a co-ordinated development of computerisation in the commercial banks following a plan laid down by a steering committee convened by the Reserve Bank of India. The plan was developed following recommendations made in the "Report of the Committee on Mechanisation in Banking Industry" issued by the Reserve Bank of India in 1984. Technical expertise is provided to the Steering Committee by the public sector Computer Maintenance Corpora-

tion Limited (CMC). The specific applications and the extent to which computer technology could be introduced have been hampered by the "Memorandum of Settlements" dated 8 September, 1983 (as amended on 17/9/84 and 29/3/87) between the Indian Banks' Association (IBA) and the Indian National Bank Employees Congress - Banking Wing of the Indian National Trade Union Congress. The steering committee has set target dates for achievement of specific implementations and written regular reports are made by the individual banks. Regular meetings are held to monitor progress and performance. The committee is working to create standards for hardware, software and communication protocols. The standards so far determined are :

- 1) Branch Level
IBM/IBM Compatible PC XT
Operating System - MS/DOS
10/20 MB Hard Disk
1 Floppy
- 2) RO/ZO Level Motorola 68020/30 Chip
VME BUS, 2MB RAM
2 x 160 MB WINCHESTER DRIVE
2x FLOPPY DISCS
600 LPM PRINTER
5 TERMINALS
OPERATING SYSTEM UNIX 5.2/5.3

The original IRONIC systems were made in the USA to specifications set down by the RBI steering committee. Subsequently two local manufacturers, E.S.P.L. and Sunray, commenced manufacturing in India. There are now seven empanelled local manufacturers approved by RBI capable of producing the required standard hardware.

14.51 Evaluation of two locally available mainframe computers for installation at head offices of banks is in progress. They are :

- 1) ICL System 39 by I.C.I.M.
- 2) An Indian manufactured version of the CDC Cyber by ECIL, "MEDHA".

Research has been undertaken to determine the standard communications protocol to be adopted. Discussions with the National Informatics Centre (NIC), Department of Electronics in Delhi indicate that concurrently with the evaluation of Communications Protocol, an investigation is being conducted in "Security

in Electronic Banking" at three levels: hardware, software and communications. During the course of field visits, it was observed that the introduction of computer technology in some banks had progressed ahead of the timetable set down by the RBI. Canara Bank, for example, have received permission direct from Government of India to install a large Burroughs mainframe, whilst Central Bank have already linked zonal computer centres with the central computer. In a number of other banks, various difficulties had slowed implementation schedules.

Land Development Banks

14.52 The National Co-operative Land Development Banks Federation sponsored a seminar on "Management Information Systems and Computerisation" in Pune in February 1986 as a computer appreciation programme for SLDB Chief Executives. The field visits confirmed that many of the SLDBs had done no evaluation of computer technology and only one visited, in Karnataka, had actually installed computers. However, at LDB Federation level, there is an understanding of the need for computers and a "Systems Analysis and Feasibility Study Report" was completed in August 1987 by International Computers Indian Manufacture Ltd. (ICIM) for the Federation and funded by NABARD's (R & D) Fund. The member banks have been asked for their views, and to indicate how they see the Federation assisting them.

State Co-operative Banks

14.53 Although some of the co-operative banks visited, had introduced computers, agricultural credit information or accounting was not processed anywhere. At DCCB level, only one bank has computerised all information relating to :

Credit Disbursement, Overdues,
Sanctions and "Payment Due"
Notice to Borrowers

Although the SCB Federation sponsored a national level workshop on "Computerisation in Co-operative Banking" in Goa in September 1985, it appears that computer activity by the SCBs has been individual and unco-ordinated. It is understood that the SCB Federation has now called for quotations from a number of manufacturers/consultants, including ICIM and Tata Consultancy Services, to conduct a study on computerisation in SCBs. The Federation will

be looking to NABARD to provide the financial resources for the study from the R & D Fund.

Co-ordination of Planning

14.54 It appears that there is no overall co-ordination of computerised information flow throughout the banking industry as a whole, although RBI is directing computerisation in commercial banks. NABARD is liaising with each of the two Co-operative Federations independently and on an ad-hoc basis with the Indian Banks' Association.

Obstacles to Computerisation

14.55 The introduction of computers into the Agricultural Credit System would certainly improve accounting systems and generate more accurate, meaningful and timely data from field level through to apex level.

14.56 However, there are a number of factors which must be considered in any possible implementation. Some of the factors are significant and will determine the level of implementation possible and the pace with which it can be achieved. The main factors are (i) the electrical power supply, which in many parts of India will be a major concern in computer installations, (ii) the environment in most primary level institutions would be totally unsuited to the installation of computers, as the current generation of computers would not be able to survive the conditions of heat, humidity and air dust content prevailing, (iii) the current agreement with the unions is one of the most limiting factors in the introduction of computers into agricultural credit, particularly in rural branches of financial institutions. The question of a further extension of computerisation in the banking industry will not be reviewed by both parties to the agreement until 8 September 1989, (iv) the question of software support and hardware maintenance in large urban areas and in geographically remote primary level branches poses a major problem, (v) the cost and time involved in training staff in the effective use of computers through all levels of the agricultural credit system would be huge, (vi) the brain drain of computer personnel will be difficult to prevent and (vii) the high cost of hardware would be well outside the meagre budget of the 92,000 plus PACSs, many of whom are operating on a marginal profit or on a loss basis.

14.57 For the reasons discussed above, it would be impractical to consider general computerisation at primary and other lower levels and hence we recommend the establishment of the computerised Management Information System (MIS) at District level. However, computerisation of accounts needs to be introduced at lower levels also, as soon as the conditions there improve and the current impediments are removed. One of such impediments is the resistance of the trade unions of the banks' staff. They argue that introduction of computerisation in banking industry at all levels will curtail future job opportunities if not result in retrenchment of the present staff. This is an erroneous impression. Even the present level of computerisation has in fact, resulted in additional jobs to many, leave alone the increase in job opportunities in the computer industry at large. The only consequence we see is the likely reallocation of the staff for various functions. Considering the benefits that will accrue to all, particularly to the customers, we have no hesitation in recommending full computerisation of the banks' accounting system in India whether commercial or co-operatives before the end of this century.

The Need for Computerisation

14.58 In spite of the obstacles to computerisation, there is an urgent and very real need to introduce computerisation in a number of areas of the agricultural credit system.

14.59 Normally the first application of computers in a financial institution is to the accounting functions, because this provides ease of operation and customer service, apart from an important segment of the Management Information requirement. However, because of the massive numbers of primary level institutions in the Indian agricultural credit system and the other factors retarding change, such as implementation difficulties, lack of standard accounting procedures and staff inertia or resistance, we do not recommend this approach. Instead a simple interim manual accounting method be implemented at all levels, until the Management Information System recommended is in operation.

14.60 The introduction of computers in staff training is an ideal medium not only to increase the efficiency of training techniques but also to create computer awareness.

14.61 Any system that is introduced must provide accurate data in a timely manner, and provide the flexibility to meet the changing requirements of the agricultural credit system. It must provide a consistent basis of generation, compilation, flow and analysis of information so that variations of data specifics and time intervals, either currently or retrospectively, can be accommodated. It must provide the necessary data elements for strategic planning and policy determination at apex level, as well as management control information for evaluation, budget comparisons and the like.

Hardware and Software

14.62 As mentioned earlier, both the Reserve Bank of India Computer Committee and the National Informatics Centre have conducted extensive evaluation of computer hardware and software requirements. These studies were for equipment to be used in similar applications to what is proposed in this report.

14.63 The recommended hardware has already been installed in a number of banks, so that its suitability for the tasks can be readily assessed, as can the performance of the software. Whatever hardware and software is ultimately selected, consideration must be given to ensure that its operation at district level processing is compatible with branch/zonal office level systems either through magnetic media or direct link. Recommendations of the above two groups should be sought. It is, however, suggested that to the extent possible the equipment selected should be compatible with branch level and Regional/Zonal Office level systems, so that processing at the district level can be facilitated, either on shared basis or through inputs provided on magnetic media by the banks, as envisaged.

14.64 The memory and storage capacity of magnetic media will need to be calculated for each individual district, as the requirements will vary according to the volume of data to be stored. The volume will also be affected by the percentage of bulked data received on magnetic media from commercial banks and co-operatives, who have already installed their own computer systems.

14.65 A separate detailed study of the districts will need to be carried out by appropriate consultants, to assess the volume of individual detailed manual records that will need to be input and maintained on the data base. This

information will be required, not only to assess the capacity of the equipment, but also to determine part of the operational costs.

14.66 The cost of the standard software developed for the processing can be spread across the network nation-wide. There should be no variations on this software because of the standardised reporting. Low cost utility parameter driven programmes to extract, manipulate and print data for ad hoc reporting, can also be provided at low cost because of the common format of the data base. Reduced software maintenance and modification costs will result from the standard design.

Computer Centre Operation and Management

14.67 Trained computer personnel are not available in large numbers in India, especially those with skills or background in banking. For that reason and the economies of scale in the purchase of hardware and software, as well as the on-going operational costs, we believe that a single computer centre operation should be established at district level.

14.68 A number of alternatives have been identified which could provide a satisfactory method of joint processing for those banks who have not introduced computerisation into their organisation. It is possible that there could be a mixture of those alternatives working satisfactorily in different states; however, a common organisation has obvious benefits.

Subsidiary Service Company

14.69 The creation of a subsidiary service company by the Management Systems and Standards Committee (MSSC) is one method that can be adopted. The activities and services of the company can be clearly defined and costed. It would be normal to conduct the operations of the company on a "user pays principle".

14.70 Obviously, where data input is from manual media, the costs would be higher than that for electronic media. However, the cost savings in terms of manpower resources in completion of returns at manual institutions would be great. The banks continuing to provide their data on magnetic media would have already expended costs on their own computer processing.

14.71 The service company should be controlled and operated along guidelines set down by the MSSC.

Use of Existing Facilities

14.72 Another possible alternative is the use of existing computer facilities already established in a bank in the district.

14.73 Obviously, there are a number of benefits in favour of such a solution. The computer centre is "already physically established, operational and/or software staff are available and, in many cases, the centre is processing a system similar to that described in Appendix XI.1 of the Study Report.

14.74 In this case also operational costs would be shared on a "time and materials" basis.

14.75 A variation of this solution is the possible use of a commercial computer processing bureau in the district. There are a number of reasons why this is probably a less attractive alternative; it would probably be more costly, and more difficult to control responsiveness to processing deadlines. On the other hand processing at another bank site is geared to meeting the same deadlines as those required by its potential "users".

National Informatics Centre

14.76 The National Informatics Centre (NIC) which is a cell in the Central Government, Ministry of Finance, has commenced operations of its system DISNIC at a number of pilot sites throughout different states of India.

14.77 The DISNIC strategy is based on installation of super mini-computers at each state capital which will be linked on-line to smaller computers of each of the 438 district centres, which provide services to the district administration. DISNIC will provide the capability to gather information on the monitoring schemes and socio-economic information required by state planning agencies and the Central Government.

14.78 It is learnt that understanding in principle has been reached with state governments, many of whom have already signed agreements to participate

in DISNIC. As the co-operative institutions which disburse approximately 50 per cent of agricultural credit in India have their apex structure only at state level, and are monitored not only by the Reserve Bank but also by the State Registrar of Co-operative Societies, the use of DISNIC could provide a very workable solution for processing of agricultural credit management information.

14.79 NIC currently has a staff of more than 800 computer professionals divided into four major infrastructure groups. The expertise of the NIC group plus the planned network would provide an ideal basis for the processing of matters relating to agricultural credit.

14.80 It is recommended that discussions be held with NIC to consider the possibilities suggested herein. We believe this vehicle could prove to be a safe, speedy and reliable way to introduce computerisation into agricultural credit at an early date.

Recommendation

14.81 Of the alternatives discussed above the consultants recommend the NIC option if this is possible. This recommendation is based on a number of factors.

- * NIC have already commenced the installation of district centre computers and establishment of the necessary sites and environment.
- * NIC have a large staff of computer specialists with the necessary software and operations skills.
- * Agreements are already being finalised with state governments which require much of the information proposed by our MIS for control of the co-operative institutions.
- * This solution would provide a quicker method of introduction of the computer MIS in agricultural credit.
- * The cost of processing will be related to the provision of extra capacity in existing equipment and infrastructure, rather than creating a totally new infrastructure.

14.82 The role of the MSSC will still be essential even with this solution. In fact, NIC would basically operate as a bureau for the processing of the agricultural credit information.

14.83 Discussions with senior executives of NIC in Delhi indicate commonality between the NIC data base and our recommended agricultural management information system data base at district level. This matter should be discussed on an official basis as soon as possible.

Management Information System

14.84 Management information is a necessary tool for the management and control of agricultural credit at the apex level. Management information really means a hybrid of people, procedures and machines which contain past and present information that can be combined with different parameters to project future information and control and monitor current operations.

Plethora of Returns

14.85 It was observed by our consultants that the primary level institutions were required to furnish numerous returns on agricultural credit either to higher level institutions or to their sponsor bank, viz., statutory returns to Government of India and RBI, returns to state governments, NABARD, DICGC and IDBI and various other requirements for special exigencies such as flood or drought. It was further observed that more than 35 per cent of the data furnished in these returns were common, though shown under different nomenclature. The multiple production of the same data in different formats, was both inefficient and costly in terms of time and resources, to the administration of agricultural credit at apex and institutional level. The New Information System (NIS) was introduced in some banks. Recently, the Sub-Committee of the Systems and Procedures Committee of the Indian Banks' Association has submitted a Report on Rationalisation of Returns in which it has been recommended that in the place of existing 189 returns to be submitted by the banks to various authorities, only 123 returns may continue to be submitted. We endorse this recommendation for implementation by commercial banks.

Data Source

14.86 Normally, the data required for management information returns on agricultural credit is obtained from the loan application/ledger record. The collation of all the data is repeated each time a return is furnished. The impact on primary level institutions particularly PACSs is very great due to no mechanisation and limited manpower resources. This is causing concern to a number of DCCBs.

14.87 The accuracy of data in a management information system is vital.

14.88 The incidence of mail taking 10 days or more between branches and district offices or PACSs and DCCBs was common. The current method which is mostly manual, is progressive accumulation of data for a return from primary level to branch level to district level; then zonal or regional level to state apex level in the case of co-operatives or all-India in the case of commercial banks. It is not surprising to find a minimum of 2-3 months average time lapse for a return to be produced at institutional level. The final set of integration of all data from all institutions at apex level is also a time consuming task, completion of which is governed by receipt of all returns. The management information received through this process, depending upon the report cycle period, is mostly of historical value only and is too outdated to be used as a planning and management tool for monitoring current performances against budget.

MIS for Financial Management and Review

14.89 The study made by the consultants indicates that there is room for improvement in monitoring of financial health. At present, there is very little emphasis on this either at national or state level. At the national apex level, the major problem seems to be that inspection is too infrequent and that it does not cover PLDBs (except branches of SLDBs), and accounts are only used for monitoring RRBs and there are problems with lack of consistency and delays and the reporting forms now in use are generally not designed to monitor financial health. Although there are some steps towards the use of budgets as a monitoring and control mechanism, their use is not widespread either as a tool for the supervisory institution or for the bank's own management.

14.90 There is generally almost no information going to management on the financial status of a bank on any regular basis.

Recommendations on Review of Financial Integrity (soundness)

14.91 It is an appropriate role for the national apex body to have responsibility for the review of the financial soundness of client banks. There is a need to link this monitoring role with that of enhancing financial integrity. A further cogent reason for assigning this role to the national level is that this can lead to easier transmigration of data and experience across state boundaries.

14.92 A commonly used methodology of financial control for financial institutions is one known by the acronym "CAMEL", which encompasses five broad areas of financial control information. These broad areas are capital adequacy, assets & liability structure, management of risk, earning performance and liquidity. The management of these variables, all equally important, assumes adequate financial and credit risk management policies and procedures for which an information system provides support. An appropriate information system must yield relevant, accurate and timely data and analytical reports for decision makers at various levels of the organisation to give them a quantitative basis for planning and control. Such a system is equally able to generate the data required for the monitoring purposes of the apex level institutions. Within the highly regulated environment of the Indian banking system, the manager's scope for decision making is strictly curtailed. Thus he has no control over interest rates and little control over his bank's capital structure or its portfolio's exposure to risk. Nonetheless there are areas of operational discretion e.g. overdues, staffing, deposit mix etc. all of which can significantly influence the institution's financial performance. Hence, the CAMEL concept is recommended selectively, to highlight those areas where management has decision making prerogatives which can affect the financial performance of the bank and those areas which must be monitored by the apex level, in pursuit of its objectives of reviewing financial integrity. The financial control and monitoring can best be achieved by evaluating the results of operations through pre-determined ratios and percentages for each broad area of financial management and comparing the results with budgetary targets and with "industry averages". The medium for channelling this information should be through periodic proforma financial reports. NABARD may require these forms to

be submitted by client banks to Regional Offices. The periodicity of these returns may be quarterly for most banks, to be reduced to monthly, ultimately. However, for institutions requiring intensive care, more frequent reporting might be necessary, for some time. However, it is better that reports be received less frequently but be thoroughly reviewed and action taken thereon, than that they be frequently received, but only ticked off and filed. NABARD should train client bank management and senior accountants in the advantages, use and preparation of the recommended reporting system.

The Need for Standards

14.93 The introduction of computers into agricultural credit for accounting and/or management information purposes can only be effective if a number of preliminary decisions are taken and implemented first. The initial priority must be the setting of agreed standards for Management Information Systems.

14.94 The major need for standardisation with MIS is with the content and furnishing of returns. The volume and redundancy of returns could be greatly reduced by overall apex direction. In addition to the standardisation of returns, a study also needs to be conducted to determine the real purpose and requirement of each return. It was observed that some of the information which is collated with so much cost and effort, is no longer used. A second major issue for consideration is the setting up of national standards for numbering systems. The RBI has introduced an institution and branch numbering system for commercial banks, to be quoted on returns. When the MICR cheque clearing system was introduced by RBI, a different system of numbering based on post codes was introduced with it.

14.95 To ease the introduction of computerisation, improve collation of Management Information and implement and control the introduction of standards for agricultural credit management information, the consultants have recommended the formation of a "Management Systems and Standards Committee". This committee should consist of one member from each of the Department of Agriculture, Ministry of Finance, RBI, Indian Banks' Association, NABARD, State Government, Federation of Co-operative Land Development Banks and the Federation of State Co-operative Banks. The representative of NABARD should be the Chairman of the committee. All the eight committee members

should be working executives and the committee should be supported by a full time secretariat to ensure implementation of directives. The major activities of this committee will be directed to the generation of accurate and meaningful data on agricultural credit. For this reason, NABARD must play the principal role in the control, direction and financing of the committee through its R & D fund.

14.96 It is recommended that this committee should be charged with the responsibility of setting of overall policy/strategy, interaction with different sections and documentation, publication and review of standards and procedures for management information systems.

Recommended Management Information Systems

14.97 The system devised above will incorporate information from manual processing at primary levels in co-operative banks or magnetic data from advanced electronic accounting machines in commercial bank branches input to a common computer processed data base at district level. The system has the flexibility to allow it to be moved down to the primary level branches or to institution level, if that is felt necessary or for cost effectiveness, with the effluxion of time. The information needed to satisfy the requirements of current returns and to provide the monitoring and control for budgeting of agricultural credit, is the information from all individual loan accounts from primary level, grouped and summated by various categories and classifications. The great volume of manual records and the tiered reporting structure has led to a rigid information flow. The inflexibility of this system has led to the introduction of additional returns, to cope with the inevitable changes required because of altered circumstances. This in turn has led to extra work at the primary levels in the manual collation of the same information in a different format to satisfy the altered requirements. This process is both wasteful and ineffective. The recommendation for the creation of a computerised district data base of account information provides a vehicle for consistent flexible reporting. The use of a computer utility programme will extract, sort and collate information by flexible user designated parameter. The availability of such a constantly updated and consistent information base, will render many of the fixed period returns unnecessary.

Credit Information Bureau

14.98 A problem which is perceived as a major one by many of the bankers, is wilful default in agricultural credit by a number of borrowers who secure multiple loans for the same purpose from different organisations. As a by-product of the district level data base, it will be possible to do a search of the file under various "Keys" such as name, location etc. across all institutions. Thus a credit checking facility can be provided which will act as a safeguard, preventing the sanctioning of multiple loans for the same purpose by different institutions and the district level data base can also become a Credit Information Bureau.

PART IV

OVERDUES IN AGRICULTURAL CREDIT

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CHAPTER XV

THE OVERDUES SYNDROME

Repayment of the loan together with interest thereon by the borrowers is central to the smooth functioning of institutional credit. The assumption while providing credit, is that its application to production generates enough production which in money terms would be sufficient to repay the loans together with interest and leave a reasonable surplus. Credit can be said to be effective only if this basic postulate is borne out. However, this in itself is not sufficient; the generation of incremental income has also to be accompanied by willingness of the user to repay. A default in repayment can, therefore, occur if either the assumption regarding production does not turn out to be valid or even when the validity of the first assumption is not in question, the second assumption is proved wrong. Efficient management of recovery of dues is, therefore not only of crucial importance but also amongst the most complex of all problems associated with institutional credit.

15.002 The incidence of overdues in the agricultural credit system has been increasing over the years and has been steadily eroding the financial soundness of the system. This, therefore, has been and continues to be the burning issue. It has consequently attracted considerable attention and has been examined by several committees and research workers. The first major comprehensive study on the subject was the one undertaken in 1974 by a committee set up by the Reserve Bank of India under the Chairmanship of Dr. C.D. Datey. Various other committees have also subsequently dealt with the issue in general terms, though the Study by the RBI Study Team of 1974 still remains the most comprehensive document on the subject.

Overdues - Basis of Computation

15.003 Stated in simple terms, overdues are loans and interest thereon not repaid on due dates. The quantum of overdues in a credit institution may accordingly vary widely and even significantly depending on the reference date. But irrespective of the reference date, the level of overdues is among the most important indicators of the financial health of a lending institution.

Levels of overdues in the credit system could be measured either in relation to 'demand' for the year as in the co-operative credit structure or in relation to 'outstandings' at the end of the year as was the case earlier in the commercial banks. At present, however, the accepted standard of measurement of overdues is in relation to 'demand'. The rationale for the 'demand' as the standard base for assessing the recovery position is that it is the quantum of loans which have fallen due and not those which are yet to become due for repayment is what is relevant in this context. Thus illustratively out of term loans of Rs.15 lakhs granted for a dugwell programme repayable in 15 equal annual instalments, the first instalment of Rs.1 lakh only will fall due at the end of the first year and if Rs.0.60 lakh is recovered, the balance of Rs.0.40 lakh i.e. 40 per cent of demand is considered as having fallen overdue. If, on the other hand, the overdues are assessed with reference to outstandings at the end of the year, they would work out to less than three per cent. Quite clearly this gives a distorted picture of the real overdue position and hence of the recovery performance. Taking the example of crop loans, assuming the sum outstanding at the end of the year is Rs.20 lakhs and if these amounts have been disbursed, as often is the case, during different periods during the year, not all would have fallen due at the end of the year. Assuming such short-term loans are issued for a period of nine months and out of Rs.20 lakhs, Rs.10 lakhs had been issued only six months prior to the close of the year, these obviously, would not be due for repayment at the end of the year and what would be due would only be Rs.10 lakhs. If out of this, Rs.5 lakhs have been collected, the overdue amount to demand for the year would be Rs.5 lakhs and it would constitute 50 per cent of demand. Whereas, if it is assessed in terms of the outstandings, the overdue amount would constitute only 25 per cent. Commercial banks have traditionally been assessing overdues in terms of outstandings and not in terms of demand as is the practice in co-operatives, although in recent years commercial banks also have started falling in line with the co-operatives. It cannot, however, still be said in all cases whether their overdues are calculated really on this basis or in terms of all loans outstanding at the end of the year. Since recovery performance is a major indicator for adjudging the quality of the loan portfolio of a lending agency, it needs to be assessed in terms of that portion of the loan which has fallen due and not of the total loans outstanding, a substantial portion of which might not have become due for repayment. It is, therefore, our considered view that overdues should

necessarily be related to demand for the year, since this alone will be a true indicator of the actual recovery performance of the lending institution.

15.004 It also seems necessary to set at rest a belief sometimes entertained that overdues in the credit system are in fact, only a euphemism for bad debts. While the high incidence of overdues in the agricultural system is undoubtedly a matter of great concern, it would be erroneous to treat these on par with bad debts. A substantial portion of overdues is often of a transitional nature. This is so because amounts which become overdue on a particular date may get repaid soon thereafter and would cease to be dues to the bank/credit institution. If this happens successively over a period of years, this would only point to the fact of fixation of due date for the repayment of the loan being not rational and needing a change. This is not to say that overdues in all cases are of this nature. The failure of the lending agency to approach the borrower for recovery of dues before the due date could also be a reason for their becoming overdues. A bulk of the overdues of this type is realisable and it is a common experience that recoveries do come, though belatedly, in a large number of cases. In fact the period-wise classification of overdues discussed later in this chapter would reveal that the quantum of overdues tends to decline sharply with age. It is those overdues which are not realised over a period of five to seven years that could be considered doubtful of recovery. But even here they are only potential bad debts and they constitute a comparatively small proportion of the total overdues at any point of time. Estimates of provisions for bad and doubtful debts made in the chapter, reveal that while the amount of overdues under agricultural loans at the end of June 1986 was quite large at Rs.3,942 crores forming 24 per cent of the total agricultural credit outstanding at Rs.16,409 crores, the estimated quantum of bad and doubtful debts was Rs.846 crores only, forming 5.1 per cent of the total agricultural loans outstanding. It is, therefore, important to realise that all overdues are not per se bad debts. They are, all the same, a matter of serious concern and should be considered a warning signal, calling for suitable steps for close and continuous monitoring of the concerned accounts.

The Magnitude of the Problem

15.005 While the factors which contribute to non-repayment resulting in

defaults and consequent overdues are analysed later, it would be useful first to take a look at the problem as it exists as well as the future outlook, having regard to past trends. As all available indicators point to, overdues seem to be increasing year after year over the past few years. In quantitative terms, the overdues of all the credit agencies at the level of the ultimate borrowers quadrupled in the last decade i.e. from Rs.853 crores at the end of June 1976 to Rs. 4,262* crores at the end of June 1986 when they constituted about 42 per cent of the total demand.

15.006 Overdues under agricultural loaning carried by various credit agencies over the last decade i.e. 1975-76 to 1985-86 may be seen from table 1.

Table 1

Overdues of the Various Credit Institutions

Agency	(Rs. crores)						
	1975-76	1980-81	1981-82	1982-83	1983-84	1984-85	1985-86
Commercial Banks (CBs)	200 (48)	727 (47)	893 (48)	1069 (47)	1351 (48)	1568 (46)	1744 (43)
RRBs	NA	54 (48)	89 (50)	158 (49)	242 (50)	322 (52)	413 (51)
Co-operatives							
1. PACSs	561 (34)	1376 (45)	1205 (50)	1308 (40)	1577 (43)	1630 (42)	1807 (41)
2. LDBs	92 (34)	291 (46)	252 (40)	269 (44)	267 (36)	285 (40)	298 (39)

(Figures in brackets indicate percentage of overdues to demand)

As the statement brings out, overdues seem to be an all pervasive phenomenon and are neutral to the type of credit institution. Despite the efforts of the different credit institutions to improve recoveries, overdues have been increasing over the years with only some exceptions (these presumably in view of better monsoons and good crop conditions in those years). Further, whereas the short-term and term loans issued by different institutions increased from Rs.1,478 crores during 1975-76 to Rs.6,825 crores during 1985-86 showing an annual average growth rate of 16.5 per cent, the total overdues against ultimate borrowers increased from Rs.853 crores as on 30.6.1976 to Rs.4,262 crores as on 30.6.1986 showing an annual average growth rate of 17.5 per cent. Thus, overdues in the aggregate grew at a faster rate than the issue of loans during the ten-year period under review.

* Includes overdues under non-ag loans of RRBs and co-operatives.

15.007 The aggregate overdues of the different systems of lending institutions ranged between 39 per cent and 51 per cent of demand in 1985-86. The overall recovery position of all agencies is, therefore, far from satisfactory. The recovery position of PACSs and LDBs is relatively better than that of the commercial banks though the latter has progressively improved, the percentage of overdues to demand having declined from 48 in 1981-82 to 43 at the end of 1985-86. The recovery is the lowest in the RRBs hovering around 50 per cent and the general trend has been towards deterioration over the years. PACSs had achieved recovery upto 60 per cent of demand in the year 1982-83 but in the subsequent years their recovery performance has marginally declined. Among the credit agencies, the recovery performance of LDBs had marginally improved from 60 per cent in 1981-82 to 61 per cent in 1985-86.

Regional Variations

15.008 A comparative position of region-wise overdues of different lending agencies under agricultural loans during 1985-86 is given in the following table :

Table 2

Overdues - Regional Variations

Sr. No.	Agency	Northern	North-Eastern	Eastern	Central	Western	Southern	Overall
1.	CBs	38.7	64.0	57.0	47.0	49.6	39.3	43.0
2.	RRBs	53.0	60.0	60.0	53.0	52.0	42.0	51.0
3.	PACSs	30.0	84.0	57.0	53.0	42.0	36.0	41.0
4.	LDBs	44.7	72.9	32.7	33.7	55.1	41.4	39.0

(Figures show percentage of overdues to demand)

It will be seen that although there were inter-institutional differences in the recovery performance in different regions, generally the Northern and Southern regions had shown a somewhat better overall recovery performance; on the other hand, recoveries were lower in the Eastern region in all credit agencies except LDBs and lowest in the North-Eastern region, both regions being economically backward.

State-wise Overdues

15.009 The state-wise position of overdues and percentage of overdues to demand in respect of agricultural lending of commercial banks, RRBs, PACSs and LDBs for the last three years 1983-84 to 1985-86 is given in tables 3 to 6.

The state-wise position of overdues during the year 1985-86, shows that the recovery performance of PACSs was above 60 per cent of demand in Punjab (79), Kerala (75), Jammu and Kashmir (70), Haryana (66), Gujarat (65) and Himachal Pradesh (61). The states having recovery of less than 40 per cent of demand comprised Orissa (33), Goa (27), Assam (9), Meghalaya (8) and Manipur (5). In the case of LDBs, the states having recovery of 60 per cent of demand and above were Punjab (86), U.P. (76), Kerala (77), Haryana (67), M.P. (66), Jammu & Kashmir (62). On the other hand, the states where LDBs recovery performance was 40 per cent or less were Assam (40), Tamil Nadu (36), Goa (36), and Tripura (26). The other states had recovery performance ranging between 40 to 60. In the case of rural branches of commercial banks, the recovery performance was 60 per cent or more in Punjab (72), Kerala (71), Tamil Nadu (63), Pondicherry (61), Haryana (60) and Andhra Pradesh (60). On the other hand, the states where commercial bank branches show recovery performance of 40 per cent or less were Manipur (21), Jammu and Kashmir (31), Assam (35), Tripura (33) and Goa (39). The overall recovery performance of RRBs was worse than that of any other credit agencies. The states in which RRBs had shown a recovery performance of more than 60 per cent of demand were Kerala (77), Tamil Nadu (65), Punjab (84), Himachal Pradesh (60) and Mizoram (63). These states, however, have only a few RRBs. The states where recovery of RRBs was 40 per cent or less were Orissa (40), Tripura (29), West Bengal (39) and Nagaland (22). The data show that recovery was consistently better in certain states viz. Punjab, Kerala and Haryana, irrespective of the type of agency disbursing credit whereas it was far from satisfactory in some other states like Manipur, Tripura, Assam and Meghalaya.

Table 3

Overdues of Commercial Banks under Agricultural Loans

(Rs. crores)

Sr. No.	Name of State	1983 - 84		1984-85		1985-86	
		Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand
1.	2.	3.	4.	5.	6.	7.	8.
I. Northern Region							
	Haryana	46.74	42.7	115.77	41.1	65.96	40.1
	Himachal Pradesh	7.38	49.3	6.90	49.4	9.54	49.1
	Jammu & Kashmir	6.16	63.3	6.61	47.6	5.71	69.2
	Punjab	95.21	39.0	88.29	29.3	107.23	28.1
	Rajasthan	59.49	52.8	75.70	51.5	80.44	51.8
	Chandigarh	8.30	85.3	20.20	59.0	29.97	65.0
	Delhi	4.85	53.4	5.51	60.3	5.76	52.1
II. North-Eastern Region							
	Assam	5.70	64.7	6.50	64.9	11.06	64.8
	Manipur	1.05	80.1	1.11	78.8	1.41	79.1
	Meghalaya	1.40	53.4	1.80	44.3	1.83	55.6
	Nagaland	0.54	33.3	0.86	55.6	1.06	58.3
	Tripura	2.48	66.5	3.04	68.3	3.96	67.5
	Arunachal Pradesh	0.09	57.9	0.12	49.0	0.12	46.1
	Mizoram	0.06	61.4	0.11	48.1	0.12	43.4
	Sikkim	0.06	21.3	0.17	28.4	0.45	50.1
III. Eastern Region							
	Bihar	55.88	61.8	71.63	62.4	67.54	57.5
	Orissa	36.85	63.6	43.16	56.6	45.42	53.9
	West Bengal	58.27	66.0	68.56	66.2	65.43	58.7
	Andaman & Nicobar Islands	0.34	76.8	0.29	81.6	0.41	71.3
IV. Central Region							
	Madhya Pradesh	71.75	57.9	82.76	55.9	102.52	55.3
	Uttar Pradesh	138.99	46.1	157.01	45.7	170.08	43.1
V. Western Region							
	Gujarat	79.96	47.2	93.59	47.0	105.86	48.8
	Maharashtra	157.93	57.7	188.02	55.9	185.12	50.0
	Dadra & Nagar Haveli	0.03	33.8	0.06	71.0	5.47	49.7
	Goa, Daman & Diu	5.97	60.7	5.84	58.3	0.07	60.8
VI. Southern Region							
	Andhra Pradesh	184.12	44.1	221.83	42.4	237.94	40.1
	Karnataka	141.32	52.0	162.84	49.6	183.01	46.5
	Kerala	37.63	32.6	46.01	30.6	57.40	29.3
	Tamil Nadu	138.79	41.8	158.68	37.6	187.54	36.7
	Lakshadweep	0.01	24.5	0.01	36.2	5.24	42.4
	Pondicherry	3.96	36.6	5.07	46.2	0.01	39.1
All India		1351.51	48.4	1638.05	45.8	1744.41	43.4

Table 4

Overdues of RRBs during the last three years, i.e. 1983-84 to 1985-86

(Rs. crores)

Sr. No.	Name of State	1983-84		1984-85		1985-86	
		Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand
1.	2.	3.	4.	5.	6.	7.	8.
1.	Haryana	6.09	46.5	3.11	48.0	11.24	54
2.	Himachal Pradesh	1.98	51.4	1.42	38.9	2.03	40
3.	Jammu & Kashmir	2.59	62.0	3.34	61.6	3.32	56
4.	Punjab	0.01	14.4	0.08	20.7	0.31	16
5.	Rajasthan	15.85	52.9	20.41	57.1	24.59	56
6.	Arunachal Pradesh	(0.10)*	16.6	(0.43)*	41.0	0.01	41
7.	Assam	4.05	44.1	6.81	57.5	7.66	50
8.	Manipur	0.03	51.3	0.12	66.9	0.17	48
9.	Meghalaya	0.72	29.8	0.10	30.9	0.34	30
10.	Mizoram	-	-	0.01	30.1	0.16	37
11.	Nagaland	(0.31)*	39.7	0.01	64.1	0.05	78
12.	Tripura	6.35	58.7	9.89	80.1	11.60	71
13.	Bihar	24.15	52.6	36.92	58.2	48.92	59
14.	Orissa	28.99	60.8	38.70	62.9	36.62	60
15.	West Bengal	19.49	62.0	18.34	55.6	31.40	61
16.	Madhya Pradesh	12.99	54.5	20.02	54.3	29.14	58
17.	Uttar Pradesh	39.20	55.4	51.85	57.5	66.09	51
18.	Gujarat	1.03	37.2	1.75	44.1	2.36	56
19.	Maharashtra	5.93	61.6	7.48	55.4	10.29	51
20.	Andhra Pradesh	29.27	40.2	43.07	50.4	62.54	54
21.	Karnataka	25.85	43.2	32.65	42.4	41.76	44
22.	Kerala	11.98	31.2	14.15	26.4	16.60	23
23.	Tamil Nadu	5.45	61.2	6.69	37.2	5.58	35
Total		242.00	49.8	321.92	51.6	412.78	51

* Figures in bracket indicate amounts in lakhs.

Table 5

Overdues of PACSs during the last three years, i.e. 1983-84 to 1985-86

(Rs. crores)

Sr. No.	Name of State	1983-84		1984-85		1985-86	
		Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand
1.	2.	3.	4.	5.	6.	7.	8.
1.	Andhra Pradesh	69.29	38.16	108.66	55.67	94.70	53.58
2.	Assam	6.52	91.31	6.52	91.31	6.52	91.31
3.	Bihar	51.77	62.99	52.72	63.15	56.47	57.10
4.	Gujarat	99.72	33.05	91.47	33.29	130.61	35.03
5.	Haryana	86.74	35.36	94.38	36.26	104.50	34.35
6.	Himachal Pradesh	5.12	35.14	5.98	36.44	7.15	38.60
7.	Jammu & Kashmir	-	-	2.18	30.06	2.18	30.06
8.	Karnataka	86.05	39.80	91.84	41.59	112.64	50.57
9.	Madhya Pradesh	128.78	49.24	136.22	45.13	161.65	44.20
10.	Maharashtra	240.00	48.48	225.00	44.55	265.00	48.18
11.	Manipur	3.59	94.97	3.59	94.97	3.59	94.97
12.	Meghalaya	1.53	42.91	1.27	37.13	1.73	91.53
13.	Nagaland	-	-	-	-	-	-
14.	Orissa	60.25	47.38	63.15	47.52	86.00	66.66
15.	Punjab	108.15	36.40	48.46	14.79	102.44	21.42
16.	Sikkim	-	-	-	-	-	-
17.	Rajasthan	77.57	41.49	105.99	47.13	111.80	45.44
18.	Tamil Nadu	134.44	55.01	157.45	57.88	169.82	48.54
19.	Tripura	3.37	89.38	3.90	86.80	3.39	34.40
20.	Uttar Pradesh	204.23	46.29	224.89	50.55	206.07	41.80
21.	West Bengal	132.11	70.12	128.92	60.75	82.90	41.00
22.	Andaman & Nicobar Islands	0.18	90.00	0.14	38.88	0.24	80.00
23.	Arunachal Pradesh	-	-	0.08	53.33	0.08	42.10
24.	Chandigarh	0.03	42.85	0.03	42.85	0.09	47.36
25.	Dadra & Nagar Haveli	-	-	0.04	40.00	0.02	33.33
26.	Delhi	0.74	40.88	0.74	40.88	-	-
27.	Goa, Damah & Diu	0.89	74.16	0.75	68.18	0.84	73.68
28.	Lakshadweep	0.04	22.22	0.04	23.52	0.06	31.57
29.	Mizoram	-	-	-	-	-	-
30.	Pondicherry	0.88	50.57	0.94	47.23	1.64	51.25
31.	Kerala	68.66	20.03	75.49	20.68	92.78	24.66
Total		1570.65	43.05	1630.84	42.16	1806.68	40.96

Table 6

Overdues of LDBs for the last three years, i.e. 1983-84 to 1985-86

(Rs. crores)

Sr. No.	Name of State	1983-84		1984-85		1985-86	
		Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand	Over-dues	Percentage of over-dues to demand
1.	2.	3.	4.	5.	6.	7.	8.
1.	Andhra Pradesh	47.96	43.80	65.79	61.92	56.23	49.29
2.	Assam	1.13	63.02	1.15	52.35	1.74	60.00
3.	Bihar	24.04	58.00	17.22	44.99	5.62	15.34
4.	Gujarat	14.65	43.79	19.57	50.07	18.51	54.89
5.	Haryana	13.63	28.40	9.27	19.11	20.99	32.53
6.	Himachal Pradesh	0.64	49.61	0.49	41.78	0.83	41.81
7.	Jammu & Kashmir	0.82	48.81	0.63	40.31	0.82	38.23
8.	Karnataka	15.78	34.55	18.32	42.72	21.37	48.78
9.	Kerala	3.33	18.93	4.28	19.89	5.06	23.27
10.	Madhya Pradesh	17.07	40.69	14.19	35.00	14.56	33.60
11.	Maharashtra	42.09	49.30	39.48	43.85	43.84	46.42
12.	Orissa	3.68	27.44	4.45	35.32	7.11	41.02
13.	Pondicherry	0.21	52.08	0.06	20.41	0.05	30.10
14.	Punjab	4.76	9.90	5.60	9.96	9.19	13.96
15.	Rajasthan	16.33	43.81	20.61	52.16	27.27	57.94
16.	Tamil Nadu	20.55	46.74	25.48	49.19	24.98	63.86
17.	Tripura	0.49	79.88	0.63	86.75	0.43	74.45
18.	Uttar Pradesh	29.38	28.10	27.93	26.10	27.10	23.70
19.	West Bengal	9.77	49.92	9.91	47.46	12.11	51.71
20.	Delhi	0.20	58.00	0.25	46.78	0.24	58.43
21.	Goa	0.20	72.47	0.19	70.00	0.18	63.91
22.	Meghalaya	-	-	-	-	-	-
Total		266.71	38.28	285.50	39.53	298.23	38.83

Purpose-wise Overdues

15.010 Data on overdues under short-term (crop) loans and term loans for various purposes like minor irrigation and land development, farm mechani-

sation, horticulture, etc. in respect of commercial banks, RRBs, PACSs and LDBs collected in the course of the field surveys conducted by our Consultants for Study II are given group-wise in table 7.

Table 7
Purpose-wise Overdues of Different Credit Institutions as
Percentages to Demand - 1986-87

	Crop loan	Minor Irri- gation	Land Deve- lop- ment	Farm Mechani- sation	Horti- culture	Bio- gas	Others	Over all
	1.	2.	3.	4.	5.	6.	7.	8.
Commercial Banks								
Group I	19	54	40	34		38	23	24
Group II	25	55	56	46	60	59	43	41
Group III	29	39	67	37	74	60	69	38
Group IV	23	35	100	27	-	84	53	36
Group V	71	61	88	54	-	47	49	55
Regional Rural Banks								
Group I	41	61	50	-	-	64	53	46
Group II	69	82	92	67	-	-	58	66
Group III	20	38	-	-	-	-	40	32
Group IV	55	76	100	100	-	-	23	44
Group V	59	78	70	-	33	-	73	70
PACSs								
Group I	40.1	-	-	-	-	-	8.1	32.6
Group II	52.0	-	-	-	-	-	15.3	47.3
Group III	25.0	-	-	-	-	-	44.0	27.6
Group IV	44.0	-	-	-	-	-	56.6	45.2
Group V	23.1	-	-	-	-	-	-	23.1
PLDBs								
Group I	-	34.6	25.7	17.4	40.2	8.6	27.0	30.7
Group II	-	32.0	56.7	3.0	49.6	57.1	82.4	45.2
Group III	-	39.3	44.4	18.4	52.9	75.8	82.2	36.9
Group IV	-	64.0	12.0	42.8	16.6	-	69.8	63.7
Group V	-	40.3	31.3	13.4	46.7	38.7	20.0	38.5

Group - I : Highly irrigated and assured rainfall areas.
 Group - II : Moderately irrigated areas.
 Group - III : Dry and monetised areas.
 Group - IV : Unirrigated and less monetised areas.
 Group - V : Hilly and tribal areas.

The data show that the overdues of commercial banks and RRBs under crop loans were much lower than those under term loans, and in PACSs the situation was the opposite. There were, however, considerable variations in the level of overdues in respect of loans for different purposes and in different regions. As a general trend, the overdues under loans for farm mechanisation were lower than those under minor irrigation schemes, land development purposes, bio-gas and horticulture, in that order.

Overdues and Classes of Defaulting Borrowers

15.011 According to the field survey conducted by our Consultants for Study II covering 73 commercial bank branches, 34 RRBs, 141 PACSs and 30 PLDBs, the incidence of overdues (i.e. percentage of overdues to demand) among different classes of borrowers, viz., marginal, small and large farmers and landless labourers as on 30.6.1986 was as shown in table 8 :

Table 8

Incidence of Overdues Among Different Classes of Borrowers

	(in per cent)				
	<u>Large farmers</u>	<u>Small farmers</u>	<u>Marginal farmers</u>	<u>Landless Labourers</u>	<u>Overall for the survey sample</u>
CBs	46	42	37	45	43.4
RRBs	46	66	48	34	51.0
PACSs	37	40	45	47	42.0
LDBs	39	49	44	-	42.0

While from these data, which relate to a particular date (i.e. 30th June 1986), no trend can be deduced, they do show that no definite relationship exists between the incidence of overdues and different classes of borrowers. They also establish the dictum that overdues in agricultural loans are universal and neutral to the type of agency and variations in the incidence of overdues as between different classes of borrowers are in most cases only marginal.

Period-wise Overdues

15.012 The position of period-wise classification of overdues, both under agricultural and non-agricultural loans, of the different lending agencies, is given in table 9.

Table 9
Age-wise Distribution of Amount of
Overdues for Different Lending Institutions

(Rs. crores)

Age Group	CBs branches			RRBs			PACs			LDBs
	Agr.	Non Agr.	Total	Agr.	Non Agr.	Total	Agr.	Non Agr.	Total	
Less than 1 years	200	NA	200	37	4	41	271	29	300	48
1 - 2	319	NA	319	86	10	96	427	130	557	43
2 - 3	291	NA	291	81	48	129	94	11	105	31
3 - 4	399	NA	399	21	8	29	292	5	297	27
4 - 5	138	NA	138	11	8	19	133	-	133	38
5 - 6	61	NA	61	10	33	43	153	6	159	36
6 - 7	73	NA	73	23	8	31	49	-	49	24
Above 7 yrs	263	NA	263	16	9	25	196	11	207	51
Total	1,744	NA	1,744	285	128	413	1,615	192	1,807	298

So far as the agricultural sector is concerned, the age-wise position as at the end of December 1986 is summarised in table 10 :

Table 10
Age-wise Distribution of Overdues - Summary Position

	<u>Upto 3 years</u>	<u>3 to 5 years</u>	<u>5 to 7 years</u>	<u>More than 7 years</u>
CBs	46.5	30.8	7.6	15.1
RRBs	71.5	11.0	11.8	5.7
PACs	49.0	26.4	12.5	12.1
LDBs	40.8	22.0	20.1	17.1

(Percentage of overdues to total overdues)

The data show that 40 per cent to 50 per cent of the overdues in commercial banks, PACSs and LDBs comprised those upto three years and around 75 per cent comprised those upto five years. A bulk of the overdues (71 per cent) in RRBs was for less than three years. This is because RRBs themselves are of recent origin; eighty seven out of 194 RRBs were less than five years old as on 30.6.1986. The proportion of chronic overdues (i.e. over five years) was thus around 17 per cent in RRBS, 25 per cent in PACSs and rural branches of commercial banks and 37 per cent in LDBs.

15.013 In the course of the field survey undertaken by our Consultants for Study II in 35 selected districts, an attempt was made to discern the relationship between certain factors and the incidence of overdues; the results thereof are summarised below :

(i) **Agro-climatic Conditions and Recovery**

15.014 The areas selected for field survey were grouped into five agro-climatic groups viz. (a) highly irrigated/assured rainfall, (b) moderately irrigated, (c) dry and monetised; (d) less monetised and unirrigated and (e) hilly and tribal. The classification of the data for each group shows the following position of the average proportion of overdues to demand and the standard deviation of these proportions :

Table 11

Group-wise Data on Average and Standard Deviation of Proportion of Overdues to Demand

Group	No.of districts	Average proportion of overdues to demand	Standard deviation of overdues to demand
Highly Irrigated/ Assured Rainfall	9	34.1	10.7
Moderately Irrigated	7	50.7	14.1
Dry and Monetised	6	38.7	15.3
Less Monetised and Unirrigated	7	57.7	25.9
Hilly and Tribal	6	60.8	19.5

The analysis shows a significant difference in the average proportion of overdues to demand for different zones. The best recovery performance was found in highly irrigated/assured rainfall areas followed by dry and monetised areas, moderately irrigated, less monetised and un-irrigated areas and finally hilly and tribal areas in that order.

(ii) **Overdues and Farm Size**

15.015 The results of the field survey conducted by our Consultants for Study II and used for estimating, at the aggregate level, the proportion of overdues to demand for different types of farmers financed by different lending agencies are indicated in table 8. As stated earlier, the data show that the phenomenon of overdues is generally neutral to the category of borrowers financed and the variations in recoveries as between different classes of borrowers are only marginal.

(iii) **Overdues and Average Size of Holding, Value of Crops and Literacy Relationship**

15.016 The correlation between the proportion of overdues on the one hand and the average size of holding, the value of major crops and the literacy rates on the other, as worked out by the Consultants for study II, are presented in table 12 :

Table 12

Value of Correlation Co-efficient between Proportion of Overdues and Average Size of Operational Holding, Value of Crops and Literacy Rate

Variables	Value of correlation co-efficient	Remarks
Proportion of overdues and average size of operational holding	0.09	Statistically insignificant *
Proportion of overdues and value of major crops	- 0.45	Moderately significant *
Proportion of overdues and literacy rates	- 0.52	Moderately significant*

* when tested with the help of student's t-test.

The correlation co-efficient between the proportion of overdues and average size of operational holding was statistically insignificant, indicating that the size of operational holding had no bearing on the recovery performance. Further, as the quantum of loan is closely related to the size of holding, it could also be inferred that overdues did not have any definite relationship with the quantum of loans. On the other hand, the proportion of overdues in a district turns out to be negatively correlated with the value of major crops grown in that district, implying that the higher the value of major crops grown in the district, the lower is the proportion of overdues. Likewise, the correlation co-efficient between proportion of overdues to demand and literacy rate in a district is negative and statistically significant, indicating that higher the literacy rate, lower the proportion of overdues in the district. This points to the probability of better recoveries with improvement in the literacy rate.

(iv) Relationship of Overdues with Size of Branch Staff

15.017 The correlation co-efficient between staff strength at the branch and the proportion of overdues to demand for each type of lending agency shows the following results :

Table 13
Correlation Co-efficient between Staff Strength and
Proportion of Overdues to Demand

Agency	Correlation Co-efficient
Rural branches of CBs	0.14
RRBs	0.13
PACs	0.42

The analysis shows that in the case of rural branches of commercial banks and in the case of RRBs, there was no significant relationship between the staff strength at a branch and the proportion of overdues to demand. However, in the case of PACs a moderately significant negative relationship exists indicating that in PACs equipped with adequate staff, the proportion of overdues to demand was less.

Problems in Repayments: Borrowers' View Point

15.018 In the course of one of the field surveys, sponsored by us through our Consultants for Study II, 1,013 defaulters to different credit agencies were interviewed with a view to ascertaining the borrowers' perception of the causality of defaults. The findings of the survey are given below :

Table 14

Borrowers' View of Causality of Defaults

Particulars	Commercial Bank Branches	RRBs	PACSS	PLDBs
1. Crop failure due to weather	10.9	33.2	23.5	19.4
2. Crop failure due to other reasons	0.6	1.0	0.7	1.5
3. Income generation inadequate	17.0	31.6	11.0	11.0
4. Instalment of repayment too high	0.4	1.6	0.4	0.3
5. Repayment schedule not suitable	0.2	-	0.4	-
6. Diversion of amount for other purposes	2.3	6.2	2.6	1.0
7. Political interference and mis-guidance	0.5	1.6	1.1	2.0
8. Lack of understanding of terms	1.1	-	0.6	1.0
9. High interest rate	0.3	0.5	0.1	-
10. Non-adjustment of earlier paid instalment	0.6	2.6	0.7	0.5
11. Unforeseen development in the household	3.9	3.6	3.0	2.3
12. Any other	7.5	5.7	3.9	6.6
13. None (No problem)	54.7	12.4	52.0	54.4
	100.0	100.0	100.0	100.0

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These data show that crop failure due to adverse weather conditions was one of the major factors to which 22.6 per cent of the respondents attributed their defaults; institution-wise the percentage was 33.2 of the defaulters of RRBs covered by the survey, 23.5 of those of PACSs, 19.4 in the case of PLDBs and 10.9 in commercial bank branches. The impact of natural calamities was felt by all categories of borrowers i.e. marginal/small farmers and large farmers. An equally important factor cited by 17.1 per cent of the respondents was the inadequate income generation; institution-wise the percentage was 31.6 of the surveyed defaulters in RRBs, 17 of those in commercial bank branches and 11 of defaulters to co-operatives i.e. PACSs and PLDBs. In this case understandably, the inadequate income generation was given as a reason by a fairly high proportion of landless labourers (25.4 per cent) and marginal farmers (17.1 per cent). Diversion of loan amount for other (consumption) purposes was one of the reasons in the case of 6.2 per cent defaulters of RRBs, 2.6 per cent defaulters of PACSs and 2.3 per cent defaulters of commercial banks. Unforeseen circumstances was relatively an important cause in 3.9 per cent cases, particularly landless labourers (5.3 per cent) and marginal farmers, than in the case of larger farmers. The largest percentage of respondents i.e. 54.7 per cent defaulters to commercial banks, 54.4 per cent to PLDBs and 52 per cent to PACSs did not indicate any specific reason which compelled them to default in repayment of dues to the credit agencies. This is, infact a "Don't Know" category; some of these could be cases of "Wilful" defaults.

Overdues under Agricultural and Non-agricultural Loans

15.019 The statistics compiled by NABARD on overdues of PACSs and RRBs give the aggregate overdues at Rs.1,807 crores and Rs.413 crores respectively but their break-up into those under agricultural and non-agricultural loaning at the macro-level is not readily available. Our field survey data reveal that the proportion of agricultural and non-agricultural overdues pertaining to the selected sample was 89:11 in the case of PACSs and 69:31 in the case of RRBs; using these as proportions, the overdues under agricultural loaning have been arrived at Rs.1,615 crores in the case of PACSs and Rs.285 crores in the RRBs as on 30th June 1986. The comparative position on that basis would thus be as indicated in table 15.

Table 15

Position of Overdues at the Ultimate Borrower Level

(Rs. in crores)

	PACSS	PLDBs	RRBs	CBs	Total
Agricultural	1,615	298	285	1,744	3,942
Non-Agricultural	192	-	128	NA	320
Total	1,807	298	413	1,744	4,262

Impact of Overdues

15.020 At the end of June 1986 overdues of all the agricultural credit agencies at the ultimate borrowers level amounted to Rs.4262 crores, whereas the total direct finance (outstandings) by all credit agencies to the agricultural sector aggregated Rs.16,409 crores. Thus, nearly 26 per cent of the resources deployed by the credit agencies for the agricultural sector were locked up in overdues and were not available for recycling. At the institutional level, the clogging of overdues had severely impaired the eligibility of the credit agencies, for refinance from NABARD. The number of primary land development banks/branches of state land development having restricted eligibility for schematic lending was 1102 or 66 per cent of the total number and 166 or 84 per cent of the total number of regional rural banks. Similarly, on account of high level of overdues, 42 RRBs did not qualify for the general line of credit and 11 out of 366 district central co-operative banks did not qualify for short-term and medium-term credit limits from NABARD during 1987-88.

15.021 Defaults which, as we have already seen, are all pervasive, involve heavy costs all round. They affect adversely the interests of both the borrower and the credit agency. As a defaulter, the borrower is cut off from any access to credit from institutions. This affects his productive enterprise even if he has some informal source of credit available because he pays a much higher price for it. Similarly, the lending capacity of the credit agency is also equally adversely affected due to its inability to recycle the resources, or to raise more resources from the higher financing agency. If the credit agency is unable to recover from its borrowers even interest due on loans,

its profitability declines and its viability is itself jeopardised after some years. This apart, a disproportionately large amount of managerial time and manpower have to be spent on monitoring the accounts in default, adding avoidable costs to transaction costs of lending operations. The worst and most expensive aspect of overdues is that the agriculturists and other related rural enterprises, still outside the purview of institutional credit, suffer on account of non-availability of adequate supply of credit for investment and working capital.

15.022 The high incidence of overdues, in the system has become a major constraint to the expansion of credit and development of agriculture in the country. Under the existing system of financing agriculture where most of the lending is done in the form of fixed loans repayable on pre-determined due dates, prompt recovery of loans is of crucial importance. In a developing economy faced with serious resource constraint, recycling of available resources assumes special significance for all institutional structures handling credit so as to ensure the optimum utilisation of available funds. Further, since repayments are expected from out of incremental income generated by the productive use of loans, recoveries serve also as an indicator of the quality of loaning.

15.023 A lending institution engaged in rural lending has, therefore, to ensure that (a) loan appraisal systems are sound so that the recovery of loan becomes assured (b) the delivery system is able to ensure timely availability of credit not only to the borrowers but also for financing inputs, marketing, storage facilities, etc. and (c) repayment schedules are realistically drawn up. In other words, rural banking institutions have to ensure that lending and recovery procedures in themselves do not lead to investment failure and, consequently, non-repayment by borrowers. This aspect is, however, dealt with separately. In the discussion which follows, we are concerned mainly with the impact of overdues on lending institutions and consequently the need for ensuring proper recovery disciplines.

(A) Borrowers

15.024 A borrower in default not only becomes liable to pay penal interest on his overdue loan amount but also loses his eligibility to obtain a fresh loan. However, in recent years loan policies have undergone a qualitative

change inasmuch as distinction is now made between 'wilful' defaulters and 'non-wilful' defaulters. Consequently, such of those who are forced into defaulting on account of causes arising out of circumstances beyond their control, the policy in vogue currently enables grant of relief to them in the form of conversion/rescheduling, etc. of the outstanding amount so that they are in a position to borrow afresh. Ordinarily, such relief is available only to (a) borrowers in areas affected by natural calamities (where the annewari declared by the state governments is 6 annas or less) and (b) the small/marginal farmers having small amount in default not exceeding 10 per cent of their eligibility under seasonal agricultural operations (SAO) loans in each case (relaxed to 20 per cent of eligibility in the case of eastern states namely Bihar, Orissa, West Bengal and Eastern U.P. as recommended by Sen Committee). In almost all other cases defaulters are deemed 'wilful' and, therefore, denied access to fresh finance whether from the agency to which they are in default or from any other.

(B) Lending Institutions

15.025 As far as the impact on lending institutions is concerned, overdues affect the overall liquidity and in due course the solvency of the credit institutions, particularly co-operatives and RRBs having serious resource constraints and impair their capacity to undertake fresh lending. In course of time, a portion of the overdues also becomes irrecoverable thereby eroding the net-worth of the lending agencies. Arrears in recovery of accrued interest affect the profitability of the institutions. This apart, a major impact of overdues on the lending agencies particularly co-operatives and RRBs having low level of their own deposit resources, is that overdues impair their capacity to obtain refinance from NABARD as recovery performance, among other things, constitutes a major item of eligibility criterion. The ability of the co-operative banks to operate on the credit limits sanctioned to them is closely linked to the level of their overdues since drawals on the credit limits are subject to the discipline of seasonality, non-overdue cover, etc. In certain states, where a sizeable number of RRBs/DCCBs, is laden with heavy overdues and ineligible for NABARD credit limits, the credit flow to the agricultural sector gets seriously affected. Normally DCCBs and SCBs in states with two tier structure, having overdues exceeding 60 per cent of demand are ineligible for credit limits. Till recently, this was a rigid criterion totally cutting off refinance for all banks having overdues in excess

of 60 per cent of demand. However, considering the need for keeping up the flow of credit to specific under-developed areas, some production schemes of national importance and also as a part of the package of measures for facilitating revival of central co-operative banks, NABARD has relaxed the criterion in several cases; for instance 'weak' DCCBs under rehabilitation programme and DCCBs in the pilot project districts in which case the cut off point has been relaxed from 60 per cent to 65 per cent. For providing adequate credit support for the cultivation of oilseeds in the areas covered by National Oilseeds Development Programme (NODP), NABARD has been sanctioning credit limits to DCCBs, otherwise ineligible therefor to the extent of their credit requirements for financing cultivation of oilseeds under NODP. In the case of banks in the North-Eastern states, the overdues criterion has been totally removed.

15.026 For schematic term loaning, the refinance facilities from NABARD are governed by eligibility criteria (EC) envisaging different levels of refinance depending on the recovery levels of the lending institutions, viz. DCCBs PLDBs, RRBs and branches of commercial banks, SCBs and SLDBs. Issues relating to eligibility criteria have been examined separately in Chapter XII.

Causes of Overdues

15.027 A wide range of factors influence the level of and the trends in overdues of the agricultural credit institutions. Although defaults are commonly attributed to adverse weather conditions, particularly to droughts/floods, in large parts of the country, their basic causes lie much deeper and range from the non-viability of the agricultural occupation itself in some cases, lack of the forward/backward linkages and infrastructural facilities and services which support agriculture, the socio-political environment in which the credit institutions are functioning, to legal and other government support available to the agricultural credit system, besides adverse weather conditions, affecting the output of crops, particularly in the rain-fed areas. These are external factors over which the credit institutions have little or no control and for their mitigation they have to depend almost entirely on the outside agencies, particularly government and its agencies. The other causes of overdues which are internal to the credit institutions themselves are inadequate supervision over credit, unsound lending policies and procedures, unsatisfactory management of the credit institutions, etc. Overdues are often the result of a combi-

nation of various factors. The different factors which lead to overdues, under both the categories are discussed in the following sections:

Factors Internal to the System

15.028 The field studies undertaken by our Consultants for Study II show that apart from non-viable borrowers whose income generated is not adequate to repay the bank loans and who constitute a class by themselves, defective loan policies and procedures, emphasis on targeting, disbursements in loan melas and ineffective supervision over credit have contributed to some extent to defaults.

i) Defective Loan Policies and Procedures

a) Crop Loans

15.029 In the case of crop loans, delays in the sanction and disbursement of loans, unrealistic scales of finance and sanction of loans in excess of the need/repaying capacity or, at the other extreme, inadequate loan amounts compelling the borrowers to resort to borrowings from money-lenders and other informal sources of credit and fixation of due dates unrelated to the harvesting and marketing seasons are among the important lacunae which have resulted in defaults. These issues have been discussed in Chapter VI.

15.030 It is also observed from the findings of the field surveys that there are several deficiencies in the implementation of the loan policies and procedures, evolved over the years, which contributed to ineffective credit flow and also incidence of overdues; e.g. although there is a provision that Technical Committees constituted for each district should, in consultation with the officers of the Agriculture Department on input requirements of various crops in different areas, lay down scales of finance for each crop, irrigated and unirrigated separately, it was observed that in many states the scales of finance were laid down by the Registrar of Co-operative Societies, on an ad hoc basis.

(b) Term Loans

15.031 In regard to term loans, field studies conducted by our consultants as also NABARD's evaluation studies have revealed several lacunae in the implementation of loan policies and procedures leading to overdues; the major among them were as follows :

- i) Selection of schemes unsuited to the areas and the borrowers. Concentration on a few types of schemes, at times only a single occupation within a limited area which affected the productive capacity or marketability of the produce and income generated therefrom. For instance, during the field studies it was observed that disbursement of cattle loans to tribals who were not traditionally rearing cattle had resulted in defaults in Tamil Nadu.
- ii) Over-emphasis on the target approach and attraction of subsidy under government sponsored schemes thereby relegating to secondary importance the economic significance of the scheme or the quality of lending.
- iii) Fixation of un-realistic repayment schedules, amounts of instalments and due dates of repayment without reference to the cash flow pattern of the borrowers. The evaluation studies conducted by NABARD have brought out the extent of wide disparity between the repayment periods for various types of investments recommended by NABARD vis-a-vis those fixed by different banking institutions in practice. Details in this regard are given in table 16. *
- iv) Fixation of low unit costs and sanction of loans for amounts less than the unit cost leading to misutilisation of the loans. NABARD's evaluation studies show that in the case of following schemes, the approved unit cost was lower than the actual cost by 16 per cent to 32 per cent and as a result, the down payment far exceeded the stipulated percentages. A few instances in this regard are given in table 17.

* Note :

In 1986 in a NABARD's evaluation study in respect of dug-well irrigation scheme in Palghat district, Kerala, it was observed for instance, that while fixing the due dates of repayment, the bank had taken into account only the date of disbursement of loan and not the marketing seasons of the crops grown. In the course of our field studies a common complaint voiced by the farmers interviewed was that the bankers were generally reluctant to allow the borrowers full repayment periods for the loans taken by them, as per norms laid down by NABARD. This is due to bankers' anxiety to ensure quick recycling of funds, but it causes hardships to borrowers in complying with the repayment schedules and turns them into defaulters.

Table 16
Disparity in Repayment Periods for Term Loans

Item of investment	Financing Bank	Scheme area	Repayment period	
			Recommended by NABARD	Fixed by Bank
Pump set	State Bank of India	Ballia, UP	9 years	5 years
Borewells	- do -	- do -	11 years	5 years
Borewells	Syndicate Bank	- do -	11 years	5 years
Borewells	UPSLDB	Lakhimpur Kheri & Jalaun, UP	11 years	9 years
Poultry	State Bank of India	Eluru, AP	6-7 years	2 years
Horticulture	Andhra Bank	Nalgonda, AP	12-15 years	5 years
Dug Well with Pumpssets	Canara Bank	Khammam, AP	11-15 years	5 years
Tractors	State Bank of India	West Godavari, AP	7 years	5 years
Dairy Development	State Bank of India	West Godavari, AP	7 years	5 years
Dairy Development	DCCB, Godhra	Panchmahal, Gujarat	5 years	3 years

Table 17
Disparity in Loans Sanctioned vis-a-vis Unit Cost

Item of Investment	Financing bank/s	Scheme area	Approved unit cost lower than actual cost by	(In per cent)	
				Stipulated down payment	Actual down payment
1. Tractors	1. State Bank of India 2. Canara Bank	1. Thanjavur & Periyar 2. Districts, Tamil Nadu	24	15	37
2. Power Tillers	3. Indian Overseas Bank 4. Union Bank of India	1. Districts, Tamil Nadu	16	15	31
3. Dairy Development	1. State Bank of India 2. Punjab National Bank	Mathura, UP	32	5-15	45 (of sample beneficiaries)

The table below gives various instances of under-financing resulting from sanction of lower loan amounts than the actual cost of investment, noticed in the course of the evaluation studies :

Table 18
Cases of Under-financing of Dug wells vis-a-vis Approved Unit Costs

Financing Bank	Scheme area	Actual cost of investment	Average Loan amount	Loan Amount as percentage of actual cost
GSCLDB	Rajkot - Gujarat	14,000	10,000	71
Bank of Baroda	Panchmahal, Gujarat	15,000	6,000	40
State Bank of India	Panchmahal, Gujarat	15,000	8,000	53
GSCLDB	Rajkot - Gujarat	8,000	5,000	62
Bank of India	Padadhari, Rajkot	13,000	10,000	77
Bank of India	Padadhari, Rajkot	21,000	16,000	74

About 60 evaluation studies conducted by NABARD and commercial banks have revealed that more than 50 per cent of the borrowers under any scheme were under-financed. As a result, the beneficiaries were either forced to raise the balance resources from the informal agencies at a much higher rate of interest or they had to settle for assets of poor quality. Field studies conducted by our consultants also showed that the bank managers often reduced the loan amounts, arbitrarily, even below the approved unit costs for various types of investments, mainly on account of their anxiety to use available resources over a large number of borrowers. This led to under-financing and drove clients either to moneylenders or to misutilize the loans.

- v) Inadequate initial grace period especially in the case of investments where the gestation period is fairly long. Raising of demand by the financing banks during these years forces the farmers either to repay from other sources and where they have no such sources, to default in repaying their dues on the due dates.
- vi) Financing of assets not in keeping with the actual farming occupation of the beneficiaries. For instance, in the case of tractor loans it was observed that the banks in many cases

had financed tractors with high horsepower (exceeding 35 H.P.) which was not related to the actual requirements of the beneficiaries resulting in over-capitalisation and higher debt burden. Lack of suitable implements and accessories had also contributed to sub-optimal use of the tractors.

ii) Absence of Linkages of Credit with Marketing

15.032 Although the All India Rural Credit Survey Committee envisaged what has been known as the Integrated Scheme of Rural Credit, in actual practice it was not given desired attention or emphasis. The case study conducted by our Consultants for Study II shows that linking of credit with marketing as a measure of recovery, has largely failed to develop except in a few cases like sugarcane cultivation in Maharashtra where co-operative sugar factories undertake effective recovery of credit through sale price of sugarcane. Firstly, the marketing societies have not become strong enough to secure better prices for the farmer members' produce. Secondly, borrowers avoid sale through marketing societies and/or sell the produce under fictitious names to avoid recovery of loans. Thirdly, the functional societies themselves are reluctant to recover dues of credit agencies lest such a step affects their procurement programmes. For example, in Madhya Pradesh the oilseeds societies and their federation have refused to recover dues on behalf of primary agricultural credit societies. Even under the scheme of monopoly procurement of cotton in Maharashtra, it has not been possible for the Cotton Grower's Federation to recover all loans due to PACSs through district central co-operative banks, although, the DCCBs in Maharashtra have a recovery rate of 56 per cent through linking.

iii) Investment Credit - Lack of Provision of Working Capital

15.033 One of the causes of overdues is the absence of proper synchronization of investment credit with working capital provision. While in the co-operative sector, this is generally attributed to investment credit and working capital being provided by two separate institutional structures viz. short-term and long-term, in the case of commercial banks including regional rural banks, the investment credit and working capital loans are disbursed by the same agency and consequently the farmers have one contact point. Field studies by our Consultants for Study I have, however, shown that sufficient interest is not taken by the commercial banks for provision of crop loans although

they carry relatively higher interest margins. The commercial bank branches seem to find the crop loan business too exacting, costly and time consuming, as the crop loan cycle repeats every year. The crop loaning activity, therefore, over-burdens the field staff of commercial banks. In the case of commercial banks and RRBs the stock reply received to our queries was that the borrowers did not need any production credit or did not apply for it. The fact remains that there exists a gap between provision of working capital needs of the borrowers under investment credit and timely catering of funds to them from the credit institutions.

iv) Lack of Access to Institutional Credit for Consumption Purposes

15.034 Our field survey has revealed that 43 per cent of the institutional borrowers were also resorting to borrowings from private sources. About 36 per cent of such households borrowed for consumption purposes and 13 per cent for social and religious ceremonies. The need for borrowings from informal sources normally arises under the following three circumstances :

- i) inadequacy of scales of finance/unit costs for meeting in full the agricultural credit needs of the farmers.
- ii) the need for sustaining the family and meeting unforeseen family contingencies like illness, birth, deaths and social/religious ceremonies.
- iii) need for acquisition of consumer durables.

In addition to the cost of inputs and hired labour, imputed cost of family labour, service charges for hiring machinery and equipment from leasing agents, etc. the cultivator incurs, between the sowing and the harvesting seasons, consumption expenses for sustenance of his family and has also to meet the cost of maintenance of agricultural machinery, tools, implements and draught animals. The scales of finance, in vogue, usually provide besides the cost of inputs, cost of hired labour and imputed cost of family labour. Though provision of credit in 'kind' reduces the farmers' tendency to divert production credit for meeting their consumption needs, there is no fool-proof method of preventing large scale diversion of funds as long as need for consumption credit exists. When such diversion of institutional credit is not sufficient to meet their consumption needs, small farmers often resort to borrowings

at high rates of interest from informal sources like relatives/friends or money-lenders. The high rates of interest on borrowings from informal sources adversely affect the farmers' repayments to the institutional credit agencies. The income generated out of agricultural operations goes first to discharge such private borrowings carrying high rates of interest and repayment of institutional loans gets lower priority, resulting in defaults.

v) **Ineffective Supervision**

15.035 In a situation where agricultural finance instead of being provided against the specific production plan of each borrower cultivator, the credit agencies are called upon to retail credit to thousands of small and economically weak tillers on pre-determined scales of finance/unit costs, close and constant supervision over sanction, disbursement and end-use of credit and its recovery assumes all the more importance. Inadequate supervision often results in improper appraisal of loan proposals, under-financing or over-financing and failure of credit agency to approach borrowers after harvesting/marketing seasons when they are in funds and are in a position to repay. Virtually non-existent or ineffective supervision gives rise to many malpractices, culminating in overdues, which range from misutilisation of credit, disposal of assets and diversion of sale proceeds for consumption purposes, diversion of funds obtained at concessional rates of interest for non-agricultural business purposes to down-right fraudulent practices like borrowing larger amounts than warranted by agricultural operations by showing inflated acreages/cropping pattern carrying higher scales of finance with a view to deceiving the lending agency and even reloading of concessional finance at higher rates of interest to the needy.

15.036 Deficiencies in supervision arrangements relate as much to the inadequacy of staff, lack of qualifications, technical knowledge, or training to staff as to the unsatisfactory quality of their work. A common feature noticed in the course of field studies conducted by our Consultants for Study II was the inadequacy of field staff in most of the commercial bank offices/branches visited. Agricultural lending involving a large number of small advances to borrowers in scattered villages calls for more man-power, more mobility and more time than for lending in urban centres. Unfortunately, the controlling offices of commercial banks guided by considerations of profitability keep down costs of rural branches generally by cutting down the staff strength

with the result that supervision gets neglected. We suspect that the banks themselves do not want to pay much attention to supervise large number of these small accounts due to high costs involved. The norms fixed by many banks envisage that the field officer or the technical officer/rural development officer should handle 500 to 750 agricultural accounts. Data regarding field Officers in position, the average number of accounts per officer, number of villages covered by agricultural loaning and percentage of overdues to demand in respect of 10 branches studied in the course of our field survey are given in table 19.

Table 19

Branch-wise Villages Covered, Amounts Advanced

Region	Branch Sr. No.	No. of Villages covered	No. of field officers	Advances		
				No. of Accounts*	Amount (In Rs.'000)	
1	2	3	4	5	6	
i) Highly Irrigated/ assured rainfall	0	1	12	1	1,421	6,278
	0	2	14	2	4,589 (2,294)	16,728
ii) Moderately Irrigated	0	3	50	1	916	5,575
	0	4	30	1	585	6,263
iii) Dry and Monetised	0	5	36	1	1,146	7,885
	0	6	28	1	522	4,248
iv) Unirrigated & Less Monetised	0	7	25	1	1,218	3,154
	0	8	24	1	925	1,479
v) Tribal and Hilly	0	9	128	3	4,755	37,516
	0	10	43	1	(1,585) 1,165	2,632

* Figures in brackets represent the number of accounts per Field Officer.

The above data reveal that with a few exceptions the charge per supervisor exceeded 750 agricultural accounts. Where the number of accounts was large and also scattered over a large number of villages, the follow-up of credit was considerably affected.

15.037 In the short-term co-operative credit structure, the supervisors of DCCBs are not comparable to the supervisors of commercial banks. The principal responsibility for recovery is that of PACSs and the supervisors of DCCBs

are only meant to assist them though in actual practice these supervisors themselves often undertake recoveries. DCCBs try to follow the norm of one supervisor for 10 societies recommended by RBI in the past. The actual position, however, varies from bank to bank. The number of supervisors per branch and their average charge of societies in the seven DCCBs visited in the course of the field survey conducted by our Consultants for Study II are given in table 20.

Table 20
Charge per Supervisor

DCCB	Position of Supervisors			
	Number per branch	PACs per branch	Average charge per supervisor	Average Number of visits
Hoshangabad	2	8	4	20 days tour
Indore	1	5	5	4
Aurangabad	2	10	5	10
Kolhapur	1	8	8	4
Pudukottai	1	8	8	12
Tirunelveli	2	13	6.5	12
Nalgonda	2	8	4	Not prescribed

The charge (number of societies) per supervisor needs rationalisation. The present practice of judging the adequacy of supervision with reference to the number of societies per supervisor is patently wrong. The charge has to be fixed taking into account the quantum of loaning, distances involved and other relevant factors rather than a pre-determined number of societies.

15.038 In the long-term co-operative credit structure, the survey findings bring out that a field officer attached to a branch of LDB had charge of 678 accounts on an average involving loaning of Rs.29.4 lakhs scattered over 53 villages. The data on group-wise villages covered, the number of accounts and the amounts handled per field staff are given in table 21. The charge per supervisor appears to be too large, particularly in the tribal and hilly areas, both in terms of the coverage of villages as also the number of accounts to be supervised and calls for rationalisation.

Table 21
Number of Villages, Accounts and Amount per Field Staff (LDRs)

Groups	No.of villages	No.of Accounts	Outstanding advances (Rs. lakhs)
1. Highly irrigated	24	1,053	64.8
2. Moderately irrigated	67	375	30.5
3. Dry and monetised	23	143	19.0
4. Unirrigated and less monetised	36	169	4.2
5. Tribal and hilly	170	1,552	46.8
	53	678	29.4

Factors External to the System

(i) Problems of agricultural economy

15.039 The increasing incidence of overdues being faced by all the agricultural credit agencies, is very closely connected with the complex nature of agricultural economy and unless the basic issues involved in agricultural sector are tackled effectively, it will be difficult to find a lasting solution to the problem of overdues. In the sphere of agriculture, given the small sizes of holdings of large number of borrowers, the basic issue is one of viability of the operating size of holding. The Working Group to Review the Flow of Institutional Credit for Rural Sector, recently constituted by RBI under the Chairmanship of Shri Annasaheb Shinde has brought out some aspects of this problem in this regard.

15.040 The period after the 1960's witnessed the world over, rapid advances in the field of agronomy, genetics and bio-technology and their impact on agricultural productivity was significant. The Green Revolution in India was, however, restricted only to a few crops, in a few regions. Considering the economy as a whole, the development thrust or the agricultural push has been rather modest.

15.041 During the 10 years span from 1970-71 to 1980-81, the number of

operational holdings has increased from 70.49 million to 89.39 million, mainly due to the continuing process of sub-division of holdings as the area operated increased by just 0.67 million hectares. Consequently, there has been a sharp reduction in the average size of operational holding from 2.7 hectares in 1960-61 to 1.8 hectares in 1980-81. The proportion of marginal holdings (below one hectare) has steadily gone up from 50.6 per cent in 1970-71 to 56.5 per cent in 1980-81. Most of the 89.39 million holdings comprise four to eight scattered plots; the fragmented land holdings in several tiny plots tend to erode the viability of the cultivator. The sustained pressure on land has led to the cultivation of even the most marginal quality lands. Further, the fact of the bulk of the cultivated land being unirrigated and thus agriculturally somewhat unstable, also adds to non-viability of small/marginal farmer and his capacity for prompt repayment of loans.

(ii) Natural Calamities

15.042 Incidence of natural calamities like droughts, floods and hail storms cause substantial damages and impair the repaying capacity of the borrowers and the resultant defaults choke up the channels of credit. This is a major cause for defaults to which, in the course of our survey, 22.6 per cent of the respondents attributed their defaults. The issues relating to management of recovery problem in the event of natural calamities have been examined in detail in Chapter XVI.

(iii) Linkages and supporting services

15.043 Schematic lending implies well orchestrated planning by various development agencies and tie up of credit programmes with other development programmes as well as establishing suitable backward and forward (non-credit) linkages. The absence of such linkages and non-availability of supporting services have been a serious lacuna and this has led to impairment of effective use of the assets impeding the productivity itself. In the case of minor irrigation schemes non-energisation of pumpsets/machinery and delays in providing power lines/connections have virtually brought many programmes to a standstill.

15.044 In Himachal Pradesh where horticulture occupies a predominant position, farmers have to suffer losses, even when they have good yields of apple crop, for want of proper institutional marketing set up and organic

link with the terminal markets. Again in the dairily development schemes, non-availability of quality animals, absence of proper fodder and feed, veterinary services, result in poor maintenance of animals and poor production and absence of marketing arrangements result in poor income often leading to defaults. For instance, in a recent evaluation study of a dairy development scheme in the Darjeeling District of West Bengal, it was observed that -

- (a) although according to the stipulation, banks were required to finance the second cow after five to six months of the purchase of the first cow, to maintain continuity in milk production the bank had allowed beneficiaries to purchase both the cows simultaneously;
- (b) In 35 per cent cases both animals financed by the banks had gone dry simultaneously and in another 33 per cent cases both the animals were in milk.

In the case of sheep breeding, goat rearing and pig breeding schemes, which had been financed by banks, it has similarly been observed that there was no marketing support. More examples could be given.

15.045 In the case of the weaker sections, the major problem in recovery arises from the failure of activities themselves not only on account of lack of linkages/supporting services but mainly due to lack of entrepreneurial skills on the part of the selected beneficiaries. This often reflects itself in their inability to select the right activity with good market potential for the product. Lack of economic strength and staying power, primitive technology, uneconomic scale of operations, etc. further compound the problems caused by ignorance and social backwardness.

15.046 In the case of crop loaning, unlike co-operatives which have within the system the necessary infrastructural organisation to some extent, the commercial banks and RRBs have no in-built linkages with input supplies on the one hand and marketing arrangements on the other. This seriously hampers the quality of their loaning.

iv) Impact of Targeting and Subsidies

15.047 Apart from the financing of the non-viable borrowers dealt with earlier,

assistance to the poorest among the poor under the loan-cum-subsidy based IRD Programme entails other aspects such as the phenomena of targeting, disbursements in Loan Melas etc. which seriously affect the recovery of bank credit. Targeting for lending is necessary and relevant where compulsive shift in the deployment of funds is needed to ensure adequate flow of funds to otherwise starved sectors. While it is advantageous to fix certain targets for loaning and focussing on the type of clientele to be assisted as also certain activities to be supported, etc., problems arise when the institutions begin to find short cuts for achieving the targets. This seriously affects the quality of lending and results in avoidable defaults.

15.048 It is also observed that in many cases, branches in their anxiety to fulfil the targets given to them fail to carry out proper appraisal of the loan proposals so as to adjudge the suitability of the activities chosen, aptitudes of the beneficiaries to undertake those activities or the adequacy of the loan amount, etc. An impression is often created that the suitability of the beneficiaries to carry out the selected activities has been fully gone into by the sponsoring agency while identifying them and the banker should not stand in the way of the beneficiaries getting the loan applied for. The beneficiary's own perception of the activity under the sponsored schemes gets so clouded by the subsidy made available under the scheme that he is unable to view it objectively as a venture which it is his responsibility to make a success of. These deficiencies adversely affected the acquisition of assets, their productive use and often resulted in delinquencies. As a result the recovery under IRDP was often much lower than that under agricultural loaning. The public sector banks could show recovery of only 42.8 per cent and 45.3 per cent under IRDP at the end of June 1986 and June 1987 respectively as against their overall recovery under direct agricultural advances which was 56.5 per cent and 57.4 per cent respectively.

(v) **Loan Melas**

15.049 Sanctioning of loans and disbursal thereof by political dignitaries at public functions popularly known as 'Loan Melas', arranged quite often, do not leave adequate time to the bankers to subject the large number of hastily collected/sponsored loan applications to normal scrutiny. In a sample study of one such loan mela covering 16 branches of a bank, 51 per cent applications were sanctioned on the very day of receipt, and in 98 per cent

cases, loans were disbursed on the day they were sanctioned i.e. the day of Loan Mela.

15.050 In the course of field survey conducted by our consultants it was observed that about 30 per cent of the responding banks/branches had participated in the loan melas. In general, the banks appeared to be unhappy about this mode of loan sanction/disbursal as the bankers felt that the normal procedures involved in the scrutiny and sanction of loans were short circuited although the responsibility for recovering the loan, squarely rested with them. In a technical sense, the loan melas also violate the canon of confidentiality between the banker and client. Further, when political dignitaries are associated with the loan disbursals, the beneficiaries as well as the public perceive it not so much as bank credit as state aid without any obligation to repay.

15.051 Some evaluation data available in respect of a few loan melas/accelerated lending programmes, organised in different parts of the country have revealed that the branch managers were expected to sanction/disburse maximum possible loan cases in these programmes. Applications were often sponsored by organisations with political affiliations, or persons holding political offices like MLAs and MLCs, resulting in direct or indirect pressure on the financing banks to sanction the maximum number, if not almost all, of the sponsored cases. Loan applications received from MLAs, 'panchayat' members, etc. included some applicants who were defaulters elsewhere and as such, prima facie, ineligible for loans. The beneficiaries were told that loans would not be sanctioned/disbursed to them unless they attended the loan melas. It was also seen that branches were often required to release loans without obtaining "No-dues Certificate". Due to time constraints, there were no visits to beneficiaries by the bank's staff in many cases and in others where inspection was carried out, it was largely perfunctory and poor in quality. As regards the activities financed, there was pronounced emphasis on the tertiary sector; in one programme 50 per cent applications were under 'service' and another 40 per cent for 'business'. In yet another programme, 98 per cent beneficiary applications were for 'trade' and the beneficiaries themselves who were contacted were not aware of the purpose for which they were financed. Finance was provided under DRI scheme at 4 per cent, irrespective of income of the beneficiaries. There were large scale misutilisations of loans; of the cases financed in one such programme misutilisation of loans

was observed in 83 per cent cases and in another in 69 per cent cases. The overall recovery ranged from 70 per cent in the case of one programme to mere 13.9 per cent in another.

15.052 Our discussions with a number of bank executives clearly brought out their anxiety over the increasing role of the so called 'social workers' in the sanction and disbursement of bank credit under poverty alleviation programmes, which had adverse repercussions on the proper utilisation and repayment of bank credit and the resultant 'wilful' defaults though the bank officials, wilting under political pressures, were often held responsible for unsatisfactory recoveries. While the objective of assisting the poor with bank credit is in itself laudable, we feel that once the government lays down the national objectives, fixes reasonable targets for banks' lending and formulates requisite programmes, there should be professional approach to scrutiny and sanction of individual loan applications and the banks should be enabled, to deal with the cases strictly according to the banking norms, as banks' resources represent the hard earned savings of millions of depositors, many of them being small depositors. In this context, our Consultants for Study I have referred to the conclusions the Central Vigilance Commission had arrived at in its 1984 Annual Report, viz. that "the loan melas breed corruption" and the Commission's suggestion, that such mass lending programmes be stopped since they assume political overtones. We share the Commission's concern and endorse their suggestion, as in our view, loan melas have deleterious effects on the functioning of the credit agencies.

(ii) Politicisation

15.053 Another disquieting development in the last few years has been the growing politicisation in the working of the credit system in general. Exhortations from political platforms for postponement of loan recovery or pressure on the credit institutions to grant extensions to avoid or delay the enforcement process of recovery has become a regular feature in recent years vitiating wholly the recovery climate. In the course of our field visits we observed that political interference was responsible for widespread defaults while the alibi ostensibly was of crop failures. Of late, there has also been a growing tendency among several states not only to show total indifference to effecting recovery of co-operative dues through coercive measures but

also to issue stay orders against recovery through coercive measures. There have also been instances (as in Haryana recently) where election manifestoes of political parties contained promises to write off agricultural dues as a bait for votes. About a decade ago, under more or less similar circumstances, the Governments of Maharashtra and Tamil Nadu had written off co-operative dues. The action of the state governments in announcing write off and assurances to do so given from the public platforms, if not on the floor of the Legislative Assemblies, have also given rise to expectations that similar concessions would be given in future. The vitiated atmosphere breeds wilful defaults as borrowers having means to repay are inclined, and at times persuaded, to hold back repayments; such wilful defaults are bound to increase in number as the borrowers expect that their loans would be written off on one pretext or another.

15.054 Apart from the fact that measures such as write off place heavy burden on the state exchequer, they generate a general psychology of non-repayment, totally vitiating the recovery climate which, in the long run, jeopardises the financial interests of the credit agencies. The measures also give rise to propaganda carried out by certain interests in political circles, champions of farmers' interests, etc. that bank loans will be written off one day or other. This causes a lot of damage to the climate of recovery and in fact, creates an ethos of non-repayment of dues to the financial institutions.

15.055 At the same time, the political slant or overtones in pushing through certain credit programmes often tend to give wrong signals to the rural borrowers and they in turn tend to treat institutional credit on par with grants or subsidies provided by government. This leads to convey an impression that no financial liability attaches to them in respect of repayment of loans provided under these programmes. In these circumstances, not only the psychology of the borrowers is adversely affected but the pattern of behaviour of the banks also gets conditioned to the expectations of repeated write off of this type. The result is that the field staff tend to slacken their recovery efforts.

15.056 Wilful defaulters are, in general, socially and politically important people, whose example others are likely to emulate, and in the present milieu, the bureaucracy in the credit agency is reluctant to touch the influential

rural elite who wield a lot of formal and informal influence and considerable power. Farmers' agitations in many parts of the country have often taken a virulent form and banners put up in many villages declaring that no bank officer should enter the villages for recovery purposes. This dampens the enthusiasm of even the conscientious members of staff of the banks working in the rural areas in their recovery efforts. The general climate in rural areas is, therefore, becoming increasingly hostile to recoveries.

Measures for Combating Overdues

15.057 Measures for combating overdues may also be broadly classified under those internal to the system and those which are external. There are, however, some grey areas which may not strictly fall under either of the two and may be partly one or the other and, therefore, merit discussion under separate heads. One such category is of those measures which relate to linkages - both forward and backward. A second would be those which may be categorised as co-ordination and infrastructural support which by and large would be the responsibility of the state. The third also lies within the state responsibilities but are a category by themselves. These relate to legal support. These are discussed in the following sections.

(a) Internal Reforms and System Streamlining-Loan Policies and Procedures

(i) Crop Loans :

15.058 For overcoming delays in the sanction and disbursement of loans we have elsewhere in this report recommended a switch over by banks from fixed duration (crop) loans to cash credit system for financing the seasonal agricultural operations in areas where perennial irrigation facilities are available and multiple cropping pattern is in vogue. To recapitulate some of our other recommendations, we have recommended that the normal credit limit statements (NCL) for short-term (crop) loans be prepared once in three years subject to certain precautions so that the procedural delays involved in the preparation of NCL statements each year are obviated and speedy disbursement of loans is facilitated. We have recommended that in areas where there is fertiliser consciousness and farmers are already accustomed to the use of fertilisers, there should be no insistence on disbursements in 'kind' and that the banks may be given discretion to determine the mode of disbursement of credit for inputs. We have further recommended that the due dates for

rabi crop loans be postponed from 30th June to 31st August at the borrower level so that repayment dates are congruent with marketing season. These improvements should remove some of the procedural deficiencies which presently cause considerable delay in disbursement of loans and thereby ensure the timeliness in availability of credit to the borrowers.

15.059 There are several other recommendations of similar nature which have been made by earlier Committees but remain unimplemented. SCB in each state should take steps to identify these and where necessary ensure that these procedural changes are implemented with diligence to make dispensation of credit more effective and utilisation of credit more productive.

(ii) **Term Loans**

15.060 In December 1983, NABARD had advised SLDBs (Commercial banks, RRBs, SCBs were also advised later) to undertake case-by-case analysis of overdues under term loans with a view to providing relief to borrowers whose defaults were on account of defective loaning on the part of financing banks resulting in shorter loan maturity period, shorter grace period than admissible, failure to provide supplementary finance in the case of incomplete investments, failure to provide re-scheduling facilities in the case of natural calamities, etc. It was observed that SLDBs which were advised to recalculate their DCB position on the basis of the case-by-case analysis, had been able to reduce their demand substantially in some cases; for instance Bihar SLDB was able to reduce the demand for 1981-82 by 22.1 per cent, Madhya Pradesh SLDB by 22.6 per cent and Karnataka SLDB by 26.2 per cent. We endorse the action taken by NABARD. Our view is that where defaults are attributable to such failures on the part of credit institutions appropriate corrective measures should be taken to rehabilitate borrowers, on a case-by-case basis to obviate the possibility of denial of institutional credit to them when they are not at fault.

15.061 During the field studies conducted by our Consultants for Study I, the common observation made by the lending agencies was that the unit costs fixed by NABARD were generally on the low side and for long period they were not revised despite the escalation in the market prices of the assets. We find that NABARD has already set up, at the level of each of its regional offices, a state level unit cost committee which reviews atleast ,

at six monthly intervals, the unit cost of the assets refinanced by it in consultation with the concerned client banks, technical officers of the state governments, etc. The unit costs fixed in these forums were in the nature of average costs with scope/margin for variations with discretion to the regional offices of NABARD to enhance at their own level, on the recommendation of the unit cost committee, unit costs upto 20 per cent, enhancement beyond that being considered by Head Office of NABARD. All the same, we feel that this is a vital matter and NABARD should ensure that unit costs for all items of investment are periodically reviewed and appropriately fixed having regard to the market prices of the assets and the repaying capacity of the borrowers. This can be also ensured if the lending banks are given freedom to sanction loans in excess of 'unit costs' fixed, say upto 10 per cent to avoid any delay in getting the prior approval of NABARD. A degree of flexibility and delegation of authority is called for in favour of lending banks in this behalf and if as a result, the lending bank becomes eligible for higher refinance, NABARD should consider such cases for sanctioning higher refinance.

iii) Synchronisation of investment credit and working capital

15.062 We would like to stress that even at the time of appraisal of an investment to be financed, the source/s of working capital needed for the investment to yield the estimated level of incremental income should be ascertained by the lending agency and in cases where term loan borrowers require working capital, necessary arrangements should be made to ensure its availability. Where the borrower, has his own resources to take care of the working capital finance, and is not required to borrow for the purpose, he should make a record of this fact in the term loan application itself.

15.063 In the case of commercial banks we do not see any resource problem for the purpose. In the case of co-operatives, the remedy would be in the effective functional co-ordination between the two structures, with PACSs functioning as the single contact point for the ultimate borrowers. NABARD we understand, is providing refinance facility to cover production credit where such credit forms an integral part of a composite development programme as in the case of plantation, sericulture, etc. NABARD had offered to provide refinance facilities to LDBs for issue of production credit in areas where the short-term credit structure was dormant/weak and unable to provide

the necessary credit support. However, we understand that this scheme has not picked up. The scheme needs to be pursued.

Supervision over credit

15.064 On the whole we find that the strength of the supervision staff engaged by the credit agencies, except perhaps in some CCBs, was inadequate to ensure effective supervision over credit. This situation has to be corrected by strengthening the staff if quality of lending is to be improved. It is, however, not sufficient to lay down precise, uniform norms in regard to the charge per supervisor. The basic criterion should be the work-load, which depends on the number of borrowing members, the volume of loan operations and non-credit business, number of villages under jurisdiction, their distance from one another, transport facilities available to the supervisors, etc.

15.065 NABARD had introduced in March 1984, a pilot project for strengthening the credit delivery system (initially in 3 districts and subsequently extended to 12 more districts), envisaging intensive supervision by increasing the strength of supervision staff, training of field staff, structuring of supervision activities and providing vehicles to improve mobility of staff. The mid-term evaluation (December 1986) of the pilot project in the initial three districts by NABARD shows that the aggregate quantum of agricultural lending issued in all three districts increased by 26 per cent over the base year 1983-84. The number of borrowers under short-term loans had increased. The banking had brought about progressive diversification in lending. The deposits of all participating banks had increased substantially and the recovery of all banks in aggregate had registered an increase of 15 per cent points in two out of the three districts. In physical terms, the consumption of fertilisers and area under HYV had increased by 73 per cent and 18 per cent respectively and there was an increase in physical units of investments financed out of bank loans, which could annually account for additional production of foodgrains worth about Rs.7.8 crores. While the pilot project has shown significant success in improving the quality of loaning, it may not be possible to replicate the scheme to other areas due to cost constraints. However, if the quality of lending is to be improved, some strengthening of staff (with due emphasis on quality and training) in all the credit agencies will have to be made. This could be supplemented by other organisational innovations like formation of self-help groups to act as links between credit agencies and the borrowers.

Such self-help groups would also help in educating the farmers.

15.066 The efforts on the part of the credit agency for recovery by approaching the borrowers immediately after the harvest season is a crucial factor in improving the recoveries. In the case of commercial banks having a large number of accounts per field officer exceeding the stipulated norms compounded by the tendency among the field officers not to stay at the branch Head Quarters, etc. adversely affected their ability to approach the farmers, resulting in considerable slackening of the recovery efforts.

15.067 In the case of co-operatives, the field survey* revealed that of the defaulter households surveyed, only 37.5 per cent reported that some action was taken against them for recovery of dues. The nature of action taken included issue of legal notices in 32.5 per cent cases and filing of suits in 47.9 per cent cases. The PACSs were generally lax in initiating legal action for recovery. Experience has by and large belied the expectations that the democratic managements of societies and local non-official co-operators would show a sense of responsibility and necessary initiative in improving recoveries. In this connection, the Informal Group on Institutional Arrangements for Agricultural Credit (1964), had observed :

"The members of the Panchayats of the primaries and the boards of directors of the banks seem to be coming under the influence of thinking which considers energetic action for timely recovery as something undesirable being likely to be unpopular".

During the period of over two decades since these observations were made, the position in this regard, has deteriorated further. In our view, the primary responsibility for recovery of dues is that of the management at the base level co-operative credit institutions, which should be assisted in their efforts at the field level by the supervisory staff of the higher agency.

15.068 Wilful defaults are often the result of the vitiated recovery climate, by borrowers who are often oblivious of the repercussions of their own actions. By withholding repayments to the credit agency, the borrower stands to lose in many ways; in most cases money is frittered away in social/religious functions of a consumption nature and the borrower is left without any means

* Survey carried out by Consultants for Study No.II.

to repay. The borrower is subjected to penal interest and exposes himself to legal action. As a defaulter, he becomes ineligible for fresh finance. His interests, therefore, lie in getting rid of his loan liabilities promptly as soon as he is in funds because prompt repayment entitles him to a fresh loan, obviates penal interest and reduces normal interest. There is an urgent need for educating the borrower on the repayment ethics with a view to bringing home to him the fact that credit is a costly input, that he should keep his interest liability to the minimum to generate optimum income from his agricultural operations for maximising his profits. This commercial discipline has to be inculcated in the farmer if he is expected to transform agriculture into a commercial proposition. We appreciate that NABARD has launched, on a pilot basis, a Vikas Volunter Vahini (VVV) Programme with a view to educating the borrowers regarding the right use of bank credit for increasing production/productivity, generating additional income with the help of which he could repay his loan, in-time. We feel that in the present environment which breeds the culture of non-repayment, there is an imperative need for efforts, on a very massive scale, for educating the borrowers both from the commercial banks and co-operatives.

15.069 Apart from supervision over sanction, disbursements and end-use of credit, systematic efforts for recovery as a part of a time bound programme, should form an integral part of the supervision arrangements in all the credit agencies. The programme may, inter alia, comprise the following package:

- i) Specific targets for improving recovery over a reasonable span of time say five years or so. The programme, in the light of the agro-climatic conditions, should lay down annual targets for recovery and specify action programme for achieving them.
- ii) The action programme should inter alia envisage case-by-case analysis of all loan accounts in default once a year to ascertain the causes of default, provision of relief, as permitted under the loan policies and rules, where default is on account of reasons beyond the control of the borrowers, institution of legal action against wilful defaulters, etc.
- iii) Annual acknowledgement of debt by borrowers.

- iv) Review and strengthening of supervision arrangements, including field staff training and structuring of supervision activities for improving contact with borrowers, on the lines of Training and Visit agricultural extension system. Review of the supervision work of the field level staff by higher level executives of the banks.
- v) Prescribing a system for writing off bad debts, estimated as such by the auditors, after exhausting all possible avenues of recovery including legal action. There should be no write off of any debt of a borrower who has disposable assets.

(b) Pledge of Produce against Dues

15.070 The field studies by our Consultants have brought out, that those who are classified as "Wilful" defaulters do not in many of these cases default wantonly. There are instances where a borrower who is willing to repay the dues on or before the due date, and has the established capacity to repay, but could do so only if he were to sell his produce soon after harvest. However, prices tend to be lower at the harvest time than what he could get if he were able to hold on to his produce for a longer time. Therefore the compulsion on the borrower to sell his produce, if only to repay the loans on due date, results in pecuniary loss to him. We feel that a mutually satisfactory way should be found to accommodate the interests of both the borrower member and the PACS. Theoretically speaking, under the system in vogue a borrower can obtain a pledge loan for a period of 91 days, which would enable him to liquidate his crop loan liability. However, the facility is rarely available in the village itself and is, therefore, infructuous. We would, therefore, recommend a practical variant. If a borrower desiring to hold on to his produce in expectation of a higher price, deposits with the primary credit society, produce of a value sufficient to cover the loan outstanding and interest thereon, the society may extend the due date of repayment by three months, with extension in repayment of the corresponding dues also being granted by the concerned higher financing agencies. With the extension of due date the borrower will not be treated as a defaulter and would be eligible for a loan for the next crop if due. As and when the society is able to sell the produce in the market on the instructions of the borrower, it could adjust the sale proceeds against the crop loan account and interest thereon and pay the

balance, if any, to the borrower. The above arrangement pre-supposes the existence of a godown, full-time paid secretary, etc. in the concerned societies.

15.071 For facilitating this arrangement, and encouraging the PACSs to take up marketing of agricultural produce of their members, at least to the extent of loans due, we suggest that a pilot scheme may be started on a selective basis. The societies selected should have the necessary infrastructural facilities viz., a full-time paid secretary, godown facilities for storage of produce, etc. After assessing the experience of the pilot project, the scheme could be extended to other societies so that the borrowers may be facilitated and enabled to clear their crop loans without having to resort to distress sale of their produce. We hope that this will also, serve as a good beginning for the PACSs to take up marketing of agricultural produce on a regular basis after sufficient experience has been gained by them under this scheme.

(c) Linking of credit with marketing and processing

15.072 Co-operative marketing as such has witnessed considerable expansion in this decade. The value of the produce marketed by the co-operative marketing societies has increased from Rs.1,950 crores in 1980-81 to Rs.4,194 crores in 1985-86. An analysis of the marketing operations of the co-operatives, however, reflects serious disparities both in terms of areas and commodities. While sugarcane, cotton and foodgrains accounted for about 75 per cent of the total agricultural produce marketed by co-operatives, over 78 per cent of their marketing operations were confined to only five states viz. Maharashtra, Gujarat, Punjab, Uttar Pradesh and Karnataka. In the remaining states, the marketing societies undertake co-operative marketing of their members' produce on a very limited scale, their main pre-occupation being distribution of fertilisers and other inputs, procurement operations on behalf of FCI, CCI, JCI and other government agencies, etc.

15.073 Processing of the agricultural produce is also presently largely restricted to a few crops like sugarcane, oilseeds, paddy, etc. for which processing is a pre-requisite to marketing. There is, however, vast scope for processing of vegetables, fruits and other horticultural produce, a sizeable portion of which is wasted resulting in heavy losses to cultivators. Recognising the importance of the problem, Government of India has recently constituted

a new Ministry of Agro-processing for giving the much needed impetus to agro-processing activity. It is, therefore, expected that substantial government assistance will be forthcoming to this sector and number of agro-processing units will come up both in the co-operative and the private sectors. Since the growers of bulk of the perishable agricultural products comprise small producers, there is ample scope for promoting processing activities on a co-operative basis and forging a link between credit and processing. Even in cases where processing units come up in the private sector as large scale enterprises, recovery of credit through processing units could be ensured if credit agencies, agricultural producers and agro-processing units enter into tripartite agreement for the purpose. Thus, there is considerable scope for marketing of agricultural produce on a co-operative basis and for stepping up the agro-processing activities so that an effective linkage could be forged between credit and marketing/processing activities.

15.074 Undoubtedly, the integrated scheme of rural credit has not worked very satisfactorily so far. Recoveries through linking were moreover confined only to a few states; in 1981-82 Maharashtra (Rs.197.45 crores), Uttar Pradesh (Rs.29.72 crores) and Gujarat (Rs.17.42 crores) together shared 92.5 per cent of the total linked recoveries. However, the generally indifferent performance of the scheme is more due to lack of attention to it rather than its potential. In Maharashtra where an effective link between credit and marketing has been forged, the proportion of recoveries effected through marketing/processing societies is quite large as will be seen from the following table:

Table 22

Demand and Recoveries through Linking in Maharashtra

Particulars	(Rs. crores)		
	1983-84	1984-85	1985-86
1. Demand	436.76	471.31	546.91
2. Recoveries	231.23	265.07	323.64
3. of (2) through linking	89.72	120.48	182.21
4. Percentage of recovery through linking to total recovery	38.8	45.4	57.2

We strongly emphasise that serious attention should be paid to the scheme of linking of credit with marketing and processing so that its potential can be more fully tapped. Even though the bulk of the co-operative marketing turnover is accounted for by only a few states, all the same the data (NCDC Annual Report 1987-88) indicate that 64 per cent of the primary marketing societies in the country are undertaking marketing business of approximately Rs.45 to Rs.50 lakhs on an average annually. So, there does exist a widespread marketing base and if serious efforts are made to increase the marketing business on the one hand and develop closer linkage with credit on the other, significant results could follow.

(c) Linkages and Supporting Services

15.075 Schematic lending implies well orchestrated planning by various development agencies and tie-up of credit programmes with other development programmes as well as establishing suitable backward and forward linkages. The absence of such linkages and non-availability of supporting services has been a serious lacuna which has led to the impairment of effective use of the assets thereby impeding productivity. For example, in the case of minor irrigation schemes non-energisation of pumpsets due to delays in providing power lines/connections have virtually brought many programmes to a standstill. In many cases of sheep breeding, goat rearing, pig breeding and milch animal schemes, which have been financed by the banks, marketing linkage has been missing, leading to these schemes turning non-viable.

15.076 We would recommend, in this context, that the Director of Institutional Finance in each state should undertake the development of specific plans and projects in consonance with projected directions in which the agricultural sector in the state was expected to progress in the next 10-15 years. The main thrust of such plan of area development would be to secure optimum exploitation of potential for growth through, on the one hand, formulation of location-specific bankable projects in different areas of the state to be financed by the banking institutions, and a planned deployment of state resources to build up the needed back-up infrastructure and linkages, on the other. It should also be the Directorate's responsibility to ensure the provision of supporting (including extension) services for the schemes, get the projects sanctioned by the banks and to follow up and monitor their implementation. With a view to ensuring that expertise of a desirable order is brought to

bear on the preparation and implementation of both the perspective plan and the projects formulated thereunder, the Directorate would require to build up an effective planning machinery of a multi-disciplinary character comprising not merely departmental officials but also specialists drawn from other competent bodies such as Agricultural Universities, etc. The Director of Institutional Finance should be a sufficiently high level government official, say of the rank of Agricultural Production Commissioner, so as to be in a position to mobilise support and co-operation from all the concerned departments of the state government, banking institutions and other concerned organisations.

(d) Political will

15.077 The growing politicisation of the credit system has already been dealt with in paras 15.053-056. This, we are afraid, is bound to affect the very process of institutional lending to the rural people and may eventually have deleterious effect on agricultural production. To check any further spread of this malady, we would stress that there is an imperative need for a strong political will and a general consensus among various political parties to give up misuse of the agricultural credit system as a means for achieving political ends, restore the sanctity of credit institutions and allow them to function as autonomous banking institutions. Unless and until this is done and well in time, the prospects of the growth of agricultural lending institutions on sound lines seem quite dim and any amount of effort by the credit agencies to improve the quality of lending and improve recovery of loans may not be of much avail. We, therefore, strongly feel that the Government of India alongwith the state governments should chalk out a concrete long-term policy, supportive of the efforts of the credit system for recovery of their dues, avoiding all extraneous considerations and taking firm and objective view in respect of 'wilful' defaulters. The adverse effects of politicization on the banking system have been discussed at length elsewhere in the report.

(e) Improvement in the legal provisions

15.078 Normally, banks and other credit institutions secure their loans by way of i) primary security of assets created with the help of the loan, ii) collateral security such as land, other fixed assets, and iii) guarantors. In the case of default in repayment of dues, the loan amount is realised after

obtaining an award or a decree from the court against the borrower and guarantors. The security norms prescribed by Reserve Bank of India for agricultural loans are given below :

<u>Types of credit facility</u>	<u>Loan amount</u>	<u>Security to be furnished</u>
1. Crop loan	i) Upto Rs.1,000	DPN/Loan agreement only
	ii) Rs.1,001 to 5,000	Hypothecation of crops
	iii) Over Rs.5000	a) Hypothecation of crops and b) Mortgage of land or Third party guarantee
2. Investment Loan		
i) Where moveable assets are created	i) Upto the cost of economic unit (where applicable) or Rs.5,000* whichever is lower	Hypothecation of assets
	ii) Others (i.e. for amounts exceeding those under (i) above	(a) Hypothecation of assets and (b) Mortgage of land or Third party guarantee
ii) Where moveable assets are not created (e.g. dugwell, development of land, etc.)	Rs.1,000 and over	Mortgage of land.

* Rs.10,000 in respect of IRDP loans.

- Note :
- In case where mortgage of land or third party guarantee has not been indicated as security, banks should not take such security.
 - In case of power tiller, even where loan amount exceeds Rs.5,000 hypothecation of the power tiller should normally suffice.
 - In states where legislation on the lines suggested by the Talwar Committee has been passed, a simple declaration creating a charge on the land offered as security will be sufficient. In such cases, mortgage of land may not be necessary.

* 'Expert Group on State Enactments (1971)' under the Chairmanship of Shri R.K.Talwar, Chairman, SBI.

Security and Group Loans

15.079 Loans could, with advantage, be given on joint and several liability to groups of persons or associations of farmers for a common purpose, although this is not a general practice preferred now. Very few loans are, therefore, given on a group-basis. We would, however, commend this practice for wider adoption because, unlike individual loans, the group loans, are secured by the joint and several liability of those constituting the group or association. Group loans have also the advantage of being backed by an implied assurance by all those constituting the group to be collectively responsible not only legally but also morally to discharge the loan liability. But even in such cases, if defaults occur and they persist, the same steps as are being taken in the case of individual loans would have to be followed. Thus, if persuasive efforts fail to bring about the desired results, the banks will need to resort to coercive legal measures as applicable to individual borrowers.

Commercial Banks/RRBs

15.080 When the Commercial banks commenced agricultural lending , they were faced with several legal impediments in obtaining immovable property as security for loans by way of registered mortgage and recovery of the loans through enforcement of the security by recourse to civil courts which was a time consuming, long drawn and costly process. For removing these difficulties Talwar Committee (1971), recommended adoption of a Model Bill envisaging certain facilities for creation of charge and recovery of agricultural dues. Though RBI recommended adoption of this Model Bill by all the state governments, seven states, viz, Andhra Pradesh, Tamil Nadu, Kerala, Nagaland, Sikkim, Jammu and Kashmir and Goa are yet to adopt the Model Bill. Even in states which have passed the enactment, necessary rules/notifications are yet to be issued for making the relative Acts operative. Moreover, the Model Bill itself suffers from certain short-comings as indicated below:

- i) The facilities for creation of 'charge' and recovery of dues are available only for agricultural loaning and not extended to non-agricultural lending, particularly under the poverty alleviation programmes. Certain state governments have extended the public Debt Recovery Acts to banks lending only under the state sponsored programmes.

ii) The rights and priorities under the charge on the immovable property taken as security for loan by a bank cannot be the same as under mortgage, e.g. a mortgage deed actually executed subsequent to the creation of charge by declaration as provided in the bill, has been interpreted as having priority over the charge.

iii) As per model bill the prescribed authority can proceed only against those properties as may be under charge and not any other property or assets. On this ground, authorities in some states have refused to entertain recovery applications.

iv) The simplified recovery procedure is not available for proceeding against the assets of guarantors; for this, banks have to resort to the normal process of law through civil courts.

v) The issue whether the legislation on the pattern of the model bill could be made applicable retrospectively, i.e. to cover advances disbursed prior to the adoption of the bill by the state government, is also not free from doubt. Apart from the short-comings in the model bill itself, the states which have adopted the bill have made several modifications which have the effect of diluting the effectiveness of the bill.

15.081 The bulk of the banks' advances to agriculture and other allied activities are for small amounts of less than Rs.10,000 where in terms of the liberalised security norms prescribed by RBI for the priority sector advances, banks are not expected to take immovable property as security except in cases of land based activities where no asset is created out of the loan. In non-farm activities, no immovable property is taken as security for loans upto Rs.25,000. In states where Model Bill has been adopted, the facility of creating a charge through declaration is being availed of by banks. However, obtaining of collateral securities/guarantors is prohibited in the case of loans to weaker sections. In the case of defaults in repayment of loans by weaker sections where neither collateral security nor guarantee is available and in a large number of instances, where assets are being sold away by the borrowers, it is often difficult for banks to realise any dues from the borrower and the loss is more or less total. Even where the asset is not completely lost, it depreciates in value very fast, e.g. cows, buffaloes or

bullocks, supplied to the beneficiaries of IRDP have hardly any resale value.

15.082 In the case of agricultural advances, the need for recourse to enforcement of security for recovery arises only in cases where the borrower is a wilful defaulter, or advances are not eligible for rescheduling. Generally, where the operations/activities have permanently and irretrievably stopped for any reason or documents are getting time-barred and the borrower is not prepared to renew them, recovery proceedings have to be taken either through the simplified procedures where available or through due process of law in the civil court. In the case of failure of advances in respect of non-weaker section loanees, Commercial Banks can, in theory, resort to (a) sale of assets created with the help of the loan, such as pumpsets, tractors, etc., (b) sale of land and (c) proceeding against the guarantors, for recovery of dues. However, wherever immovable property in rural areas is to be disposed of, the difficulty arises in finding a suitable buyer, as outsiders are prevented from purchasing by co-ordinated action by the local people. Hence, landed security does not enhance the realisability of the advances. As suggested by the Study Team on Overdues and also by CRAFTICARD, the state governments should arrange to purchase mortgaged lands brought to sale in recovery proceedings launched against defaulters. The field studies taken up by our consultants have revealed that adequate assistance is not available to the banks from the state governments in taking action for recovery. The services of recovery officers are not made available to the required extent. Legal delays and inability of the state governments quickly to take effective action for enforcing Recovery Certificates has been encouraging wilful defaulters. On an aggregate basis, the public sector banks are reported to have filed till December 1986, a total of 10.7 lakh suits involving an amount of about Rs.2,300 crores. This excludes their dues involved in recovery of loans being attempted in the normal course as also the loans written off as bad debts. It was reported that State Bank of India, local Head Office, Patna alone has nearly 30,000 recovery cases pending in Bihar due to lack of adequate number of designated officers for recovery. The Government machinery deployed for the this work is stated to be too busy with governmental work to assist in the recovery of bank loans. Likewise, in Rajasthan out of 36,000 recovery certificates filed as in June 1986, 32,300 were pending. In Haryana, as in March 1987, out of 28,900 cases filed, 22,800 were pending.

15.083 The existing legal process is costly for the banks. Apart from considerable time taken at every stage of legal process through adjournments in a number of cases, the final decisions turn out unfavourable to banks partly or completely. Thus, there are instances where interest rates have been considerably reduced. Even cases of decreed amounts being much less than the suit filed amounts are not found wanting. The working of the existing legal machinery increases the cost of recovering bank dues. By and large, the present legal system appears to be fitted in favour of the borrowers. The impact of reduction of interest directed by courts has to be viewed in relation to the rising cost of banking operations, vis-a-vis the low interest charged on lendings to weaker sections under various schemes. It is difficult to make an assessment of the extent of income loss on this account and its effect on profitability. In view of the foregoing, the Tiwari Committee, set up by Government of India, had recommended the need for special legislation. We suggest that the comprehensive legislation, which is underway, may be expedited. In the interim period it is suggested that commercial banks may be vested with special powers, similar to those conferred on State Financial Corporations by their statute, pertaining to rights of the institution, in case of default, to recall the loans before the agreed period, special provisions for enforcement by the State Financial Corporations and procedure to be followed by courts. Similar provisions could be incorporated in the Banking Companies (Acquisition and Transfer of Undertakings) Act.

Co-operatives

15.084 Under the provisions of the Co-operative Societies Acts, a Primary Agricultural Credit Society has a first charge on the crops/other agricultural produce, cattle, fodder for cattle, agricultural or industrial implements or machinery, etc. of a member raised or purchased with the aid of loan from the co-operative society. For instance, Section 38 of the Rajasthan Co-operative Societies Act, 1965, provides that subject to any prior claim of the government in respect of land revenue or any money recoverable as land revenue,

- i) any debt or outstanding demand owing to a co-operative society by any member shall be the first charge upon the crops and other agricultural/industrial implements or machinery, raw material for manufacture, any finished products manufactured from such raw materials belonging to such member;

- ii) no member shall transfer any property which is subject to a charge except with previous permission in writing of the co-operative society which holds the charge; and
- iii) any transfer of property made in contravention of the above provision shall be void.

Similar provisions exist in some other state enactments as for example, Section 35 of the Andhra Pradesh Co-operative Societies Act 1964 and Section 47 of the Maharashtra Co-operative Societies Act 1960. Law prohibits a member who creates the charge from alienating the property subject to charge and any alienation made in contravention, is considered as null and void. Sub-section 3 of Section 40 of the Tamil Nadu Co-operative Societies Act makes it obligatory on the the part of the member to deposit or entrust with society such property as is subject to charge, if the society so desires, till the debt or demand of society is fully satisfied. Since this provision confers a special kind of privilege on the society, the other states may also incorporate it in their Acts, if it does not exist.

15.085 In the case of long-term loans it has become obligatory for LDBs under the existing provisions of the Co-operative Societies Acts to obtain mortgage of land as security for their loans as issue of debentures by LDBs is at present linked to mortgages obtained by them. The bye-laws of LDBs, therefore, invariably provide for obtaining mortgage of land and other immovable properties of the borrower or government guarantee, as a security for issue of loans. While security of land may be relevant in this context, the procedures for taking mortgage of land are complicated and time-consuming. In order to simplify them the Hazari Committee had recommended a new form of security i.e. a special charge known as "gehan" which could be effected by a mere declaration by the borrower, and at the same time would have all the characteristics of a mortgage without its cumbersome formalities. While it was thought that this method of creating only a 'charge' instead of 'mortgage' would facilitate loaning, not only legal opinion on the effectiveness of the charge, differed, but it was found that the procedure for creating a charge was as cumbersome and as time consuming as a mortgage because a charge cannot be created without establishing the ownership rights.

15.086 Since this recommendation has not been found to be practicable, the alternative method recommended by CRAFTICARD and certain other

committees is the introduction of a revenue pass book system duly recognised by Law. The pass book may contain details relating to the title of a person to the immovable property held by him and all other relevant particulars such as location, survey numbers, boundaries, extent of land or other immovable properties, assessment, etc. Under this system, it is expected that the banks should be able to advance loan to any farmer only with the help of the revenue pass book held by him, create a charge on the land mentioned therein without reference to any other documents and thus disburse the loan in the shortest possible time. Any charge created in favour of the financing bank in the above manner will have priority over other charge and mortgage. It would be obligatory on the part of all banking institutions to make endorsement in the pass book for all loan transactions. A farmer will have to produce the pass book to the revenue officer from time to time for updating it from the revenue records. The introduction of a revenue pass book with statutory recognition will eliminate the need for execution of various documents by the borrower and will enable the banks to sanction loans with least delay. It will also save the borrower, the expenditure related to stamp duty, registration charges, etc.

15.087 In the case of default in repayment of loans, the Co-operative Societies Acts provide for simplified procedure of obtaining award through officers of Co-operative Departments to whom powers of Registrar of Co-operative Societies are delegated and executing the same as per procedures laid down in the Acts and Rules in various states. Though the legal provisions are generally exhaustive the incidence of overdues in co-operatives is progressively increasing in many states. With a view to improving the effectiveness of the legal process of recovery following suggestions are made :

i) **Provision for grant of recovery certificate by Registrar**

15.088 The arbitration procedure for obtaining award is time-consuming and results in delays in recovery of co-operative dues. Some Co-operative Societies Acts, for example Section 101 of the Maharashtra Co-operative Societies Act, Section 64A of Jammu & Kashmir Co-operative Societies Act, Section 104 of the Haryana Co-operative Societies Act provide for issue of recovery certificate by the Registrar of Co-operative Societies on demand from the society or on his own motion. This certificate is regarded as a decree passed by the competent court and is executed as such by any

of the modes provided for under the Act. This procedure circumvents filing of disputes by the society, appointment of arbitrator and all the process that follows thereafter and reduces both time and expenses.

ii) Sale of property without intervention of the Court

15.089 In case where 'gehan', mortgage or hypothecation has been created or executed in movable or immovable property in favour of a co-operative society/bank and there is a default in repayment of dues, the Section 19 of the Kerala State Co-operative Societies Act empowers the Committee of the Society/Board of such bank to bring to sell the property to which hypothecation/mortgage relates without the intervention of the court.

iii) Delegation of Registrar's powers to officers of the banks

15.090 Under Section 137 (4) of the Maharashtra Co-operative Societies Act, the Registrar or a person authorised by him can direct conditional attachment of the property until the arrears due to the Land Development Bank are paid. Further, under Section 156 (i) of the Maharashtra Co-operative Societies Act, Registrar of Co-operative Societies can empower an officer of a co-operative bank to recover the amounts under decree by attachment and sale of property.

iv) Purchase by State Governments of Lands put to Auction

15.091 Even where decree is obtained by a society/bank and land is put to auction, banks experience considerable difficulties due to lack of bidders at the auction. In such cases, banks are left with no alternative but to acquire the land themselves and hold it as a 'non-banking' asset. The banks find it difficult either to sell the land or even take over its possession and ensure any return therefrom. For mitigating these difficulties, the Study Team on Overdues of Co-operative Credit Institutions had recommended that the state governments should themselves purchase the land put to auction because with the authority at their command they will be able not only to take possession of lands but also to dispose them off by sale or on long term lease.

v) Declaring Officers of Co-operative Banks as Public Servants

15.092 Provision may be incorporated in the Co-operative Societies Acts

to declare officers of co-operative banks as 'Public Servants' so that they would get legal protection and would be more effective in recovery work.

15.093 Provisions on the above lines would improve the credit agencies recourse to security taken for loans. We, therefore, suggest that similar provisions may be made in the Co-operative Societies Acts/other relevant Acts in other states, which do not contain such provisions, for facilitating effective recovery of dues through coercive measures.

Enforcement of Legal Provisions

15.094 The existing legal framework for recovery in many states is quite exhaustive. Although enormous powers have been vested in the Registrar of Co-operative Societies and in some cases in the central co-operative banks, the existence of large number of defaulters and large proportion of chronic defaults only show that the special remedies available under the Acts have not been made effective use of. There seems to be considerable laxity on the part of the managements of co-operatives in initiating prompt action for recovery through coercive measures, whenever required. In cases where recoveries are not forthcoming within a year of default, persuasive methods of recovery could be deemed to have failed and managements of co-operatives should initiate coercive action for recovery in all cases where overdues exceed one year. Similarly, the recovery of chronic overdues i.e. over three years could normally be expected only through execution of awards.

15.095 It was also observed that even in cases where co-operatives had initiated legal action for recovery, there have been considerable delays in the disposal of arbitration cases and execution of the awards obtained. Published data, (NABARD 1986) in respect of co-operative societies show that at the end of June 1982 as many as 5.06 lakhs arbitration cases involving an amount of Rs.95.85 crores and 12.60 lakhs decrees under execution involving Rs.202.2 crores were pending. The disposal of arbitration cases and the execution of decrees is delayed due to paucity of government staff and their pre-occupation with other duties entrusted to them. In view of the abnormally high level of overdues, and the large number of defaulters involved, it seems inevitable that coercive action for recovery against a much larger number of defaulters would be necessary. The magnitude of the work involved and

the need for large scale expansion of credit which pre-supposes better recoveries, call for the state governments to play a much larger role in recoveries. For expediting the legal process of recovery, we recommend that state governments should not only increase adequately the strength of the staff entrusted with these duties but build up for the purpose an exclusive machinery which would be able to pay undivided attention to this task.

15.096 The above suggestions are intended to improve the legal framework for enabling the credit agencies or higher tier agencies to proceed against the security obtained for the loans. Simultaneously, certain legal and administrative measures will have to be initiated which could prove effective deterrent to "wilful" defaults in repayment of agricultural dues. These are discussed below :

i) The overdues Study Team had recommended that a defaulter member as also the surety of a defaulter should not only be disqualified from being elected or appointed or being continued on the Managing Committee of a society but should also be denied fresh finance and voting rights in an election or in the general body meeting. We recommend that suitable provisions to this effect may be incorporated in the Co-operative Societies Acts of states which have yet to frame legislations to give effect to the above recommendation. We further recommend that a PACS/PLDB which is in default to the higher financing agency (i.e.DCCB, SCB or SLDB) and where the default exceeds 50 per cent of demand at the end of the preceeding co-operative year, may be denied voting rights in the general body meeting or election of the bank to which it is affiliated.

ii) While identifying causes of overdues, it was observed that on account of lower rates of interest governing agricultural loans, there was tendency to divert these loans for other business. As an effective deterrent to such misutilisation, the bye-laws of the PACS/PLDBs should contain a provision for imposition of penal interest in such cases, at least at three per cent p.a. above the normal rate.

iii) Section 145 of the Tamil Nadu Co-operative Societies Act empowers the financing bank to publish names of members from whom any debt or outstanding demand is due to a society if the financing bank considers it

necessary in the public interest or for recovering the debt. We recommend that provisions on these lines may be made in other State Acts with a view to improving the recovery climate in the states.

15.097 The need for a simplified procedure for legal action for recovery of agricultural dues is now well recognised. For historical reasons (i.e. because co-operatives alone constituted the credit agency for agriculture till the mid-sixties) requisite provisions for simplified procedures have been incorporated in the Co-operative Societies Acts of the various states enabling the credit co-operatives to obtain awards and execute the decrees obtained from officers of the co-operative departments whom the powers vested in the Registrars of Co-operative Societies in this behalf are delegated. Later on in early 1970's, when commercial banks were inducted into agricultural credit, the need for simplified legal procedures was sought to be met, under the Model Bill recommended by the Talwar Committee, by vesting powers of arbitration, etc. in the designated officers of the Revenue Departments of the state governments. This has given rise, at the state government level, to two separate administrative arrangements for simplified recovery of agricultural credit, one in the co-operative department for credit co-operatives and another in the revenue department (in states where legislation on the lines of Model Bill has been enacted and rules framed etc.) for commercial banks and RRBs; and in both cases, in many states, the administrative arrangements are grossly inadequate, as there are staff constraints and the authorised staff have to attend to recovery cases in addition to their own duties, giving rise to accumulation of cases, delays in obtaining awards, delays in executing the decrees, etc. Since both co-operatives and commercial banks would continue to constitute permanent components of the agricultural credit system in the country, the long-term perspective calls for a co-ordinated approach in the matter of recovery process. The ultimate solution to the problem will lie in having a single common legal framework covering both co-operatives and commercial banks, constitution of special tribunals at the state level and a single special department in each state exclusively entrusted with the task relating to execution of awards obtained through such special tribunals. We stress the need for such a machinery in the context firstly, of the inability of the existing revenue and co-operative departments in most states to cope with the work of recovery of agricultural credit through legal action and

secondly, the large scale expansion of agricultural credit that has been projected for the next 10 - 12 years i.e. till the end of the century which is conceivable only if perceptible improvement in the recovery of agricultural credit can be achieved and requisite support from the government machinery for the purpose is made available.

15.098 Whatever may be the improvements in the legal framework and the measures taken to strengthen the administrative machinery to effect recoveries speedily and in full, the desired objective will not be achieved unless the Government of India and the state governments create the necessary climate for recovery and urge on the farmers to repay their dues and bring pressure on the credit institutions to collect them. The Reserve Bank of India and NABARD have a vital role to play in impressing on the banks the importance of loan recoveries at meetings and conferences which should be specially held to review the progress of recoveries periodically.

Estimate of Provisions for Bad and Doubtful Debts

Age-wise pattern of Overdues

15.099 It has generally been observed that the higher the age of overdues, the lower are the chances of their recovery and hence greater possibilities of such overdues turning bad. It is, therefore, important to take a look at the age-wise pattern of overdues in order to get some idea about the provisions to be made for bad and doubtful debts arising from agricultural lendings. Data obtained from a field survey* given in table 23 and 24 throw light on the age-wise distribution of overdues for the different types of lending agencies.

15.100 Assuming that the age-wise pattern of overdues obtained from the field survey data is representative of the pattern of overdues at the aggregate level, the age-wise quantum of overdues arising from agricultural loaning by various credit agencies could be estimated as given in table 24.

15.101 The agency-wise and age-wise position of overdues is given in table 25.

* Report of Consultant for Study II

Table 23

Age-wise and Institution-wise Pattern of Overdues

In percentages

Age group	Commercial Banks			RRBs			PACs			LDBs	
	Agri. sector	Non Agri. sector	Over-all	Agri. sector	Non Agri. sector	Over-all	Agri. sector	Non Agri. sector	Over-all	Agri. sector	Non Agri.
Less than 1 yr.	11.5	35.2	16.6	13.1	5.8	10.8	16.7	14.3	16.4	16.2	-
1 - 2	18.3	10.9	16.7	30.1	6.8	22.8	26.5	68.1	30.9	14.3	-
2 - 3	16.7	16.5	16.7	28.3	25.5	27.5	5.8	5.9	5.8	10.3	-
3 - 4	22.9	8.4	19.7	7.3	5.8	6.8	18.1	2.6	16.5	9.3	-
4 - 5	7.9	6.4	7.5	3.7	6.8	4.6	8.3	-	7.4	12.7	-
5 - 6	3.5	5.9	4.0	3.6	28.5	14.5	9.5	3.2	8.8	12.1	-
6 - 7	4.1	6.7	4.7	8.2	7.8	8.0	3.0	-	2.7	8.0	-
Above 7	15.1	10.1	14.1	5.7	3.0	5.0	12.1	5.9	11.5	17.1	-

Table 24

Age-wise Distribution of Amount of Overdues for Different Lending Institutions

(Rs. crores)

Age Group	Commercial Banks			RRBs			PACs			LDBs
	Agri.	Non Agri.	Total	Agri.	Non Agri.	Total	Agri.	Non Agri.	Total	
Less than 1 year	200	NA	200	37	4	41	271	29	300	48
1 - 2	319	NA	319	86	10	96	427	130	557	43
2 - 3	291	NA	291	81	48	129	94	11	105	31
3 - 4	399	NA	399	21	8	29	292	5	297	27
4 - 5	138	NA	138	11	8	19	133	-	133	38
5 - 6	61	NA	61	10	33	43	153	6	159	36
6 - 7	73	NA	73	23	8	31	49	-	49	24
Above 7 yrs.	263	NA	263	16	9	25	196	11	207	51
Total	1,744	NA	1,744	285	128	413	1,615	192	1,807	298

Table 25
Overdues of different Credit Institutions
at the end of June 1986

	(Rs. crores)				
	Commercial bank branches	RRBs	PACs	LDBs	Total
Upto 3 years	810	204	792	122	1,929
3 to 5 years	537	32	426	65	1,060
Above 5 years	397	49	397	111	954
	<u>1,744</u>	<u>285</u>	<u>1,615</u>	<u>298</u>	<u>3,942</u>
	=====	=====	=====	=====	=====

It is the accepted policy to make larger provision for bad and doubtful debts in respect of old outstanding advances. In our view it would be reasonable to make bad debts provisions at one percent of overdues upto three years, 15 per cent for overdues between three and five years and 70 per cent for those exceeding five years. On this basis, the provisions which would have to be made for bad debts arising out of agricultural loaning and their correlation with the total loaning in respect of each credit agency, have been worked out in table 26.

Table 26
Estimates of Bad Debts and their relationship to Loan Outstandings

	(Rs. crores)		
Agency	Total agricultural loans outstanding as on 30.6.1986	Estimate of Bad debts	Percentage of (3) to (2)
(1)	(2)	(3)	(4)
Commercial Banks	8,416	367	4.3
RRBs	1,004	41	4.1
PACs	4,323	350	8.1
LDBs	2,666	88	3.3
	<u>16,409</u>	<u>846</u>	<u>5.1</u>
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As the table shows the percentage of estimated bad debts to loan outstandings seems the highest in PACs as compared to LDBs, commercial Banks and

RRBs. This is because the entire loan portfolio of LDBs, and to a large extent, that of commercial banks and RRBs comprises term loans, substantial portion of which represents only current loans, which have not fallen due for repayment. Similarly, unlike co-operatives, the commercial banks and RRBs enjoy, in respect of their agricultural loans, the credit guarantee cover of the DICGC and are able to write off periodically, part of their bad debts after invoking the guarantee cover. In the case of co-operatives, as write off of bad debts is subject to elaborate procedural formalities including prior approval of the RCS, it is seldom resorted to and, therefore, the irrecoverable dues accumulate and continue to appear on their balance sheets year after year. These factors appear to account for the apparently large incidence of estimated bad debts in PACSs as compared to that in other agricultural lending institutions.

Bad debts - Write off

15.102 An analysis of the overdues shows that both in regard to co-operatives and commercial banks, the overdues exceeding five years constitute a significant proportion of the total overdues. One of the reasons for accumulation of chronic overdues is the lack of a realistic policy to assess the bad and doubtful debts and undertake write off of the dues which after exhausting all efforts for recovery, including legal measures, are proved to be ultimately irrecoverable. In the co-operative sector, primary agricultural credit societies are not in a position to create adequate bad debts reserves to cover the estimated bad debts as nearly 40 per cent of them incur losses and profits in the case of remaining societies are too small to create bad debts reserves after providing for other commitments as per provisions in the Co-operative Societies Acts/Rules, with the result that the bad debts reserves in most cases fall woefully short of the estimated bad and doubtful debts. There is also a general apprehension that write off even on a small scale may give wrong signals to the borrowers and spoil the recovery climate. There is generally no practice of actually writing off, periodically, the bad debts assessed as such by the auditors. The procedures for write off are also unduly complex requiring the Registrar's prior permission, etc. The cumulative effect of all these factors is that the bad debts go on accumulating year after year and continue to be shown as part of overdues. More or less the same position exists in central co-operative banks as well, as may be seen from table 27.

Table 27

Position of Bad Debt Reserves vis-a-vis Estimated Bad Debts in DCCBs

DCCB	Bad Debts *	(Rs. lakhs)		
		Bad Debt Reserves		
		30.6.84	30.6.85	30.6.86
Palamau	24	6	6	7
West Champaran	79	19	19	19
Sonepat	89	12	12	13
Hoshangabad	19	1	1	1
Indore	32	8	10	12
Aurangabad	124	102	114	130
Kolhapur	234	224	224	226
Pudukottai	45	36	39	45
Tirunelveli	132	61	64	67
Nalgonda	53	26	28	31

* Estimates of National Bank for Agriculture and Rural Development

15.103 The land development banks do not generally consider any of their loans as bad and doubtful of recovery because all loans are secured against mortgage of land. However, all such secured loans are not necessarily realisable; there are also legal and other basic constraints to sale/transfer of ownership of land. Experience shows that land development banks may not be able to avoid write off of some portion of their loans; such as infructuous investments, as there is no arrangement for compensation or insurance or credit guarantee cover for taking care of these loans. As a sequel to the case-by-case study of overdues suggested by National Bank for Agriculture and Rural Development, the National Co-operative Agricultural and Rural Development Banks' Federation had set up a small group for evolving procedures for estimating bad and doubtful debts which has suggested that the land development banks may adopt either of the following two procedures for strengthening their reserves for bad and doubtful debts :

- 1) Provide 25 per cent of the overdues in the age group 5-10 years plus 100 per cent of overdues exceeding 10 years ; or

- 2) Provide 10 per cent of the total overdues of the bank irrespective of their age.

Of the two alternatives, our preference is for the first.

15.104 While stressing the need for a definite policy to assess the bad debts and to undertake, periodically, writes off of the debts which after exhausting all measures for recovery including legal action, have proved to be ultimately irrecoverable, we recommend that NABARD may issue specific guidelines to co-operative credit institutions regarding write off of such bad debts.

15.105 The result of the present practice which entails that provision for bad debts cannot be made if there are no profits to create them from, is that PACSs and PLDBs most of which are only marginally profitable, set aside each year only very marginal amounts, if at all, as a cover for bad debts although many have high level of overdues. This approach ignores two fundamental factors - firstly, that debts become irrecoverable whether the bank is making profit or not and secondly, that the balance sheet must show current assets at the net realisable value.

15.106 We, therefore, recommend that the credit agency, irrespective of whether it earns profit or not, should make every year, adequate provisions to fully cover the anticipated bad debts. These provisions should be made a charge against the profit and loss account. We are deliberately suggesting a departure from the existing accounting practice because in the first place, in our view, the profit which ignores the fact of bad debts and the need for an appropriate provision therefor, is merely an illusory profit. The result of the revised procedure would inevitably be that many institutions which are showing profit to-day would start showing losses. It is best that real position comes out in the balance sheet. Secondly, it is always possible for the credit agency to wipe out the resultant losses from its future profits and really strengthen its financial position. The provisions so created should be deducted from the assets in the balance sheet to show the estimated net realisable value of the assets. It follows that at the end of an accounting year, the provision made by any credit agency should equal the estimation of bad and doubtful debts, as made by the auditor or such higher estimate as the credit agency itself may make.

The Problems of Overdues - An Overall Assessment

15.107 As stated in para 15.005 of this chapter, the overdues at the end of 1985-86 amounted to Rs.4,262 crores in aggregate in the three streams of the credit system. They formed around 40 per cent of the demand for the year 1985-86. By all standards this is a very high level which none of the systems can afford to sustain for a long time. Unless the overdues are substantially reduced, the recycling of funds will get seriously affected which in turn will reduce the quantum of resources available for lending purposes. Recycling of resources is as important as mobilisation of additional resources, if not more.

15.108 The analysis attempted in the Chapter so far deals with the issues which cause overdues and their impact both on the institutions which lend and the borrowers who are their beneficiaries. Overdues, as pointed out repeatedly, are all-pervasive and neutral to the type of institution supplying credit. Further, the problem of overdues cannot be studied in isolation for it is the result also of the larger environment in which both the credit agencies and the borrowers function including the non-viable nature of farming itself in case of a significant number of farmers, which cannot be made viable by credit alone but by a whole set of planning and development measures to be undertaken by the government. Hence, not only the measures recommended in this chapter but several other measures suggested elsewhere in the report will also contribute substantially to bring about improvement in the recovery of agricultural credit. This section brings out briefly such measures which impinge on recoveries per se and spells out a perspective plan as an overall objective for the credit agencies for improving their recoveries.

15.109 The causalities of overdues are many-both external to the agencies deploying credit and those which are internal to the operations of the credit delivery system. The external factors i.e. those beyond the scope of activities and operational control of the credit agencies relate to the environment in which the credit agencies function and extend to the whole structure of agricultural production, if not the entire rural economy. The susceptibility of the large parts of the country, to repeated drought in the unirrigated areas where agriculture is mainly dependent on rainfall, and of large areas

to floods resulting in extensive crop damages impair the repaying capacity of the borrowers and disrupt the credit delivery system at all levels. This problem has been separately discussed in detail in Chapter XVI. Our analysis leads us to the conclusion that to the problem of flood/drought prone areas, the existing stabilisation arrangements envisaging postponement of loan recovery through rescheduling of dues is not the right solution. We consider that a better solution to the problem may lie in a suitably evolved comprehensive crop insurance scheme which would indemnify the cultivators against crop losses in the year of natural calamity itself and would obviate the need to carry over liabilities to the subsequent years.

15.110 Another important external factor to which defaults in the repayment of agricultural loans are attributed, is the inadequate income generation from the production efforts with the help of bank credit. This is a problem which as the earlier analysis shows, extends on the one hand to the structure of agricultural production system itself and on the other, to the category of clientele the credit agencies are required to serve. The preponderance of small and scattered holdings prevalent in our agriculture does not lend itself to realising the fuller potential of improved technology even when irrigation facilities are available and intensive cropping with the use of improved inputs is undertaken. Development of agriculture through adoption of improved technology is uneven as between different states as also in different areas within the same state. In states like Punjab and Haryana, which have an average size of land holdings almost twice that of the national average and also the percentage of irrigated area, with the added benefit of a long standing consolidation of holdings programme, the improved technology adopted by the farmers has led to significant increase in productivity and production; or in Kerala where the farmer has adopted multiple cropping and shifted to plantation crops, not only agriculture but the entire rural economy has shown signs of prosperity. This prosperity of agriculture/rural economy is reflected in increased income generation to the borrowers and, therefore, the repayment performance of borrowers in these parts of the country has been substantially better than in Eastern/North-Eastern regions, at the other extreme, which are yet to be brought into the main-stream of agricultural development. Development of agriculture in backward areas/regions is thus an important pre-requisite to the improvement in recoveries and here we stress the role of the state in creating an effective infrastructure

of research and extension, with particular emphasis on development of suitable technology for rainfed crops in these areas. What is required is the up-gradation of rural economy in general and agriculture in particular for generation of higher income for the borrowers. As regards the clientele of rural credit agencies itself, many of whom are below the poverty line, we have dealt with their problems separately in the Chapter XXI on "Poverty Alleviation Programmes" and have made appropriate recommendations for improving the content and implementation of IRDP and other programmes to bolster income generation and to elevate the borrowers progressively above the poverty line.

15.111 Another major factor which seriously affects the production efforts and optimising benefits is the lack of adequate backward/forward linkages, infrastructure and supporting services for agriculture. While the lack of adequate input supplies and extension services for transfer of technology from laboratory to the farm level affects the production effort itself, the inadequacy of arrangement for marketing of agricultural output or agro-processing where necessary as a pre-requisite for marketing, or of transport of produce to the terminal markets affects seriously the income of the farmers and their repaying capacity. The importance of infrastructure and supporting services as a pre-condition for effective recycling of credit can hardly be over-emphasised. With a view to giving an impetus to the infrastructure build up, we have recommended the establishment, in each state, of a multi-disciplinary organisation with a major role and responsibility of attending to fairly long term planning for agricultural development, formulation of area specific schemes, development of backward and forward linkages and building up of necessary infrastructure facilities needed by the agricultural sector.

15.112 Perhaps the most important factor directly impinging on the recovery efforts is the overall climate of recovery. A borrower may derive full benefits from his agricultural pursuits and at the same time may, with impunity, default in repayment because of external instigations. This constitutes, as brought out earlier in this Chapter, one single major factor contributing to the large incidence of overdues under agricultural loans. We find that the increasing politicisation of lending institutions and credit programmes ostensibly for sub-serving political objectives, has been progressively under-

mining the credit disciplines in recent times. Considering the deleterious effects such trends have on the functioning of agricultural credit system, we have, as a measure for mitigating the adverse effects, suggested the need for creating the necessary political will and observance of a code of ethics so as to induce non-interference in the functioning of credit agencies. This, we consider, as essential if credit agencies are to continue lending full credit support to the agricultural sector, in consonance with its fast expanding and diversifying needs.

15.113 The number of borrowers with adequate repaying capacity withholding repayment of their dues is on the increase. The delays in legal action and more importantly the political support they enjoy in the area are a contributory factor to this phenomenon. It needs to be ensured that such wilful defaults are not only not condoned but are dealt with severely. This is important because any laxity in dealing with the wilful defaulters would in turn generate a climate of resistance to repayment by others, thereby vitiating all efforts made by the lending institutions towards effective recoveries. We have examined, in this context, the existing legal framework and have suggested various improvements therein for facilitating the recovery of overdues through legal measures. We should, however, emphasise that the measures we have recommended, would hardly produce the desired results if they are not backed by strong political will. Central and state governments should realise this and take appropriate measures to create necessary climate for recovery.

15.114 As far as factors internal to the credit system are concerned, they relate to the structural weaknesses of the credit agencies, deficiencies in the loan policies and procedures, in-effective supervision and improper monitoring of the end-use of credit, etc. Our review of the two streams of co-operative credit system in the separate chapters has shown that the primary co-operative credit institutions, both in the short-term and the long-term structures, are by and large weak, non-viable and ineffective. The urgent need, therefore, is to take effective steps to revitalise and strengthen these institutions within a time - bound programme. To this end, we have recommended several measures such as appointment of full time paid secretaries and other staff, staff training and certain incentives to secretaries of PACSs to function effectively. For improving and simplifying the loan

policies and procedures, the introduction of the cash credit system for financing seasonal agricultural operations in areas having perennial irrigation and multiple cropping is more suitable and has been recommended. Rationalisation of unit costs and scales of finance with reference to the cost of the assets/cost of cultivation and the repaying capacity of the borrowers, fixation of realistic repayment schedules for term loaning, postponement of rabi due date by two months to 31st August to allow sufficient time for marketing, need for ensuring working capital finance to borrowers under term credit are other recommendations in this behalf. As 'non-wilful' defaults are often a result of the lacunae in loan policies and procedures, we have further recommended that a case-by-case analysis of defaults should be undertaken and corrective measures taken to rehabilitate the borrowers to obviate the possibility of denial of credit to them, when they are not at fault.

Recoveries - Programme of Action

15.115 Overdues are at once a symptom and a cause of the weakness of the credit system, compounded further by the socio-economic environment in which the system operates. The problem of overdues cannot, therefore, be got over merely by measures focussed on recovery procedures and mechanisms. We have made a number of recommendations in the Report which seek to upgrade and strengthen the total framework, structure and management of the credit system. These would call for concerted action for their implementation, both in precept and practice, by the government as well as the credit institutions at all levels. We also believe, if necessary action is taken and the suggested measures implemented, it should lead to a general invigoration of the system and also a substantial improvement in the recovery of agricultural dues. We have indicated the time-frame of action for some of our recommendations. It cannot be over emphasised that unless overdues are contained within an acceptable level, the large scale expansion in the quantum of credit to meet the demands of the agricultural sector, as projected by us, for the next decade upto the year 2000 AD cannot fructify.

15.116 All the same, while a multi-faceted programme of action for the strengthening and vitalisation of the credit system and improvement in the socio-economic milieu is essential which in itself will mitigate many of the causes of overdues, it is equally necessary that a programme of action

be also developed to deal directly with the endemic problem of overdues. A two-pronged approach appears desirable in this behalf; one, that deals with accumulated overdues, and the other which seeks to contain further growth of overdues, i.e. fuller recovery of the current demand. At present, in the assessment of the performance of any credit institution in respect of recovery, both the current demand and overdues demand, including the penal interest or the overdue interest capitalised, are lumped together. The problem of recovery of old overdues has many complexities, and we have brought out these problems in considerable detail in this chapter. Legal procedures for recovery are time-consuming and quite formidable even if the defaulter has assets and income enough from which recovery can be secured. The enforcement of the security of land, where such a security has been taken, is itself not easy, as practical experience has shown. In the lumping together of the two categories of demand - current and overdue the results of even the most serious recovery efforts are, therefore, at best marginal, leaving behind a sense of despair at having to do an intractable task and a dampening of the motivation for any determined action in future. In the circumstances, it is best that any programme of action in respect of recoveries should have separate performance norms for current demand and for overdues.

15.117 We propose that a definite target should be stipulated requiring all credit institutions and each of their branches to progressively raise their recovery performance under current demand to a level of at least 80 per cent within a period of three years, say by June 1992. In areas having perennial irrigation and resultantly a more developed agricultural economy and also in areas with a multiple cropping pattern in cash crops economy, the target should be a recovery of more than 90 per cent of the current demand. Strictly speaking, the target for recovery of current demand should have been more than 95 per cent but considering the present level of performance we feel that the target of 80/90 per cent proposed by us would be realistic and capable of achievement in a period of three years. Effort should, of course be to achieve it even earlier and then go forward to a still higher level of performance. Those institutions which already are in this performance bracket should endeavour to achieve full recovery under current demand. The target proposed by us is not difficult to achieve if the credit institutions build up the necessary field machinery, maintain regular contacts with the

borrowers, monitor the end-use of credit and arrange to effect recoveries as and when the loans fall due for repayment.

15.118 Simultaneously with the performance of securing optimum recovery of current demand, which will act as a check on the growth of fresh overdues, the accumulated overdues, which are quite sizeable and continue to depress the financial standing of the credit institutions, have also to be vigorously tackled under a specific time-bound action programme of recovery. We would, however, not like to suggest a overall specific time-span for this programme, like we have done for the recovery of current demand, because the nature, age and circumstances of these overdues will vary from institution to institution. These will have to be analysed, most likely on case to case basis at least in respect of older overdues (say, of more than 3 years duration) and appropriate line of action, including legal action, drawn up for each institution individually. To what extent a part of these overdues has become "bad debts" will also have to be determined and recourse taken to their writing off and/or provision to be made for augmenting correspondingly the bad debt reserves. We would also like to stress that in cases where the overdues are attributable to procedural deficiencies or institutional failures it would be a wise policy to take appropriate measures to rehabilitate these borrowers if they are "non-wilful" defaulters. The short point intended to be made here is that while a specific target oriented time-bound programme of action for recovery of overdues must be made by each institution, the duration of this programme will vary from institution to institution and has to be fixed for each institution individually in the light of its own situation. Broad guidelines, however, can be laid down by NABARD.

15.119 We would like to add that the programme of action, both for the current demand and overdues, should in the case of PACSs be drawn up by the DCCB, and in the case of PLDBs, by the SLDB, in consultation, of course, with the PACSs and PLDBs. In the case of commercial bank/RRB/SLDB branches the programme will be drawn up by their higher level administrative echelons. It should also be enjoined upon higher level institutions in co-operatives and higher level offices in commercial banks (including RRBs) to monitor, and assist in effective implementation of this programme. Also crucial to the success of the programme is the active support and co-operation of the Department of Co-operation and other state government

agencies in the recovery efforts of the credit institutions as well as in other aspects of the programme. We would also like to commend to NABARD to consider what specific incentives it can give to those institutions which have successfully taken the action expected of them under the programme and have actually achieved the targets laid down. Reserve Bank should review the recovery position twice a year with the Chief Executives of commercial and co-operative banks.

PART V

RISKS IN AGRICULTURAL LENDING

XVI NATURAL CALAMITIES : CROP INSURANCE
 AND OTHER RELIEF MEASURES

XVII RISK IN AGRICULTURAL LENDING :
 CREDIT GUARANTEE COVER

CHAPTER XVI

NATURAL CALAMITIES-CROP INSURANCE AND OTHER RELIEF MEASURES

It may be observed from the previous chapter that the lending institutions viz. the commercial banks, RRBs and co-operatives are characterised by a high rate of credit delinquency in their agricultural portfolio; they are able to recover only about 55 to 60 per cent of recoverable dues i.e., demand. In the result the low recoveries have been progressively impairing the capacity of lending agencies to ensure a smooth flow of credit. An important factor contributing to the problem of non-repayments has been the frequent recurrence of natural calamities like droughts, floods, etc. causing extensive damage to crops in some parts of the country practically every year. Such damage, in turn, impairs the farmers' capacity to repay their dues to the lending agencies. Over the years this problem has assumed critical proportions both from the point of view of recovery of dues of the credit agencies and of the interests of agricultural production. The facility of rescheduling/rephasing of loans envisaged to take care of this problem has been found to be inadequate to provide any real relief to the agriculturists or to the lending agencies due to the frequent occurrence of natural calamities. The frequent rescheduling or rephasing of production loans results only in substantial increase in the indebtedness of the farmers much beyond their repaying capacity. Therefore, unless a remedy is found to overcome this problem by providing adequate relief to the agriculturists in the event of the crops getting damaged/destroyed, it is difficult to find a lasting solution to the problem of overdue in the agricultural credit agencies. It is in this context, we believe, that a comprehensive crop insurance would be a more appropriate mechanism to provide relief to the farmers affected by such natural calamities and through this process to lending agencies in their recovery efforts.

16.02 Agriculture in large parts of the country is still dependent on monsoons despite increasing step up, since mid-sixties, in tapping the irrigation potential through major and minor irrigation schemes during the successive five year plans. As experience has shown and regional rainfall data indicate, the distribution of annual rainfall varies widely from year to year in different parts of the country. While some areas are susceptible to droughts, some others are sub-

jected to floods every year. The drought areas have been classified as (a) chronically drought prone (annual rainfall upto 750 mm), (b) drought prone (annual rainfall between 750mm and 1000mm), and (c) occasionally drought areas (annual rainfall between 1000 mm and 1500 mm). The scanty rainfall regions of Western India are also the regions where variability is high (40 per cent to 60 per cent). The interior regions of the Southern Peninsula experience the widest variation of 40 per cent to 100 per cent although during the north-east monsoon, these experience a somewhat less variable rainfall (less than 40 per cent). Using the annual and south-west monsoon rainfall data from 1901 to 1960 for about 500 stations, the Irrigation Commission (1972) had identified the following areas as drought prone and chronically drought prone in the country :

Table 1

Drought and Chronically Drought Areas in India

a)	Drought areas (20 per cent probability of rainfall deficiency of more than 25 per cent of the normal)	i) Gujarat, Rajasthan and adjoining parts of Punjab, Haryana, Western Uttar Pradesh and West Madhya Pradesh.
		ii) Madhya Pradesh, Maharashtra, interior Mysore, Rayalaseema, South Telengana and parts of Tamil Nadu.
		iii) A small portion of North-west Bihar and adjoining Eastern Uttar Pradesh.
		iv) A small portion of North-west Bihar and adjoining portion of West Bengal.
b)	Chronically drought affected area (40 per cent probability of rainfall deficiency of more than 25 per cent of normal)	Western Rajasthan and Kutch.

Similarly, some parts of the country are susceptible to frequent floods, e.g., some areas of Assam are affected almost annually by Bramhaputra floods.

Thus, as far as agriculture is concerned some regions are susceptible to "high risk"

16.03 As a solution to the impairment of the repaying capacity of the cultivators affected by crop failures due to natural calamities like recurring droughts and/or floods and the resultant dislocation of the credit system as such, the All India Rural Credit Survey Committee (1954) had recommended stabilisation arrangements envisaging conversion/rescheduling of agricultural dues of the affected borrowers to the credit agencies. Under the existing stabilisation arrangements, initially instituted in the co-operative credit system, the farmers affected by a widespread natural calamity are eligible for conversion of short-term loans into medium-term loans for three years. In the event of recurrence of natural calamities during the currency of the conversion loan period, the converted dues are rephased/rescheduled over a period of five to seven years and in some cases even upto 10 years. In the case of term loans, the instalments falling due in the calamity years are postponed/rescheduled. If in the course of such rescheduling, following incidence of successive natural calamities, it is observed that the aggregate debt burden exceeds the repaying capacity of the borrowers, credit agencies are expected to write off the excess debt burden in the case of small/marginal farmers with the financial assistance from the Agricultural Credit Relief Funds.

16.04 For providing relief to the borrowers, "Agricultural Credit Stabilisation Funds" have been established at the levels of the central and state co-operative banks and at the national level in NABARD. The resources required for the conversion operations are to be provided by the concerned DCCB, SCB, state government and NABARD in the ratio of 15:10:15:60 respectively. The co-operative banks meet their share in the conversions from the resources available in their Agricultural Credit Stabilisation Funds/general funds, NABARD from its National Rural Credit (Stabilisation) Fund and the state governments from their budgetary resources. In practice, there is flexibility in the operations and in cases where large scale conversions are involved in successive years and the amounts in the stabilisation funds of a DCCB/SCB are not adequate to meet its respective share, or a state government has difficulties in meeting its share, NABARD provides commensurately larger quantum of loans from

NRC (Stabilisation) Fund. For instance, as in the past, during 1987-88 when several parts of the country were affected by severe drought/flood conditions, NABARD had agreed to reduce, on merits of each case, the share of SCBs from 10 per cent to five per cent, DCCBs from 15 per cent to five per cent and also that of the state governments from 15 per cent to five per cent. For the purpose of write off of the converted/rephased dues exceeding the repaying capacity of the borrowers in the event of successive natural calamities, some state governments have constituted the State Agricultural Credit (Relief) Funds from budgetary allocations. The Government of India has also recently announced its decision to constitute a relief fund at the national level. The Committee constituted by the Government of India for working out the details regarding the creation of the National Agricultural Credit Relief Fund (NACREF) has recommended, in October 1988, that relief under the scheme be provided, in the event of three successive natural calamities, for writing off the first conversion loan and interest thereon. It will initially be confined to borrowers growing foodgrains, pulses and oilseeds and availing crop loans upto Rs.7,500 from commercial banks, RRBs and co-operative credit institutions. As recommended by the Committee, the corpus of the NACREF would be Rs.75 crores to be contributed by the Central and state governments on a matching basis. Assistance to the extent of 90 per cent of the amount to be written off will be available from the NACREF while the credit institutions will be required to bear the burden of the balance of 10 per cent from their own resources.

16.05 Under the existing arrangements, relief under stabilisation arrangements is provided to the affected borrowers when (a) the crop yield in the affected areas as estimated by the state government is 50 per cent or less of the normal yield, and (b) state government remits/suspends collection of land revenue/other government dues from the farmers in the affected areas. The relief is confined to loans issued for unirrigated crops only.

16.06 The stabilisation arrangements have also been extended to the commercial banks and the RRBs. While commercial banks are expected to provide relief to affected borrowers from their own resources, RRBs are eligible, from the year 1986-87, for refinance facilities from NABARD upto 70 per cent of the conversions; of the balance, medium-term conversion loans upto

25 per cent of conversions, are to be sanctioned to RRBs by the sponsor banks and remaining share of five per cent of the converted amount is to be met by RRBs themselves from their own resources.

16.07 In the case of commercial banks, it was observed in the course of field survey that in quite a few branches the work of providing relief to borrowers affected by natural calamities was neglected. Inadequacy of staff to cope with even normal items of work, tendency of the defaulters to avoid bank staff thereby defeating/delaying fresh documentation were among the reasons cited for the failure to provide conversion/rescheduling facilities, though in the process banks' recovery performance was adversely affected and borrowers, treated as defaulters, were rendered ineligible for fresh finance. It is necessary that the controlling offices of the commercial banks attach due importance to this work and ensure that their rural/semi-urban branches provide relief to borrowers affected by natural calamities by converting/rescheduling agricultural loans falling due for repayment in the calamity years.

16.08 A major lacuna in the stabilisation arrangement, however, is that it seeks to find solution to the problem largely through rescheduling of debts with a view to postponing their recovery to a future date. This arrangement is basically intended for and workable in areas where the incidence of natural calamities is occasional, the concept of rescheduling being based on the expectation that one or two disaster years will be followed by three to four normal crop years which will enable the borrower to meet the arrear loan liability in respect of the earlier bad crop seasons. During the currency of a conversion loan, borrower has to face the loan liability of repaying instalments of the converted/rescheduled loans in addition to that in respect of his fresh crop loan and instalment of normal medium-term loan, if he is a borrower under term loans also. Assuming the repaying capacity of the cultivator, having value of his gross produce upto Rs.5,000, at 58.33 per cent, the Study Team on Overdues of Co-operative Credit Institutions (1974) had calculated that the debt liability of the cultivator would exceed his repaying capacity in case he is exposed to (a) three successive crop failures if he had borrowed only under short-term loans, and (b) two successive crop failures if he had also borrowed under normal medium-term loan in addition to his crop loan.

16.09 In the case of successive natural calamities, the stabilisation arrangements do envisage write off of debt burden exceeding the repaying capacity of the borrower; for this purpose the Survey Committee had recommended that Relief and Guarantee Funds may be established both at national level by Government of India and at the state level by the respective state governments, and augmented annually through budgetary grants. However, these provisions have largely remained on paper due to the absence of the Relief Fund at the national level, paucity of resources in the Relief Funds at the state level where they have been constituted by the state governments coupled with inhibitions harboured by all concerned regarding the adverse repercussions, such write offs may have on the overall recovery climate:

16.10 As provisions for write off with the help of assistance from the Relief Funds have so far remained inoperative, if not virtually non-existent, relief under stabilisation arrangements by way of rescheduling was sought to be given for longer periods with a view to accommodating the accumulated debt burden within the repaying capacity of the affected borrowers. Thus, conversions and rephasing of converted dues which was initially envisaged upto three to five years, was extended upto seven years in 1974 in terms of the recommendations of the Overdues Study Team. Recently, with a view to meeting the unprecedented drought of Kharif 1987 in large parts of the country, NABARD had advised co-operative banks to allow, in cases of farmers affected by drought/floods for three years in succession, rescheduling of each year's dues for a period of seven years i.e. rescheduling of the total dues over a period upto 10 years. It is, however, too sanguine to assume that, in such chronically drought/flood prone areas, the borrowers would have the benefit of normal crop years over the next decade to be able to repay the dues as rescheduled. Should the borrowers have to face incidence of natural calamity during the currency of such rephased loans, which it would be only reasonable to expect, they would neither be able to repay the instalment under the converted loans falling due in the calamity year nor the current crop loan for that year and would be compelled to default, thereby rendering the whole scheme infructuous.

16.11 Even if conversion/rephasing facilities are allowed upto a period of seven years, the stabilisation arrangement can work if only one or two years are drought affected in a seven year cycle. If the frequency of calamities

is more, which it is in several chronically drought prone areas, the borrower's debt burden would exceed his repaying capacity and it would have to be written off. In the absence of operative provisions for write off, in areas susceptible to repeated natural calamities, conversion/rescheduling which adds to the debt burden of the borrowers, often in excess of their repaying capacity, merely results in postponing the problem of default to a future date. In most of the cases of repeated natural calamities, rephasing/rescheduling of dues is being effected in a routine manner, without assessing the repaying capacity of the borrowers in each individual case with the result that the affected borrowers, unable to meet their increased debt obligations, are compelled to commit defaults in repayment of converted/rephased instalments and are consequently rendered ineligible for fresh loaning in the subsequent years.

16.12 It has also been the experience that the relief arrangements are often used not necessarily for the benefit of the genuinely affected borrowers. Studies conducted by RBI in some states had revealed that in several cases the assessment of crop damages made by state government machinery, often under pressures from local politicians, was quite liberal and in many cases it was observed that relief by way of conversions/rescheduling was extended more with a view to circumventing the discipline of repayment of agricultural loans, on the due dates. Such misuse of the stabilisation arrangements has led to accumulation of the debt burden of the borrowers in several states.

16.13 Even when arrangements for establishment of the Relief Fund at the national level are finalised and policy of write off introduced (i.e. write off of one crop loan in the event of two to three successive crop failures as the case may be), the borrowers would still have to carry over the burden of old conversion dues in addition to current crop loans. There will also be obvious limitations on granting relief by way of write off repeatedly, owing to the repercussions such write off would have on the climate of recovery, which already stands vitiated. Relief in the form of write off is again confined, at least at present, to only small/marginal farmers due to hesitation in extending this facility to medium/large farmers who would continue to be saddled with excessive debt burden. These limitations show that constitution of a relief fund for write off alone can hardly make stabilisation arrangements a workable solution to the problems of affected borrowers. In fact, the stabili-

sation arrangement was envisaged primarily to solve the problems of the credit institutions and to keep open the channels of credit in the co-operative credit structure rather than those of the borrowers who, under this arrangement, continue to carry over the burden of old dues, with remote prospects of ever getting debt free and starting their business on a clean slate. It is, therefore, our view, as has been the experience over the last three decades, that relief by way of stabilisation arrangements is not an adequate answer to the problems of such borrowers much less of the farmers in chronically flood/drought prone areas.

16.14 Crop insurance could no doubt be one answer. But there are areas which are chronically drought prone such as the Kutch district in Gujarat or Western Rajasthan where incidence of drought is successively felt year after year. As far as these areas are concerned, it is open to question whether even a comprehensive crop insurance scheme could sustain the loss on a continuing basis. It has been the experience that in the years of drought, the farmers in the areas have ultimately to fall back on some ancillary activities which the local natural resources provide when they are unable to cultivate their lands. In our view it is necessary that the Government of India/concerned state governments undertake area-specific studies on the impact of drought and other natural calamities on agriculture and allied activities in these chronically drought/flood prone areas, identify the non-farm activities that support the farmers in the calamity years and draw specific plans for developing such non-farm activities as a principal source of livelihood for the people in such areas. It is also necessary to examine if such areas could be excluded from the crop insurance scheme.

16.15 As these areas receive very scanty rainfall even in normal years, farming activities, as are possible, will have to be pursued through adoption of dry land farming techniques. Further, considering the low level of farm output and frequency of droughts which characterise these areas, the system of financing agriculture in these areas cannot be the same, as prevalent in the rest of the country.

The Existing Crop Insurance Scheme

16.16 The Government of India introduced, with effect from 1 April 1985 (i.e. Kharif season 1985), a crop insurance scheme known as "Comprehensive

Crop Insurance Scheme" (CCIS) throughout the country. The Scheme is implemented by the General Insurance Corporation of India (GIC) on behalf of the Government of India and the state governments. The scheme covers all farmers availing of crop loans from commercial banks, co-operative credit institutions and RRBs for raising certain specified crops. The crops so specified as at present are rice, wheat, millets, oil-seeds and pulses and the scheme operates in defined areas for each crop notified by the Union Ministry of Agriculture. The insurance cover forms a 'built-in' part of the crop loans. The sum insured is 150 per cent of the crop loans for eligible crops disbursed to the beneficiaries during the season. From Kharif 1988 season, the sum insured has been reduced from 150 per cent to 100 per cent of the crop loan subject to a limit of Rs.10,000 per farmer. The premium for the insurance cover, which is two per cent of the sum insured for rice, wheat and millets and one per cent of the sum insured for oilseeds and pulses, is included as a part of the scales of finance for these crops. At the time of disbursal of the loan, the premium is deducted for payment to GIC. In the case of small/marginal farmers, 50 per cent of the insurance premium is subsidised and the subsidy is shared equally by the Central and state governments.

16.17 The scheme has since been extended to all states and Union Territories. The defined area for each crop, notified by the Union Ministry for Agriculture, may be a district/tehsil/taluka/block or a smaller contiguous area. If the actual average yield per hectare of the insured crop for a defined area, determined on the basis of crop cutting experiments in the insured season, falls short of the specified threshold yield, all the insured farmers growing that crop in the defined area are deemed to have suffered the shortfall in the yield and the scheme provides cover against such a shortfall. Where the data of yields obtained through crop cutting are not available, the methodology for assessing the shortfall is decided by GIC in consultation with the Ministry of Agriculture. Eighty per cent of the average yield per hectare of the crop for the defined area during the last five years (or such shorter period as may be decided for the area for which data are available by crop cutting experiments/alternative methodology) is taken as the threshold yield of the crop in the defined area. In order to induce the low risk areas to join the scheme, the Cabinet Committee on Economic Affairs has decided to

enhance the indemnifiable limit from 80 per cent to 85 per cent and 90 per cent depending upon the co-efficient of variation and calculation of threshold yield on the basis of the moving average of the preceding three years. If there is a shortfall in the actual average per hectare yield of the insured crop as compared to the threshold yield, each insured farmer growing that crop in the defined area will be eligible for indemnity calculated as under:

$$\text{Amount of Indemnity} = \frac{\text{Shortfall in the yield}}{\text{Threshold yield}} \times \text{Sum insured by the farmer}$$

The concerned state government acts as co-insurer to the extent of 33.33 per cent for the schemes introduced in the state. Thus, the claims under CCIS are paid by Government of India and the concerned state government in the ratio of 2:1. For Union Territories the entire claim is borne by GOI. For this purpose, state governments have set up the State Crop Insurance Funds each with an initial corpus of Rs.1-2 crores to be contributed equally by the state governments and the central government; the size of the Fund for each state is determined in consultation with the concerned state government, the Union Ministry of Finance and the Union Ministry of Agriculture.

16.18 As regards the operation of the scheme, it may be observed that the quantum of the aggregate crop insurance cover, which, in practice is equivalent to the institutional loan amount for the insured crops in Kharif 1985 and Rabi 1985-86 was Rs.780 crores, forming about 24 per cent of the estimated institutional crop loans for all crops during 1985-86 at Rs.3254 crores. Data regarding the insurance premia collected and claims paid during the seasons Kharif 1985 to Rabi 1987-88 are given in table 2.

16.19 The actual operation of the scheme during its initial two to three years has brought up some of the basic lacunae of the scheme, which have been discussed below.

16.20 First and foremost, the scheme is applicable only on a voluntary basis leaving it to the option of the state governments to identify the crops and definite areas to which the scheme would apply, with the result that only those states where risks in agriculture are comparatively high have opted for the scheme. States like Punjab, Haryana and areas like Western U.P. have not evinced any interest in the scheme. Even states participating in the scheme have left out of coverage those areas where crop yields are stable

Table - 2

Operations of the Comprehensive Crop Insurance Scheme 1985-88

(Rs. crores)

Season	Area covered (lakh hect.)	No.of farmers insured (lakhs)	Amount of Premia Collected	Total claims paid	Total claims payable	Total of (5) + (6) i.e. claims paid/payable
1	2.	3.	4.	5.	6.	7.
i) Kharif 1985	53.73	26.36	9.42	82.88	1.02	83.90
ii) Rabi 1985-86	23.18	12.12	4.48	3.11	-	3.11
iii) Kharif 1986	77.40	39.56	14.99	154.33	12.46	166.79
iv) Rabi 1986-87	21.00	11.28	4.52	2.85	5.00	7.85
v) Kharif 1987	84.42	47.34	19.09	8.98	267.58	276.56
vi) Rabi 1987-88	32.37	21.28	8.85	-	11.41	11.41
			<u>61.35</u>	<u>252.15</u>	<u>297.47</u>	<u>549.62</u>
			=====	=====	=====	=====

The total losses of the Comprehensive Crop Insurance Scheme were of the order of Rs.84 crores for Kharif 1985, Rs.164 crores for Kharif 1986 and Rs.287 crores for Kharif 1987 season. The total losses borne by the Central and State Governments under the scheme are steadily increasing from season to season. Consequently, insurance cover has been reduced from Kharif 1988 season from 150 per cent to 100 per cent of the crop loan subject to a ceiling of Rs.10,000 per individual farmer so as to reduce the Government's burden.

as far as production of crops covered under the scheme is concerned. Thus, the absence of the basic canon of insurance business, viz., principle of cross subsidization with premia income from areas of stable crops paying for the areas having unstable crops is conspicuous in the scheme. With the selection of adverse/unstable crop yield areas, the losses under the scheme are mounting year after year, and instead of insurance, the scheme has assumed the complexion of a welfare measure.

16.21 Secondly, there is no uniformity in the basic unit (which is a district in some states, taluka or block in others) for determining the threshold yield and assessment of the actual yield in the calamity affected area for invoking the insurance cover. Even a taluka or a block is too big in size as a unit for the purpose, as incidence of calamity is rarely uniform all over the taluka/block; some villages are badly affected while others have normal yields, and this diversity increases with the increase in the size of the basic unit. This often leads to an anomalous situation. If the overall actual average yield of an insured crop in the taluka/block is less than the threshold yield, the farmers cultivating that crop in the taluka automatically become eligible for relief under the scheme, including those in some villages where crop yield is above the threshold yield and the resident borrowers are prima-facie not in need of the relief. On the other hand, genuinely affected borrowers in villages in some other talukas having overall actual average yield above the threshold yield may be denied the insurance benefit. One outcome of the large size of the unit with reference to which threshold yields are fixed and crop damages are assessed is that unduly large amounts of indemnities get paid out than warranted, had indemnity been confined to those genuinely affected by the insured calamities.

16.22 Thirdly, the experience regarding the operation of the scheme in the last three to four years shows that its main deficiency is its non-viability. While a solution to this imbalance was sought by reducing the aggregate amount of insurance cover from Kharif 1988 from 150 per cent to 100 per cent of the crop loan, in the process the relief to the affected borrowers might get reduced to below the production cost which we feel should be the sum insured. The incidence of calamities like droughts/floods is quite widespread in various parts of the country and losses sustained by borrowers turn out to be so substantial that it would not be possible to operate the scheme and make it

viable if the insurance premia are kept as low as one or two per cent. It appears that the premia rates were kept low deliberately to make the scheme acceptable to the farming community initially. The expectation that the scheme would be implemented on a compulsory basis in all states making cross subsidization possible also failed to materialise. As a result, the indemnities paid far exceeded the premia collected, and the scheme has resulted in being an open end scheme with undetermined liability of Government and concealed subsidies with the Central and state governments sharing the entire liabilities exceeding the income from premia. There is apparently a need to set the premium rates based on an actuarial basis.

16.23 While on the one hand, the scheme has proved to be non-viable, it has, on the other hand, also failed in its basic objective of indemnifying the farmer's losses or at least, absolving him fully or partially of his crop loan liability from institutional agencies. Considered in this context, the basic deficiencies of the scheme may be briefly summed up as follows :

- i) Firstly, the threshold yield of the selected crop is fixed on the basis of the average yield per hectare of the selected crop for the previous five years, or shorter period as determined. In chronically flood/drought prone areas, in a cycle of five years, two or even more years are often drought/flood affected when the crop yield is substantially low. Since threshold yield is fixed with reference to the running average for the previous five years including the calamity years, the threshold yield so fixed is itself so low that farmers often do not qualify for any relief even when their crops sustain damages due to natural calamities. It is, therefore, necessary that years of natural calamity are excluded while fixing the threshold yield i.e. for the purpose of insurance cover, damages are assessed with reference to 'normal' yield and not the 'average' yield.
- ii) Secondly, under the scheme, the ceiling for indemnity is fixed at 150 per cent of the crop loans availed of by the borrowers (from Kharif 1988 season the sum insured has been reduced from 150 per cent to 100 per cent of the crop loan subject to maximum limit of Rs.10,000 per farmer); the actual relief based on the

formula for determining indemnity, however, varies depending on the extent of crop failure, since the calculation is based on the threshold yield and the actual average yield and a certain percentage of the loss to be borne by the borrower himself. With the reduction, in the sum insured to 100 per cent of the crop loan, the indemnities under the crop insurance scheme stand reduced to only 37.5 per cent of the crop loan in cases where the crop damages are 50 per cent (i.e. in cases where under the stabilisation arrangements the borrower is not required to repay any part of the crop loan which gets converted into medium term conversion loan). In cases where the crop losses are total, the indemnities he would get under the crop insurance scheme would cover only the amount of his crop loan in full but not the interest payable thereon. The basic objective underlying crop insurance is to protect the farmer from losses arising out of the insured risks and enable him to continue his business operations. For this purpose, some quarters believe that the crop insurance cover should enable him at least to repay his entire loan liability and interest thereon to the institutional credit agency to obviate default so that he is eligible for loan afresh for carrying out his agricultural operations. Even at this point, the uncompensated losses beyond the loan amount gave rise to the charge that the scheme was only crop loan insurance scheme which would merely insulate the lending institution against default of its loan and would not provide any relief to the farmer against his crop losses beyond the amount of crop loan.

- (iii) Thirdly, the scheme presently covers only specific crops, viz., rice, wheat and millets, oilseeds and pulses in defined areas for each crop notified by the Union Ministry of Agriculture. It is our view that the scheme should cover all cultivated areas and the principal crops cultivated (for instance, in areas where the horticulture crops predominate, they should come under the purview of the scheme if the actuarial studies justify it).

Crop Insurance Abroad

16.24 In many other countries, where crop insurance has been attempted it is characterised by complex administrative problems of implementation and has become very costly in financial terms. Nevertheless, in some countries like Japan and Philippines, the crop insurance has met with considerable measure of success. In this context, the salient features of the crop insurance scheme in Philippines, a developing country facing more or less similar financial constraints like India, are given below.

Crop Insurance Scheme In Philippines

16.25 The Philippines crop insurance programme was launched on 7th May 1981 to compensate the farmers and the lending institutions in respect of losses arising from damages to standing crops from such natural calamities as floods, typhoons, droughts and pest infestation. For administering the crop insurance scheme, Government of Philippines has established 'The Philippine Crop Insurance Corporation (PCIC)', a corporate body with an authorised capital of P 750 million and paid up capital of P 250 million, head office in Manila, and functioning through its 12 regional offices.

Types of insurance

i) The crop insurance cover is extended to two crops, palay (paddy) and corn. This apart, the PCIC has also introduced a live stock insurance programme extending insurance cover to cattle, caribou, swine and poultry.

Participants

ii) Crop insurance is automatic for all farmers obtaining production loans from lending institutions for palay and corn under the supervised credit programme. The insurance scheme is optional for the non-borrowers i.e. self financed farmers.

Calamities insured

iii) The farmers are insured against losses caused by natural calamities such as typhoons, floods, droughts, earthquakes and volcanic eruption, plant diseases and pest infections. The losses on account of avoidable risks attribu-

table to the neglect by the insured or his household are not indemnified.

Insurance period

iv) The insurance cover is on the crop season basis and covers the period from direct seedling or transplanting upto harvesting. The insurance cover being only in respect of standing crops, the harvested produce does not carry any insurance cover.

Insurance Cover

v) The amount of crop insurance cover for palay and corn is based on the value of the production inputs as prescribed by the Department of Agriculture (DA), plus cost of labour, the maximum amount of insurance cover was limited to 125 per cent of the production cost, the ceiling set by the then National Food and Agriculture Council. In the case of self financed farmers, they have the option to insure upto 125 per cent of the production loan ceiling. There was an overall ceiling on insurance cover of P 3750/- per hectare for rice crop and P 6000 per hectare for corn crop as at the end of 1987-88.

Premia

vi) Insurance premia are being fixed on an actuarial basis, separately for rice and corn crops with reference to the incidence and the extent of damages to crops; premium for rice crop insurance was pegged at 8 per cent of the sum insured whereas that for corn crop was pegged at 13 per cent.

vii) Insurance premia are shared by the farmer, the financing bank extending the credit to him and the Government. The premium sharing was as follows for rice and corn crops :

	Rice Crop		Corn Crop	
	Borrow- ing farmers	Self- financed farmers	Borrow- ing farmers	Self- financed farmers
A) For cover upto loan amount/ production cost				
Farmer's share	2.0	2.0	2.5	2.5
Lending institution's share	1.5	-	1.5	-

Government share	4.5	6.0	9.0	10.5
Total Premium	8.0	8.0	13.0	13.0
B) For additional 25 per cent insurance cover				
Farmer's share	2.0	2.0	2.5	2.5
Government share	6.0	6.0	10.5	10.5
	8.0	8.0	13.0	13.0

Government also bears a share in the PCIC's operating expenses at three per cent of the sum insured under the rice crop insurance. The premia rates have been fixed, and reviewed/revised, in the light of the indemnities the PCIC is called upon to pay, the objective being to make the scheme viable by itself. For instance, in the case of corn crop insurance, till 30th June 1987, when the premium was seven per cent of amount covered, it was observed that the ratio of total premia collected to claims paid worked out to 1:3. The premium was, therefore, raised with effect from 1.7.1987 to 13 per cent of the amount covered. Since the premium is more than what farmers would be in a position to bear, it is shared by lending agencies and heavily subsidised by Government. The farmers' share is kept lower than the lowest loss rate for 12 agro-climatic regions of the country. The borrowing farmers are automatically covered by crop insurance and the application for production loan itself serves as application for crop insurance. The farmers' share in the premium is deducted from the loan amount and he is given certificate of insurance cover. The self financed farmers file their application for crop insurance before planting of crops, with the nearest regional office of PCIC.

Assessment of crop losses

viii) The insurance cover is on an individual basis (i.e. PCIC undertakes to indemnify crop losses sustained by individual farmers) and not on an area basis as in India. Assessment of crop losses is made by a Team of Adjusters in the case of each farmer who files a Notice of Loss (NL) with the PCIC office.

The Team of Adjusters consists of three persons

- i) Representative of PCIC,
- ii) Municipal Agricultural Officer of the Department of Agriculture,
and
- iii) Team leader of the Department of Agrarian Reform.

The Team assesses in the case of each insured farmer the extent of crop damages which forms the basis for payment of indemnities by PCIC.

Payment of indemnities

ix) The loss is compensated if it is more than 10 per cent of the average normal yield determined for the area. The loss may be total or partial; it is considered total if it is of a nature preventing continuation of the crop operations. The total loss is compensated to the extent of actual cost of the production inputs already applied or estimated cost of inputs appearing in the farm plans/budget. In the case of rice crop insurance, for instance, the indemnities with reference to the stage of production are as follows:-

25 days after seeding	₱ 2064.60 per hectare
35 days after vegetation	₱ 2424.25 per hectare
42 days after vegetation	₱ 2793.30 per hectare
49 days after vegetation	₱ 3070.30 per hectare
59 days after vegetation	₱ 3161.85 per hectare

On the other hand, damage to crops is considered partial if cultivation operations could be continued profitably. The partial loss is assessed after actual harvesting and compensation paid on the basis of the following formula :

$$\text{Indemnity} = \frac{\text{Estimated Normal Yield} - \text{Actual Yield}}{\text{Estimated Normal Yield}} \times \text{Amount of cover}$$

Crop loss amounting to 90 per cent or more of the average normal yield is considered to be total loss. The claims are paid after the Team of Adjusters have submitted their report to PCIC regional office. Generally, indemnities for the total loss are paid within 45 days from the notice of loss while those for partial losses are paid after the actual harvest has been determined.

Government assistance to the insurance schemes

x) The national Government provides both financial and administrative support to the crop insurance schemes. Apart from the premia subsidies directly borne by Government, Government provides direct subsidies towards part of the operating expenses, the balance being met from earnings on investment of share capital, contributed by Government.

Operational results of the Scheme

xi) The number of farmers covered by the palay crop insurance scheme had increased from 1.08 lakhs in 1981 to 1.80 lakhs in 1983, though thereafter the number had declined to 1.60 lakhs in 1985 and 1.11 lakhs in 1987. The aggregate amount of insurance cover provided by the PCIC increased from P 265.46 million in 1981 to P 865.10 million in 1985 which fell to P 665.95 million in 1987. The proportion of non-borrowing/self-financed farmers to total insured steeply increased from 1.8 per cent to 28 per cent in 1983 and further to 57.6 per cent in 1987, when the number of insured non-borrowing farmers had far exceeded that of borrowing farmers. Similar trends are seen under corn crop also. Data regarding insurance premia collected from farmers under palay crop and indemnities paid are given in table 3.

Table 3

Statement showing the amounts of premia collected and indemnities paid

Year	Insurance premia collected	(million pesos) Indemnities paid out
1981	21.237	7.492
1982	32.812	24.718
1983	35.689	33.212
1984	36.963	53.085
1985	69.209	71.417
1986	61.874	98.144
1987	63.276	53.193
1988	56.243	46.993
(Upto Sept.88)	377.303	388.254

On a comparative level, since 1981 PCIC experienced four good crop years out of 7 resulting in a net retained earning of ₹138.304 million at the end of December 1987.

Crop Insurance - a major plank

16.26 Out of nearly 70 per cent of the cultivated area dependent on uncertainties of rainfall in India, large parts where annual rainfall is less than 1500 mm. are subject to droughts. Similarly, some parts of the country are susceptible to frequent floods. If experience over the last three decades is any indicator, the stabilisation arrangements have failed to provide an adequate answer to the loan repayment problems of the borrowers affected by natural calamities since the postponement of dues envisaged thereunder has merely culminated in increasing the debt burden of the borrowers. What these borrowers need is a measure of relief which will redeem them, once for all, of their loan liabilities commensurate with the crop losses sustained by them and enable them to resume their agricultural operations on a clean slate. In view of this, it is our considered view that crop insurance scheme conceived on the right lines and implemented effectively should form a major plank of the agricultural development strategy in the years to come.

16.27 Doubts are sometimes raised regarding the prospects of success of a crop insurance scheme in India in the context of the large proportion of the cultivated area prone to droughts/floods and the lack of success of the comprehensive crop insurance scheme already in vogue. As for the former, even in a country like Philippines where crop insurance scheme has been a success, agriculture is no less exposed to natural calamities. The percentage of irrigated area to the total cultivated area in Philippines is as low as around 17 as compared to over 30 in India. Apart from droughts, agriculture in Philippines is susceptible to frequent typhoons and floods as a major cause of crop damages. In 1988 Philippines was hit by the worst typhoon/floods which damaged the rice and corn crops by 10.2 and 4.25 per cent respectively, in addition to the losses of 2.96 per cent and 7.91 per cent due to drought. In comparison, notwithstanding the severest drought of 1987-88, the decline in the foodgrains production in India was only 4.8 per cent over the earlier year. It would, therefore, appear that it is not the scale of the natural calamities to which agriculture is exposed but the structure of the crop insurance

scheme and the effectiveness of its implementation which ultimately determine the prospects of its success.

Remedial Measures

16.28 In this context, we are suggesting below measures for overcoming the major shortcomings of the existing Comprehensive Crop Insurance Scheme :

- i) Since selection of crops with highly fluctuating yields and of only the unstable crop yield areas by the state governments has led to heavy losses under the scheme, to work as an insurance scheme, the possibility of adverse selection should be eliminated by such measures as automatic coverage for all borrowing farmers raising the selected crops in the state.

- ii) For obviating the payment of indemnities to those not genuinely affected by crop damages, entailed in the present day 'area approach', we feel that the ideal and ultimate solution may lie in having crop insurance on 'an individual basis' replacing the 'area approach' which characterises the existing scheme. However, this would entail evolving of an elaborate, if not costly, administrative machinery for the purpose which, we are aware, would not be possible administratively or organisationally to build up, in the foreseeable future. There is, therefore, no other option than the 'area approach' for the time being. With a view to ensuring that the benefit of crop insurance is confined only to genuinely affected borrowers, it is desirable that the basic unit for determining the threshold yield and assessing the crop damages is reduced to agro-climatically homogeneous group of small number of villages, with a specific programme of having 'a gram panchayat' as a unit for fixing the threshold yields and assessing the crop damages under the crop insurance scheme, in the near future. Considering that in countries like Japan and Philippines where insurance cover is provided to farmers on an individual basis and the insurers assess the crop losses in each individual case, it should be possible to estimate, in the near future, the crop losses on a gram panchayat-wise

basis, with a view to ensuring relief only to the genuinely affected farmers. This is likely to reduce substantially the amount of indemnities payable under the scheme, and remove the inequitable situation of indemnification method found in the present scheme.

iii) A major factor contributing to the non-viability of the scheme is the unduly low level of premia - as low as one per cent of the sum insured for oil seeds and pulses and two per cent for rice, wheat and millets. In this context, we find that in some countries like Japan and Philippines where crop insurance is being implemented successfully, the insurance organisations are required to fix the insurance premia computed more or less on actuarial basis at a fairly high level. The insurance premia fixed under the crop insurance scheme in Philippines are given in table 4.

Table - 4

Insurance Premia Applicable in Philippines

	(In percentage)			
	<u>PADDY</u>		<u>CORN</u>	
	<u>Borrowing farmers</u>	<u>Self-financed farmers</u>	<u>Borrowing farmers</u>	<u>Self-financed farmers</u>
Farmer's share	2.0	2.0	2.5	2.5
Lending institution's share	1.5	-	1.5	-
Government's share	<u>4.5</u>	<u>6.0</u>	<u>9.0</u>	<u>10.5</u>
	8.0	8.0	13.0	13.0

In Japan, where the Agricultural Insurance Scheme is operated, through the Agricultural Mutual Relief (AMR) Associations or local Governments, the Ministry of Agriculture, Forestry and Fisheries determines the premium rates, for each AMR Association/local government on the basis of annual insurance damage rates of each Association/local Government in the past 20 years and the share of Government therein ranges between 50 per cent and 70 per cent as shown below :

(In percentage)

Paddy (Rice)		Mugi (Wheat)	
Premium Rate	Govt. Share	Premium Rate	Govt. Share
Upto 2	50	Upto 3	50
2 to 4	55	3 to 6	55
Above 4	60	6 to 9	60
		9 to 12	65
		More than 12	70

In these countries, the premia had to be fixed at a high level commensurate with the incidence of crop damages; however, having regard to the lack of ability of the farmers themselves to bear the premia burden, the premia are heavily subsidised by the concerned governments. In Japan, the government share in the premia ranged between 50 and 70 per cent whereas in Philippines the government share was 80 per cent in some cases. The overall incidence of natural calamities in many parts of India is not less than that in Japan or in Philippines and, therefore, it may be difficult to operate a crop insurance scheme, on a viable basis, with premia as low as one or two per cent on a uniform and ad-hoc basis. Similarly, there are wide variations in the incidence of crop damages in different parts of the country; as such the crop insurance premia have to be fixed not uniformly but they should be commensurate with the damage-risk, if the Comprehensive Crop Insurance Scheme is to function on a viable basis. This can be accomplished only if the premia rates are fixed on an actuarial basis for different agro-climatic regions having more or less the same degree of risk arising from natural calamities, higher premia for high risk areas and lower for low risk areas. Since the premia rates so fixed, particularly in the high damage risk areas, are likely to prove too high for the farmers to bear, they will have to be subsidised by government with a view to reducing the burden on the farmers to be within their tolerance limits. Similarly, instead of having uniform rates, crop-wise, throughout the country as at present, the advisability of adopting realistic differential premia rates on an actuarial basis for different areas/agro-climatic regions, crop-wise, based on the actual yield data for earlier 10 year period and having regard to the frequency and incidence of crop losses in each area, should be studied. We, therefore, recommend that insurance premia may be fixed

on an actuarial basis for different agro-climatic areas, crop-wise and the burden of the premia be shared among the insured farmers the lending agency and the government. Since the lending agency is a beneficiary under crop insurance, as its loans get automatically recovered through the insurance scheme and it is spared the efforts and costs of recovery, it would only be logical to expect it to bear a small share in the premia. We, therefore, suggest, subject to what the actuarial studies will indicate, that the premium be shared among the farmers, the lending agency and the Government, the share of the farmers and the lending agency being kept to the minimum.

16.29 In certain areas where crop yields are unstable due to their susceptibility to repeated natural calamities, the premia for different crops, calculated on an actuarial basis may turn out to be too high, necessitating heavy subsidisation by Government. In view of this, the possibilities of reinsurance within the country or abroad, could be explored with a view to diversifying the risks involved in insuring the crop yields. We understand that such recourse to reinsurance is being taken in some countries like Philippines.

16.30 It may be argued that fixation of premia on an actuarial basis and their subsidiation, on the scale envisaged, by Government would make the scheme financially too costly to operate besides perpetuating the subsidies-direct and indirect-to the agricultural sector which, as it is, has been heavily subsidised. However, in our view, the overall financial burden on Government intended in our proposal may not be larger than what Government is already called upon to shoulder under the existing scheme. Even under the existing scheme, Government of India and the state governments are bearing the entire financial burden of indemnities payable to farmers over and above the premia collected and, therefore, our recommendation regarding government subsidising the premia may not involve much additional financial burden to the government. On the contrary, a desirable switch over from concealed subsidies and indefinite liabilities implicit in the existing scheme to open subsidisation, as obtaining in some other countries, would facilitate streamlining the government's financial liabilities in the scheme while at the same time ensuring that the scheme functions on a viable basis by itself.

16.31 Secondly, when the crop insurance scheme modified on the lines

suggested in the forgoing paras is implemented, it would reduce substantially the reliance of the credit system on the existing stabilisation/relief arrangements and consequently reduce, if not obviate, the need for financial assistance which government—both Central and state—provide in considerable measure, in the form of diversion of dividend in excess of three per cent on Government share capital for augmenting the stabilisation funds in the state/central co-operative banks level, grants-in-aid for augmenting stabilisation funds at the state co-operative bank level, budgetary allocations for strengthening the relief fund at the state level and proposed relief fund at the centre, etc. Further, legitimate overdues under agricultural loaning arise mainly because of the proneness of agriculture to natural calamities and due to the unsatisfactory nature of relief in vogue; such debts ultimately turn irrecoverable and, therefore, subject matter of claims under the credit guarantee schemes of DICGC. If borrower farmers are adequately indemnified under the crop insurance scheme, not only the reliance on stabilisation/relief arrangements but that on the credit guarantee cover for agricultural loans would also be considerably reduced and subsidisation of agriculture will in no way be larger than what it is at present.

16.32 As regards the basic objective of the scheme, viz., indemnifying the borrower-farmers' crop losses, the question is the extent to which the insurance scheme may seek to indemnify the losses. In Japan, for instance, the insurance cover provided to the farmer under the Agricultural Insurance Scheme extends to the income from the crop (i.e. prices listed by the Ministry of Agriculture, Forestry and Fisheries multiplied by the insured yield) and is not confined either to the cost of cultivation or the crop loan. In Philippines, the insurance for paddy and corn crops covers the cost of production which is equivalent to 125 per cent of the amount of the crop loan for production inputs so that a farmer, in case he is a borrower from credit agency, gets some indemnity over and above the crop loan taken by him. We realise that considering its financial implications, it is neither possible nor desirable, on moral considerations, for any crop insurance scheme to attempt to indemnify the entire market value of the anticipated gross produce since such high indemnities would reduce the borrowers' incentive and motivation to exercise due care and diligence in their farm operations since the indemnity under crop failure would indemnify him against his expected income also. It is, therefore, our considered

view that indemnities be confined only to the cost of inputs including labour and cost of production credit (i.e. interest payable on crop loan). Since one of the major inputs especially in the case of small/marginal farmers is their own labour and that of their family members, the indemnities, we feel, should cover a reasonable amount as imputed cost of family labour. We, therefore, recommend that the sum insured may be so fixed as to cover cost of production including the interest payable on crop loan and a reasonable amount to take care of the imputed cost of the family labour of the borrower.

16.33 In our view, the crop insurance scheme suitably amended on the lines suggested above to remove its present flaws and improve its effectiveness would contribute in a substantial measure to the agricultural development by removing a major impediment to (i) an un-interrupted flow of credit supply and stable income from agriculture to the farmer and (ii) reducing the incidence of overdues of the credit institutions by taking the abnormal risk entailed in natural calamities and other risks off the shoulders of the farmers and the credit institutions.

16.34 At present, the General Insurance Corporation of India (GIC) is implementing the scheme on behalf of the Government of India and the state governments; 50 per cent of the administrative expenses incurred by GIC in implementing the scheme are being borne by the Ministry of Agriculture, Government of India. Apparently, the idea behind entrusting the implementation of the scheme initially to GIC was that it had gained some experience in implementing the pilot crop insurance scheme and also that the GIC was the sole agency carrying on general insurance business. GIC, however, implements the scheme, only as an agent, on behalf of the Government of India/state governments which are bearing the entire liabilities in respect of the insurance claims.

16.35 With the introduction of insurance premia on an actuarial basis to make the scheme viable, the organisation implementing the scheme would have to assume the financial responsibility for the scheme, which GIC as presently constituted may not be able to assume. GIC itself could be suitably restructured so that with its past experience it may assume the financial responsibility of the crop insurance scheme. However, considering the GIC's

heavy involvement in its primary task of general insurance business, loading it further with the full responsibility, including financial responsibility, of implementing the crop insurance scheme, is likely to make its range of activities too unwieldy. The policy pursued in India in the area of institution building has been one of decentralisation; whenever any activity/function, has assumed special importance, which calls for a greater degree of administrative and financial involvement, a separate organisational structure, appropriate for the enlarged function, has been set up. Thus, when industrial development and financing thereof came to assume a degree of importance to warrant whole time attention of a specialised institution, the functions were hived out from RBI and the Industrial Development Bank of India (IDBI) was established, as an altogether separate institution. So was the case in the area of agricultural credit where the functions of Agricultural Credit Department of RBI and Agricultural Refinance and Development Corporation (ARDC) (which was an associate institution of RBI) were hived out to form the NABARD. On similar lines, and as an exercise in decentralisation, we would recommend that Government of India may set up, under an act of Parliament, a separate corporation for carrying out the crop insurance scheme.

16.36 Finally, we recommend the setting up of an Expert Committee consisting of actuaries, insurance experts, accountants, agronomists, meteorologists, agricultural economists, etc. to conduct a comprehensive study of the proposed crop insurance scheme, with a view to operationalising the scheme. Some of the aspects in need of the study are those indicated in this Chapter such as, the entire rationale and justification for adopting a crop insurance scheme in the Indian, context, the threshold yield (Para 16-23) (i), whether area approach or a modified area approach or individual approach (para 16-28 (ii), the administrative machinery and its viability, premium rates and subsidies (para 16-28) (iii), the amount insured (para 16-32), incidence of risks and rates of losses. It is also recommended that the rationalisation of the Credit Guarantee and the Deposit Insurance Schemes as well as various issues raised in relation thereto in the following chapter be included in the terms of reference of the aforesaid Committee.

CHAPTER XVII

RISK IN AGRICULTURAL LENDING - CREDIT GUARANTEE COVER

Credit Guarantee Schemes

In the context of larger and larger involvement of the commercial banks, in lending for the priority sector with a major shift in emphasis away from security based loaning approach since the early seventies, it was considered necessary to provide some incentives to them so as to cover the increasing risk of losses entailed in such loaning. The Credit Guarantee Corporation of India Ltd. (CGCI) was accordingly established by the Reserve Bank of India, in January 1971, as a public limited company under the Companies Act, 1956, to provide guarantee cover to the lending institutions against the risks involved in lending for the priority sector including lendings to small agricultural borrowers. About a decade earlier, in January 1962, RBI had already established the Deposit Insurance Corporation (DIC) as a wholly owned subsidiary of the Reserve Bank of India, to provide some measure of protection to depositors, particularly the small depositors from the risk of loss of their deposits arising from bank failures. Since the aims of both the corporations were cognate in that both sought to extend a measure of protection, one to the banks and the other to the depositors and as the resources of DIC were comparatively larger than those of CGCI, it was considered advantageous to merge these two institutions. The Deposit Insurance Corporation, thus took over the undertaking of the Credit Guarantee Corporation of India Ltd. with effect from 15th July 1978 and the Corporation was renamed Deposit Insurance and Credit Guarantee Corporation (DICGC). The transfer was effected to integrate the twin and cognate functions of giving protection to small bank depositors and providing to banks, guarantee cover for their credit facilities to certain categories of small borrowers belonging to the weaker sections of the community.

17.02 The DICGC is a wholly owned subsidiary of Reserve Bank with a paid up share capital of Rs.50 crores, contributed entirely by the Reserve Bank. The Corporation maintains three funds, viz., General Fund, Deposit Insurance Fund and Credit Guarantee Fund. The share capital of the Corporation is held in the General Fund and the establishment and other administrative expenses are met entirely from the interest on investments made out of this Fund.

The Deposit Insurance Fund is built up by the premia received from the insured banks and augmented by interest earned on the Fund investments. The Deposit Insurance Fund is utilised exclusively for meeting the deposit insurance claims. To the Credit Guarantee Fund on the other hand are credited guarantee fees received and interest on investments made out of the Fund. The Credit Guarantee Fund is used solely for meeting the credit guarantee claims. The amounts to the credit of these funds to the extent they are not required for the immediate use under the two schemes, are invested in securities of the Central Government as required by law. Repayments received by the Corporation by virtue of its rights of subrogation, in regard to the insurance and guarantee claims paid, are credited back to the respective funds. Nevertheless Section 25A of the DICGC Act does permit the Board to transfer/utilise amounts from the Deposit Insurance Fund to the Credit Guarantee Fund and vice-versa subject to certain safeguards. We are, however, concerned in this chapter mainly with the guarantee schemes operated by the Corporation.

17.03 Among the guarantee schemes introduced by the Corporation, the Small Loans Guarantee Scheme, 1971, in force since April 1971, covers, among others, the credit facilities granted by commercial banks and RRBs to farmers and agriculturists. The Small Loans Guarantee Scheme, 1971 covers advances granted to borrowers undertaking various types of agricultural and allied activities such as raising of crops, poultry farming, pisciculture, dairy farming, animal husbandry, etc. The guarantee cover has been varying from time to time; currently with effect from 1 January 1985 the guarantee cover is provided at 60 per cent of the amount in default. The Corporation does not guarantee losses to the full extent of default; its liability is limited to certain ceilings prescribed for the purpose. The ceilings operative till 31st March 1989 were as indicated in table 1. The rate of guarantee fee till 31st March 1989 was 0.75 per cent per annum, with a concessional rate of 0.50 per cent per annum in the case of small borrowers having credit facilities not exceeding Rs.25,000 in the aggregate per borrower and 0.25 per cent per annum for RRBs for five years from the date of joining the scheme. The guarantee fee has since been raised with effect from 1 April 1989 to 1.50 per cent per annum on a uniform basis.

Table 1

Ceilings on Claim Liability Prescribed by Corporation

<u>Activity</u>	<u>Ceiling on claim</u>
<u>Farmers and Agriculturists</u>	Rs.
i) Seasonal agricultural operations	2,500
ii) Reclamation or improvement of land, construction and deepening of irrigation wells, installation of pumpsets for drawing water, purchase of cattle, machinery or equipment or the acquisition of any other capital assets (or for repairs to these assets)	10,000
iii) Conversion of facility granted for financing of seasonal agricultural operations due to famine, flood, etc. into a term or instalment credit	7,500
iv) Pisciculture	37,500
v) Sericulture	18,750
vi) Animal Husbandry	15,000
vii) Poultry Farming	22,500
viii) Dairy Farming	15,000
ix) For acquiring shares in any co-operative society or in any other body corporate engaged in the manufacture of sugar or in any other processing activity	1,000

17.04 Later in 1982, the Small Loans (Co-operative Credit Societies) Guarantee Scheme was formulated with a view to providing guarantee cover for advances granted by co-operative credit institutions at the primary level for agriculture and allied activities. The scheme was offered on a pilot basis to :

- (i) Primary agricultural credit societies with 'A' or 'B' audit classification continuously for the past three years and having full-time paid secretaries and affiliated to district central co-operative banks enjoying 'A' class audit classification for a similar period of past three years; and

- (ii) PLDBs/branches of SLDBs with overdues not exceeding 25 per cent of demand and having unrestricted eligibility for fresh lending continuously for the past three years.

Although, 2,476 PACSs, 159 PLDBs and 200 branches of SLDBs were found to be eligible for participation in the scheme, only 14 PACSs and four PLDBs had evinced some interest, but had not till December 1988 executed the necessary agreements. Thus, this scheme had not evoked sufficient interest and had failed to take off in the case of co-operatives.

17.05 Some general comments about the guarantee cover may be made at this stage. These, briefly are :

- i) Although the Small Loans (Co-operative Credit Societies) Guarantee Scheme (1982) was introduced for the benefit of co-operatives, it has failed to take off and, therefore, the agricultural loaning of the co-operative banking structure has remained almost outside the purview of the credit guarantee cover. The reasons adduced for this are:
 - a) the scheme was extended only to societies with audit classification of 'A' and 'B' affiliated to 'A' class banks and not to all the societies. The co-operators resented this, as no invidious distinction of this kind had been made in the case of commercial banks and in fact even in the case of regional rural banks.
 - b) The co-operators felt that the rate of guarantee fee at 0.65 per cent was high and this cut into the slender interest margins enjoyed by the co-operatives.

We are of the view that the co-operative credit structure which plays an important role in catering to the credit needs of the agriculturists, majority of whom belong to the weaker sections and are small/weak farmers, should be brought under the purview of the guarantee schemes. We recommend that DICGC should formulate a suitable scheme covering all the co-operative credit institutions at the primary level more or less on the same lines as the Small Loans Guarantee Scheme applicable to Commercial Banks and RRBs.

- ii) The ceilings laid down by the DICGC in respect of the maximum claim liability of the Corporation for a borrower, (e.g. Rs.2,500 for seasonal agricultural operations or Rs.10,000 for term loans for investments in agriculture, etc.) fixed as far back as in 1971 were found to be too low in the present context. Considering the increase in the scales of finance/unit costs in the last 15 years following escalation in the general price level, DICGC has taken a decision to raise these ceilings as follows, effective from 1 April 1989 :

<u>Loans to farmers and agriculturists</u>	<u>Earlier Ceiling</u>	<u>Revised Ceiling</u>
i) Crop loans	Rs. 2,500	Rs. 10,000
ii) Loans for developmental activities	Rs. 10,000	Rs. 20,000
iii) Conversion loans	Rs. 7,500	Rs. 30,000
Overall ceiling in respect of loans to farmers and agriculturists	Rs. 37,500	Rs. 60,000

We would recommend in this connection that DICGC should periodically review these ceilings to take into account the cost escalation and revise them appropriately. We would also recommend that the revised ceilings, effective from 1 April 1989, may be submitted for a review, to the Expert Committee of Actuaries, Accountants, Agricultural Economists, etc., the constitution of which is recommended in paragraph 16.36 of Chapter XVI.

Impact of Guarantee Cover

17.06 It may be difficult to establish any direct relationship between increase in volume of credit and availability of the guarantee cover, but over the years, there has been a substantial step up in the flow of institutional credit to the weaker sections of the community covered by the guarantee schemes, which may have been difficult to achieve without the guarantee cover. Further, over the years, the DICGC has extended guarantee cover for credit facilities granted even prior to the introduction of this scheme. The Corporation's schemes have also covered advances to landless agricultural labourers, medium-term conversion loans, loans for purchase of shares in co-operative sugar factories, gobar gas plant loans, etc. This has served as an incentive to the banks to increase and diversify credit to the non-traditional sectors and small borrowers.

As a result of the increased level of loans granted by the banks to the farmers, the guaranteed advances of the Corporation increased year after year and with them also the amount of claims lodged.

Viability of the DICGC

17.07 There has been a phenomenal rise in the level of advances guaranteed under the Corporation's guarantee schemes from Rs.208 crores in 1972 to Rs.18,854 crores at the end of 1987. As regards agriculture and allied activities, the guaranteed advances to the farmers and agriculturists which stood at Rs.134.67 crores in 1972 at the inception of the scheme have registered a rise to Rs.6,428.29 crores forming 58.4 per cent of the total guaranteed advances at the end of June 1987. The percentage share of the agricultural advances guaranteed had declined from 65.5 per cent in 1972 to 58.4 per cent at the end of June 1987. This is mainly because the proportionate share of other types of advances such as transport operators, retail traders, had shown an increase.

17.08 As a result of the increased loans granted by banks as reflected in the increase in the quantum of guaranteed advances, the amount of claims lodged with the Corporation and paid by it has also shown an increase, in the last five to six years, as may be seen from the table 2:

Table 2

Guarantee Fees Collected, Guarantee Claims Lodged and Paid by Corporation

<u>Year</u>	<u>Guarantee fee receipts</u>	<u>Guarantee claims lodged</u>	<u>Claims paid</u>
1982	57.67	34.11	12.86
1983	71.17	60.42	21.37
1984	87.91	115.69	40.90
1985	105.66	186.90	83.86
1986	127.25	245.86	110.96
1987	145.17	386.95	211.01

The guarantee claims submitted by the credit agencies far exceeded the guarantee fees received by the Corporation continuously from the year 1984 and in 1987 the claims actually paid by the Corporation had also exceeded the guarantee fees received and formed 145 per cent of the latter. In regard to agricultural advances, while the amount of guaranteed advances rose from

Rs.845.64 crores in the year 1977 to Rs.6020.34 crores in the year 1986 i.e. seven-fold, the claims lodged increased at a much faster pace from Rs.4.32 crores to Rs.78.16 crores i.e. twenty-fold during the same period. Both, in terms of number and amount, the claims have shown a phenomenal increase. The number of accounts and amounts of such claims, which were 14,056 for Rs.4.32 crores in 1977 increased to 3,54,063 involving an amount of Rs.78.16 crores at the end of 1986. As a percentage to guaranteed advances, the claim receipts have steeply increased from 0.5 in 1977 to as much as 1.30 in 1986 and further to 2.00 in 1987. The sizeable increase in the claims lodged is stated to be due to the simplification of the claim procedures by the Corporation during the period and the increasing awareness and familiarisation amongst banks with procedures for the invocation of guarantees. The analysis of the claims received during the calendar years 1984, 1985 and 1986 according to the amounts shows that claims upto Rs.2500 accounted for a major portion of the claims received. The percentage of such claims was 79.2 (numberwise) and 47.80 (amount-wise) in 1986 for commercial banks; the corresponding percentages for RRBs were 79.6 and 54.9. Another interesting feature is that while the percentage of overdues to demand during the last four years has remained static (ranging from 45 per cent to 48 per cent), the percentage of claim receipts of the total guaranteed advances has steeply risen from 0.47 to as much as 1.30 during the same period. The analysis of claims lodged according to reasons, as indicated by the concerned banks for loans becoming doubtful of recovery reveals that the highest percentage of loans becoming bad or doubtful of recovery has been on account of 'wilful' defaults by the borrowers. The percentage of such claims (number-wise) which was 26.46 in 1984 has gone upto 44.80 in 1986 the respective percentages (amount-wise) worked out to 27.92 and 47.66. This could be ascribed to the general deterioration in the recovery climate in the country.

17.09 The Corporation had a deficit of Rs.202.30 crores in the Credit Guarantee Fund for making adequate provision to meet the liability on account of the claims lodged upto 31st December 1987. Thus, the Corporation had to resort to transfer, albeit temporarily, of an amount of Rs.264.72 crores from the Deposit Insurance Fund to the Credit Guarantee Fund to enable

Corporation to meet the guarantee claims for the year 1987. All the three funds together viz. the Deposit Insurance Fund, the Credit Guarantee Fund and the General Fund at the disposal of the Corporation in the aggregate also showed a net deficit of Rs.134.70 crores after providing for liabilities on an actuarial basis. The financial position of the Corporation had steadily deteriorated as became evident in its working results during the year 1987 which showed that the operations of the three funds showed an excess expenditure of Rs.78.89 crores over income.

17.10 It is thus clear that operation of the credit guarantee schemes under the existing dispensation is not a viable proposition so far as DICGC is concerned as not only the claims lodged but also those actually paid far exceed the guarantee fees received. The difference between the claims lodged and those paid represents claims pending processing or those awaiting clarification, bulk of which is eventually paid, the percentage of claims rejected to the claims lodged being only 2.5 in the case of small borrower schemes and four under SSI schemes. The percentage of claims lodged to guaranteed advances worked out to two at the end of 1987 (the percentage being 2.3 in respect of Corporation's Small Borrower Schemes, and 1.7 for SSI Schemes) whereas the rate of guarantee fee effective from 1st April 1989, was 1.5 per cent on a uniform basis.

17.11 The situation has led to the question being raised whether the provision of the guarantee cover which was initially intended to induce the banks to lend to the priority sectors has any relevance in the changed context when banks are required under directives from the Reserve Bank to ensure that their advances to the priority sector constitute a specific percentage of their total loaning. There is also the apprehension that the DICGC cover is counter-productive since this has resulted in complacency among the banks and they tend to be lax both in the appraisal of loan proposals and recovery efforts in respect of advances coming under the purview of the guarantee cover. We are, however, not inclined to agree with this perception. In our view, the risks involved in lending to the weaker sections/priority sectors on preferential terms, relaxing the usual norms of security, etc. do exist irrespective of whether the banks have any option or are compelled to finance these sectors upto the prescribed levels. In fact, in the latter case the risks, becoming unavoidable

are required to be borne and provided for by the banks. Similarly, lacuna regarding slackness in recovery could be remedied by making adequate recovery efforts a pre-condition for invocation of the guarantee cover. In our view, the risks entailed in the priority sector lending, as envisaged, are indispensable and, therefore, the guarantee cover has become an imperative for affording protection to the banks and their depositor clientele. The question that needs to be squarely addressed, in this context, is how best to ensure the viability of the Corporation's guarantee schemes, without jeopardising the viability of the credit institutions.

17.12 We are also of the view that the expedient resorted to by the Corporation such as transfer of amounts from the Deposit Insurance Fund to the Credit Guarantee Fund, in the long run is likely to do more harm than good as it jeopardises, in the process, the viability of the Deposit Insurance Scheme as well. The Expert Committee (July 1989) constituted by the DICGC has recommended that the Deposit Insurance Fund should be maintained at a level of 0.50 per cent of the total insured deposits, which worked out to Rs.377.56 crores at the end of June 1989. However, the fund got reduced to a level of Rs.84.13 crores as a result of transfer of Rs.264.72 crores to the Credit Guarantee Fund during the year 1987. When banks are already faced with competition from various alternative instruments of investments available to the Public, there should be no compromise with the viability of the Deposit Insurance Scheme, even on a temporary basis, lest it should affect the ability of the Corporation to meet the deposit insurance claims as and when they arise. The Corporation should, therefore, refrain from transferring amounts from Deposit Insurance Fund to the Credit Guarantee Fund. With a view to preclude such transfers, beyond certain limits which may be fixed, we would recommend that the provisions under section 25A of the DICGC Act be suitably amended.

17.13 Further, we feel that repeated transfer of amounts from one fund to another is entailed when one fund is continuously in deficit (the accruals to it falling short of the drawals thereon on a year to year basis) while the other continues to be in surplus. Since contributions to both the funds (viz., the Credit Guarantee Fund and the Deposit Insurance Fund) are forthcoming mainly from the banking institutions, it should be possible to build up these

funds to the requisite levels with reference to the actual draft thereon. We, therefore, consider it necessary that the deposit insurance premia and the credit guarantee fees be fixed on an actuarial basis for building up the relative funds to appropriate levels so that the accruals to them match the withdrawals therefrom, on a year to year basis.

17.14 For mitigating the problem of the Corporation's viability, the following courses merit consideration:

- i) rationalisation of the terms for invocation of the guarantee cover;
- ii) increase in guarantee fee; and
- iii) Government share in higher guarantee fees particularly in respect of credit facilities to 'risk' prone borrowers under government sponsored schemes.

1) Rationalisation of terms

17.15 Presently, a credit institution has to comply with the following three conditions for invoking the guarantee cover :

- a) The advance under guarantee has not been repaid within one month from the date on which the notice of demand for repayment of the entire dues has been served on the borrower;
- b) The advance is treated by the credit institution as bad or doubtful of recovery; and
- c) It is provided or accounted for as such in the books of the credit institution.

In many cases the credit agencies invoke the guarantee within a period of one to three years from the date of defaults and cases are not rare when credit agencies have invoked guarantee cover within one year from the date of disbursement of the original advance. The Corporation's guarantee cover is against bad advances and not against mere defaults and it cannot be said that, in all such cases, the advances would necessarily have turned bad or doubtful of recovery or even credit agencies would have exhausted all possible

avenues for recovery including legal action for acquisition of the assets created out of the loan. Since it will be virtually impossible for the Corporation to verify whether courses open to the credit agency for recovery have been exhausted (this at best could be test checked only at the time of statutory inspections of the banks/branches) the Corporation may lay down the following two further conditions for invoking the guarantee cover :

- i) a period of three years should have elapsed between the due date for loan/instalment(s) of loan and the invocation of guarantee ;
and
- ii) the credit agency should have exhausted all possible avenues of recovery including legal action against the borrowers.

This would ensure that banks take adequate measures for recovery before invoking the guarantee cover.

17.16 Data in tabel 2 show that there has been a steep rise in the claims lodged with the Corporation from year to year. As indicated earlier, while invoking the guarantee cover the credit institutions are required to furnish to the Corporation a certificate that the specific advance in respect of which claim is lodged is bad or doubtful of recovery and that it has been provided or accounted for as such in the books of the banks. The Corporation scrutinises/settles the claims on the basis of such certificates but it has not been verifying the bonafides of the certificates to satisfy itself regarding the genuineness of the claims. Considering the ever increasing volume of claims and financial liability entailed, we feel that it is necessary for the Corporation to test-check the claims lodged i.e. undertake detailed investigation into a small sample of claims lodged by deputing its staff to visit branches of concerned banks/lending agencies, inspect their records, if not, interview the concerned borrowers, etc. to satisfy itself independently that the credit agency has taken necessary steps for recovery and that the concerned advances are in fact irrecoverable. For this purpose, we recommend that the Corporation may establish a suitable administrative machinery for test-checking the claims lodged.

II) Increase in Guarantee Fees

17.17 The measure at (i) above may help give more time for recovery of the loans reducing the number and amount of claims to some extent but it may not be an adequate solution to the problem of Corporation's viability. This is because the quantum of bad debts under guaranteed advances is likely to be much higher than what would be taken care of by the existing guarantee fees. Talking of agricultural advances, in respect of which data are readily available, we find that an estimate of overdues of over seven years (a large portion of which is likely to turn irrecoverable) under agricultural advances by commercial banks, RRBs and co-operatives aggregated Rs.526 crores as on 30.6.86 and formed 3.2 per cent of the respective outstandings at Rs.16,409 crores. With effect from 1st April 1989 the Corporation has increased the guarantee fee to 1.5 per cent on a uniform basis in respect of all guaranteed advances. This increase may not, however, be adequate to ensure the viability of the Corporation's guarantee schemes. Certain projections attempted by the Corporation on the basis of the past trends show that the level of guaranteed advances may rise from Rs.18,854 crores in 1987 to around Rs.40,300 crores in 1991 and the corresponding claims that would be lodged would rise from Rs.387 crores in 1987 to around Rs.755 crores in 1991. Even with the increased rate of guarantee fee at 1.50 per cent on a uniform basis, the guarantee fee receipts estimated at Rs.605 crores may still fall short of the estimated claims by Rs.150 crores in the year 1991, besides leaving uncovered the gap of about Rs.265 crores in the Guarantee Fund which existed at the end of 1987. With a view to ensuring the viability of the Corporation's guarantee schemes, it is necessary that the guarantee fees are determined on an actuarial basis so that the accruals to the Credit Guarantee Fund would match with the claims made thereon in any year. In this connection, we recommend that the issue of determining the appropriate guarantee fees may be referred to the Expert Committee consisting of the actuaries, accountants, agricultural economists, etc., the constitution of which we have recommended separately in paragraph 16.36 of Chapter XVI.

17.18 While a rise in the guarantee fee, that may be necessary, may help ensure the viability of the Corporation, the adverse impact thereof on the viability of the credit agencies cannot be ignored. Our analysis of the lending costs and margins available to the credit agencies under agricultural loans

shows that the lending agencies are already facing constraints of margins in the rate of interest vis-a-vis transaction costs involved and, therefore, in our view, they have no capacity to absorb at their level any further increase in the guarantee fees. While we are recommending, in a separate chapter, increase in the interest margins to the credit agencies at different levels to take care of the transaction costs, risk costs, etc. these margins will still be inadequate if the credit agencies are called upon to bear, at their level, the increase in the guarantee fees. We, therefore, recommend that the guarantee fee liability of the lending agencies be limited to 1.5 per cent, as at present. As regards any increase in the guarantee fees that will be entailed after the fees are determined on an actuarial basis, it is our view that this should be subsidized by Government in view of the fact that the claims on the scale they arise at present are mostly on account of the higher risks involved in the mandatory nature of the priority sector lending, the credit agencies are called upon to undertake.

III) Government assistance for guarantee fees

17.19 While the above measures may take care of viability of the Corporation in respect of a major portion of the guaranteed advances, the Corporation's ability to meet liabilities arising out of advances under the poverty alleviation programmes might still be in doubt. Unlike other advances, these are issued, prima-facie, to borrowers who are more risk-prone. The programme no doubt envisages that the borrowers would, with the help of credit/assets provided, lift themselves above the poverty line, but past experience shows that the incidence of overdues in respect of these loans is heavier than that under agricultural loans and, therefore, a larger portion of such advances is likely to turn out to be bad or doubtful of recovery. It would be beyond the scope of credit agencies with the limited margins available to them, to bear higher guarantee fees calculated separately, on an actuarial basis, that such lending may entail. We fail to see any solution to this impasse - that is, ensuring the viability of the Corporation and also at the same time that of the lending agencies - other than government stepping in to bear either (i) the difference between the higher guarantee fee entailed in respect of loans under the poverty alleviation programmes taking into account the incidence of bad debts under these advances and the normal guarantee fee, or (ii) provide to the commercial banks (including RRBs) risk fund contribution at two per cent of the loans disbursed under poverty alleviation schemes.

Exemption from Income Tax

17.20 Another factor which requires reconsideration is the Government decision to subject the Corporation to the Income Tax. Till the year 1986 the Corporation remained outside the purview of the Income Tax Act. The Corporation has, however, been advised that it will no longer be exempted from the provisions of Income Tax Act from the year 1987. The Corporation is essentially a service institution which operates on a "no profit" basis and declares no dividend. Any income which the Corporation earns is only notional inasmuch as the entire surplus is appropriated towards building up of the Deposit Insurance Fund and the Credit Guarantee Fund. The Corporation is working solely for ensuring operationalisation of Government's Social objectives; institutions like IDBI, NABARD engaged in pursuit of like objectives have been exempted from liability to pay Income Tax, Surtax and any other taxes in respect of income, profits and gains accruing to them. In addition, the Corporation is insulating primarily the nationalised banks against losses incurred on loans advanced under state directives in the fulfilment of the Government's social objectives. In the circumstances, we do not see any rationale in the Government taxing the Corporation and hence we recommend that Government of India should grant exemption to the Corporation from payment of Income Tax, Super tax or any other tax on its income, profits and gains, on a permanent basis.

Establishment Expenses

17.21 The Corporation's staff and establishment expenses have also been rising; they increased from Rs.1.73 crores in 1984 to Rs.4.81 crores in 1987. We suggest that at least during the next five to six years i.e. till the end of VIII Plan, the RBI should bear the entire cost of the staff of the Corporation. This measure would provide much needed financial relief to the Corporation and help it in building up its funds. After all, the Corporation is a fully owned subsidiary of Reserve Bank of India from which bulk of its staff has also been drawn.

PART VI

CERTAIN CRITICAL ISSUES RELATING TO CREDIT SYSTEM

XVIII INTEREST RATES, COSTS AND MARGINS

XIX AUTONOMY OF CREDIT INSTITUTIONS

CHAPTER XVIII

INTEREST RATES, COSTS AND MARGINS

One of the basic functions of banks is to facilitate the channelling of funds from the 'savers' to the 'users'. This intermediation by the banks has therefore necessarily to aim at providing the best possible returns to the 'depositors' who are the savers, at minimum cost to the 'borrowers' who are the users of the funds. The structure of financial intermediation thus comprises the savers (depositors), the users (the borrowers), and the banks (the intermediaries), functioning in symbiotic relationship with one another. Implied in this intermediation process is also a fair trade off between the two objectives of maximum returns to the savers and minimum cost to the borrowers. However, in order that resources (savings) are effectively mobilised, it needs to be ensured that the interest offered to the savers is (a) attractive enough to have a preference for bank deposits as compared with alternative avenues of investment, and (b) these resources are lent to the borrowers for viable projects who are able to generate enough surpluses with the use of such funds so that they could both repay the loans on time and pay the interest on the loans at rates sufficient for the banks to meet the operational costs and make adequate profit. This, no doubt, assumes a wholly market oriented environment and not when markets are distorted as it is in the Indian context, owing to serious maldistribution of incomes and a host of other factors and therefore, needs correction. It is in this background that an administered rate structure came to be evolved in the Indian banking system. The main objective of the system so evolved has been to work towards maximising the return on their deposits to the savers while subserving the objective of extending credit to preferred sections and sectors at concessional rates. But this policy has not been without its serious adverse effects. Commenting on these adverse effects, the Sukhamoy Chakravarty Committee (1985) appointed by Reserve Bank of India (RBI) to review the working of the monetary system noted (page 173 of the Report) that among others :

- i) the administered interest rate system has grown to be unduly complex and contains features which have reduced the ability of the system to promote the effective use of credit;

- ii) concessional rates of interest appear to have allowed projects of doubtful viability to be undertaken;
- iii) the policy of insulating the banks from price competition to customer service has not served to promote high standards of customer service; and
- iv) the administered interest rate system has been found to be lacking the flexibility necessary for augmenting the pool of financial savings by effecting suitable changes in the deposit rates from time to time as the low profitability of banks has made banks wary of increasing the average cost of deposits.

18.02 The Committee, also noted that in the present stage of development of Indian money market and capital market, interest rates cannot be left entirely to market forces to determine. A fair degree of regulation is necessary so as to provide for an orderly mobilization of financial savings for the purpose of planned economic development as well as in the interest of viability of operations of banks of widely ranging sizes in terms of deposits and advances and differing greatly in regard to the quality of their human resources. We are in agreement with the basic approach of the Committee in regard to administered rates. While recognizing thus the inevitability of a certain degree of regulation, the system of administered interest rates, requires to be suitably modified so as to eliminate its adverse effects on profitability of banks, atleast substantially if not fully. This has assumed a sense of urgency since the changes in the last few years resulted in lowering the interest rates on loans but at the same time increasing the rates on deposits. These have in fact, had the contrary effect as brought out in the statement given on the next page. It will be observed from the statement that while the cost of deposits increased, the interest rates on agricultural loans (short-term) showed a declining trend. Further, this reduction has been of the order of two to three percentage points for different loan slabs resulting in the overall lower interest income to the credit system from agricultural advances.

Maximum interest payable on deposits with commercial banks					Interest rate on short-term agricultural advances (Direct loans)				
Date	Savings deposits	Short-term deposits upto 90 days	Fixed deposits		Date	Upto Rs.5000	Rs.5001 to Rs.15000	Rs.15001 to Rs.25000	Over Rs.25000
			91 days and more but less than 1 year	Maximum					
1.3.81	5.00	3.00	7.00	10.00	2.3.81	12.50		15.00	17.50
1.3.82	5.00	4.00	7.00	10.00	1.4.83	11.50		14.00	16.50
26.10.82	5.00	4.00	7.00	11.00	20.10.83	11.50	12.50	14.00	16.50
8.4.85	5.00	8.00	8.00	11.00	1.4.85	11.50	12.50	14.00	16.50
27.5.85	5.00	4.00	8.00	11.00	1.4.87	11.50	12.50	12.50 to 14.00	14.50 to 15.50
1.4.87	5.00	4.00	8.00	10.00	1.3.88	10.00	11.50	14.00	15.50
4.4.88	5.00	4.00	8.00	10.00	10.10.88	10.00	11.50	12.50 to 14.00	
27.3.89	5.00	6.00	8.00	10.00	1.3.89	10.00	11.50	12.00	14.00 to 15.50

As on 30th June 1989 the interest rates on deposits and loans to agriculture (direct) stood as under :

Deposits

<u>Category</u>	<u>Rate of interest</u> (per cent)
Current	Nil
Savings	5
Term	
46 days to less than 1 year	6 to 8
1 year to less than 2 years	9
2 years and above	10
SCBs, DCCBs & RRBs can pay 1/4 to 1/2 percent more.	

Loans and Advances (direct) to Agriculture

<u>Category</u>	<u>Rate of interest</u> (per cent)
A. <u>Short-term loans</u>	
Upto Rs.7,500	10.0
7,500 to 15,000	11.5
15,000 to 25,000	12.0
Above 25,000	14 to 15.5
B. <u>Term loans</u>	
<u>Purpose</u>	<u>Rate of interest</u> (per cent)
a) Minor irrigation & land development	10.0
b) Investment for diversified purposes for borrowers other than small farmers	12.5
c) For small farmers	10.0

18.03 Profitability, it is well recognized, is a function of the spread available to the banks between the rates of income and expenses. The spread in turn depends upon (a) the cost of raising resources comprising deposits and borrowings (the lower the cost, higher will be the spread), (b) the income earned on the

investments and loans made out of the resources (the higher the income, higher will be the spread), while the profitability will be a function additionally of the internal efficiency of the bank and the volume of business handled, (the higher the efficiency and the larger the volume, the higher will be the profitability.

18.04 It is thus obvious that a bank will get a higher spread or a margin, if the cost of raising deposits and borrowings could be reduced. However, borrowings at concessional rates will adversely affect the higher financing institutions and lower rates of interest on deposits will wean the depositors away from banks to other institutions where higher and more positive real interest rate is available. There is, therefore, very little that the banks can do to reduce the cost of resources. Moreover the cost cannot be reduced in the face of the Government offering more attractive rates on their borrowings and allowing such rates on public sector bonds. In fact, there is some justification even to improve the interest rates on deposits. But these are not static positions and will change with change in the environment.

18.05 With such a wholly regulated interest rates both on deposits and loans and advances, the banks have virtually no control over either the costs of raising the resources or the income they could earn by lending the same to the various sections of borrowers. The only course open to the banks, if they have to keep their head above the water is therefore to bring down the operational costs to as low a level as possible. But the banks' ability to do so is considerably restricted because of the ever increasing establishment costs following the continuous hikes in wages and the phenomenal expansion of branches undertaken, again, under state directive. The net result is the progressively declining profitability of the banks. We have, therefore, the intractable problem of low margins in both the commercial and co-operative banking systems. The basic question thus is how in the face of such heavy odds, profitability could be increased.

18.06 The Government and the Reserve Bank have fixed the interest rates on various types of loans and advances. Further, they have also prescribed certain quantitative targets for the credit to be made available to different sectors at Concessional rates of interest which are either below or only marginally above the cost of raising resources by banks. Though the banks have lately been

allowed some freedom to charge a higher rate of interest to certain classes of borrowers, in practice their ability to do so is limited. Cross subsidisation which is a logical corollary of concessionality of interest or in other words, the preferential treatment to priority sectors, would also not be possible on an unlimited scale even to the commercial banks and is totally non-existent for the RRBs while it is only marginal in the case of co-operatives. Clearly, therefore, the banks will not be able to earn adequate income to ensure their viability unless interest rates on loans which at present are uneconomic are adequately raised.

18.07 It is known that the higher the internal efficiency and the larger the volume of business, the higher will be the margin available to a bank. This is so because the cost per unit of operations, would in this event be lower. But the point to note in this connection is that there are severe limitations on a bank's ability to so reduce the costs since it has been found from the case studies undertaken by us that the establishment costs i.e. man-power and related costs form about 80 per cent, while the other overhead costs consisting of rent, post and telegraph, telephone charges, taxes, legal expenses, stationery etc. form practically the whole of the balance 20 per cent of the total operational costs leaving little or no scope for any reduction on this score. A bank's ability to work on cost reduction measures is therefore confined to improving efficiency through simplified procedures, greater decentralisation and increasing mechanisation and computerisation. Unit cost reduction could come about also through an increase in the volume of business. Thus while banks will need to closely watch their operational costs and take effective measures to reduce these as part of ongoing operations, they must simultaneously also diversify their activities and services so that the volume of business increases substantially to reduce the per-unit cost of their operations. The answer to low margins would therefore largely lie in the success they achieve in this vital area of improving internal efficiency and productivity which at present is by and large, considered low by international standards.

18.08 Although efforts with all the inherent limitations on these at improving the volume of business and the internal efficiency calls for the urgent attention of the banks' managements, there is need to have a serious second look at the administered lending rates especially in the area of concessionality. Commenting

on this the Sukhamoy Chakravarty Committee (1985) has said as follows :

"The impact on profitability of banks and other financial institutions of interest policy, based on widespread use of concessional interest rates, needs to be recognized. In the interest of promoting effective use of credit on the one hand, as also operational efficiency of lending agencies on the other, it would appear that in the present structure of interest rates, there is considerable scope for eliminating concessional interest rates or reducing the extent of concessionality, apart from reducing the number of categories for which different concessional rates are specified.

The objective of improving productivity in the industrial and agricultural sector calls for a reorientation of the present interest rates structure with a view to permitting more efficient use of funds by the borrowers."

18.09 On the specific question of the administered interest rates the Chakravarty Committee had made certain suggestions. The relevant recommendations are given below :

	<u>Nominal interest rates</u>
Bank deposits with a maturity of 5 years or more	Expected long-term inflation rate + positive real rate of return of not less than 2 per cent per annum. The nominal rate to be determined by the RBI as the maximum rate payable on bank deposits.
Basic (minimum) lending rate of banks	Maximum nominal deposit rate fixed by the RBI + 3 per cent per annum, banks being free to adopt higher lending rates.

Apparently, the Committee wanted RBI to fix only a maximum rate for deposits and a minimum rate for loans and advances, leaving other rates to the banks to decide. If the above recommendations are to be given effect to, under the existing conditions the basic (minimum) lending rate will work out to 13 per cent, since the maximum rate of interest on deposits presently fixed by RBI is 10 per cent. Even this will mean an increase of three percentage points over the lowest rate of 10 per cent charged to the ultimate borrowers in agricultural sector since 1st March 1988. As regards the banks' lendings to the priority sector, the Committee has observed that there was need to rationalise the number of concessional rate categories. The Committee was not inclined to

recommend more than two rates for the concessional loans, one being equivalent to the basic minimum lending rate and the other (to be determined by RBI consistent with Government policy in respect of sectors which need somewhat preferential treatment) below this rate.

18.10 There is also a view that in the long run, concessional credit neither benefits the borrowers nor the lending institutions. Firstly projects of doubtful viability come to be financed by banks. Secondly, the borrowers become prone to misutilize or divert cheap credit for other purposes instead of investing it in the projects for which they have borrowed and end up with a default to the lending agency. The lending agencies, on the other hand, suffer from inadequate return of income on the interest rate charged and in the case of default the increased cost of supervision and recovery, apart from the risk cost of such credit as it becomes totally or substantially unrecoverable.

18.11 Another dimension to the concessionality in lending under an administered system is that the concessionality to the ultimate borrower necessarily involves larger concessionality in the refinance provided by the national level institutions like NABARD. This in turn, affects their own viability for want of adequate margins between their cost of raising resources and the cheap lending rates charged on refinance. Above all, too low a rate of interest generally tends to get equated with grants even as too high a rate comes to be equated with usury.

18.12 We have given careful thought to all the aspects of concessionality and are of the view that while in the context of present day socio-economic milieu, a degree of concessionality needs to be retained in favour of the very weak sections of the community, there is hardly any justification for continuing such concessionality in the case of other borrowers. We are also in agreement with the recommendation of the Chakravarty Committee that the interest rates structure needs to be modified reducing the extent of concessionality and the number of categories which are eligible for concessional rates at present. Accordingly in the case of loans for agriculture with which we are concerned, we propose to have only one category which will be eligible for concessionality. This would be a narrow and very clearly defined one comprising only the small and marginal farmers and other weaker sections.

(The NABARD definition may uniformly be adopted for the purpose in view of the several definitions currently in vogue). And the rate (concessional) applicable to this category will itself be fixed at 1.50 percentage points above the highest rate of interest allowed on deposits of scheduled commercial banks. We do not however envisage that this concessionality will be a permanent feature. In due course, as the weaker sections become viable borrowers (farmers/entrepreneurs) the concessionary rate of interest could be progressively withdrawn. The other category would be of the rest of the borrowers where the rate of interest will be free from central regulation, subject, however, to a ceiling which we propose be the existing maximum of 15.50 per cent. The details of these recommendations are discussed later in this Chapter.

Cross Subsidisation

18.13 Concessionality in interest rates carries with it its logical corollary of cross subsidisation. Thus under a system of administered rates which provides for concessionality for a wide range of borrowers and/or sectors, a lending institution could work at a profit only when there is scope, to the extent required, for cross subsidisation. In the three systems of banking in India viz., commercial banks, RRBs and the co-operatives, it is only in the case of commercial banks that there is real scope for meaningful cross subsidisation inasmuch as they lend to all sectors including big industry, trade, commerce etc. As for the other two systems, while the co-operatives have again some scope though limited since there is no bar on their lending to other than weaker sections, there is no scope whatsoever for the RRBs for any cross subsidisation since they lend only to weaker sections and that too at concessional rates. But even in the case of commercial banks the question arises whether the scope is unlimited and if not, the extent of such scope. These questions are examined below.

18.14 Data on scheduled commercial banks' credit classified according to in the statement given on the next page. As the data show, the main source of cross subsidisation for the commercial banks is the bracket which earns above 16 per cent return. These advances, however, seem to be showing a declining trend inasmuch as their percentage to the total advances, declined from 46.1 in June 1983 to 44.3 in June 1986.

	(Rs. crores)			
<u>Interest rate range</u>	<u>June 1983</u>	<u>June 1984</u>	<u>June 1985</u>	<u>June 1986</u>
Upto 10 per cent	1211.4 (4.8)	1516.8 (5.5)	1801.7 (5.8)	2381.5 (6.8)
Above 10 to 14 per cent	9387.7 (36.7)	10991.7 (40.1)	12790.3 (41.0)	13162.0 (37.7)
Above 14 to 16 per cent	3162.0 (12.4)	3279.0 (11.9)	3774.6 (12.1)	3933.4 (11.2)
Above 16 per cent	11794.7 (46.1)	11663.8 (42.5)	12829.3 (41.1)	15477.9 (44.3)
Total	25555.8 (100)	27451.3 (100)	31195.9 (100)	34954.8 (100)

(Figures in bracket indicate percentage to total)

Source : Report on Currency and Finance (by RBI) 1987-88

18.15 Because of the cash reserve ratio (CRR) (currently 15 per cent) and the statutory liquidity ratio (SLR) (currently 38 per cent), 53 per cent deposits are invested at an average rate of return of about 8 per cent. The SLR includes one per cent of the deposits generally held in cash on hand or in current account with other banks, earning no income at all. There is thus virtually no profit margin available to the banks on this part of deposits at all. The surplus of income, therefore, has to come from the remaining 47 per cent of the deposits invested in other assets, mainly the loans and advances. Of these only 55.5 per cent, i.e. about 26 per cent of the total deposits only, earn higher income at rates above 14 per cent to cross subsidise the losses incurred on deposits invested in CRR, SLR and mandatory credit at uneconomic rates of interest. In other words, the banks' ability to cross subsidise is rather limited and as and when the coverage of mandatory credit, as also the requirements of CRR and SLR are increased, the ability of the banks to cross subsidise, will come under severe strain. As CRR and SLR are instruments of the central bank for management of credit and monetary policy and beyond the scope of this review, we limit our recommendation to the extent and scope of mandatory credit. We recommend that considering the costs involved and their adverse effect on lending agencies, the borrowers entitled for concessional credit should be clearly defined so that the benefits do not go to any category other than those so defined.

Costs and margins

18.16 We now come to the question of costs and margins. In doing so, we are considering the issues in the light of the policy considerations spelt out in the preceding paragraphs.

18.17 Since interest rates, costs and margins are among the more important factors influencing financial viability of lending institutions, this was one of the five identified areas for specific study to be undertaken by the consultants (No. iv) The main objective of the study was to assess whether the currently available margins to various credit institutions were sufficient, taking into account the costs of their lending operations in agricultural credit and, if not, to make suitable recommendations so as to ensure that the lending institutions are assured of adequate margins.

18.18 The Study by the Consultants was based on select institutions in the different regions of the country having regard to the factors such as the proportion of gross area irrigated to the total cropped area, proportion of households reporting institutional debt, and the trend in the flow of production credit. Institutions selected for the study included Primary Agricultural Credit Societies (PACs), District Central Co-operative Banks (DCCBs), State Co-operative Banks (SCBs), Primary Land Development Banks (PLDBs) and State Land Development Banks (SLDBs) under co-operatives and the Head Offices and branches of public sector banks under commercial banks, and the Regional Rural Banks (RRBs).

18.19 Of the total number of institutions selected for the study about 80 per cent were ground level units viz. PACs, PLDBs, branches of SLDBs and branches of commercial banks. The remaining were apex and the intermediary level institutions. Keeping in view the time constraint, 315 offices in all were selected for the study. Of the 250 ground level units selected for study, 115 were co-operatives and 135 were branches of commercial banks and those of RRBs. The state-wise position of the sample units in the co-operative sector functioning at different levels is presented in table 1 while that of commercial banks is given in table 2.

18.20 Consultants II had also examined inter alia the question of costs and

margins of the different types of lending institutions. Similarly, our secretariat had also carried out, though on a restricted scale, some case studies. In our analysis of costs and margins in this chapter we have, therefore, drawn upon the data from these two studies as well.

Table 1
Coverage of the Study
(Co-operative Structure - Units selected)

State	LDB		Co-op			Number of farmers
	SLDB	PLDB	SCB	DCCB	PACS	
1.	2.	3.	4.	5.	7.	8.
1. Andhra Pradesh	1	5	1	3	14	60
2. Assam	1	2	1	1	5	30
3. Haryana	1	1	1	1	5	30
4. Himachal Pradesh	1	1	1	1	4	30
5. Kerala	1	3	1	1	4	85
6. Tamil Nadu	1	1	1	2	9	50
7. Orissa	1	4	1	2	8	70
8. Maharashtra	1	3	1	6	25	85
9. Meghalaya	1	1	1	0	3	30
10. Uttar Pradesh	1	4	1	5	13	30
TOTAL	10	25	10	22	90	500

Table 2
Commercial Banks
State-wise position of units selected

State	Commercial Banks		
	HO	RO	BR
1. Andhra Pradesh	1	2	15
2. Assam	1	1	3
3. Haryana	-	-	5
4. Himachal Pradesh	1	1	4
5. Kerala	-	-	13
6. Tamil Nadu	1	2	17
7. Orissa	1	1	6
8. Maharashtra	1	1	20
9. Meghalaya	-	-	2
10. Uttar Pradesh	1	1	20
TOTAL	7	9	105

HO - Head Office
RO - Regional Office
BR - Branch

Concepts and terms used - Definitions

18.21 The definitions of terms and concepts referred to in the study undertaken by the consultants and used in this chapter are set out below. The costs envisaged in the agricultural credit system are broadly categorised as financial costs, transaction costs and risk costs.

Financial Costs (FC)

18.22 These are the actual costs of raising the financial resources and include interest payments on all categories of deposits and borrowings in the aggregate.

Transaction Costs (TC)

18.23 The transaction costs are essentially the organisational costs for carrying out the day-to-day operations of the institutions. These comprise (i) manpower related, (ii) office/space related, (iii) statutory and (iv) others. Our consultants, have further segregated the total transaction cost of an institution into cost of agricultural credit, non-agricultural credit and non-credit activities such as trading, public distribution system and other banking activities.

Risk Costs

18.24 These could be the actual writes off or reserves created for bad and doubtful debts. The amount of claims paid by the Deposit Insurance and Credit Guarantee Corporation (DICGC) is used as an approximation to bad debts in commercial banks and regional rural banks. In respect of co-operatives, the risk costs have been arrived at as explained in paragraph 18.36.

Income

18.25 This represents interest income on agricultural loans/advances only except where the position is indicated for the institution as a whole. It must however be stated in this connection that this has certain limitations. For, these do not, strictly speaking, stand on all fours with the corresponding income component inasmuch as costs of funds are worked out on the total resources whereas the incomes relate only to earnings from agricultural lendings. Illustratively, the position is that the difference as our case studies have shown is within the tolerance limits. It is only 0.04 less in the case of SCB, 0.29 in the case of DCCB and 0.87 in the case of PACS. (vide para 18.49 (iv))

Margins

18.26 Margins are the difference between costs and income. The difference between the interest income and financial cost is the interest margin or interest spread. This is referred to as the Gross Margin (GM) or the nominal interest margin to differentiate it from the net margin (NM) which is the difference between the gross margin and the transaction cost. Margins have been worked out separately for agricultural credit business and for the institution as a whole. The study covered a period of three years viz. 1983-84, 1984-85 and 1985-86 for the co-operatives and 1984, 1985 and 1986 for the commercial banks and regional rural banks.

Co-operative Credit Structure

18.27 The average financial and transaction costs as also the gross and net margins in respect of agricultural lending by the different constituents of the credit system as brought out in the study on the basis of data collected for the years 1983-84 through 1985-86 are analysed sector-wise in the following sections.

18.28 The data in so far as they relate to the cooperative credit structure are given in table 3.

Table 3

Gross and Net Margins on Agricultural Lending

Institution	Income	Financial cost	Gross Margin	(Per Rs.100/- of loans outstanding)	
				Transaction cost	Net Margin
PACS	12.09	9.90	2.19	5.40	(-) 3.21
DCCB	11.56	7.47	4.09	3.18	(+) 0.91
SCB	9.59	7.56	2.03	1.51	(+) 0.52
PLDB	10.17	7.78	2.39	3.39	(-) 1.00
SLDB (Federal System)	7.88	6.44	1.44	1.35	(+) 0.09
SLDB (Unitary System)	9.88	6.51	3.37	4.04	(-) 0.67

It will be observed from table 3 that the financial costs are highest in the case of PACS largely on account of low turn over and as between the SCB and DCCB, it is higher in the case of SCB which has higher proportion of internal

resources, a substantial portion of which is in the form of term deposits for which higher interest rates have to be paid.

18.29 As the analysis brings out, the agricultural credit delivery system in the co-operative sector at the grass root level, is prima facie not financially sound inasmuch as the net margin works out to (-) 1.00 and (-) 3.21 in respect of PLDB and PACS respectively. The net margin would however be even more negative if the costs of overdues and bad debts are added. It would be observed from table 3 that the gross margin available at grass root level is about 2 per cent in the case of co-operatives. Viewed in the context of high transaction costs and low gross margins, the process of financial intermediation by the co-operative banking system is resulting in a negative performance, its extent varying from institution to institution.

18.30 In what follows, we therefore, proceed to examine the question of appropriate margins on agricultural loans with reference to each type of lending institution. Needless to state, the findings of the study would need corrections for variations in the assumptions made or even a shift of the emphasis in regard to the assumptions. Further, due weightage is also to be given to the factors which determine the income and costs in the light of the existing position obtaining at each level of the institutions comprising the sample. This is a very complex task as the samples has revealed the pattern of income and costs uneven as among the various institutions and states. The inter-state as well as intra-state variations are also quite high. In the circumstances, the only alternative is to proceed on the basis of the average position of the institutions on an all India basis and suggest an appropriate range of margins to be retained by the institution concerned. An attempt is made to examine these functional aspects and in the overall context, the adequacy of existing margins for each type of institution in the co-operative credit sector.

Primary Agricultural Credit Societies

18.31 The primary agricultural credit societies (PACSs) are the ground level institutions engaged in dispensing short and medium term loans. Though the sample size is 90, the data from five of them being highly deviant, have not been included in the analysis. Even within 85 PACSs, the variance is observed on almost all the aspects as may be seen from table 4.

Table 4

General Information - Primary Agricultural Credit Societies

Sl. No.	State	Number of PACSs		Number of Villages per Society	Total Population in the Limits of the Society ('000)			Distance from a village (Kms.)	
		Total	Only Credit Business		Minimum	Maximum	Average	Nearest	Farthest
1.	Andhra Pradesh	7	Nil	5	4.20	20.00	10.60	2	8
2.	Tamil Nadu	8	3	6	6.00	23.00	14.00	1	8
3.	Kerala	6	4	3	-	-	20.00	1	8
4.	Maharashtra	22	17	8	0.80	28.00	6.00	1	20
5.	Haryana	4	Nil	7	5.80	10.20	7.40	1	12
6.	Himachal Pradesh	2	1	6	1.60	2.80	2.10	1	5
7.	Assam	5	Nil	24	13.00	45.00	32.00	1	25
8.	Meghalaya	4	Nil	17	3.00	10.00	6.00	1	10
9.	Orissa	6	Nil	11	4.50	20.00	10.40	1	8
10.	Uttar Pradesh	21	Nil	21	8.00	23.00	14.00	1	18
Total/Average		85	25	12	-	-	12.00	1	12

Table 4 (contd.)

General Information - Primary Agricultural Credit Societies

Sl. No.	State	Family size	No. of Families			No. of Members Per Society	Area Cover- age**	No. of Borrowing Members	Effective Cover- age +
			Minimum	Maximum	Average				
1.	Andhra Pradesh	4.65	900	4300	2280	1392	61	446	19.56
2.	Tamil Nadu	4.50	1333	5111	3111	1515	49	530	17.04
3.	Kerala	5.39	-	-	3710	2671	72	1629	43.91
4.	Maharashtra	5.16	155	5426	1162	745	64	405	34.85
5.	Haryana	6.30	920	1669	1174	553*	47	381	32.45
6.	Himachal Pradesh	5.19	308	539	404	284*	70	54	13.37
7.	Assam	5.46	2380	8241	5860	3872	66	774	13.21
8.	Meghalaya	4.66	652	2146	1287	274	21	14	1.09
9.	Orissa	5.57	807	3590	1867	1177	63	541	28.98
10.	Uttar Pradesh	5.24	1526	4389	2671	1804	68	1081	40.47
Average		-	950	4473	2236	1395	62	668	30.00

* Based on secondary sources.

** Area coverage is the ratio between the number of members and the number of families in the limits of the society.

+ Effective coverage is the ratio between the number of borrowing members and the number of families in the limits of the society.

Note : i. Societies which are abnormal (N=5) are not considered for the analysis. Hence the sample size is 85.

ii. All averages computed for PACSs are 'weighted averages', weights being the number of institutions in these states. Weighted average is computed in view of varying sample size from state to state. As against this, simple average has been computed for the other institutions.

18.32 As the figures in Table 4 bring out, there are variations, in some respects, quite high even, as between the actuals in a state and the averages of various states. Most of the PACSs engage themselves in the non-credit business also. If the highly deviant figures of Maharashtra are ignored, barring less than 10 percent PACSs which do only credit business, all others undertake non-credit business as well. In the matter of area coverage, the number of villages covered on an average by a society was 12 and the farthest village covered by the society a distance of 12 kms. The average number of members per society was 1395 which was 62 percent of the total number of families within the limits of the society. In the matter of certain financial parameters also, the units in the sample have shown sharp variations. The statewise position regarding these different aspects is given in table 5.

Table 5

Certain Financial parameters of PACS - Statewise Position

State	(Rs. lakhs)							
	Share Capital	Deposits	Borrowings	Financial cost (Per cent)	Agricultural advances	Interest Income (Per cent)	Gross Margin (Per cent)	Transaction cost (Per cent)
Andhra Pradesh	2.05	1.16	12.71	9.80	11.41	11.38	1.58	4.38
Tamil Nadu	2.19	1.74	16.52	10.18	18.66	11.18	1.00	5.34
Kerala	3.62	81.29	20.98	7.60	52.50	14.31	6.71	5.47
Maharashtra	2.15	0.33	6.61	8.30	7.24	10.92	2.62	6.32
Haryana	2.97	1.07	15.19	11.20	20.80	13.00	1.80	4.30
Himachal Pradesh	2.78	0.22	1.52	11.50	0.50	13.00	1.50	5.40
Assam	1.15	0.04	2.90	7.60	1.70	13.50	5.90	10.80
Meghalaya	0.51	0.23	3.54	8.20	3.28	8.40	0.20	3.20 [⊙]
Orissa	1.23	0.63	8.77	9.90	9.72	11.30	1.40	1.65 [⊙]
Uttar Pradesh	2.16	0.45	6.83	10.75	8.02	13.60	2.85	5.19
Average	2.09	6.31	9.19	9.90	12.19	12.09	2.19	5.40

⊙ The transaction costs are low due to subsidy given to PACS.

The above sample relates to comparatively larger societies. There had been a higher coefficient of variation (ranging between 10 to 66) in the case of financial and transaction costs in the different states, but in respect of income

from agricultural credit, the coefficient of variation has been less than 20 per cent in almost all the states, implying lower intra-state variations in income from agricultural credit. The transaction costs were found to move in a narrow range of 4.50 per cent to 5.50 per cent in the case of the majority of states except in the case of Assam and Kerala. The gross margin had also stabilised at about 2 per cent in respect of the PACSs barring the exceptional cases of Kerala and Assam.

18.33 As PACS is, as already discussed, normally engaged in both credit and non-credit activities and considering both these activities, the society as a whole has a net margin of 1.22. However, ignoring the extremely deviant margins of Haryana and Himachal Pradesh as also the subsidy element in Meghalaya and Orissa, the net margin for the same works out to 0.03 only as will be seen from table 6.

Table 6
Margins Realisable by PACSs
(Average of the Societies for Different States)

State	Agricultural Credit		Society as a whole		
	Gross Margin	Net Margin	Total Cost	Total Income	Net Margin
Andhra Pradesh	1.58	(-) 2.80	12.70	13.00	(+) 0.30
Tamil Nadu	1.00	(-) 4.34	11.98	11.60	(-) 0.38
Kerala	6.71	(+) 1.24	8.10	8.20	(+) 0.10
Maharashtra	2.62	(-) 3.70	18.01	17.81	(-) 0.20
Haryana	1.80	(-) 2.50	12.40	22.80	(+) 10.40
Himachal Pradesh	1.50	(-) 3.90	14.10	24.60	(+) 10.50
Assam	5.90	(-) 4.90	13.40	13.00	(-) 0.40
Meghalaya	0.20	(-) 3.00	8.30	7.80	(-) 0.50
Orissa	1.40	(-) 0.25	8.10	12.10	(+) 4.00
Uttar Pradesh	2.85	(-) 2.34	10.70	11.90	(+) 1.20
Weighted Average	2.19	(-) 3.21	12.56 (13.01)*	13.78 (13.04)*	(+) 1.22 (0.03)*

Note : In the absence of subsidy, net margins for Meghalaya and Orissa are (-)6.10 and (-) 2.60 respectively.

* Values when highly deviant figures of Haryana and Himachal Pradesh are not considered and effect of subsidy in Meghalaya and Orissa is ignored. Very high positive net margins in respect of Haryana and Himachal Pradesh are due to the non-credit business handled by the societies situated there.

As the table brings out, the net margins for the society as a whole in respect of most of the states become positive though the margins in respect of agricultural credit business only were negative. However, the societies in the states of Maharashtra and Tamil Nadu continue to show negative net margins. It may not be out of place to mention in this context that in these two states the number of societies engaged in non-credit business is less as compared to other states implying that the non-credit business undertaken by the societies earns enough margin and in a large number of cases this is able to subsidise the losses incurred by the societies in respect of agricultural credit business.

18.34 One of the important factors affecting the margins realisable is the size of the society measured in terms of its working capital. There is a strong association between the size of a society and the transaction costs. This association is in the nature of a quadratic type, that is, the transaction cost decreases with the increase in size upto a certain point and thereafter increases along with the increase in size. For the purpose of analysis, the societies according to their size have been grouped into four categories. The details are given in table 7.

18.35 The break-even levels of agricultural credit operations for different categories are given in table 8. It will be seen from the table that the small societies (i.e. size of less than Rs.5 lakhs) will have to increase their business i.e. advances by more than six times (i.e. by 620 per cent), staff strength remaining the same i.e. without any increase in staff, to achieve the break-even level. However, the larger societies can achieve break-even levels by increasing their business by 40 to 70 per cent, with the existing staff, which is quite possible.

18.36 The Consultants IV have adopted two different approaches for estimating the risk costs in respect of PACS. The first approach involves computing the proportion of the reserves created for bad debts in the total agricultural advances. The second approach is to express the risk costs as a proportion of

Table 7

Size Impact on Costs and Margins - PACSs

Size (Rs. lakh)	Average Working Capital (Rs. lakh)	Agri. Advances (Rs. lakh)	Finan- cial costs	Credit Income	Agricultural Credit			Society as a whole		
					Gross Margin	Transa- ction cost	Net Margin	Total Income	Total costs	Net Margin
Less than 5	3.18	1.15	9.42	10.34	0.92	6.62	(-)5.70	18.68	18.44	(+)0.24
5 - 10	7.16	4.53	10.06	11.82	1.76	5.06	(-)3.30	12.67	12.46	(+)0.21
10 - 20	15.63	9.95	9.86	12.32	2.46	4.23	(-)1.77	11.35	10.57	(+)0.78
20 and above	63.00	33.00	8.68	12.50	3.82	5.32	(-)1.50	11.05	10.93	(+)0.12

Advances in Rs. lakh.

Income, Costs and Margins for Rs.100 outstanding advance / Rs.100 working capital.

Table 8

Break-even Analysis

Size (Rs. lakhs)	Break-even Level) (Rs. lakhs)	Existing Agricultural Advances (Rs. lakhs)	Volume Increase Required (Per cent)
Less than 5	8.28	1.15	620
5 - 10	13.00	4.53	190
10 - 20	17.00	9.95	70
20 and above	46.00	33.00	40

the overdues over three years to the demand. The reserves created for bad debts amount to 1.05 per cent of the outstanding agricultural advances. The estimate of the bad debts at 15 per cent of overdues above 3 years amounts to 1.78 per cent. The risk cost, as an approximate estimate, is placed at one per cent of the outstanding advances by the consultants.

18.37 It will be observed from the data in table 6 in paragraph 18.33 that the net margin for a PACS is minus 3.21 in respect of its agricultural lendings. The negative net margin would further increase due to the reduction in the rate of interest on loans for seasonal agricultural operations for over Rs.15,000 upto Rs.25,000 from 12.5 - 14 per cent per annum to a uniform rate of 12 per cent per annum effective 1st March 1989. The NABARD had, effective 1st March 1988, reduced the rate of interest on loans upto Rs.7,500 to 10 per cent (the earlier rate was 11.5 per cent for loans upto Rs.5,000 and 12.5 per cent for loans over Rs.5,000 and upto Rs.10,000). This reduction however, did not adversely affect those PACS which depended mostly on refinance from DCCBs, since the rate of interest on refinance was also reduced from 9 to 7.5 per cent. However, where the societies have involved their own resources in agricultural lendings on a substantial scale, the negative margin is seen to have gone up further.

18.38 Thus if agricultural lending operations of a PACS have to be financially viable, a higher gross margin than presently available will be necessary. In view of need for aggressive deposit mobilisation by co-operatives and as in the present state of Indian money market more and more attractive instruments with

fiscal concessions are available to tap the saving of the people, we do not propose any reduction in the interest rates on deposits. Any reduction is bound to have serious adverse repercussions on mobilisation of internal resources. Secondly, our analysis has revealed that the transaction costs comprise mainly manpower related costs which constitute about 80 per cent of the total cost. The balance of about 20 per cent is on account of rent, stationery, postal and telephone charges, audit fee, etc. Therefore, the only alternative open is to make adjustments in the lending rates or to make available the borrowed funds at cheaper rates to the co-operative system. In the event of choosing the first alternative viz. of a reduction in the rates of interest payable by PACS, to the higher institutions, PACS, which raises internal resources through deposits (mobilized at a higher cost of about 10 per cent per annum on an average as the figures relating to Kerala State show) would be in a disadvantageous position as every rupee lent by it to agriculture would result in a net loss. Besides, this raises certain fundamental issues concerning the very survival of the credit co-operatives as healthy financial intermediaries. Elsewhere in the report, we have recommended several measures for the revitalisation and strengthening of the co-operative banking system. Among these, self reliance in point of resources through aggressive deposit mobilization is of primary importance. Therefore any measure which places a premium on increased reliance on refinance support to the system and discourages deposit collection would, in our view, be ultimately destructive of the system. Considered thus, we are left with the only alternative of leaving the credit systems to regulate its interest rates in a manner that enables the systems to pay for the cost of the resources it raises and also the costs for servicing both the deposits and loans with a cushion to ensure its survival and growth, keeping in view, however, the social objective of extending reasonable concessionality for the very weak.

18.39 To enable agricultural lendings by PACS to be self supporting, the gross margin should be adequate to cover the transaction cost and the risk cost and leave some surplus to take care of future eventualities and safeguard the interests of higher level institutions also, in addition to the interests of members who contribute to the share capital. The transaction cost of PACS which is 5.40 per cent in respect of select units as given in table 3, works out to about 4.5 per cent when the badly managed societies are excluded. The risk cost would amount to about one per cent. About 0.5 per cent may be required for generating

adequate surplus to enable the society to make the credit operations profitable. Thus the gross margin required for a PACS in respect of its agricultural credit will be about 6 per cent. Accordingly the economic rate of lending will have to be such that it yields a gross margin of 6 per cent. But account has also to be taken of the need to ensure a degree of concessionality in the interest rates for the small and marginal farmers. This rate itself, in our view, should be 1.50 percentage points higher than the highest rate of interest on the deposits by scheduled commercial banks, which is at present, 10 per cent per annum. This would ensure that money borrowed at concessional rates is not re-deposited at higher rates offered by other institutions. In respect of other borrowers, the ceiling rate of interest on advances may continue to be the present ceiling of 15.5 per cent per annum. We are recommending this ceiling since the absence of any ceiling may open up the possibilities of an unduly high rate in a segmented market as ours.

District Central Co-operative Banks

18.40 A District Central Co-operative Bank (DCCB) is in the middle of the three-tier co-operative system making advances mainly to the PACSs which are its members. Certain basic financial information about the sample units are given in tables 9 and 10.

18.41 It would be observed that the average working capital of a DCCB is about Rs.3,671 lakhs, 81 per cent of which is on account of deposits (59 per cent) and borrowings (22 per cent). The rest 19 per cent comes from their owned funds (share capital and reserves). The agricultural advances made by a bank, on an average are Rs.2,024 lakhs which amount to 85 per cent of the total advances and 55 per cent of working capital. There are considerable inter bank variations evidenced by the spread in the advances of as low as Rs.136 lakhs in Kangra (Himachal Pradesh) and as high as Rs.6,787 lakhs in Madurai (Tamil Nadu). It may be interesting to note that the units in the states of Tamil Nadu and Maharashtra, though conducting much higher volume of business, exhibited mutually divergent situations.

18.42 As the analysis brings out, the DCCBs have net margin of 0.91 per cent in respect of their agricultural advances. The gross margin earned by them is 4.09 per cent which is much higher than 2.19 per cent earned by the PACSs

Table 9

**General information and Sources and Cost of Finance
(District Central Co-operative Banks)**

								(Rs. lakhs)
State/DCCB	No. of PACSs	Staff Strength	Share Capital	Deposits	Borrowings	Deposits & Borrowings	Financial cost (Per cent)	Total Working Capital
<u>ANDHRA PRADESH</u>								
1. Chittoor	302	198	153.85	535.85	820.20	1356.13	8.32	1765.20
2. Guntur	369	97	276.89	832.83	1020.00	1852.83	10.21	2556.58
3. Karimnagar	258	211	261.47	758.21	1915.29	2673.50	7.41	3411.45
<u>TAMIL NADU</u>								
1. Trichy	1006	487	171.49	3466.46	1143.13	4609.59	9.04	5348.76
2. Madurai	447	766	405.20	4950.13	2920.13	7870.33	11.18	9826.29
<u>KERALA</u>								
1. Trichur	425	169	172.50	2838.50	344.03	3182.53	7.00	3819.42
<u>MAHARASHTRA</u>								
1. Sholapur	845	771	341.63	4213.70	567.61	4781.31	8.00	5993.00
2. Kolhapur	868	918	513.79	8634.75	254.45	8889.20	7.01	10607.79
3. Wardha	402	358	96.67	1414.28	155.98	1570.26	5.41	2064.03
4. Aurangabad	678	-	223.89	2165.15	1416.77	3581.92	5.80	4445.65
5. Chandrapur	533	405	130.72	1720.42	135.88	1856.30	5.00	2204.44
6. Jalna	445	307	80.32	1129.80	370.52	1500.32	5.00	1809.56
<u>HARYANA</u>								
1. Kurukshetra	196	-	172.82	985.40	1565.97	2551.37	6.85	3165.56

Table 9 (contd.)

General Information and Sources and Cost of Finance
(District Central Co-operative Banks)

State/DCCB	No. of PACSs	Staff Strength	Share Capital	Deposits	Borrowings	Deposits & Borrowings	Financial cost (Per cent)	Total Working Capital
<u>HIMACHAL PRADESH</u>								
1. Kangra	107	159	375.10	3472.46	81.25	3553.71	8.25	4295.06
<u>ORISSA</u>								
1. Nayagarh	157	117	115.48	345.11	690.87	1035.98	7.50	1285.78
2. Angul	190	174	157.72	346.00	893.07	1239.07	7.60	1654.09
<u>UTTAR PRADESH</u>								
1. Kanpur	202	161	118.66	1102.93	548.89	1651.82	6.66	1989.07
2. Varanasi	303	146	120.54	948.34	811.84	1760.18	7.07	2096.92
3. Nainital	431	128	113.82	2071.28	119.24	2190.52	6.69	2574.53
4. Moradabad	388	161	178.69	1208.66	743.48	1952.14	9.45	2515.63
Average	428	319	209.00	2157.02	825.93	2982.95	7.47	3671.44

Table 10

Advances, Income and Margins
(District Central Co-operative Banks)

State/DCCB	Outstanding advances (Rs. lakhs)		Per Rs. 100/- outstanding agricultural advance				Bank as a whole			
	Total	Agricultural	Income	Gross Margin	Transaction Costs	Net Margin	Total Costs*	Total Income*	Margin	
<u>ANDHRA PRADESH</u>										
1.	Chittoor	1342.33	1208.43	12.41	4.09	3.40	(+) 0.69	9.62	11.80	(+) 2.18
2.	Guntur	1802.70	1552.00	13.35	3.15	3.60	(-) 0.45	10.26	10.61	(+) 0.35
3.	Karimnagar	2427.92	2017.38	11.44	4.03	3.66	(+) 0.37	8.68	8.97	(+) 0.29
<u>TAMIL NADU</u>										
1.	Trichy	3622.63	3562.56	11.87	2.83	2.85	(-) 0.02	10.27	10.35	(+) 0.08
2.	Madurai	7382.24	6787.30	13.80	2.62	2.64	(-) 0.02	11.26	12.03	(+) 0.77
<u>KERALA</u>										
1.	Trichur	2522.77	1766.00	10.30	3.30	2.90	(+) 0.40	8.57	9.79	(+) 1.22
<u>MAHARASHTRA</u>										
1.	Sholapur	3869.68	3508.00	11.47	3.47	1.97	(+) 1.50	8.67	14.47	(+) 5.80
2.	Kolhapur	6573.42	5892.46	10.72	3.71	2.52	(+) 1.19	8.68	11.93	(+) 3.25
3.	Wardha	1160.13	929.60	10.32	4.91	4.02	(+) 0.89	7.87	9.64	(+) 1.77
4.	Aurangabad	3085.70	2931.40	10.11	4.40	3.67	(+) 0.73	9.59	10.44	(+) 0.85
5.	Chandrapur	1038.00	896.55	11.50	6.50	5.47	(+) 1.03	10.36	11.31	(+) 0.95
6.	Jalna	1308.72	995.00	13.29	8.29	3.15	(+) 5.14	6.80	11.54	(+) 4.74

Table 10 (contd.)

Advances, Income and Margins
(District Central Co-operative Banks)

State/DCCB	Outstanding advances (Rs. lakhs)		Per Rs. 100/- outstanding agricultural advance				Bank as a whole		
	Total	Agricultural	Income	Gross Margin	Transaction Costs	Net Margin	Total Costs*	Total Income*	Margin
<u>HARYANA</u>									
1. Kurukshetra	2368.84	2071.00	11.19	4.34	2.36	(+) 1.98	9.56	10.56	(+) 1.00
<u>HIMACHAL PRADESH</u>									
1. Kangra	1186.45	136.25	12.32	4.07	1.91	(+) 2.16	9.03	14.50	(+) 5.47
<u>ORISSA</u>									
1. Nayagarh	1027.97	716.10	10.35	2.85	2.30	(+) 0.55	8.02	8.96	(+) 0.94
2. Angul	1281.76	1231.00	10.60	3.00	2.15	(+) 0.85	7.82	10.51	(+) 2.69
<u>UTTAR PRADESH</u>									
1. Kanpur	1268.37	847.89	10.67	4.00	3.82	(+) 0.18	8.70	8.87	(+) 0.17
2. Varanasi	1364.45	978.33	11.09	4.02	3.73	(+) 0.29	8.36	8.73	(+) 0.37
3. Nainital	1278.14	965.25	11.84	5.15	4.21	(+) 0.94	6.74	9.11	(+) 2.37
4. Moradabad	1669.80	1494.75	12.57	3.03	3.29	(-) 0.26	9.52	9.77	(+) 0.25
Average	2379.10	2024.36	11.56	4.09	3.18	(+) 0.91	8.92	10.69	(+) 1.77

(+1.01)**

* Expressed as a proportion of working capital in percentage.

** When the highly deviant values in case of Sholapur, Kolhapur, Jalna and Kangra DCCBs are ignored.

in respect of their agricultural lendings. Though, the average transaction cost works out to 3.18 per cent, it is below 3 per cent in the case of larger banks in the sample.

18.43 The exercise carried out by us to have some supplementary data in regard to costs and margins and to get a feel of the position after the new interest rates were enforced from 1st March 1988 revealed that there has been a drop of about one percentage point in the interest income in respect of the agricultural advances of DCCBs. Though the full impact of the NABARD's instructions in regard to sharing of interest margins at different levels in co-operatives is not yet available (the final actual refinance rate applicable to the concerned DCCB was to be determined in June 1989 on receipt of data pertaining to monthly outstandings), certain broad trends had emerged which indicate that the DCCBs require a higher margin as the present arrangements do not adequately compensate them.

18.44 To enable the agricultural lending by DCCB to be self supporting, the gross margin should be adequate to cover the transaction costs and leave some surplus. The transaction costs of a DCCB amount to about 3 per cent. Therefore, a DCCB needs to get a gross margin of about 3.5 per cent. The rate of interest that can be charged by a DCCB to PACS in respect of agricultural advances may, therefore, be so fixed that the resulting gross margin is not less than 3.5 per cent for a DCCB.

State Co-operative Bank

18.45 The State Co-operative Bank (SCB) is the apex body in the three tier co-operative system dispensing credit mainly to the District Central Co-operative Banks which are its members. The average working capital of an SCB is about Rs.349 crores. Though the size of the SCBs in the sample varied from Rs.170 crores to Rs.1,175 crores in respect of the working capital employed by SCBs of Kerala and Maharashtra, there was not much variation in case of the income and transaction costs per Rs.100 of the agricultural advances made by them. The data pertaining to Assam and Meghalaya, being highly deviant have, however, been ignored. The details are given in tables 11 and 12.

18.46 The average outstanding agricultural advances of a bank at Rs.13,300

Table 11
Sources and Costs of Finance
State Co-operative Banks

State	Share Capital	Deposits	Borrowings	Deposits & Borrowings	Financial Cost (per cent)	Total Working Capital
Andhra Pradesh	1523.17	14131.66	12958.69	27090.35	9.21	34384.57
Tamil Nadu	543.52	17904.28	12402.20	30306.48	8.54	35520.59
Kerala	566.72	9703.30	3608.35	13311.65	8.11	17059.31
Maharashtra	1419.17	95311.38	3008.78	98320.16	8.76	117500.66
Haryana	479.85	5870.59	9515.52	15386.11	7.75	18017.00
Assam	181.60	6638.08	170.07	6808.15	5.00	8573.55
Meghalaya	119.76	1744.55	36.51	1781.06	5.00	2028.63
Orissa	728.98	3027.53	10601.90	13629.43	7.76	17171.44
Uttar Pradesh	1863.65	34849.68	16410.39	51260.07	7.89	63974.70
Average	825.16	21020.12	7634.71	28654.77	7.56	34914.49

(Rs. lakhs)

Table 12
Advances, Income and Margins
State Co-operative Bank

State	Outstanding advances (Rs. lakh)		Per Rs.100/- outstanding agricultural advances				Bank as a whole		
	Total	Agricultural	Income	Gross Margin	Transaction Costs	Net Margin	Total Costs*	Total Income*	Margin
Andhra Pradesh	26092.41	18099.33	9.33	0.12	0.40	(-) 0.28	7.60	8.01	(+) 0.41
Tamil Nadu	27785.49	13070.80	10.73	2.19	1.03	(+) 1.16	8.12	8.70	(+) 0.58
Kerala	10059.34	4564.21	9.80	1.69	0.68	(+) 1.01	6.90	8.10	(+) 1.20
Maharashtra	64478.04	38687.00++	9.30	0.54	0.86	(-) 0.32	8.10	8.34	(+) 0.24
Haryana	14774.35	13833.95	8.95	1.20	0.45	(+) 0.75	7.10	7.85	(+) 0.75
Assam	4159.52	1360.99	9.06	4.06	3.10	(+) 0.96	6.17	7.53	(+) 1.36
Meghalaya	887.85	413.24	11.73	6.73	5.90	(+) 0.83	8.10	8.23	(+) 0.13
Orissa	14883.78	8606.79	8.60	0.84	0.61	(+) 0.23	6.74	8.10	(+) 1.36
Uttar Pradesh	45816.79	21064.14	8.84	0.95	0.60	(+) 0.35	6.81	7.69	(+) 0.88
Average	23215.29	13300.05	9.59	2.03	1.51	(+) 0.52	9.29	8.06	(+) 0.77

Note : The figures do not include those of Himachal Pradesh.

* Expressed as a proportion of the working capital in percentages.

++ Approximate.

lakhs form 57 per cent of the total advances. The average income realisable is Rs.9.59 per Rs.100 of loans outstanding under agricultural advances. The average financial cost being Rs.7.56 per Rs.100, the gross margin works out to 2.03 per cent which covers transaction costs of 1.51 per cent to leave a surplus of 0.52 per cent.

18.47 The quick case studies undertaken by us revealed that the cost of deposits was about 9.50 per cent in apex banks in the states of Kerala, Karnataka, Andhra Pradesh and Maharashtra. The proportion of borrowings in the agricultural advances was found to be about 50, implying that 50 per cent of the advances were made out of internal resources comprising owned funds and deposits. Though the present cost of internal resources is one per cent lower than the cost of deposits this is bound to increase in future as incremental deposits collected are likely to be mainly high cost deposits. Although the study by the consultants shows the transaction cost of SCB at 1.51 per cent, our case studies have shown that it varied from 0.53 to 1.76 per cent but was nearer 1.00 per cent in majority cases.

18.48 It is but essential that the SCB has a minimum gross margin of 1.50 per cent so as to cover its transaction cost of about one per cent in respect of agricultural advances and to leave a surplus of about 0.5 per cent. The rate of interest on agricultural loans to DCCBs by SCB would therefore need to be so fixed that the emerging gross margin is not less than 1.5 per cent for the SCB.

18.49 To summarise the position, in the co-operative sector, the gross margin required at PACS, DCCB and SCB levels will be 6 per cent 3.5 per cent and 1.5 per cent respectively. It should however be clarified here that :

i) A gross margin of 6, 3.5 and 1.5 per cent is required by PACSs, DCCBs and SCBs respectively to cover the transaction cost, risk cost and to allow for a small profit. In other words if agricultural lending has to be viable on its own without any cross subsidization from other sources, these costs need to be covered by the gross margin available to these institutions on their agricultural lending.

ii) The transaction cost referred to above includes the servicing cost of raising resources viz. borrowings and deposits as well as the pre and post

disbursal costs in respect of loans and advances granted out of these resources. Since the cost of servicing the borrowings are very small as against the costs of servicing the deposits, the total transaction cost of agricultural lending will be higher or lower depending upon the proportion of borrowings and deposits utilised for granting agricultural advances. In other words, the transaction cost of agricultural advances will vary in different institutions and at different points of time.

iii) Since gross margin will be realised by the lending institution by way of spread between its financial cost of resources invested in agricultural loans and interest income on such loans it will be necessary to work out the two rates by each institution separately as resources raised are used for agricultural and non-agricultural business. The financial cost indicated in table 3 for different institutions like SCB, DCCB and PACS is in respect of all their resources including borrowings and deposits whether used for agricultural or non-agricultural lending purposes.

iv) The financial cost of the resources used exclusively in agricultural lendings by co-operatives would be lower than the overall financial cost because they use in addition to their resources, a sizeable part of the resources used for agricultural lending out of resource from NABARD which carries a concessional rate. Besides, cost of servicing such borrowings is also very small as compared to the cost of servicing deposits. This is evident from a few case studies undertaken by us in states like Maharashtra, Andhra Pradesh and Karnataka. In brief the position is as under :

<u>Overall Financial cost of resources</u>		(Amount per Rs.100)
	<u>Total resources</u>	<u>Resources used in agricultural lending</u>
SCB	7.56	7.52
DCCB	7.47	7.18
PACS	9.90	9.03

These case studies have further shown that prior to 1.3.1988 the cost of raising deposits was higher than the cost of borrowings by about 2.50, 1.00 and 1.25 per cent in the case of SCBs, DCCBs and PACSs respectively as it may be seen from the following :

	<u>Cost of borrowings (per cent)</u>	<u>Cost of deposits (per cent)</u>
SCB	6.69	9.36
DCCB	7.05	8.07
PACS	9.29	10.50

Since effective 1-3-1988 the refinance rates have been further reduced by NABARD the difference has also further widened with cost on borrowings reduced by about 1.50 per cent. This, did not however affect the margins available to the co-operatives materially as lending rates to them by the higher financing agencies were also reduced effective 1-3-1988.

v) This is an illustrative average position only; the real position will vary from institution to institution depending upon the share of borrowings in the resources used for agricultural lending. The more the borrowings, the lower will be the financial cost and vice-versa.

vi) We have not recommended specific interest rates for the three tiers of co-operatives but only indicated the likely ranges of rates that would need to be charged to ultimate borrowers by PACS viz. for the lowest bracket a concessional rate of 11.5 per cent and the rate for all the rest being freed from regulation except for a ceiling of 15.5 per cent under the maximum. These rates are recommended on the basis of existing pattern of administered interest rate system. The lending rates of DCCBs/SCBs and NABARD may have to be fixed by NABARD/RBI keeping in view the findings of this study and requirements of the above margins based thereon.

vii) It is necessary that if the interest rates for any category of borrowers are fixed at below the financial cost plus transaction costs in pursuance of Government policy in this regard, the short fall in the interest actually charged and the economic rate should be made good to the institution by the Government.

Land Development Banks - Federal System

Primary Land Development Banks

18.50 The general information and the sources and cost of finances of Primary

Land Development Banks (PLDBs) are given in tables 13, 14 and 15.

Table 13

State-wise Average Transaction Costs of PLDB: Federal System

State	Transaction Costs on Rs.100 Outstanding Advance		
	Minimum	Maximum	Average
Andhra Pradesh	1.68	4.83	3.56
Tamil Nadu	2.38	4.72	3.55
Kerala	1.49	1.97	1.68
Haryana	-	-	3.04
Assam	-	-	5.68
Himachal Pradesh	-	-	4.29
Orissa	1.63	2.21	2.01
Average	-	-	3.39

It would be observed from these tables that there are substantial inter-state variations in working capital, number of employees, coverage, financial costs, transaction costs, etc. of PLDBs.

18.51 On an average the income generated by a PLDB is Rs.10.17 per Rs.100 of agricultural advances. The financial cost being Rs.7.78 per Rs.100, the gross margin works out to 2.39. The transaction cost on an average being Rs.3.39, a PLDB loses Re.1.00 on every credit transaction of Rs.100. The details are given in table 16.

18.52 In addition to the income due to advances, the banks also earn on their investments which when taken into account provides a net margin of Re.0.28 on every Rs.100 working capital as may be seen from table 16. However, when the effect of extreme values of Tamil Nadu are ignored, the net margin on an average amounts to (-) 0.38.

Size impact on costs and margins

18.53 The size of a PLDB has a significant impact on financial costs, income

Table 14

General Information Pertaining to Primary Land Development Banks (PLDB)
(State-wise Average per PLDB)

State	Sample Size	No. of Villages	No. of Members	No. of Borrowing Members	Proportion of the borrowing Members (Per cent)	Families in the limit of the Bank ('000)	Area Coverage* (Per cent)	Effective Coverage+ (Per cent)	Staff (Total) (No.)	Strength of the Field Staff (No.)
A : PLDB - Federal System										
Andhra Pradesh	4	121	13218	9940	75	40.4	33.0	2.4	26	13
Tamil Nadu	2	101	6550	2490	38	93.3	7.0	2.7	19	14
Kerala	3	47	14046	7504	53	189.2	7.4	4.0	19	10
Haryana	1	160	4500	3348	74	42.1	10.7	8.0	22	7
Himachal Pradesh	1	615	3280	1344	41	525.2	0.6	0.2	24	5
Assam	1	20	2663	248	9	36.6	7.3	0.7	3	1
Orissa	4	1168	12358	9135	74	117.7	10.5	7.7	25	12
Total/Average	16	319	8088	4858	52	149.2	10.9	3.7	20	9
B : Unitary System @										
Maharashtra	3	333	11382	7479	66	115.9	9.8	6.5	18	-
Uttar Pradesh	5	330	4042	2582	64	91.5	4.4	2.8	5	-
Total/Average	8	332	7712	5031	65	103.7	7.1	4.7	11	-

* Area coverage is the ratio between number of members and the number of families in the limits

+ Effective coverage is the ratio between number of borrowers and the number of families in the limits

@ Branches of SLDB.

Table 15

Sources and Cost of Finance
(State-wise Average for PLDB-Federal)

State	Share Capital	Reserves for Bad & Doubtful debts	Deposits	Borrowings	Deposits & Borrowings	Financial cost (Per cent)	Total Working Capital
Andhra Pradesh	30.14	0.50	0.42	268.86	269.28	8.54	315.45
Tamil Nadu	15.65	0.07	-	114.81	114.81	8.03	163.98
Kerala	38.10	2.23	0.12	474.82	474.94	6.53	519.55
Haryana	2.86	-	-	439.14	439.14	7.67	515.76
Assam	1.86	0.07	-	10.43	10.43	7.70	17.69
Himachal Pradesh	29.26	-	-	137.88	137.88	8.34	167.14
Orissa	15.18	0.07	2.32	278.66	280.98	7.65	290.82
Average	19.01	0.59	0.41	246.37 (65)	246.78	7.78 (8)	284.34 (64)

Figures in the brackets refer to coefficient of variation.

Table 16

State-wise Average Gross and Net MarginsPLDB : Federal System

(Rs.100 outstanding advance/working capital)

State	Agricultural credit			Banks as a whole				
	Income	Financial Cost	Gross Margin	Transaction Costs	Net Margin	Total Costs	Total Income	Margin
Andhra Pradesh	10.10	8.54	1.56	3.46	(-) 1.90	11.37	10.10	(-) 1.27
Tamil Nadu	12.24	8.03	4.21	3.55	(+) 0.66	7.85	12.10	(+) 4.25
Kerala	7.90	6.53	1.37	1.68	(-) 0.31	7.43	8.89	(+) 1.46
Haryana	9.83	7.67	2.16	3.04	(-) 0.88	9.54	9.73	(+) 0.19
Assam	10.70	7.70	3.00	5.68	(-) 2.68	8.64	7.07	(-) 1.57
Himachal Pradesh	10.76	8.34	2.42	4.29	(-) 1.87	10.30	8.60	(-) 1.70
Orissa	9.65	7.65	2.00	2.01	(-) 0.01	8.31	8.92	(+) 0.61
Average	10.17 (9.82)*	7.78 (7.74)*	2.39 (2.08)*	3.39 (3.36)*	(-) 1.00 (-) 1.28*	9.06	9.34	(+) 0.28 (-) 0.38*

* On ignoring the extremely deviant figures relating to Tamil Nadu

from advances and transaction costs, and the same are reflected in the margins also. The details of these are given in the tables 17 and 18.

18.54 The overdues above 3 years as a proportion of the advances outstanding work out to about 1.6 per cent. The reserve for bad debts amounts to 0.50 per cent. The risk cost is estimated at about one per cent of the outstanding advances.

18.55 To enable the PLDB to be self supporting in respect of its advances for agriculture and allied activities, the gross margin should be adequate to cover the transaction cost and the risk cost and leave some surplus. The transaction cost of a PLDB is about 3.5 per cent and the risk cost is about one per cent. About 0.5 per cent may be required for generating adequate surplus to enable the society to make the agricultural credit profitable. Thus the gross margin required for a PLDB will be about 5 per cent. For this purpose it may be necessary to increase the lending rates. While doing so it has, however, to be ensured that an element of concessionality in the interest rates for the small farmers is retained. At present the rate of interest charged for term loans for agriculture and allied activities (excluding minor irrigation and land development) for medium and large farmers is 2.5 percentage points above the rate of interest charged for small farmers. In respect of term loans for minor irrigation and land development same rate of interest is charged for all categories of borrowers. The rates of interest for small farmers and for the medium and large farmers may be so fixed that the resulting gross margin will not be less than 5 per cent for the PLDB.

State Land Development Bank - Federal System

18.56 The financial particulars of the SLDBs under the samples are given in tables 19 and 20. The inter-state variations can be seen from these tables. It would be observed that the average annual working capital of a SLDB is Rs.173.05 crores and the contribution from external sources is 82 per cent. The wide inter-state variations in working capital would be evident from the fact that it is as low as about Rs.7.73 crores in Himachal Pradesh and as high as Rs.436.02 crores in Andhra Pradesh. The coefficient of variation is about 80 per cent.

Table 17
Size-wise Average Costs and Margins in Agricultural Credit
PLDB : Federal System

Size (Rs. lakh)	Total Working Capital (Rs.lakh)	Advances (Rs.lakh)	Income	Per Rs.100/- Outstanding Advances			Break-even point (Rs.lakh)	Volume Increase Required (Per cent)	
				Financial Cost	Gross Margin	Transa- ction costs			Net Margin
Less than Rs.100	56.66	36.89	11.65	8.35	3.30	5.26	(-) 1.96	59	60
100-300	163.37	104.81	10.47	8.21	2.26	3.25	(-) 0.99	151	44
300 & Above	484.22	390.00	9.04	7.17	1.87	2.13	(-) 0.26	441	13

Table 18

Break-even Points of Operation (Volume of loans and advances) for Various Levels of Transaction

Size : Rs. 100 - 300 lakhs				Size : Rs. 300 lakhs & above			
Transaction Costs (Per cent)	Increase in Transaction Costs (Per cent)	New Transaction cost (per cent)	Break-even Point (Rs. lakh)	Transaction Costs (Per cent)	Increase in Transaction Cost (Per cent)	New Transaction cost (per Cent)	Break-even Point (Rs. lakh)
3.25	5	3.41	158	2.13	5	2.24	466
3.25	10	3.58	166	2.13	10	2.34	489
3.25	15	3.74	174	2.13	15	2.45	511
3.25	20	3.90	182	2.13	20	2.56	533

It is noteworthy that as the size increases, the costs decrease.

Table 19

State-wise Sources and Cost of Finance
(State Land Development Banks)

									(Rs. lakhs)
State	No. of Regional Offices/ Branches	No. of PLDBs	Share Capital	Reserve for Bad & Doubtful Debts	Deposits	Borrowings	Deposits & Borrowings	Financial cost (Per cent)	Total Working Capital
A. Federal System									
Andhra Pradesh	22	218	1347.75	256.18	68.54	37068.84	37137.38	6.74	43602.43
Tamil Nadu	18	182	712.82	1200.00	521.29	15312.16	15833.45	7.25	22863.14
Kerala	10	36	548.59	91.14	77.47	16224.18	16301.65	6.64	18976.13
Haryana	4	71	840.61	104.90	32.25	21716.21	21748.46	6.44	24689.98
Himachal Pradesh	42	19	98.85	0.23	1.12	640.21	641.33	6.75	773.35
Assam	NIL	21	91.43	0.24	3.73	792.27	796.00	4.60	961.16
Orissa	12	54	447.34	44.03	65.98	7403.62	7469.60	6.64	9272.61
Average	15	86	583.91	242.39	110.05	14165.36	14275.41	6.44	17305.54
B. Unitary System									
Maharashtra	276	-	3842.66	825.96	1076.99	32868.06	33945.05	6.48	47219.44
Uttar Pradesh	288	-	3341.33	738.48	74.95	36213.09	36288.04	6.53	48206.84
Average	282	-	3592.00	782.22	575.97	34541.00	30116.55	6.51	47713.14

Table 20

State-wise Average Advances, Costs and MarginsState Land Development Banks

(Rs. per 100 outstanding advances/working capital)

State	Avances (Rs. lakhs)	Agricultural Credit				Bank as a whole			
		Income	Financial Cost	Gross Margin	Trans- action Cost	Net Margin	Total Costs	Total Income	Margin
<u>A. Federal System</u>									
Andhra Pradesh	33446.32	8.35	6.74	1.61	0.61	(+) 1.00	6.32	6.76	(+) 0.44
Tamil Nadu	16579.90	8.60	7.25	1.35	1.22	(+) 0.13	6.14	6.83	(+) 0.64
Kerala	13736.00	8.30	6.64	1.66	0.66	(+) 1.00	5.80	7.83	(+) 2.03
Haryana	18503.50	7.53	6.44	1.09	0.43	(+) 0.66	6.08	7.20	(+) 1.12
Himachal Pradesh	635.84	8.60	6.75	1.85	2.80	(-) 0.95	8.36	8.44	(+) 0.08
Assam	696.51	7.00	4.60	2.40	1.97	(+) 0.43	5.58	6.23	(+) 0.65
Orissa	6994.50	6.76	6.64	0.12	1.79	(-) 1.67	3.62	7.40	(+) 3.78
Average	12941.80	7.88	6.44	1.44	1.35	(+) 0.09	5.99	7.24	(+) 1.25
<u>B. Unitary System</u>									
Maharashtra	33237.36	8.95	6.48	2.47	3.18	(-) 0.71	9.81	7.20	(-) 2.61
Uttar Pradesh	31220.55	10.80	6.53	4.27	4.90	(-) 0.63	9.10	9.10	0.00
Average	32228.95	9.88	6.51	3.37	4.04	(-) 0.67	9.46	8.15	(-) 1.31

18.57 The transaction costs of SLDBs are around 1.35 per cent. In view of the increasing trend in the establishment cost, the transaction costs may be assumed at 1.5 per cent. Further 0.5 per cent may be required for generating adequate surplus. Thus the SLDB will require gross margin of two per cent. The rate of interest to be charged by SLDB to PLDB should be such that the gross margin available for the SLDB is not less than two per cent. It should be clarified in this connection that the gross margin requirements for a PLDB and the SLDB under the federal system are for enabling each of the two institutions to work profitably as a separate entity, and are not to be aggregated although it is incidentally observed from table 3 that the gross margins presently available to the structure as a whole i.e. the PLDB and SLDB taken together, earns a gross margin higher by 0.46 per cent under a federal system as compared with the unitary system.

State Land Development Banks - Unitary System

18.58 The states of Maharashtra and Uttar Pradesh have a unitary system of land development banks. The general information of these banks is given in table 19 and 20. It will be observed therefrom that the average annual working capital is about Rs.477 crores, of which the borrowed funds amount to about 63 per cent.

18.59 The average cost of raising resources in these two states is 6.51 per cent. The income from agricultural loaning is about 9.88 per cent, the gross margin thus being 3.37 per cent. The net margin works out to (-) 0.67 per cent, the transaction costs being 4.04 per cent. The net margin for the institution as a whole is (-) 1.31. Further, the risk cost of one per cent will also have to be provided for. It will be observed from table 20 that SLDB (UP) is able to break even for the bank as a whole, while the SLDB (Maharashtra) is having a negative net margin of 2.61 per cent. However in respect of agricultural finance, the net margin of SLDB (Maharashtra) is only (-) 0.71. To enable the SLDB in unitary system to be self supporting in respect of its advances for agriculture and allied activities, the gross margin should be adequate to cover the transaction cost and the risk cost and leave some surplus. The transaction cost is about four per cent and the risk cost is about one per cent. About 0.5 per cent may be required for generating adequate surplus to enable the bank to make the agricultural credit profitable. Thus the gross margin required is 5.5 per cent. The rates of interest for small farmers and for the

medium and large farmers may be so fixed that the emerging gross margin will not be less than 5.5 percent for the SLDB in the unitary system.

Regional Rural Banks

18.60 In the case of RRBs, financial cost, transaction cost and margins have been analysed for the system as a whole. The general information about the Regional Rural Banks is given in table 21. It would be observed that on an average each bank's area coverage is about 14000 square kilometers. The number of borrowers per branch at 708 is marginally higher than 668 borrowing members per PACS.

Table 21

General Information pertaining to Regional Rural Banks

Bank	Total Area (Sq.Km.)	Total Population (Lakhs)	Branches (No)	Borrowers (No)	Per Branch Borrowers (No.)	No. of families (Lakhs)	Effective coverage (Percentage)
1. S.V.G.B.	15152	27.47	66	69969	1060	5.90	11.80
2. S.A.G.B.	19134	26.18	67	50448	843	5.60	10.08
3. P.G.B.	NA	33.30	150	154704	1031	7.40	20.90
4. N.M.G.B.	5676	29.70	118	172128	1459	5.51	31.23
5. A.I.G.B.	17790	36.65	48	12428	259	7.10	1.75
6. G.G.B.	2716	28.00	112	89899	803	4.44	20.24
7. H.G.B.	15250	17.59	91	37786	415	3.42	11.04
8. P.G.B.	27217	79.06	134	59367	443	14.47	4.10
9. K.B.N.R.K.I.	14262	8.25	43	12751	297	1.77	7.20
10. R.K.G.B.	12527	26.70	68	35282	519	4.79	7.36
11. A.G.B.	9344	36.29	113	74061	655	6.92	10.70
Average	13907	31.74	92	69893	708	6.12	12.40

18.61 Information on some of the key aspects of the working of the RRBs as a system worked out from the data pertaining to December 1986 is given in tables 22 and 23.

Table 22

Financial Information on certain key aspects - Regional Rural Banks

	<u>Rs. crores</u>
Deposits	1,715
Advances	1,785
Borrowings	995

Table 23

Key Index of working results - cost and margins

	<u>Per Rs.100/-</u>
Transaction cost per Rs.100 of advances	6.90 (A)
Average rate of earning per Rs.100/-	11.00 (B)
Average cost of funds (per Rs.100)	7.80 (C)
Gross Margin	3.20 (D)
Net Margin	(-) 3.70 D-A

Source : Report of Consultant II on 'Role and Effectiveness of Lending Institutions'.

It would be observed from the figures given above that a RRB incurs a net loss of Rs.3.20 for every Rs.100 advanced by it. Since the total lending of a RRB is confined to the target group which has the benefit of the concessional rate of interest, the gross margin and net margin figures are almost the same for both agricultural and other advances.

18.62 For RRBs to be self supporting in respect of their lending operations, the gross margin should be adequate to cover the transaction cost and the risk cost and leave some surplus to take care of future eventualities and build up adequate reserves. The transaction cost and the risk cost being Rs.6.90 and Rs.1.25 (vide para 18.24) respectively, the gross margin requirement in the case of a RRB would be Rs.8.65 per Rs.100/- of advances, taking Rs.0.50 as the surplus required at the minimum. Since the financial costs is Rs.7.80 and the transaction costs, etc. are Rs.8.65, the minimum lending rate will have to be 16.45 per cent per annum. The

RRB caters exclusively to weaker sections for whom we have in fact recommended concessional or lower interest rate. We therefore, face a situation in which RRB will need to have lending rate of 16.45 per cent. This obviously is not possible since the target group of RRBs will wholly consist of borrowers whose interest rate on loans will be in the lowest band. Consequently the RRBs could hardly ever become viable. For this reason, among others it has been recommended elsewhere in this report that the RRBs be merged with the concerned sponsoring banks.

Commercial Banks

18.63 Certain key financial indicators for the commercial banks as a system, revealed from the analysis of financial performance of the sample units selected by the consultants are given in table 24.

Table 24

Key Indicators of working results - Commercial Banks

		(Amount in Rs.)
Average rate of earning per Rs.100	:	11.62
Average cost of funds (per Rs.100)	:	7.48
Transaction costs	:	6.00
Gross margin	:	4.14
Net margin	:	(-) 1.86

18.64 It would be observed that the cost of raising resources of Rs.100, on an average is Rs.7.48 for a commercial bank as a whole and there are not much variations in this regard from bank to bank. The average income realisable due to agricultural advances is Rs.11.62 on Rs.100 outstanding advances resulting in the gross margin of Rs.4.14. The transaction cost in respect of agricultural credit is estimated to be between Rs.6 and Rs.7.50 on Rs.100 of loans outstanding. However, the same may be taken to be nearer Rs.6 rather than Rs.7.50, as the transaction cost of the majority of the commercial banks is around Rs.6. Hence, for further analysis Rs.6 is taken as the transaction cost. The net margin, thus, works out to be (-) 1.86. The risk cost is estimated at one per cent according to the claims settled by DICGC. However, the institutional margin in respect of the commercial banks i.e. considering all the income generating activities and the corresponding expenses, is estimated

to be about Rs.0.20 for every Rs.100 working capital deployed by the bank.

18.65 The general information about the branches of commercial banks categorised as urban, semi-urban and rural is given in table 25.

Table 25
General Information about Commercial Bank Branches
Visited by Our Consultants

Particulars	Urban	Semi-Urban	Rural	Average/Total
1. No. of units	9	22	69	100
2. Staff strength	33	17	12	15
3. Deposits (Rs. lakhs)	383	181	68	211
4. Cost of Deposits	7.61	7.06	6.71	7.13
5. Working Capital (Rs. lakhs)	445	237	83	255
6. Advances (Rs.lakhs)	145	115	52	104
* 7. Transaction costs	4.21	4.02	4.71	4.31
* 8. Gross Margin	3.94	4.38	4.66	4.33
* 9. Net Margin	(-)0.27	(+)0.36	(-)0.05	(+)0.01
@10. Gross Income	9.54	8.50	9.34	9.13
@11. Gross Expenses	9.34	8.46	9.80	9.20
@12. Margin	(+)0.20	(+)0.04	(-)0.46	(-)0.07

Note : * pertain to agricultural credit

@ pertain to bank as a whole.

18.66 It would be seen from the above that the transaction cost is higher in the case of rural branches as compared to urban and semi-urban branches. A noteworthy fact is that more number of branches with agricultural advances of Rs.50 lakhs and above have lower transaction cost as compared to those branches which have agricultural advances of less than Rs.50 lakhs as may be seen from table 26.

18.67 It would be observed from table 25 that the rural branches as a whole have a small negative margin. However, the rural branches of commercial

Table 26

Agricultural Advances & Transaction Costs

Agricultural Advances (Rs.in lakhs)	Transaction costs on Rs.100			Total
	Less than 5	5-7	7 and above	
Less than 20	58	21	21	100
20 - 50	74	18	8	100
50 - 80	76	23	1	100
80 and above	100	-	-	100

banks earn a higher margin for agricultural advances as their financial costs are lower as compared with other financing agencies viz. co-operatives and RRBs who pay higher interest rate of 1/4 to 1/2 per cent on deposits.

18.68 It would be observed from paragraph 18.64 that the transaction cost on account of agricultural credit operations by a commercial bank is about six per cent. In view of the estimated risk cost of one per cent, the gross margin requirement works out to be seven per cent in respect of agricultural lendings by a commercial bank to enable it to be self supporting. The concessional rate of interest applicable to the small farmers for crop loans and the concessional rate applicable to small farmers in respect of term loans issued by PLDB would also be applicable to the similar borrowers who will be availing of credit from commercial banks. In respect of the other advances there should be no regulation in respect of the rate of interest. However, the ceiling rate of interest on such advances may be fixed at 15.5 per cent per annum. The rates of interest on agricultural loans to the different classes of borrowers by size or purpose may be so fixed as to yield a gross margin of not less than seven per cent.

National Bank for Agriculture and Rural Development (NABARD)

18.69 The total direct institutional finance in the country for agriculture and allied activities dispensed by all the formal lending institutions together stood at Rs.15,883 crores at the end of June 1986. Of this, NABARD's contribution was about 45 per cent. It will be seen from table 27 that NABARD's contribution in proportionate terms has remained almost the same during 1984-85 and 1985-86. The trend appeared to be that the share of co-operatives (both production as well as investment credit) in the NABARD's refinancing volume was on the decline over the years. In contrast to this, the share of both CBs and RRBs have increased in the process.

Table 27

Refinance from NABARD

Institutions	Share of NABARD in total Agricultural Credit					
	Total Loans outstanding as on 30th June			Of which from NABARD as on 30th June		
	1984	1985	1986	1984	1985	1986
Co-operatives	5734	6367	6896	2692	3185	3335
Scheduled Comm. Banks	5280	6613	8116	2099	2669	3331
Regional Rural Banks	509	693	871	207	347	505
Total	11523	13673	15883	4998	6201	7171

NABARD Margins

18.70 The results of the analysis of NABARD's margin, based on the data for the year 1983-84 through 1986-87, as revealed by the annual financial statements, are summarised below :

Scenario I

i.	Proportion of equity in the working capital	:	46.26
ii.	Proportion of debt in the working capital	:	46.39
iii.	Debt - Equity ratio	:	1:1
iv.	Proportion of advances to working capital	:	78.00
v.	Gross income realisable for every Rs.100 of working capital	:	6.85
vi.	Gross expenditure for every Rs.100 of working capital	:	3.38
vii.	Margin	:	3.47

Scenario II

18.71 Scenario I does not take into account the opportunity cost of equity, which if taken into account at the rate of six per cent will result in increasing the gross expenditure to Rs.6.17 for every Rs.100 working capital and the NABARD's margin will therefore be 0.68 per cent.

Scenario III

18.72 NABARD's lending rates in respect of short-term credit especially for

co-operatives stand reduced, effective from 1st March 1988. The lending rates for SCBs are determined by the proportion of average borrowings from NABARD to the average outstandings. Such lending rate is estimated (by Consultant IV) at 4.60 per cent. Considering that other things remain unchanged, there will be marginal decline in NABARD's income, with the result, the margin can be estimated at about 0.60 per cent. The growth rates of total income and cost of NABARD are about 14 per cent and 7 per cent respectively per annum. In view of this, the margin is likely to remain at about 0.60 per cent.

18.73 This margin of about 0.60 per cent is fairly adequate so long as NABARD confines only to refinancing activities. A higher margin for NABARD will be required to enable it to take up developmental activities aimed at improving the financial health of the client credit institutions and for taking up more promotional activities.

The Emerging Position in Brief

18.74 Given the scenario of administered rates of interest and the concessionality in favour of weaker sections in India, the margins available to lending institutions have tended to become narrower. The available margins are not enough and hence the profitability and viability of credit agencies are endangered. Financial viability of lending agencies is essential for improving and enlarging the quantity and quality of their services to meet the future challenges.

18.75 With the introduction of service area approach, it is expected that there will be intensive financing in rural areas for seasonal agricultural operations, and there would be increasing adoption of project approach to lending in respect of investment activities. These improvements, however, are likely to reduce the transaction costs for agricultural finance. Consequently, there would be a reduction in the margin requirements. But this would take time, may be a few years, during which period the position of some of the critically placed institutions will be further affected. It is in the light of these considerations that we have, as already discussed, come to the conclusion that the gross margin required in respect of agricultural lending only, for each of the institutions would be as follows :

<u>Institution</u>	<u>Gross Margin</u>
1. PACS	6.0 per cent
2. DCCB	3.5 per cent
3. SCB	1.5 per cent
4. PLDB	5.0 per cent
5. SLDB-Federal	2.0 per cent
6. SLDB-Unitary	5.5 per cent
7. RRB	8.65 per cent
8. CB	7.0 per cent

The margin needed for RRBs at 8.65 per cent to function on a viable basis is, on the face of it, disproportionately high, and given the restricted classes of borrowers they are expected to serve, it is on all counts an impossible task to work up to. It is in view of this among others, that we have elsewhere in the report, recommended their merger with the more resilient sponsor banks so that the commitment to serve these classes of borrowers could be honoured without any further external subsidies to keep the institutions going. Unlike the RRBs, in whose case their lendings are substantially, if not wholly, for the weaker sections with little or no scope for cross subsidisation, in the case of commercial banks, there is considerable scope for cross subsidisation. In co-operatives also, there is some scope for cross subsidisation though not in all cases necessarily or on the same scale as in the case of commercial banks. The gross margins which are in fact nominal interest margins as shown above are the requirements of such margins purely for the agricultural loans portfolio to attain viability solely on these operations. With the scope for cross subsidisation increasing the institution concerned would however be able to live with even somewhat lower margins. But it must also be stated in this connection that the gross margins at the SCB and DCCBs level as shown are merely indicative of the margins required for these institutions to work on a profitable basis with a portfolio consisting of only agricultural loans at the existing levels of interest rates. In these cases also, as the scope for cross subsidisation increases, the gross margin requirements will be lower. It also follows therefore, that the gross margins separately indicated for SCB, DCCB and PACS are not to be aggregated and the resulting sum of 11 per cent construed as the margins required for the structure as a whole. The margins shown against SCB and DCCBs constitute the basis for determining the permissible limits of internal resources that can be deployed

for agricultural lending at existing levels of interest rates without jeopardising the viability of these institutions.

Certain concluding observations

18.76 In closing it must be said that given the highly complex administered rate structure on the one hand, and mandatory lending to certain target groups involving a high degree of concessionality on the other, to subserve the social objectives set out by Government, policy formulation on interest margins becomes an all the more a difficult task. In addressing this task in this chapter, we had to reformulate the future policy framework keeping in view in the first place, the need to maintain both the mandatory lending and the concessionality but within the tolerance (or in other words, absorbable) limits of the credit system. Further, having regard to the market distortions, the danger of leaving interest rates entirely to market forces, and consequently, the need to have a certain degree of regulation regarding interest rates had also to be recognized. Secondly, we had to keep in view the fact that a long period of over administered rates had brought about certain distortions in the credit system. We had also to take note of the fact that the viability of intermediaries viz., the institutions comprising the credit system, cannot be considered in isolation of the viability of the other participants in the intermediation process, viz. the suppliers of funds and the users of these funds. But their health, it was recognized would not by itself perhaps be a sufficient condition for ensuring the viability and strength of the credit system. For, the environment impacting the working of the credit institutions comprising the policy, the legal, and regulatory framework as well as the political and economic climate under which the institutions operate, had also to be conducive to their efficient functioning. We have discussed in the relevant chapters among others, these aspects as well which impinge on the health of the credit system.

18.77 Important as the general considerations are and critical to interest rate policy, our immediate major concern in this chapter is margin requirements. It therefore needs to be restated, if only to re-emphasise the point, that margins are not merely a function of interest rates paid on raising resources and incomes earned on loans and advances, but equally a function of transaction cost, which in turn is a function of institutional efficiency and the volume of

business handled. Therefore given the interest rates on deposits and loans, the endeavour both in co-operative and commercial banking systems, has to be towards improving the quality of service and increasing the volume of business so that the transaction cost per unit is brought down to the minimum. The experience of commercial banking system has demonstrated that this is possible. For instance, the ratio of establishment expenditure (salary, pension, gratuity, provident fund and other expenses pertaining to staff) to the total expenses (establishment expenses and other expenses such as stationery, printing and interest paid on deposits and borrowings including refinance) of the system which stood at 23.44 per cent of the total expenses when the loan outstanding was Rs.6.73 lakhs per employee as on December 1984, has according to a study made by Indian Banks' Association, since come down to 22.54 per cent as on December 1986 with the level of loan outstanding rising to 7.92 lakhs per employee. Similarly, another exercise carried out by the public sector banks reveals that the cost of supervising Rs.100 of the agricultural advances has come down from Rs.3.25 in 1984 to Rs.2.84 in 1986. The findings of the two studies clearly point to the fact that with quantitative expansion of and qualitative improvement in the business, the economies of scale would operate increasingly resulting in lower per unit cost and consequent higher margins. Elsewhere in this report we have made a number of suggestions for improvements in these areas.

CHAPTER XIX

AUTONOMY OF CREDIT INSTITUTIONS

The commercial banks in a short span of two decades since nationalisation have witnessed massive expansion both in their branch network and diversification of their loan portfolio. This expansion has not, however, been without the concomitant stresses and strains to which the system has been increasingly subjected. One area where the system has experienced considerable strain has been the large scale recruitment of personnel, their training in the new skills and orientation to the new challenges as well as their placement over widely dispersed branches in the remotest of areas. While banks have taken several steps including reorganisation of their internal structures, the strain persists and we have made some suggestions in this regard in the earlier chapters. A major casualty has been the quality of their credit portfolio as reflected in the mounting overdues of agricultural loans and sticky advances locked up in sick units in the industrial sector. A precise estimate of overdues in the industrial and trade sectors is difficult since unlike in the case of agricultural advances where loans are advanced for specific periods, the working capital advances for trade, commerce and industry are by way of cash credit and the prospect of non-recovery becomes discernible only when the units have actually turned sick. However, even on this reckoning, the overdue loans to sick units aggregated Rs.10,972 crores working out to 17.4 per cent of advances outstanding against this sector. Overall recovery of agricultural dues has hovered within the range of 55 per cent to 60 per cent of demand accounting for overdues at 40 per cent to 45 per cent of demand. While the yield on investments has increased, primarily as a result of a higher return offered on Government paper, the average yield on advances has declined steadily. Two factors which account for the declining return on advances are :

- (a) progressive reduction in interest rates on priority sector advances; and
- (b) increasing volumes of non-performing assets.

The increase in recent times of the SLR and Cash Reserve requirements have also contributed to this in some measure on account of the pre-emption of substantial portions of their deposit resources from deployment in advances,

although the increase in the yield on Government paper in recent times and the interest allowed on CRR beyond the basic minimum have both helped the banking system to keep their losses on the pre-empted portion to the minimum. Similarly, while this (the pre-emption) has reduced the quantum of loans locked in overdues through a reduced volume of lendings to high risk areas, it has adversely affected the banks' capacity for lendings which gave substantially higher interest returns carrying minimum risks thereby bringing down the scope for cross-subsidisation. The net result has been an erosion on the profitability of the banks over a period of time. Figures from published balance sheets show that as a percentage of working funds, profits ranged in the region of 0.09 to 0.17 between 1984 and 1987 respectively. The low levels of profitability the system has touched, coupled with its somewhat declining trend indicative of the system heading towards serious financial crisis, have been causing concern all round. We share this concern.

19.02 While one reason for the declining profitability is the increasing involvement of the banks in 'priority lendings', otherwise known as 'mandatory credit' which entails 'target setting', it would not be correct to lay the blame entirely on such lendings. The phenomenon of declining profitability is, in our view, more the result of the irrational manner in which the enlargement of the coverage of, and the enhancement in, the rate of concessionality for the 'mandatory credit'. Also, such 'mandatory credit' in itself need not lead to 'declining' profitability below the tolerance level of a bank if the deployment of the resources of the banking system in support of the social concerns of the state is so regulated that it ensures that the higher yields on the commercial lendings of the banks are adequate not only to make good the losses arising from the concessional lendings but also provide enough cushion for maintaining the banks' viability. In other words, the malaise lies in the loan portfolio of banks which yields low returns with high risk-costs being stretched beyond limits which the banking system could contend with.

19.03 We also firmly believe that in directing the banks to take up such areas of social responsibility, their right to make commercial judgement on specific credit proposals should not be subordinated to the judgement of the administrative machinery of the Government. And to the extent Government directed lendings are stretched beyond what the element of cross-subsidi-

sation in the banking system permits, the Government should assume the burden. Similarly, in the co-operative banking system, partnership in its equity by the state governments which was intended to infuse financial strength into the system and not to interfere with the democratic management of the co-operative institutions has, however, had the curious and contrary effect of governments' total interference with the system in its management and operations. In the result, we have both the systems totally controlled by the Government - the state governments in the case of co-operatives and the Central Government in the case of commercial banks including the RRBs. The control has become so complete today in both the institutional structures that in a sense, a large part of credit from both streams, seems to be taking after the age old form of 'Taccavi'.

19.04 This is not to suggest that credit systems in the country have to distance themselves from development programmes or that they should not be involved. On the contrary, we believe that the banks must fully involve themselves in supporting such development programmes as the Government might evolve in the furtherance of its social objectives. The point we would, however, stress is that once the priorities have been determined and the target groups specified, within these groups, prudent commercial judgement of the banker should prevail in the selection of the individual loanees and the sanction of projects and loans to them. It is interference with the bank managements' discretion to exercise such judgement in loan sanctions and enforcement of recovery of such loans including those in respect of poverty alleviation programmes that we are opposed to. If appraisal procedures and established credit norms are short-circuited to suit populist goals and if serious inroads are made into the functional autonomy of the institutions, that will ultimately be destructive not only of the credit delivery system but in the long run, of the programme itself where credit has to play a socially desirable goal. It is also not our intention to suggest that the credit component may not carry certain concessionality either, but such concessionality has to be in a manner that firstly, the beneficiary does not perceive the loan merely as a grant and secondly, as for the institution, it is not denied due compensation for financial and service costs of such credit. After all, the basic objective of building a credit component into such programmes is that in combination with the subsidy, the vast masses of beneficiaries could be brought within the process of the credit discipline so that when the projects turn viable,

they would have become used to these disciplines. If this does not happen, such programmes are likely to bring about, even in the best of circumstances, only larger numbers getting caught in what may be described as a 'debt-trap', their indebtedness mounting rather than their activities becoming economically viable even over a period of time and their deriving the expected benefits by development banking.

19.05 The short point that we wish to stress is that while the Government might lay down sectoral priorities in the deployment of resources and within the priority sector such of the programmes which are intended to subserve the social objectives in conformity with the state policies aimed at the economic development of the large masses of people, the banks will have to be left free to exercise their banking judgement in the appraisal as well as sanction of individual loan applications within the identified sectors and beneficiary groups. The limits upto which banks may involve their funds for the purpose should themselves be determined by the Reserve Bank taking into account the capability of the system for cross-subsidisation. External intervention of any kind in these areas, besides weakening the credit system, could also lead to the progressive dilution of the accountability of the administrators of credit in the system. Secondly, such interference cannot be totally free from the pressures of the political system under which the Government functions and nothing can spell greater danger to the credit system than this. In the chapter on 'Co-operative Banking System - An Overview', we have already referred to the growing politicisation and external pressures on the credit system. These are dealt with in greater detail in the following sections.

Populist Approach to the Credit System

19.06 In Chapter V we have referred to the report of the CRAFTCARD as well as the report of the Venkatappiah Committee on the role of National Co-operative Societies and their strong plea for depoliticisation of these institutions. During our visits to different institutions in various parts of the country, we were told about the growing external pressures, particularly pressures, from government functionaries on the credit agencies including the commercial banks and RRBs. While in the co-operatives politicisation as we had occasion to discuss in an earlier chapter, generally starts with the political functionaries taking up the reins of management in these institutions either through the normal electoral processes, albeit with the use of political

influence and where this fails, through wholesale supersession of elected boards by the state governments, in commercial banks, this is done through nomination of Directors whose qualification is their acceptability to the Government rather than their professional credentials as was intended both under social control and the scheme for nationalisation. Furthermore, during the last three years or more, full boards have not been constituted in any of the twenty nationalised banks in the public sector and these banks are functioning with only the Government and Reserve Bank nominees on their boards who often reflect Government's concern rather than share with the Chairman-cum-Managing Director of the bank concerned, their professional judgement in taking banking decisions on the proposals coming up before the Board. In some banks, however, the employee representatives do continue on the Boards under court orders.

The Co-operative Credit System

19.07 The areas in which, and the extent to which Government interference and other external influences operate in the working of the co-operative banking system have been dealt with at a great length in the Chapter on 'Co-operative Banking System - An Overview'. To briefly recapitulate, the more vulnerable areas are, as in the case of nationalised banking system, (a) management and (b) sanction and recovery of loans. In both areas, interference operates largely through politicisation. In management, such politicisation works at two levels. In the first place, attempt is made to capture the management through the customary electoral process. When this fails, such control is taken over through arbitrary supersession of the elected boards by invoking powers vested in government. At the second level, this control is further buttressed by placing government officials to hold key positions such as Chief Executives in co-operative banks. While political groups capturing management either through the electoral process or supersession of boards results in serious set-backs in the working of the institutions when another group or their patrons come to power in the state, the imposition of the government officials at the top level, affects the morale of the banks' staff and creates, among the qualified and experienced employees, a sense of frustration which becomes a serious constraint to banks building up their own cadres of key personnel. The cumulative effect of all these has been the growing erosion in the viability of the co-operative banking system. We have already referred to the tendency on the part of state governments to show total indifference to either effecting or helping recovery of dues to the co-operatives, more especially close to

general elections to the State Legislative Assemblies or national Parliament. What is more, they even exhort people from political platforms, not to repay their dues. There have also been instances, as we have pointed out elsewhere in this Report, of the election manifestos of political parties containing promise of write-off of co-operative dues, as a bait for attracting votes. It is often argued that a government measure such as this, viz., write off, does not put the credit system per se, into loss because the government concerned makes good the amount, but it has been observed that in practice, once the loans are written off, the governments adopt an attitude of indifference to honouring the commitment. Besides such indiscriminate write-off generate a general psychology of non-repayment vitiating the recovery climate which, in the long run, is likely to affect adversely the financial health of credit agencies. The impact of such a measure on the credit administrators has also been counter-productive.

19.08 Equally adverse has been the impact of officialisation in the co-operatives, to which there is already an earlier reference. In most cases these officials have neither the requisite experience nor are they able to bring in any degree of professional management. In fact this stifles the personnel of these institutions developing professionalisation within the cadre. The deputationists are in addition subject to frequent transfers resulting in lack of their enduring interest or involvement in the development of the institutions. We have illustrated this with relevant data in Chapter V. Thus, while in Uttar Pradesh the co-operative banking system is wholly officialised with the positions of Chief Executive of both apex institutions and DCCBs filled in by officers on deputation from state government, in Rajasthan, Punjab, Karnataka and Haryana most of the CCBs are headed by departmental staff. Similarly, in Punjab not only Managing Directors, but Deputy General Manager, Inspectors, Assistant Inspectors, Establishment/Statistical officers in the SCB are all officials belonging to the state government, while in Bihar the approved staffing pattern itself stipulates the manning of the institutions at the higher levels by government officials placed on deputation. Similarly, in West Bengal, three top officials in each co-operative bank have got to be government officials on deputation. There has been in almost all cases infiltration in the ranks of supervisors as well. In the process, the major casualty has been the professionalisation of management in the co-operatives.

Commercial Banks and RRBs

19.09 In regard to state control whether in its sweep or depth, the position in the commercial banking system including the RRBs is no different from that in the co-operatives, except that in the case of the co-operatives, the concerned government is the state government while in the case of the former it is the Central Government. Commercial banks today are as over-controlled, over-regulated and over-managed by the Central Government as the co-operatives are by the state governments/RCS concerned. In commercial banks it is primarily in the implementation of the special programmes which are ostensibly intended to subserve certain identified social objectives that politicisation manifests itself most brazenly. Particular mention may be made in this connection to the poverty alleviation programmes. It is not our contention that the banking system has either no social obligation or that poverty alleviation should not be a top priority on the agenda of the Government. On the contrary, we do recognise that in a welfare state, the Government has a special commitment to the removal of poverty. Equally strongly, the banking system in the context of socio-political milieu in the country, particularly after nationalisation, cannot absolve itself of its social obligations to assist the Government in its programmes intended to subserve some of the social objectives. But the point which needs to be taken note of is that in all programmes relating to fulfilment of social objectives, there is an area which can be clearly demarcated where the responsibility could be substantially shared by the banking system without weakening its structure. Such issues are subject matters of discussion in dealing with topics such as IRDP, role of RRBs etc. We would, however, like to refer to the CRAFTICARD view that the responsibility of the banking system should be confined to those classes of beneficiaries who with bank finance can graduate to viable status. The others should quite clearly be the responsibility of the state. In the discussions here, however, where we deal with politicisation, the immediate context is the manner in which Government's ownership of the banking system comes to be used as an instrument to promote interests of a 'populist' nature more than the fulfilment of the social objectives which are intended to be subserved through bank finance. An instance in point is the growing compulsion on banks to provide financial assistance to projects which are not even potentially viable and borrowers whose commercial viability cannot be improved with bank finance. Put differently, when programmes which ought to be funded from Government resources are sought to be funded through bank finance,

they do endanger the financial stability of the banks and, therefore, in the long run are destructive of the institutional structure without ultimately subserving, in any appreciable measure, the furtherance of the programme itself. The danger is all the greater where the beneficiaries of such programmes are selected not on the basis of the very criteria laid down under the programmes themselves, but are selected on extraneous considerations and are given loans without proper scrutiny, allowing the message to percolate to the beneficiaries that even the loan component under such programmes represents assistance from the Government. In the result, they (the beneficiaries) do not get to realise the bank-client relationship in respect of the related transactions. This leads, and has in fact led, to large scale defaults to the banks. What is even more dangerous is that within the banking system itself, this kind of loaning generates a psychology of permissive lending in regard to the other types of lending as well, with all its deleterious effects on the system.

19.10 Yet another example of external pressures operating on the commercial banking system is the phenomenon of disbursement of loans, particularly, those under the poverty alleviation programmes at public rallies which in common parlance is known as Loan Melas, but described in the official circulars and literature as accelerated loan programmes/disbursements. Certain studies conducted by some of the banks have revealed that a large number of beneficiaries who have been disbursed loans at these Loan Melas have been identified not only not by the banks or even by governmental agencies but by political party functionaries. Many instances have been brought out by these studies, of the loan applications not having been scrutinised adequately or at all or not even collected well in advance. There have also been instances where the beneficiaries under these programmes whose loan applications had been duly scrutinised and loans sanctioned, but refused disbursement unless they came to the rally where a particular designated political functionary in Government disbursed the loans. As has already been alluded to, where a political functionary disburses a loan and not the bank which sanctions it and provides the finance, the bank-client relationship gets lost and the bank's authority to demand repayment gets equally eroded. A further dimension to this is that since these are subsidy-linked loans, the borrowers are unable to make a distinction between the subsidy and the loan portions, more so when a political functionary in Government distributes the loans. This would be evident

from the fact that recoveries under IRDP loaning are lower than those under other rural/agricultural loans.

The National Bank for Agriculture and Rural Development (The NABARD)

19.11 Visualised as the apex body for the agricultural credit system at the national level and established less than a decade ago, the NABARD operates within the framework of broader policies and guidelines laid down by the Reserve Bank and Government of India. It has consequently evolved itself essentially as an instrument of, and a technical agency for the formulation, execution and monitoring of national policies in relation to the working of the agricultural credit system. As envisaged by the CRAFTCARD and provided for in its statute, the NABARD is, in a sense, the outcome of an exercise in the decentralisation of the functions of the Reserve Bank. Accordingly, while the operational areas have been entrusted to the NABARD the overall policy rests with the Reserve Bank and Government of India. Nevertheless NABARD's counsels and advice has continued to form the basis of such policies.

19.12 In operational matters relating to agricultural credit, NABARD has emerged as the apex body at the national level. Its responsibilities in this area include statutory inspections of the co-operative banks as well. The NABARD has however, to face constraints of a varied nature in many of its operational areas. These constraints arise more from the pressure on either its client institutions or from the Government - Central Government pressures on commercial banks in the areas of priority sector lending and poverty alleviation programmes and state government pressures on the co-operative credit system resulting in arbitrary writes off, interest subsidies and politicisation of their management all of which ultimately erode NABARD's effectiveness in its ordering or re-ordering of the operations of its client banks. Thus, in the case of NABARD, Governmental and political interferences are somewhat indirect rather than direct and this make its tasks of containing the pressures even more difficult. To take one instance, the reductions in interest rates announced in 1988-89 budget for agricultural loans across the board, has left the NABARD with no working margin on the refinance provided by it to the co-operative banking system from out of the general line of credit from the Reserve Bank. Another instance is the interest subsidies announced by some of the state governments which have brought down the effective interest rates resulting in the NABARD's credit disciplines for the co-operative credit system inoperative in these states besides the uncertainty it has generated in the proper use of credit

by the borrowers. The various steps taken by the NABARD to mitigate the adverse effects of these measures by Government initially met with considerable resistance from the concerned state governments. It was only with the Government of India stepping in that the conflict could be resolved. This apart, the reduction in interest rates on agricultural loans has robbed the co-operative credit system of its even otherwise low margins at different levels on the refinance provided by it and NABARD had to work out certain arrangements for compensating the co-operative credit system and to restore to it the margins it had earlier.

19.13 The governmental and other pressures which adversely affect the working of NABARD and its effectiveness in enforcing the needed credit disciplines on the credit delivery system are thus more in the nature of the impact of the mounting pressures on its client banks. These and the steps which need to be taken have been discussed under governmental pressures on, and autonomy of, the co-operative credit system and the commercial banks. The situation calls for the NABARD establishing closer relationship with the client banks and, if necessary, use more meaningfully and effectively, the leverage it has through refinance coupled with the statutory status its inspections enjoy over the co-operative banking system to stem the state governments' pressures on the co-operatives.

The Reserve Bank

19.14 What has been a disconcerting trend is the growing inroads by the Government into the areas of responsibility of the central monetary authority, viz., the Reserve Bank itself. Illustratively, to take one area which is its direct responsibility as the Central Bank of the country, it is its responsibility to formulate the regulatory framework relating to the ebb and flow of short-term credit and this area is, therefore, best left to its sole discretion. But in recent years, there has been an unhealthy trend of interference with such regulatory framework even if unintended, resulting in a serious threat to the health of the banking system. The distortions which have taken place as a result of several authorities in their own ways deciding or influencing the ultimate interest rate on short-term crop loans is a clear case in point. Reference has already been made to the reduction in interest rate on crop loans across the board as it were, in the last two budgets. This as we have already pointed out, necessitated the Reserve Bank and the NABARD in making

ad-hoc arrangements for a system of compensation to the co-operative banks to maintain their slender margins. Quite clearly, such an ad-hoc arrangement cannot be a substitute for a rational and stable interest rate structure.

19.15 A more disturbing trend in evidence in recent times has been the provisions of interest subsidy by state governments on crop loans effectively reducing the interest rate on such loans. Such interest subsidy at present is 5.5 per cent in Andhra Pradesh, whereas such subsidy varies from 2 to 5 per cent in other states like, Maharashtra, Tamil Nadu and Kerala. While the state governments direct the co-operative credit system to take the subsidy into account and lend the crop loans at the lower rate, the subsidy amount itself is not made good to the credit system on time. As at the end of December 1988, state governments owed to the co-operative credit system in the aggregate nearly Rs.170 crores on account of interest subsidy. Inclusive of other dues from state governments, the amount was as high as Rs.350 crores. While it is true that under Reserve Bank's directive, the NABARD has taken certain steps to combat this unhealthy trend, the distortions it has brought about as between states and as between different sectors cannot be rectified in the near future. This apart, such interest subsidies which in effect involve the borrowers being provided production loans at a very low rate are liable to be misused, because the borrowers could reinvest these in fixed deposits or relend them at higher interest. This could eventually affect adversely agricultural production itself because of such misapplication of the loans. These considerations apart, such interest subsidy interferes with the Central Banking function under a regime of administered interest rates on short-term loans. There cannot quite clearly be parallel centres of authority pursuing disparate interest rate policies.

19.16 Historically, the institution of a separate central monetary authority in the form of the Central Bank represents the recognition of the community's desire to have a discretionary element in the management of the monetary system in the country. Viewed in this context, the autonomy of a Central Bank is not merely a matter of academic interest, but is a matter of serious concern in a practical sense, in areas relating to counselling action and initiating measures in monetary management. While there are areas which are clearly the direct responsibility of Government and there are some other areas in which the Government and the Central Bank are both equally concerned,

it needs to be recognised that there are areas which are very clearly the direct concern of the Central Banking authority. The delineation of the areas of responsibility in this connection is of vital importance. It is in this context that it becomes necessary to invest the Central Bank with adequate authority not only in the formal sense but also in a practical sense so that it could function freely in areas which are directly its concern. Any undermining of that authority by Government will be the negation of the rationale of setting up a Central Bank as well as delineating its functions. The main function of a Central Bank and in India, of the Reserve Bank of India, above everything else is to control bank credit and all the other responsibilities that go with this besides regulating the issues of currency. The founding fathers of the statute under which RBI functions had envisaged an environment in which the Bank could effectively exercise its duties free from any governmental interference. It is to this end that it has been provided for in the Act that the Finance Secretary who represents the Government on the Board has no voting right.

19.17 The perceptions about the role of the Reserve Bank within the Government themselves especially when the question of nationalisation came up for consideration, were quite clear. It was emphatically stated that it would be the Government's concern to ensure that Reserve Bank's autonomy as a Central Bank will be fully respected. Thus winding up the debate on a Private Members' Bill in February 1947 demanding the nationalisation of the Reserve Bank, the Finance Member in the Interim Government, inter alia, said -

" . . . When we talk of nationalisation and if we decide to nationalise the Reserve Bank, we must see that whatever constitution is framed for that Bank, although it will be public ownership, it will not play the part of a subservient agent of the Government, whatever it may be at the time."

Again when the nationalisation bill was actually introduced by Government in the Central Legislature in September 1948, the Finance Minister in winding up the debate assured the House that -

" Although the framework of the administrative authority is being changed, we would see to it that the Reserve Bank of India continues to function as a fully autonomous body"

And yet more than four decades after these assurances became part of the proceedings of the Central Legislature (now the national Parliament), and the provisions inbuilt in the Statute to ensure this, the Bank's functional freedom, seems to get increasingly abridged.

Conclusion

19.18 The thrust of agricultural credit policy in India as discussed in this and various other chapters of this report has been its progressive institutionalisation and a degree of concessionality in interest rate on refinance from RBI to the co-operatives which until the sixties were the sole institutional purveyors of agricultural credit. Since the introduction of social control in 1967 followed by nationalisation of the banks in 1969, the policy of the top-down flow of concessionality from RBI to the co-operatives and the commercial banks in certain specified areas of investment finance has been supplemented by certain social obligations laid on the commercial banking system across the board which include participation in the credit-linked poverty alleviation programmes under which a subsidy component is built-in so as to make the programme viable in respect of individual loans. Against this background of the banking system being called upon to support a variety of programmes involving as it does what might be described as social banking, the banks can function effectively and the programmes expected to achieve the goals set, only if the credit system could operate free from external pressures and with the type of business efficiency associated with a healthy banking system. Any participatory arrangements on an institutional basis assumes mutual respect as between the parties and also respect for their respective roles. This is particularly necessary where financial risk-taking is involved by any one of the parties. Thus when banks are called upon to participate in Government programmes and the former are to take the load of risks in lending, their autonomy in areas which are their responsibility, viz., appraisal, sanction, disbursement and recovery of loans need to be fully respected irrespective of whether the institutions are nationalised or not. In the absence of such respect for the institutions by the Government, institutionalisation of credit itself ceases to have much relevance. There is also bound to be progressively an erosion of the financial health of these institutions which needs to be guarded against. Such progressive erosion of the respect for such institutions portends danger of a dimension which it is perhaps difficult even to assess at this stage. But we should add here that in stressing the urgent need to

arrest the increasing trend towards the progressive infringement of the authority of the credit system, our concern mainly is to draw attention to the dangers ahead, signs of which are in fact already evident. In other words, the case for respecting the autonomy is not for autonomy for its own sake, but autonomy in the larger interests of the healthy survival of the system and the State's social programmes which the system is called upon to support. In fact the gravity of the situation has been brought to public attention by the Union Finance Minister himself recently. In replying to a question on resumption of NABARD refinance in one of the states, the Finance Minister said in the Rajya Sabha on July 20, 1989 that neither the Centre nor the state governments should interfere in the working of banks, as this may result in the collapse of the system. It is hoped that this renewed thrust of non-interference in the working of the banking system would provide the much needed sense of direction to the agricultural credit system in discharging the onerous tasks assigned to them.

PART VII

ROLE OF THE APEX LEVEL

XX THE ROLE OF THE APEX LEVEL INSTITUTIONS,
RESERVE BANK OF INDIA AND GOVERNMENT

CHAPTER XX

THE ROLE OF THE APEX LEVEL INSTITUTIONS, RESERVE BANK OF INDIA AND GOVERNMENT

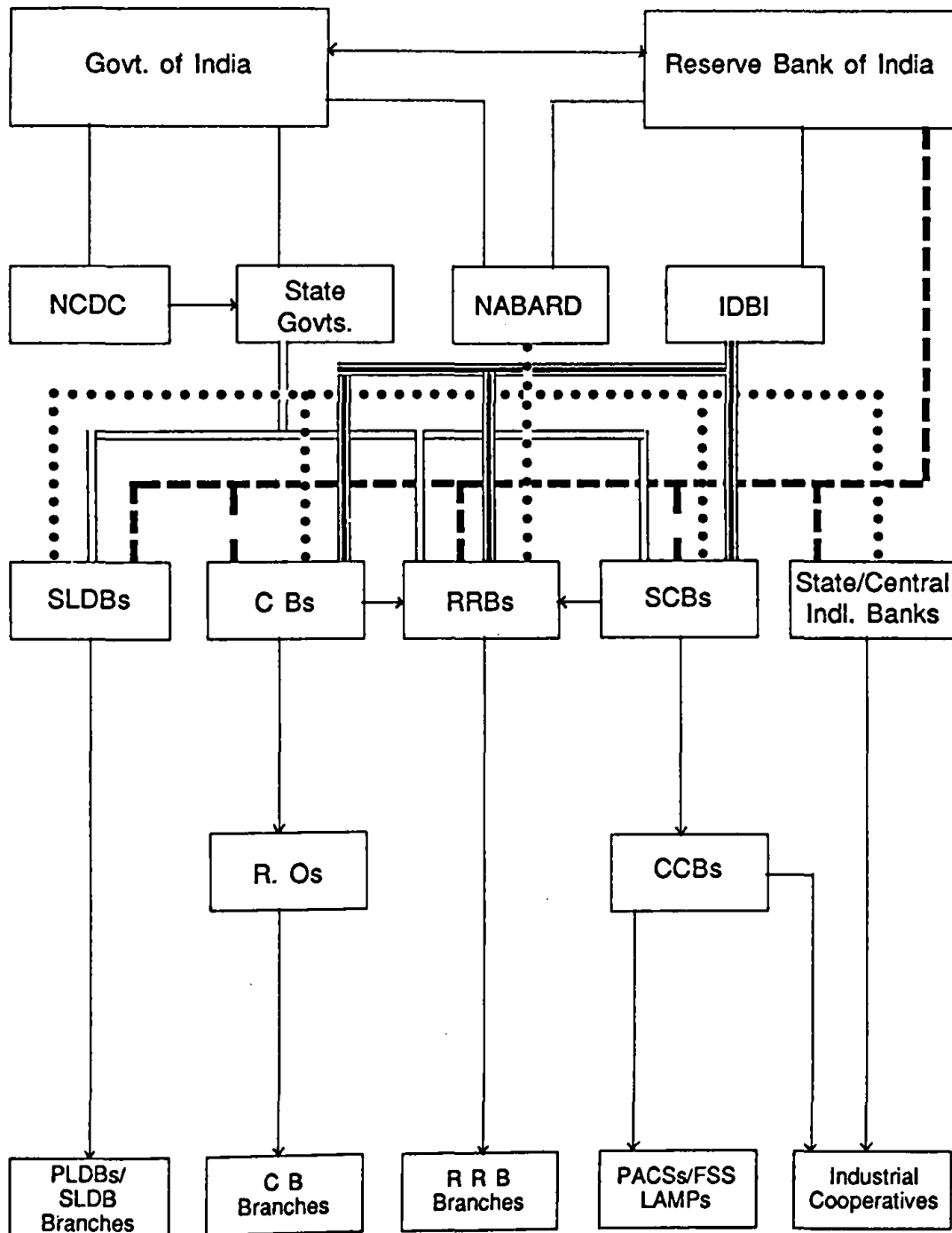
There had been general recognition from early days that with the country's vast size in area and population, the administrative machinery of Government needs to reach millions of people in several hundred thousands of far flung and widely dispersed villages, for effective governance. The revenue units which originally constituted the focal points of administration came to be established before and during the British days. With the passage of time, the provision of essential public services also came to be organised more or less on these lines, but the organisation of financial infrastructure was a much later development. When this came to be organised, banking and financial institutions developed along the lines of organised trade and commerce and hence came to be located in the metropolitan cities, larger towns and rail heads or ports. Even the indigenous money lenders who extended credit support to the farmers in the villages drew their strength through their close association and identification with the urban based financial infrastructure and therefore did not operate in the best interest of the farmers. Growing monetisation of the village economy on the one hand and mounting indebtedness and consequent alienation of land, etc. on the other, necessarily compelled the state machinery to take steps for institutionalising credit and extend the coverage down to the villages wherever possible. It was in this context, as has already been referred to, that the state machinery turned its attention to co-operatives. With Independence, however, there was a more determined effort to institutionalise credit and enlarge its coverage. Following the recommendations of the Rural Credit Survey Committee, not only effort but policy of the Government and of the Reserve Bank came to be directed towards making co-operatives the sole purveyors of rural credit. Nevertheless at the end of a decade and a half it was realised that with the new breakthrough in agricultural technology, the demand for credit increased phenomenally. As a result and as the Rural Credit Review Committee recommended, there was a need for a shift in policy towards a multi-agency approach to agricultural credit. Meanwhile, 14 major commercial banks came to be nationalised. This was followed by the induction of commercial banks in a large way

to extend agricultural credit support and an expansion of their branches to cover the far flung rural areas in the country. The organisation of RRBs in 1975 was yet another attempt in taking commercial bank credit not only to unbanked areas in the remote corners of the country but also to cater exclusively to the weaker sections of the society. In the result, there are today three streams of credit operating in the rural areas (a) the co-operatives, (b) the commercial banks, and (c) the RRBs.

20.02 Each of these three streams has its own distinctive organisational features; but in common all of them have a structural pattern which provides a machinery for dispensing credit at the village level. Whereas the organisation of the higher levels is by and large federal in the case of co-operatives, it is unitary in the case of RRBs and commercial banks. In the latter case there are controlling offices at the intermediate levels accountable to the head office organization at the top operating through a net work of branches. But all the three streams are ultimately linked, either through the state apex organisations in the case of co-operatives or through the head office organisations in the case of RRBs and commercial banks, to the NABARD for drawal of resources to supplement their own. In certain areas where the provision of credit is for the non-agricultural sector, they are linked to the IDBI as well at the national level. These national level apexes are themselves, in varying degrees, directly linked to both the Government of India in respect of broad framework of policy objectives and most of them, to the Reserve Bank in respect of policy, funding and operational control. The structural pattern of the various sectors in the credit system from the base level to the national level is illustrated in the chart on next page.

20.03 Broadly speaking, the apex level organisations render two kinds of services to their lower level affiliates/units or beneficiary institutions, first as intermediaries for provision of financial support and second to help strengthen the latter's institutional capabilities. It is also expected of the apex institutions that they help in programming and ensuring the needed co-ordination in the efficient allocation of financial and other resources among various states/regions or sectors and monitor such programmes.

EXISTING INSTITUTIONAL SET-UP FOR RURAL CREDIT



20.04 The apex institutions at the national level significantly concerned with agricultural and rural credit, besides of course NABARD, are the National Co-operative Development Corporation (NCDC), Industrial Development Bank of India (IDBI), Rural Electrification Corporation (REC) and National Co-operative Union of India (NCUI). In this Chapter, we discuss their functions, operations and relationships inter se, in so far as they relate to rural credit.

NABARD

20.05 The role and functions of NABARD, which is the apex operating body for the agricultural credit system, have already been dealt with in detail in Chapter IX. But NABARD is as yet to become effective enough in its leadership role, particularly in bringing about the needed co-ordination among the other apexes. We have suggested inter alia that NABARD needs to be more aggressive in its developmental and co-ordinating roles and proactive in the use of its R&D Fund in promoting new lines of rural development.

20.06 We have observed elsewhere in the Report that the development of PACSs should be entirely the responsibility of the higher tiers in the co-operative credit system. We have reiterated CRAFTCARD's recommendation for the setting up of Primary Co-operative Development Fund (PCDF) by the SCBs/CCBs for the specific purpose of providing the PACSs with substantial financial assistance in the form of grants and subscriptions for equipping them with adequate and competent staff so that they improve their image as full-fledged multi-purpose societies. Although NABARD had communicated the recommendations to the SCBs and the state governments and had even followed them up with Central Government (GOI), the Fund has not been set up at any level. We would strongly commend speedy action for the setting up of the Fund by the SCBs and CCBs by compulsory contributions at a stipulated rate from out of their annual profits. NABARD in turn may have to widen the scope and liberalise its financial assistance intended for the benefit of PACSs. We recommend that NABARD should contribute by way of grants to the PCDFs maintained in each of the SCBs from out of its R & D Fund, the extent of such assistance depending on the programme content of upgrading PACSs in the respective states and also the number of societies to be covered by the programme.

National Co-operative Development Corporation

20.07 Efficient utilisation of credit and its prompt repayment were, according to the Rural Credit Survey Committee, of crucial importance in ensuring optimal recycling of funds and consequently providing an assured and uninterrupted supply of credit. The Survey Committee was also of the view that these objectives could be achieved in the Indian context only if provision of credit was integrated with processing and marketing and storage so that the cultivator was assured of the most economic price for his produce. It was in keeping with the need for such an intergrated scheme of rural credit that they recommended strengthening of the co-operative credit delivery system and several other institutional mechanisms for securing the optimal benefits from the use of credit. One such mechanism, as we have already referred to in Chapter V, was the conversion of the Imperial Bank into State Bank of India with a mandate for opening an adequate number of rural branches for extension of commercial credit to support marketing and processing activities in conjunction with production credit by the co-operatives. The other mechanism recommended was the constitution of National Co-operative Marketing and Warehousing Board for the promotion and development of marketing, processing and warehousing through co-operative organisations. This Board was set up in 1956. Later, however, it was felt that the concept of the Board was inadequate to meet the needs of the situation and that warehousing by itself was a requirement which needed an independent and extensive set up. In 1963, therefore, the Board gave way to two statutory corporations, established by the Act of Parliament, viz., the National Co-operative Development Corporation (NCDC) and the Central Warehousing Corporation. NCDC is a specialised developmental organisation charged with planning, promoting and financing the development of co-operative programmes of marketing, processing and storage of agricultural produce and the supply of inputs. Its assistance extends also to programmes allied to agriculture, e.g., poultry, fishery, dairy development etc. The Corporation has, with its flexibility of approach to suit varying conditions in different parts of the country and tailoring its assistance accordingly made a deep impact on business development in these fields of co-operative activity. It has also assisted the co-operatives in building up technical capabilities in their functional areas, in preparation of feasibility and project reports and in the training of their personnel.

20.08 In setting up NCDC, the intention was that so far as co-operative development was concerned, there would be greater co-ordination between the Reserve Bank's Agricultural Credit Department, which was charged with the responsibility of funding the co-operative system by way of credit for production and the NCDC which was to promote and finance the development of infrastructure of co-operative marketing, processing and storage etc. which constitute the essential forward linkages of production. Accordingly, consequent upon the formation of NABARD and with the transfer of the ACD functions of the RBI to this new organisation, the co-ordination as earlier envisaged was to be worked out between the NABARD and NCDC. Thus although the NABARD instead of the RBI is now represented in NCDC's governing council and board of management, the operational relationship between the two institutions are minimal. In theory, both institutions could finance several agro-industrial projects in the co-operative sector, but so far there has been no joint funding. The possibilities of joint funding and/or NABARD refinancing the NCDC on mutually agreed programmes, particularly in the field of processing and development of appropriate co-operative projects in comparatively less developed states, need to be seriously examined.

20.09 We would like to make special mention here of an innovative programme initiated by NCDC about two years ago (1986-87) as part of its promotional role, viz., the Integrated Co-operative Development Programme. The programme relates to a whole district, whereunder the local resource potential of the selected district is assessed by a specially constituted multi-disciplinary team of experts and then suitable programmes of investment and strengthening of the co-operative infrastructure are devised to secure fuller exploitation of that potential. The focus of development is not only on agriculture and allied activities, but also on non-farm activities to benefit the artisans and landless labourers etc. Both loan assistance and grants are given under the programme. While financial assistance could always have been available for viable investment projects, the noteworthy feature of this programme is to strengthen the essential linkages among various types of co-operative organisations and to upgrade the existing manpower and physical infrastructure in all these organisations, including PACSs, for effective implementation.

Not being concerned with the development of agricultural credit, the NCDC was earlier not taking interest in the development of PACSs, except for storage. Under the programme, however, other infrastructural requirements of PACSs, e.g., their counters and cash handling facilities, are also assisted through suitable grants. Grants have also been given under this programme to PACSs for enabling them to give monetary incentives to their personnel for increased business performance. The specially constituted team remains in the district for the duration of the programme and helps in implementing and monitoring it. The team is located in the co-operative institution most appropriate in the circumstances of the district, which may even be a credit institution such as the DCCB. The main ethos of the programme is that it has no pre-determined patterns of assistance, whether loans or grants, these are tailored to what the local needs and gaps postulate. The purposes of assistance, whether investment projects or infrastructure development, are also likewise determined by the needs revealed in the survey. Of the 38 districts so far approved under the programme, project formulation has already been sanctioned in 27, and projects finalised and implementation begun in 11 districts. The programme has been on the ground effectively for hardly a year. It is, therefore, too early to evaluate it. All the same, devised as it is, it holds promise of establishing a methodology of planning and implementation of co-ordinated area (district) development. We would strongly recommend that NABARD should take note of this programme and work out with NCDC the modalities of joint support to it.

20.10 The Consultants III have recommended that NABARD and NCDC agree on a means of co-operation or appropriate division of labour at the operational level, for reasons both of economy and programme effectiveness. A possible co-ordination mechanism may be regular (e.g. quarterly) meetings of a NCDC-NABARD Co-ordination Committee with representatives of all concerned departments represented, similar to the regular meetings of the IRDP Task Force and NABARD-RPCD (RBI) Co-ordination Committee. We endorse this recommendation.

INDUSTRIAL DEVELOPMENT BANK OF INDIA

20.11 IDBI is not only the apex level for industrial finance but also the largest source of institutional finance for industry, including small and medium industry (SMI). It operates mainly through the 18 State Financial Corporations (SFCs), in each of which it has a 50 per cent shareholding. It provides primary refinancing to them, also to the 19 State Industries Development Corporations (SIDCs), to CBs, SCBs and RRBs - subject to annual limits and including both rupee and foreign exchange, the latter deriving mostly from World Bank loans.

20.12 IDBI carries on extensive promotional activity, financed from a Small Industries Development Fund (SIDF) of Rs.2800 crores. For identification and training of entrepreneurs, it underwrites in part the programme of the Entrepreneurial Development Institute in Ahmedabad. It runs other institutes for less advanced training at Lucknow, Patna, Bhubaneshwar and Bhopal, and is planning another for the North Eastern Region. It has sponsored and supported Technical Consultancy Organisations to advise SSIs on project preparation, feasibility studies, diagnose and plan for rehabilitation, etc. in 17 states.

20.13 IDBI's and NABARD's functions overlap in the financing of SSI and processing industries. According to the Consultants III there is no formal division of work but only sporadic ad-hoc consultation between them. IDBI leans to the view that NABARD should confine its financing to agro-based industries, with all others looking to IDBI. At present, however, the option to approach the financing agency rests with the primary financing institutions.

20.14 The proposal that NABARD limit its SSI financing only to agro-industry would tend, according to Consultants III to undercut its ability to plan and co-ordinate well-balanced, diversified IRD schemes. They have recommended that it be receptive to, indeed actively invite, IDBI's participation in the formulation and implementation of the industry-related aspects of such schemes.

20.15 Consultants III have recommended that both institutions should form

a NABARD-IDBI Co-ordination Committee (similar to REC's and NCDC's Co-ordination Committees) as a vehicle (i) to ensure optimal co-operation at the operational level in the promotion and funding of SMI schemes, and entrepreneurial training and development; and (ii) to provide a forum where the proposal for a Small Industries Bank, announced in the 1988-89 budget, can be further discussed.

20.16 In this connection we note the move of the GOI for setting up a Small Industries Development Bank of India (SIDBI). The related modalities are also, it is understood, being worked by GOI (MOF) and that the following broad areas of operational demarcation have been arrived at :

- 1) State Finance Corporations, twin-function SIDCS and urban co-operative banks may seek refinance from SIDBI exclusively in respect of the assistance provided by them to SSI/tiny/decentralised sector units. RRBs will seek refinance exclusively from NABARD.
- 2) Assistance provided to all units in SSI/tiny/decentralised sectors in rural areas (as defined in NABARD Act) by commercial banks/regional rural banks/co-operative banks (other than urban co-operative banks) shall be refinanced by NABARD.
- 3) In the case of assistance provided by state co-operative banks to SSI units not located in the rural areas, it was noted that presently NABARD is providing refinance, for working capital as also for term-loans. At the same time it was noted that IDBI is also providing refinance against term-loans sanctioned by SCBs/DCCBs. It was, therefore, agreed that in these cases the status quo may be maintained (i.e. refinance may be provided either by SIDBI or NABARD as the case may be).
- 4) It was also agreed that under aegis of RBI, a Committee for co-ordination of the activities of SIDBI and NABARD may be constituted and it may include Development Commissioner, SSI (GOI) besides RBI, NABARD and SIDBI.

The Government of India is, however, as yet to take a view on this issue. It may, therefore, be pointed out at this stage that the charter of NABARD which requires it to promote rural development includes rural industrialisation as well. Certain traditional sectors such as KVIC and SK & VI Board and the handloom industry are concerned with the rural economy and the units in these sectors financed by banks if need to be refinanced, could continue to be the responsibility of NABARD. Even activities in the modern sector of small/tiny industry in rural areas could be the responsibility of NABARD. We are inclined to so recommend in view of NABARD's better ties with and its avowed empathy for rural institutions.

Rural Electrification Corporation

20.17 The Rural Electrification Corporation (REC) established as a Government of India undertaking in 1969, in pursuance to one of the recommendations of the Rural Credit Review Committee, is mandated to provide financial assistance by way of loans to the State Electricity Boards for extending electricity to rural areas. In the view of the Review Committee, planned irrigation constituted one of the principal objectives of long-term institutional credit for agriculture and that such planned rural electrification was a necessary adjunct to planned irrigation. In other words, the programmes of rural electrification were expected to be complementary to the schemes for construction of wells and installation of pumps, such as those which were financed project-wise by the Agricultural Refinance Corporation (later the Agricultural Refinance and Development Corporation and now the NABARD). In the Committee's view, the fruitful utilisation and prompt repayment of institutional credit provided for these purposes would depend greatly upon the simultaneous extension of the supply of electricity to the relevant areas. Against this background, the question of raising resources required for financing rural electrification is intimately related to the general problem of production-oriented rural credit with which the NABARD is concerned.

20.18 To start with, the financial resources of REC consisted of a grant of Rs.105 crores provided out of PL 480 counter-part funds and a proportionate matching grant of Rs.45 crores by Government of India (in the ratio of 70:30)

under an agreement between GOI and USAID. But as REC's operations expanded, the size of budgetary resources had also expanded, supplemented by additional funding by IDA and later through public borrowings. Simultaneously, it was found necessary to take advantage of assistance available from banks and specialised credit institutions. Accordingly, in 1977 the Reserve Bank constituted a Working Group with Shri B. Venkatappiah (then a director on the Central Board of Reserve Bank and also Chairman of REC) to examine how REC for some of its special programmes could draw upon the financial resources available from the commercial banks and other specialised credit institutions. In pursuance of this recommendation of the Working Group, the Reserve Bank agreed that one way in which REC could harness financial resources from the banks and financial institutions would be in relation to programmes of pumpset energisation under the Special Projects Agriculture (SPA). It was agreed that these programmes could be funded jointly by REC, the then ARDC (now the NABARD) and commercial banks in equal proportion. This was expected to take care of provision of adequate transmission and distribution net work on a scheme to scheme basis so that agricultural consumers are assured of uninterrupted supply of power for their pumpsets. Before it is sanctioned by REC and sent to NABARD and the nominated participating bank for sanction of the share of assistance, each SPA scheme is subjected to detailed techno-economic appraisal by REC which include verification of the technical parameters relating to adequacy of electrical distribution system for availability and supply of power. REC also monitors the execution of these programmes so as to ensure that the various stipulations laid down had been carried out.

20.19 However, over a period of time, while on the one hand the coverage of pumpsets energisation under SPA has itself enlarged, NABARD has been refinancing simultaneously energisation under normal programmes through commercial banks and LDBs on a fairly large scale. Since these programmes are not projectised, they are not subject to technical scrutiny specially those relating to adequacy of the system support. The SEBs under pressure from state governments tend to defer, on account of financial constraints, implementation of plans for the needed electrical support for ensuring reliable

supply. As a result, the system gets overloaded, power supply goes erratic causing even burning of distribution transformers. Further at the consumers' terminals also, the motors get burnt out on account of tail-end low voltage in the system. A further dimension to the problem is a host of other factors caused by avoidable delay in the release of their share of the loans sanctioned under the SPA programmes. Under the agreed arrangements, REC releases 40 per cent of its one-third share of the total loan for acquiring inventory. NABARD and the participating commercial banks take anywhere from three to six months to release their 40 per cent of the one-third share.

20.20 We have in the circumstances, two recommendations to make. One, NABARD should not normally refinance any rural electrification scheme unless they have the technical clearance from REC. Should there be constraint of resources and consequently a certain prioritisation becomes necessary, SPA schemes should have the first claim. Two, where there is delay in release of NABARD's and the nominated bank's share, NABARD may provide interim finance to the full extent of NABARD's share to be adjusted against releases to be made in due course. Needed modification in this regard may be made in the relative SPA agreements between REC, SEB, NABARD & CBs. REC may also have to be recognised as an institution eligible for direct finance under Sec.30 of NABARD Act for this purpose.

20.21 The Consultants III have recommended that the banks and NABARD should insist on strict observance of the REC recommended and ISI approved specifications for pump-sets and motors. As of now, NABARD's refinance is available only for pump-sets/motors with ISI specifications and hence in our view no further modification of policy as such is needed.

20.22 As the Consultants have pointed out, a NABARD-REC Co-ordination Committee should be set up to improve institutional communications and develop common areas of interest, such as non-traditional sources of energy. We endorse this recommendation.

National Co-operative Union of India

20.23 The NCUI activity which is relevant to our consideration is training of personnel in the co-operative sector including co-operative credit. It has set up the National Council for Co-operative Training (NCCT). NCCT is the apex entity for a large number of co-operative training institutions in the country. The Vaikunth Mehta National Institute for Co-operative Management (VAMNICOM) trains senior executives. At lower levels there are Co-operative Training Colleges (CTCs) for mid-level staff, such as managers and inspectors and Junior-Level Training Centres (JLTCs) for grass root functionaries. These JLTCs according to Consultants III though large in number, are insufficient to meet the staff training needs of thousands of credit and non-credit co-operatives; and what is more, the standard and content of the training courses are far from adequate for the planning and management of IRD schemes. We have dealt in Chapter XIII the appropriate agencies/arrangements for training and the specific role of NCUI as existing and as envisaged by us.

20.24 We agree with Consultants III that NABARD should co-ordinate with NCUI to make optimum use of the experience and training skills that the NCUI/NCCT network possesses. As detailed in Chapters IX and XIII, NABARD will have to directly involve financially and otherwise, in the training arrangements needed for the agricultural credit system.

The Proposed NCBI & the SCBs/SLDBs Federations

20.25 The two co-operative credit structures have at present no apex at the national level, but each of the two structures has organised federation at the national level, namely the (i) National Federation of State Co-operative Banks (SCB Federation) and (ii) National Federation of Co-operative Land Development Banks (LDB Federation) registered in 1960. The Federations are both non-equity based and obtain annual subscriptions from member banks. They also get some assistance from the Central Government/NABARD. Both the Federations confine their activities to spokespersonship functions and consultancy services. While they have provided forums for their constituents for discussions of common interest, compiled important statistics relating to co-operative

banks and published quarterly journals, they have not been able to function effectively as spokesmen of the co-operative banking system in view of the fact that not being banks they have no representation in banks' forums and in the consultations which Reserve Bank holds with banks.

20.26 The responsibilities of the two federations are thus very limited. They are neither business organisations nor national apexes of the two structures. We have, therefore, recommended the setting up of NCBI which would fill the systemic gap at the national level and provide a national apex for the co-operative banking system as a whole. We have dealt with the role and functions of the proposed National Bank in Chapter VIII.

Reserve Bank of India

20.27 From its inception, the Reserve Bank of India has recognized and been conscious of the fact that in the Indian context, it has, as the central monetary authority, a strategic role in promoting the development of a balanced, equitable and self-reliant agriculture. Its effort in this direction all along has, therefore, been to develop an efficient system of rural credit which is a crucial element of any sustainable and viable strategy for modernisation of the rural economy and not less importantly, removal of poverty. These compulsions of the Indian economy were recognised by the framers of the Reserve Bank of India Act and the law provided for the Bank's special responsibility in this sphere. Flowing from this, in striking contrast to the working of other central banks, the Reserve Bank had involved itself actively in the area of institution building in rural credit. The Bank's efforts in this direction in the socio-economic context of the country, were to ensure that the rural credit system served not merely the cause of accelerated growth, but also facilitated greater equity in the development process. To this end, the Bank had been steadfast in its endeavour to promote a sound and balanced growth of the co-operative credit movement. As part of such endeavour, the Bank also devoted sustained attention to overcoming the structural and organisational weaknesses of the co-operative credit system. However, with the technological changes and the dynamic growth which Indian agriculture witnessed in the sixties, the demand for credit surged forward and agriculture

became a commercially viable proposition, opening up an area of profitable deployment of resources even for commercial banks. In the new context, while not minimising the key role of the co-operatives, the Reserve Bank recognised the need for supplementing their efforts in meeting the growing demand for agricultural credit and carved out a distinct, albeit supplementary, role for the commercial banks to fill the visible gaps in the rural credit system. The rapid expansion of the organized rural banking system - the massive widening and deepening of the rural credit system since independence could thus be attributed to the innovative steps and leadership role of the Reserve Bank.

20.28 Taken together, the vast network of co-operative credit institutions and commercial bank branches, no doubt provide today an effective engine for both growth and modernisation of the country's rural economy. But credit, it needs to be recognised, is a delicate instrument which requires careful handling. Signs of strain often on account of lack of proper care have already become visible. Mounting defaults, inadequate pre-sanction appraisal of loan applications, permissive lending etc. all of which we have addressed ourselves in the Report are symptomatic of the malaise that is creeping in. These have to be tackled firmly and with imagination and understanding, and in this the Reserve Bank's innovative approach and the Governments' - both Central and State - active collaboration are of crucial importance.

20.29 We recognise that with the establishment of the NABARD in July 1982 and the transfer to it of the direct responsibility in the sphere of actual delivery of rural credit, Reserve Bank's involvement in rural credit is now in the second remove, that is, via NABARD. But this change should in no way affect the Reserve Bank's concern for the orderly growth of the rural credit system. Moreover, as the central bank of a country which derives about 35 per cent of GDP coming from agriculture and 65 per cent of population deriving income from agricultural pursuits, the RBI cannot afford to be a passive body in ensuring for it, the needed health in this vital sector of the economy. Flowing from this, the RBI has a wide area of direct responsibility in policy formulation in regard to credit deployment for both co-opera-

tive and commercial banking systems, provision of general line of credit for NABARD for the short-term loan operations of the co-operative banking system, annual allocation from its profits to the National Rural Credit (Long Term Operations and Stabilisation) Funds of the NABARD, the issue of bonds/debentures by NABARD itself and the SLDBs as a part of general public borrowing programme and with reference to co-operative banking system itself the statutory responsibilities under the Banking Regulations Act, as applicable to co-operatives. These responsibilities in this wider sphere are presently under the charge of its Rural Planning and Credit Department (RPCD). Besides, the residuary statutory functions which are confined to sanctioning of the general line of credit and advising the Secretary's Department of RBI about annual allocations to the statutory funds of the NABARD, RPCD's functions are largely in the area of follow up of priority sector advances. In relation to NABARD's activities, the regional offices of the RPCD receive from them, copies of inspection reports and other statutory returns on SCBs and DCCBs. Though Section 54 as amended after the passing of the NABARD Act enables the RBI to issue directives to NABARD and conduct studies on rural credit, etc., and certain studies on RRBs and IRDP have been undertaken, no systematic study of problems of rural credit or of the state of co-operative credit has been attempted which could provide a basis for policy formulation in these areas. Since policy formulation is an important aspect of the responsibility vesting in RBI, it would be necessary for the RPCD to take up indepth studies of the problems of agricultural credit, be they relating to commercial banks or co-operatives but in the latter area, in collaboration with NABARD so that there is a regular flow of feedback of field problems to enable policy adjustments from time to time. The special studies which could be taken up, to cite a few, are (i) overdues in the commercial banking system, (ii) impact of state partnership in the co-operative credit system, (iii) periodical review of costs and margins in rural lending both in the commercial and co-operative banking systems, (iv) increase in agricultural costs and repaying capacity, (v) impact study of special programmes aimed at improving the economic conditions of the poor, and (vi) status studies of the working of co-operative systems separately for each state. This is of course not an exhaustive enumeration of all the

possible studies, but only an illustrative one. It is further necessary that the studies are taken up at regular intervals. Besides, the regional offices of RPCD should be able to emerge as the focal points of co-ordination between the state government agencies, co-operative banks, the regional office of NABARD and the commercial banks in the respective states. The RPCD should, therefore, be suitably strengthened to fulfil these onerous responsibilities devolving on it. Here we would like to make a mention of a few specific issues of crucial importance.

Overdues in Commercial Banks

20.30 Since the supervision and control over the commercial banks lies with the RBI, we would consider that it has a special role in exercising vigilance on recovery of agricultural loans by commercial banks. In Chapter XV and elsewhere in the Report, we have made a number of suggestions for bringing down the overdues within a specified time frame and to this end we have also recommended that each of the credit agencies, in the case of commercial banks at the branch level, should draw a definite plan of action. While in the case of co-operatives, the NABARD could be expected to monitor this, in the case of commercial banks, the responsibility would lie with the Reserve Bank and we recommend that the Reserve Bank should create a special cell to keep a close watch on the recovery of dues under the agricultural loans by the commercial banks.

Inspections by NABARD

20.31 Our Consultants III have observed that the quality of NABARD inspections needs to be upgraded. The Reserve Bank of India has already the power to conduct its own inspections of banks inspected by NABARD, but this power has not been exercised. While it is a means for Reserve Bank to check on the adequacy of NABARD inspections, it is rather time consuming and possibly disrupting to the banks concerned. The Consultants have, therefore, recommended that Reserve Bank may consider taking up a limited programme of quality control reviews of NABARD inspections periodically. We are in agreement with this suggestion. Clearly, the Reserve Bank personnel assigned to this duty must have a reasonable level of expertise and experience in inspections of banks.

Interest Rates

20.32 In Chapter XVIII dealing with Interest Rates, Costs and Margins, we have suggested certain changes in the interest rate structure to the ultimate borrowers in respect of agricultural loans. Since the administered interest rates are determined by the Reserve Bank of India, we would recommend that the Bank keeps in view our recommendations in this regard and make suitable adjustments in the interest rates.

Machinery for Policy and Co-ordination

20.33 There is in our view a need for a greater degree of, and more systematic consultation and co-ordination between RBI, NABARD and other apex institutions in policy matters relating to agricultural credit. Earlier, the Agricultural Credit Board (ACB) of RBI was discharging this role. With the establishment of NABARD, the ACB of Reserve Bank ceased to exist. In the absence of any alternative machinery to fill the void, the RBI itself set up in November 1985 a high level standing committee. In 1986 NABARD, however, formed a Standing Committee on Co-operative Credit but this committee did not meet even once. In the following year, the NABARD constituted an Advisory Council as provided in the NABARD's statute with the result that there is a high level committee both in RBI and NABARD. The Consultants III have observed that the terms of references of both these committees are more or less similar; so also its membership, and hence have suggested that NABARD's Advisory Council be entrusted with the co-ordination role. But as already mentioned, there are certain specific areas concerning overall policy formulation and co-ordination connected therewith on matters relating to agricultural credit which is distinctly within the sphere of the responsibility of the RBI while the responsibility for the implementation of these policies and the monitoring thereof fall in the domain of NABARD. Both the committees have, therefore, their own respective roles. The Reserve Bank Committee could on the one hand provide a forum for review from time to time, of policies relating to the agricultural credit system as a whole in the country and bring the needed co-ordination among the various apex bodies including the NABARD and on the other function as an empowered high level machinery for effective consultation with the Central and state

Governments. Having regard to the nature of their responsibilities, the frequency of the meetings of RBI committee could, however, be limited to once in six months, while the NABARD's Advisory Council would have to meet oftener, atleast once in a quarter.

Role of Government

20.34 We have already described on the one hand the weaknesses and the dangers implicit in Government interference in the working of the credit system and on the other, either the inaction or at times positively discouraging measures taken by the Government, and in particular the state governments, in tackling the problems of overdues. We have also pointed out the areas where a direct intervention either in terms of policy assistance including financial assistance is called for in the effective use of credit and smooth functioning of credit institutions. These include provision of infrastructure, particularly in areas of backwardness, of subsidies in credit linked poverty alleviation programmes and to meet losses arising from implementing state directed credit programmes for subserving social objectives. Above all in Indian conditions, Governments' responsibility in effective co-ordination of the activities of various government agencies and programmes so as to harness all these to the common objective of optimising the benefits of credit use and through such purposive use of credit, the development of rural areas, is of crucial importance.

20.35 There is, in the first instance, a direct responsibility of the Government in such special contexts, such as in times of famine and unprecedented floods, or droughts. Other special contexts will relate to :

- (a) Special development plans, particularly infrastructural development for economically backward areas and classes of people;
- (b) Special assistance programmes and plans therefor, for tribal people and tribal areas; and
- (c) Special policies of rehabilitation and/or upliftment of those for whom the credit linked poverty alleviation programmes are of doubtful validity.

Direct Government assistance in such well defined contexts such as these is needed rather than burdening the credit system with the responsibility of undertaking concessionary credit programmes to be operated by credit agencies even in conjunction with Government agencies.

20.36 Drought and flood relief has always been the responsibility of the State. In the context of the massive support being extended by the credit system for crop production and agriculture by and large still dependent on the vagaries of monsoon, farmers borrowing for crop production but affected by natural calamities need to be provided with reasonable relief. We have dealt in Chapters XVI and XVII with the manner in which and the extent of the relief the banks and other institutions can provide under such conditions. Banks, under the stabilisation arrangements can only defer or prolong the repayment period. Crop Insurance unless extended to cover all crops may not serve the purpose. It is, therefore, necessary that in case of consecutive crop failures of say 3 years or more, that part of institutional credit availed by the farmers which is in excess of his repaying capacity has to be written off. The Survey Committee, 1954 envisaged the Agricultural Credit Relief Fund to be set up by Government of India and state governments and to be used for the purpose of write off. The Study Team on Overdues, 1974 spelt out the modalities in this regard. Unfortunately this remained uncomplished for long. Following the February 1988 Budget announcement, however, the Government of India has set up a Committee to work out details which we understand has been done. We recommend that the National Agricultural Credit Relief Fund be set up early and relief to affected farmers be extended in a systematic manner. This would also do away with the need for ad-hoc write off measures resorted to sometimes by some state governments

20.37 Another area where the state government agencies could play a significant role is in providing a network of extension services. As we see it, the role of extension work, and in a sense, of an economic partnership between the state and the cultivator are complementary activities and the two should go hand in hand. Wherever necessary, new techniques of extension and cultivator participation should be worked out. This will have to be done, in particular, in relation to specific composite programme of development. In our view the administrative and educative aspects of extension work have to be made conjoint and to the extent feasible, with the participation between the state and the primary producer. This is an area of responsibility which comes within the purview of state governments, but would need assistance from the Central Government. We do not envisage any direct role for the Government in providing agricultural credit as such, but it will have to play a critical role in creating conditions

conducive to the growth of institutional credit for agriculture and rural development. To this end, the state governments will in the first instance have to remove some of the impediments which today stand in the way of the smooth working of the credit system and consequently uninterrupted flow of credit.

20.38 The new agricultural strategy assumes improved techniques and use of modern inputs. The success of this will accordingly depend to a large extent on the timely and adequate provision of the required supplies and services from different sources. Past experience has shown that programmes in several cases have floundered for want of sufficient co-ordination of the various agencies involved. Another area in which Government could play a significant role is in relation to both stability and adequacy of prices for agricultural commodities which is an area that is distinctly a Central Government responsibility. Several steps have already been taken, to cite only two instances, the establishment of the Food Corporation of India and the setting up of the Agricultural Prices Commission. Prices are an important factor for promoting development because the new strategy involves the use of high cost inputs. Land tenures and tenancy systems are another area in which the state governments can make a substantial contribution towards facilitating the operations of agricultural credit institutions. We have already referred to this elsewhere in this Report. The Government could also help speed up the process of recovery of loans by ensuring prompt action against defaulters. The Government should ensure that both the legal provisions and staff for execution of decrees are adequate. This aspect has also been discussed in detail already.

20.39 In Chapter XII, we have suggested various measures to be taken as part of institutional strengthening for the co-operative institutions in both the short-term and long-term structures. However, the ultimate success of the institutional strengthening programme would largely depend on the effectiveness with which the tasks which lie within the responsibility of the state governments are acted upon. The state governments' responsibilities lie both in financial terms and organisational support during the period the concerned lending institutions are under the ISP. The financial responsibility would primarily include additional share capital contribution where necessary and provision of additional staff for speedy recovery. Its organisational support is necessary in the area of execution of decrees for the recovery of overdues.

20.40 Another area in which state governments' active assistance is called for is in providing the necessary legislative support in matters where we have recommended changes in the Co-operative Societies Acts elsewhere in this report. Speedy action in this respect is crucial to the success of the whole scheme.

20.41 To sum up, the Reserve Bank and the Governments - Central and State would have to play a vital role in the matter of co-ordination. While the Government will have an additional role in providing, where situation warrants, legislative and physical infrastructural support, the Reserve Bank's direct involvement in the policy formulation is equally significant. Though the responsibility in regard to operations in the area of rural credit stands transferred to NABARD, Reserve Bank's role in evolving appropriate policies aimed at strengthening the rural credit system is no less significant. In our view the Reserve Bank will, therefore, have to be proactive in this very crucial area.

PART VIII

**CREDIT LINKED
POVERTY ALLEVIATION PROGRAMMES**

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XXI INTEGRATED RURAL DEVELOPMENT PROGRAMME
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CHAPTER XXI

INTEGRATED RURAL DEVELOPMENT PROGRAMME

Background

In the early stages of planned economic development in the country, it was believed that the process of economic growth would sooner rather than later transmit the benefits of economic development widely through the society, including the poorer sections of the population. Growth, in other words, would trickle down and percolate among all segments of the population. Such an assumption about the trickle down effect, however, implies a high degree of homogeneity in the socio-economic matrix of the society and a fairly high mobility of the population. This did not exist in the country at that stage of development. Moreover, the rate of growth of the economy continued to be relatively slow. Consequently, the benefits of development and growth did not seem to be reaching all layers of the society, particularly the poorer sections. Increasing emphasis has, therefore, been laid in the successive Five Year Plans of the country on progressive reduction of inequalities in income and removal of poverty through specially designed policies and programmes of both self employment and wage employment, depending upon the nature, abilities and skills of the target population. The Integrated Rural Development Programme (IRDP) and some other programmes which are supplemental to it and some which preceded it, were conceived essentially with this object of securing growth consistent with social justice.

21.02 The IRDP or any one of the other poverty alleviation programmes of the Government would normally have been outside the scope of this Review. However, the involvement of institutional credit in conjunction with fiscal subsidies in these programmes is a matter of concern to us because of its impact on the credit system. Our major concerns are :

- i) the extent of involvement of bank credit for poverty alleviation programmes;
- ii) impact of these programmes on the participating credit institutions;

- iii) method for improving the effectiveness, monitoring and control of these programmes; and
- iv) the role of the credit system in these programmes in future.

Integrated Rural Development Programme

21.03 The Community Development Programme initiated in 1952 during the First Five Year Plan was in a way the forerunner of most rural development programmes in India. It created the primary infrastructure of basic extension and socio-economic developmental services in rural areas, and combined with it a self-contained budget (known as the schematic budget) for each Community Development Block to secure balanced promotion of diverse developmental activities in the area. The programme expanded fast, indeed too fast for its own good, and came to cover the whole country earlier than it was intended to originally. The principal orientation, however, of this programme, apart from its emphasis on self-help and group action, was towards securing an allround development of the community through change in attitudes, and creating better awareness of developmental possibilities and making available the means to achieve these. Removal of poverty and income disparities among various sections of the community as such was not a part of its central design. Undoubtedly, the benefit particularly of agricultural extension services was first of all taken by those farmers who were better endowed with land resources. The compelling need of the country to achieve self-sufficiency in food inexorably pushed the extension agency to securing quick results. This inevitably entailed greater attention to better endowed farmers who in aggregate owned the bulk of the cultivated area in the country. The new agricultural technology, which is scale neutral was still a few years away. Therefore, even the Intensive Agricultural District Programme (IADP) which was subsequently introduced in 1960-61 by-passed the small farmers. It is against this background that special programmes specifically addressed to small and marginal farmers, i.e., Small Farmers Development Agency (SFDA)/ Marginal Farmers and Agricultural Labourers (MFAL) were launched in 1971. Several other special programmes such as Drought Prone Areas Programme (DPAP), Desert Development Programme (DDP), Hill Areas Development Programme (HADP), Tribal Areas Development Programme (TADP), Command Area Development Programme (CADP) etc., were also initiated during the seventies, to cater to the specific regional needs and problems. The Food for Work Pro-

gramme was started in 1977 to provide work for rural poor during periods of slack employment. While the special programmes operated for a span of years in selected areas and also in several cases simultaneously in the same area and for the same target groups in a large number of blocks in the country, none of them covered the whole country. It was felt that in order to deal with the huge dimensions of rural poverty in the country, a far more ambitious programme was needed. Thus, IRDP in its present form has its origin in these special programmes and was introduced in 1976-77, primarily to remove the deficiencies under the erstwhile SFDA and MFAL programmes. IRDP with some modifications was implemented on an expanded scale in 1978-79 in 2,300 blocks in the country, of which 2,000 had co-terminus coverage with SFDA/MFAL, DPAP and CAD programmes. With another 300 blocks added during 1979-80, IRDP covered 2,600 blocks by March 1980. The programme was to be extended to 300 new blocks every year. However, during 1980-81 the Government of India (GOI) took the major policy decision to extend the benefits of the programme to the target group families in all the 5,011 blocks in the country, from 2nd October 1980. With effect from the same date, SFDA which was implemented in selected areas was merged with IRDP. IRDP was also included as a component of the "New 20 Point Programme" announced by the Prime Minister in January 1982. IRDP, as it has finally emerged, aims at raising the level of living of the poorest families in the rural areas above the poverty line on a lasting basis by giving them income generating assets and access to credit and other inputs. The target group mainly included small and marginal farmers, agricultural and non-agricultural labourers, rural artisans and scheduled castes and scheduled tribes. The Sixth Plan (1980-85) aimed at providing specific assistance to 3,000 families on an average in each block out of the estimated 10,000-12,000 families living below the poverty line (i.e., Rs.3,500 per annum for a family). Overall, the Sixth Plan had envisaged assistance to 15 million families at the rate of 600 per block, per year, including at least 30% belonging to Scheduled Castes and Scheduled Tribes (SC/ST). Of these 600 families, approximately 400 families were expected to be benefited through agriculture and allied activities, 100 through village and cottage industries and the remaining 100 through service sector activities. The Plan also envisaged a financial allocation of Rs.1,500 crores to be shared equally between the Centre and the States. This amount was mainly to be utilised by way of subsidy (ranging between 25 per cent to 33 1/3 per cent of the investment cost) for the identified beneficiaries to undertake the investment. This subsidy was to be supplemented by credit from co-operative and commercial banks to the

extent of Rs.3,000 crores. The total ground level investment under IRDP was estimated at Rs.4,500 crores. As conceived during the Sixth Plan, the IRDP involved (i) selection of persons below the poverty line, (ii) selection of activities suitable to the area, (iii) marrying of the activities with the selected beneficiaries according to their needs, and (iv) provision of credit for the chosen activity.

Administrative Arrangements for IRDP

At Central Level

21.04 The Department of Rural Development in the Ministry of Agriculture, GOI has the overall responsibility of implementation of IRDP. A Central Committee on IRDP and allied programmes has been constituted to assist the Department. Secretaries of various Central Government Departments including a representative from Prime Minister's office and the Secretaries of Rural Development Departments of the States are members of this Committee. The Secretary, Department of Rural Development, Government of India is the Chairman of the Committee. The functions of this Committee are mainly, framing and revision of guidelines for the programmes, ensuring effective implementation of guidelines and reviewing progress of the programmes. The Committee provides a forum for a continuous dialogue with the State Governments regarding implementation of IRDP.

At State Level

21.05 The Department of Rural Development of the State Government or any other Department to which the subject of rural development has been allocated is responsible for planning, implementation, monitoring and evaluation of the programme at the state level. A State Level Coordination Committee has been provided to assist this Department in discharging these responsibilities. The Chief Secretary/APC/Development Commissioner acts as the Chairman of this Committee. The heads of important development departments are members of this Committee, in addition to a representative from Central Government. The Committee provides leadership and guidance to District Rural Development Agency (DRDA) in planning, implementing and monitoring of the programme. There is also a Project formulation-cum-Monitoring Cell at the state level to help in the implementation of the programme. The Cell consists of subject matter specialists and other experts.

At District Level

21.06 The programme is implemented through DRDAs at the district level. These agencies are registered societies under the Registration of Societies Act. They are generally headed by the Collector/Dy. Commissioner or Chief Executive Officer, Zilla Parishad, depending upon the practice prevailing in the State. The DRDA has a governing body which comprises Collector, all MPs/MLAs of the district and other important officials in the field of development and banking. The Chairman/President of DRDA is empowered to form an executive committee to assist DRDA. Overall responsibility for planning, implementation and monitoring and evaluation of IRDP rests with DRDA. The DRDA keeps the district level and block level agencies informed of the basic parameters, the requirements of the programme and tasks to be performed by various agencies. It coordinates and oversees the surveys, preparation of perspective plans and Annual Action Plans of the blocks and finally the preparation of a District Plan. The staff of DRDA consists of subject matter specialists on credit, rural industries, statistics etc. who help in the preparation of District Plan.

At Block Level

21.07 The Block is the basic unit for preparation of perspective and annual action plans. The Block Development Officer (BDO) is required to perform the role of the Chief coordinator in the block and also see that plans are prepared in time and implemented effectively. The BDO is assisted by Extension Officers in different disciplines. Village Level Workers (VLWs)/Gram-Sevaks/Gram-Sevikas who maintain contact with individual households in the villages, are also attached to BDO office. Survey of individual families and preparation of the list of families according to their poverty status is the responsibility of block staff. The list of such beneficiaries should be placed before the Gram Sabha (Village Assembly) for approval. The choice, willingness and ability of the identified beneficiaries are also required to be ascertained at the Village Assembly. The loan application forms of identified beneficiaries are forwarded by the Block Office to the concerned branch of the financing bank. The banks scrutinise these applications and sanction loans according to the prescribed norms. Along with the loan amount, banks also disburse subsidies in conformity with the prescribed schedule. Such subsidy funds are kept by DRDA in savings bank accounts with the participating bank branches.

Review of IRDP under the Sixth Plan

21.08 The physical and financial progress of IRDP during the Sixth Plan is indicated in table I.

Table I
IRDP Performance in the Sixth Plan

Sr. No.	Items	Targets		Achievements				
		1980-85	1980-81	1981-82	1982-83	1983-84	1984-85	1980-85
1.	Total allocation (Rs. crores)	1500.00	300.66	250.55	400.88	407.36	407.36	1766.81
2.	Central allocation (Rs. crores)	750.00	127.80	153.36	204.48	207.72	207.72	901.08
3.	Central release (Rs. crores)		82.58	128.45	176.17	194.23	206.96	788.39
4.	Total expenditure (Rs. crores)	1500.00	158.64	264.65	359.59	406.09	472.20	1661.17
5.	Total term credit mobilised (Rs. crores)	3000.00	289.05	467.59	713.98	773.51	857.48	3101.61
6.	Total investment mobilised (Rs. crores)	4500.00	447.69	732.24	1073.57	1179.60	1329.60	4762.78
7.	Total no. of beneficiaries covered (lakhs)	150.00	27.27	27.13	34.55	36.85	39.82	165.62
8.	No. of SC/ST beneficiaries covered (lakhs)	50.00	7.81	10.01	14.06	15.37	17.38	64.63
9.	Per capita subsidy (Rs.)	1000.00	582.00	975.00	1041.00	1102.00	1186.00	1003.00
10.	Per capita credit (Rs.)	2000.00	1060.00	1723.00	2066.00	2099.00	2153.00	1873.00
11.	Per capita investment (Rs.)	3000.00	1642.00	2698.00	3107.00	3201.00	3339.00	2876.00
12.	Subsidy-Credit Ratio	1:2	1:1.82	1:1.77	1:1.98	1:1.90	1:1.82	1:1.87
13.	Sectorwise coverage (per cent)							
	(a) Primary sector		93.56	83.02	68.70	58.90	54.5	
	(b) Secondary sector		2.32	4.92	15.70	13.20	15.7	
	(c) Tertiary sector		3.12	12.06	15.60	27.90	29.8	

Source: Seventh Plan - 1985-90, Vol.II, Planning Commission, Government of India, P.52-53.

21.09 Although physical and financial targets have been exceeded, several deficiencies in the implementation of IRDP have come to light during the Sixth Plan. Considering the fact that a programme of this dimension functioning in diverse environments was launched with relatively little or no preparation,

these deficiencies were only to be expected. In a way, the Sixth Plan period could be called as a period of trial for IRDP during which the programme gradually came to be known and stabilised.

Evaluation of IRDP in Sixth Plan

21.10 A number of organisations, Governmental and autonomous bodies as also individuals have undertaken evaluation of IRDP from time to time. The nationwide studies are those which were carried out by :

- (i) Programme Evaluation Organisation of Planning Commission, Government of India (1985),
- (ii) Reserve Bank of India (1984),
- (iii) National Bank for Agriculture and Rural Development (1986),
- (iv) Institute of Financial Management and Research, Madras (1985), and
- (v) State Bank of India (1987).

21.11 In addition, regional studies have also been carried out by state governments, NABARD and other research organisations. The major deficiencies of IRDP as brought out by these studies are summarised below :

- (i) Since financial allocation and physical targets under the programme were determined on uniform basis per block, without reckoning the incidence of poverty or the size of the population or potential of the area, it resulted in the selection of ineligible families in some cases and poor coverage in respect of some areas.
- (ii) 15 to 20 per cent of the beneficiaries had been identified wrongly. The main reasons for wrong identification were :
 - (a) Reliance on lists prepared under erstwhile SFDA where the identification was based on land holding rather than on income.
 - (b) Non-involvement of people's institutions and financial institutions in the survey and selection of beneficiaries.
 - (c) Collusion between Government functionaries and vested interests.
- (iii) Leakages through corruption and malpractices especially among beneficiaries who were unaware of the details of the programme. Hiking of prices

of assets supplied under IRDP, provision of sub-standard assets, etc. were indulged in by dealers in collusion with DRDA/bank staff.

- (iv) Preponderance of animal husbandry schemes particularly milch cattle, irrespective of the potential for the same in the area.
- (v) Excessive concentration on the primary sector activities, particularly during the initial years.
- (vi) Absence of backward and forward linkages, and non-observance of cluster approach were the major problems in implementation. Steps were not taken to provide institutional support to supply raw materials and arrangements for marketing. Thus, during the Sixth Plan, IRDP did not have an area approach nor the expected integration among various sectors. The individual families were picked-up for assistance, rather in an adhoc manner to fulfil targets of the number of families to be covered.
- (vii) Inadequacies in banking infrastructure particularly in the North-East Region affected credit flow. The other deficiencies of the banking system were insufficient scrutiny and delay in the disposal of loan applications, absence of supervision and follow-up, insistence on security, stipulation of unrealistic loan repayment schedules etc. Too much time and efforts were spent on the processing and disbursement of IRDP loans and this adversely affected the working of banking institutions.
- (viii) Although IRDP was meant for the poorest of the poor, it was often found that this target group did not have the necessary absorptive capacity. In such cases the assets kept by them had turned out to be a burden.
- (ix) There was no mechanism within the credit institutions to study or monitor the impact of the loan, the assets created, additional production generated, incremental income derived, etc.
- (x) Although IRDP was originally conceived as a resource based total development plan for a block into which specific beneficiary oriented schemes

of poverty alleviation were to be integrated, this emphasis was totally lost, as it got implemented.

IRDP Under the Seventh Plan

21.12 IRDP continues as the major poverty alleviation programme under the Seventh Plan. The progress of IRDP during the first four years of Seventh Plan is indicated in Table 2 :

Table 2

IRDP Performance in the Seventh Plan

Sr. No. (1)	Items (2)	Targets 1985-90 (3)	Achievements			
			1985-86 (4)	1986-87 (5)	1987-88 (6)	1988-89 (7)
1.	Total allocation (Rs. crores)	2358.81	407.36	543.83	613.38	687.95
2.	Central allocation (Rs. crores)	1186.79	205.93	277.31	310.60	345.00
3.	Central release (Rs. crores)	-	207.10	279.67	299.72	330.84
4.	Total expenditure (Rs. crores)	-	441.10	613.38	727.44	768.46
5.	Total term credit mobilised (Rs. crores)	4000.00	730.15	1014.88	1175.35	1231.42
6.	Total investment mobilised (Rs. crores)	-	1171.25	1628.26	1902.79	1999.88
7.	Total no. of beneficiaries covered (lakhs)	200.00 (100 lakhs of old families)	30.60 (of which old 9.25)	37.47 (of which old 15.46)	42.47 (of which old 18.00)	37.72 (of which old 8.00)
8.	No. of SC/ST beneficiaries covered (lakhs)	60	13.23	16.80	18.99	17.50
9.	Per Capita Subsidy (Rs.)	1333 (Old) (New)	1011.00 1260.00	1178.00 1478.00	1270 1526	1413 1718
10.	Per Capita Credit (Rs.)	2667 (Old) (New)	1952 2051	2412 3033	2514 2944	2935 3350
11.	Per Capita Investment (Rs.)	4000 (Old) (New)	2693 3311	3590 4511	3784 4470	4348 5069
12.	Subsidy Credit Ratio	1:2 (Old) (New)	1:1.9 1:1.6	1:2.0 1:2.0	1:2.0 1:1.9	1:2.0 1:1.9
13.	Sectorwise coverage : (per cent)					
	a) Primary Sector	-	42.1	46.1	41.16	41.81
	b) Secondary Sector	-	15.8	18.4	18.54	19.32
	c) Tertiary Sector	-	42.1	35.5	40.30	38.87

Plan Strategy

21.13 The major thrust in the Seventh Plan is to remedy the weaknesses observed during the Sixth Plan period. The Seventh Plan indicates that the various anti-poverty programmes would be better integrated by adopting a three pronged strategy as under :-

- (i) Such programmes would be formulated and implemented in a decentralised manner with the participation of people's organisations at the grass root level like Village Panchayats, Panchayat Samitis, Zilla Parishads, etc.
- (ii) Planning at the district level involving various disciplines and departments would be made more purposive and co-ordinated.
- (iii) The emphasis would be on group oriented activities for beneficiaries through promotion of co-operatives, registered societies, informal groups, etc.

21.14 The approach to the Seventh Plan reiterates the goal of bringing down the percentage of population below the poverty line to less than ten by 1994-95. For the Seventh Plan period, the rural poor families have been further classified as (i) destitutes (income group Rs.0 to Rs.2,265) (ii) very very poor (income group Rs.2,266 to Rs.3,500) (iii) very poor (income group Rs.3,501 to Rs.4,800) and (iv) poor (income group Rs.4,801 to Rs.6,400). The revised poverty line during the Seventh Plan is Rs.6,400. However, with the objective of reaching the poorer among the rural poor, the cut-off line of Rs.4,800 as annual household income for selection of beneficiaries has been stipulated under the plan. (Even here the first preference for identification is for families with income below Rs.3,501 and only after they have been exhausted, the families in the next slab of Rs.3,501 to Rs.4,800 would be identified). These households will be provided assets with the help of credit and subsidy to enable them to generate income sufficient to cross the revised poverty line. Only after all such families are covered, those in the income bracket of Rs.4,801 to Rs.6,400 would be taken up for assistance. The Seventh Plan envisages the target of assisting 20 million households. This includes the supplementary dose of assistance to 10 million beneficiaries assisted during the Sixth Plan, who could not cross the poverty line. The stipulation that 30 per cent coverage should be of women beneficiaries has been continued. Similarly, 30 per cent assisted families would be drawn from Scheduled Castes and Scheduled Tribes. The ceilings on subsidy fixed during the Sixth Plan are to

continue during the Seventh Plan. The average subsidy per household is expected to be stepped up from around Rs.1,000 in the Sixth Plan to around Rs.1,333, so as to increase the per capita investment to around Rs.4,000 during the Seventh Plan as against Rs.2,876 during the Sixth Plan. The banking system is expected to play a major role in the programme by providing credit to the extent of Rs.4,000 crores during the plan period. In view of the interstate variations and disparities in the incidence of poverty, 50 per cent of the outlays under the programme for the first two years are to be made on the basis of equal allocation per block as in the Sixth Plan and the remaining 50 per cent on the basis of incidence of poverty determined by the NSSO survey. From the third year onwards, the allocation would be based entirely on incidence of poverty.

Certain Procedural Changes

21.15 With a view to streamlining and improving the implementation of IRDP, the Department of Rural Development has undertaken concurrent evaluation of IRDP through various research institutions. The results of these concurrent evaluations have been very useful to re-orient the programme during the Seventh Plan. An experiment of cash disbursement of financial assistance under IRDP in 22 selected blocks all over the country was initiated in April 1986. Under this system assistance in respect of the following cases is to be disbursed in cash to the borrowers :

- (i) Purchase of assets of standard type, make or brand name marketed by reputed suppliers,
- (ii) Industries, Services and Business (ISB) sector schemes in which a number of sundry items are to be bought and the amount of assistance is not more than Rs.3,000, and
- (iii) Purchase of animals.

21.16 In some cases this has eliminated middlemen, reduced delays in loan disbursement by banks and given freedom to the borrowers in selection of assets at comparatively cheaper rates. In some other cases the system has resulted in mis-utilisation of the loan amount and purchase of substandard quality of assets by beneficiaries. Evaluation reports on implementation of IRDP indicated that on an average 50 per cent to 60 per cent of the assisted families during

the Sixth Plan could not cross the poverty line. A scheme envisaging supplementary assistance to help these borrowers, subject to the condition that they are not defaulters and have maintained assets in good condition or have lost them due to reasons beyond their control, has been introduced. Such supplementary assistance would, however, be subject to the overall subsidy ceiling applicable to families. The physical target of 10 million families for supplementary assistance is expected to be covered during the first three years of the Seventh Plan.

Impact of IRDP Lending on Financial Institutions

21.17 As mentioned before, the credit component of IRDP and the involvement of financial institutions particularly commercial banks and RRBs in the programme has been substantial. The concurrent evaluation for the period October' 85 to September'86, revealed that commercial banks accounted for 69 per cent of the loans, RRBs 23 per cent and co-operatives eight per cent. More or less the same pattern was observed during January - September 1987. As at the end of June 1986, the number of IRDP loans of commercial banks stood at 64 lakh accounts with an outstanding of Rs.1,267 crores. Such a massive increase of loaning by the banking system has had the following impact :

- (i) Overdues under IRDP have been higher particularly in the case of commercial banks. As against the recovery in respect of direct agricultural advances by public sector commercial banks at 56.5 per cent and 57.4 per cent for the years 1985-86 and 1986-87 respectively, the recovery rates under IRDP for the corresponding years of these banks were 42.8 per cent and 45.3 per cent respectively. The banks at their Regional Office level should establish a suitable machinery to keep a continuous watch on the recovery of dues under IRDP.
- (ii) The main reasons for non-recovery of loans under IRDP were inadequate income generation and tight repayment schedules. The increased income derived from the assets under IRDP eroded due to compelling obligation to meet family expenses as well as repayment of old private debts. Because of this, there is a view to the effect that consumption loan should be provided as part of the IRDP lending.
- (iii) The large number of applications under IRDP and the low average size of loans increased the workload and administrative costs of the branches.

The Study* by our consultants showed that in selected branches there was an increase in the number of applications by 199 per cent in the case of commercial banks and 69 per cent in the case of RRBs. The workload has also been higher due to the increase in overdues and the necessity to monitor and follow-up the overdue loans. Overall, there were complaints that staff was inadequate to meet the increasing work-load, particularly in the case of rural branches.

- (iv) The bankers viewed IRDP loans as targets imposed on them from the top. The general impression going around was that they need not adhere to the accepted banking norms which otherwise they would have followed in such cases. Almost all proposals sent by the BDO were sanctioned. Such dilution in the quality of appraisal had resulted in deterioration of lending standards under IRDP. Many bankers found it difficult to change their traditional attitude and involve many small borrowers in their portfolio. Often their urban ethos came in conflict with the demands imposed by such development banking.
- (v) Banks also found it difficult to distinguish between those poor who could make productive use of loans and those who could not. Consequently in the name of IRDP, loans were granted to persons whose only qualification was their poverty and not necessarily any ability to use the funds productively and repay the loan.
- (vi) Substantial increase in the IRDP loaning has diluted the concept of schematic lending of the banks. Schematic lending has by and large become automatic lending and most banks depend on sponsored applications and some walk-in business to complete their targets in rural lending.

Bankers' view

21.18 Case studies undertaken at our instance have revealed several deficiencies in the implementation of IRDP from the point of view of the bankers. Major problems experienced by the bankers are :

- (i) The overwhelming majority of branch managers felt that under IRDP, identification was not being done properly by the BDO. The loan applications were being sponsored from different villages without taking into consideration the market potential or infrastructural facilities. The BDO

* Consultant Study I, "Agricultural Credit in General", Chapter VI.

himself decided the activities for the beneficiaries and not the beneficiaries themselves, resulting in a mismatch between skills and the proposed activity in many cases.

- (ii) Adequate attention was not paid to availability of suitable assets and in consequence the size of the unit tended to be lower than the prescribed norms.
- (iii) Nearly 50% of the branch managers interviewed pointed to the ineffectiveness of the lead bank forums in sorting out the problems of the banks relating to provision of infrastructural facilities.
- (iv) Many branch managers felt that once the loan was disbursed, the relationship between the BDO and the beneficiaries ended. The bankers were left alone to pursue the recovery of loans. Bankers wanted that the sponsoring authorities should also assume some responsibility for recovery.
- (v) Several relaxations made in respect of eligibility criteria, rate of interest, collateral security etc. imparted a special status to IRDP loans. Consequently, branch managers often neglected to calculate even the repaying capacity of the individuals sponsored under IRDP.
- (vi) The bankers felt IRDP lending as irksome for the following reasons:
 - (a) lack of freedom to choose the borrowers or the economic activities,
 - (b) general apprehension that the beneficiaries selected would not be in a position to make productive use of loans and repay the advance,
 - (c) lack of adequate planning by DRDA to identify income generating activities,
 - (d) compulsion to fulfil the targets imposed from above, and
 - (e) general disregard of viability of activities by government functionaries who in effect choose borrowers as well as activities.

IRDP - An Overview and Critique

21.19 As stated earlier, the Indian economy, mainly because of low growth rates over successive plan periods, had belied the expectations of any significant "trickle down" effect. The developmental problems had been further aggravated by high population growth and increasing marginalisation of agricultural holdings due to constant sub-divisions through inheritance. The numbers of the rural poor, therefore, continued to grow, Plan after Plan, despite various noteworthy

developments in diverse fields. It was in this context that the IRDP was born. There are a number of persons who are critical of the rationale and economic concept of this programme. Though named as Integrated Rural Development Programme, it, right from its very inception, was never conceived and operated as an integrated programme of rural development, seeking to secure fuller exploitation of local resource potential and the development of the necessary supportive socio-economic infrastructure, and by thus generating heightened economic growth in the area affording the poor the needed opportunities for wages and self employment on an ever-growing basis. It is not our intention here to enter into a discussion on these issues as it would be outside the scope of our enquiry. Looking, however, to the staggering dimensions of rural poverty, we do recognise the justification and validity of a programme which seeks to make a direct intervention on behalf of the specifically identified poor families by giving them access to productive assets and enabling them to increase their levels of income above the poverty line. Even more importantly, the very fact of the millions of these participating poor families getting exposed to the discipline and commercial behaviour patterns, inherent in their involvement with institutional credit, can be a factor of profound social and economic significance in a modernising society.

21.20 As we have pointed out earlier, there have, however, been many deficiencies and inefficiencies in the manner in which the programme has been implemented. Besides the numerous evaluation and impact studies, the findings of field studies conducted by our consultants and our own field visits and discussions with a wide cross-section of borrowers, bankers and other officials make us believe that IRDP could emerge into an effective poverty alleviation programme if certain modifications could be brought about in its implementation. The inefficiencies and inadequacies exist at all stages of implementation, starting from the very identification of potential beneficiaries, to determining for each beneficiary the specific bankable activity appropriate to his skill and capability and the market potential, to supervision and follow-up of the borrower to see that he is getting the best out of the productive asset and finally to ensure recovery of the loan.

21.21 In practice, over the years the programme has been reduced essentially to a set of targets to be fulfilled in terms of coverage of persons and credit

given. Such an approach has led to a decline in the standards of loaning and a growing cynicism in the bank branches' staff about the seriousness and sincerity of the government officials, charged with the implementation of this programme, towards its objects. It should be a matter of serious concern that the proportion of beneficiaries who have actually crossed the poverty line (Rs.6,400 per annum) through assistance under this programme is only 12-13 per cent for the country as a whole, with most states being below this average. In some of the states which are above the national average, it has been noted that these states were the ones where the percentage of beneficiaries wrongly selected from income levels higher than Rs.6,400, was also the highest.* Thus, if this factor is discounted, the national average would in fact, be lower still. It also needs to be noted that in these computations of incremental income, the instalments of loan repayment do not seem to have been adjusted. If that were to be done, as it ought to be, the percentage of those having actually crossed the poverty line will further decline. Looked at from the point of view of the incremental income accrued, the Concurrent Evaluation for the period January-December, 1987, as also earlier Evaluation, indicates that as many as 22 per cent beneficiaries had no incremental income at all (which can only mean that the asset itself did not exist** or was not being used), 10 per cent had incremental income between Re.1 and Rs.500, 17 per cent between Rs.501 and Rs.1,000, 24 per cent between Rs.1,001 and Rs.2,000 and 27 per cent above Rs.2,000. If the loan repayment instalments are adjusted against this incremental income, there will be almost half the beneficiaries i.e. those in the incremental income range of Re.0 to Rs.1,000 who will have no real incremental income, if not a net deficit. Of the rest, even in cases where there is some incremental income after adjustment of loan instalment, the fact of incremental income itself should be a matter of no great satisfaction to the implementer of the programme if it falls significantly short of his crossing the poverty line, which is basic objective of the programme. The comparative picture (in percentages) of different incremental income ranges as revealed by the two aforementioned Concurrent Evaluation studies by the Department of Rural Development, GOI is given in table 3 :

* Concurrent Evaluations of IRDP for October 1985 to September 1986 and January-December 1987, Department of Rural Development, Ministry of Agriculture-February 1987/August 1988.

** Analysis of Concurrent Evaluation sponsored by Government of India for October 1985 to September 1986 indicates that on all India level 29 per cent of the assets were not intact. (P.66)

Table 3

Income from Assets

Concurrent Evaluation Period	Income range in rupees				
	0	1-500	501-1000	1001-2000	Above 2000
Oct. 1985 to Sept. 1986	24	11	15	24	26
Jan. 1987 to December 1987	22	10	17	24	27

21.22 With this kind of performance, those beneficiaries who fell in the category of 'destitutes' (pre-assistance income range of Re.0 to Rs.2,265) and 'very very poor' (income range of Rs.2,266 to Rs.3,500) could hardly be expected to cross the poverty line of Rs.6,400.

21.23 If, therefore, the programme has to have its central object of removal of poverty to be substantially fulfilled and credit is to play such a dynamic role in it, major changes must occur in the concept and practice of IRDP. First, there must be meaningful village, block and district level planning (see Chapter X) to diagnose what activity will be profitably pursued by IRDP participants, at what scale and with what additional services. This planning process must include representation from rural banking system, experts at the block level and local leadership to ensure that all critical elements are well matched. Any credit plan for any size of area, in order to be meaningful has to have the backing of a carefully conceived development plan for that area. This requirement is even more important when the object is to provide productive credit to the target group of the most disadvantaged. Asset financing cannot be undertaken as an isolated activity. For example, poultry and dairy activities cannot be financed on a scattered basis because in that case produce assembling and marketing, servicing centres, input provisioning etc. cannot be organised economically for sustaining the scattered production activities. Appropriate backward and forward linkages with the production activity are similarly necessary for the success of the so-called ISB activities also, highlighting the need for a

planned project approach to such financing. The Seventh Plan recognised this critical deficiency in the implementation of the programme and had envisaged that this gap would be filled. A number of instructions and guidelines were also issued by the GOI and by some State Governments in their turn, to bring this about. However, for want of clear operational modalities and systems having been laid down in this behalf, this approach was not being followed and the entire attention of the DRDA authorities and the financial institutions was focussed on achievement of physical and financial targets in terms of numbers. The concept of IRDP needs to be re-oriented from the present one in which the provision of credit is seen as the complete instrument of uplift to a concept where all services and inputs needed are made available to make the new enterprise succeed, i.e. credit is only the means by which the recipient commands those services and inputs.

21.24 Second, targeting must be realistic in terms of resources and opportunities available. Uniform targets for all blocks, irrespective of varying poverty levels and potential for development, only make the programme mechanistic and far from productive. The Seventh Plan had envisaged that in view of the interstate variation and disparity in the incidence of poverty, a part of the financial outlay under the programme was to be apportioned on the basis of an equal allocation to each block and the balance on the basis of incidence of poverty determined by the NSSO survey. However, in practice we found that in almost all the States no such consideration actually prevailed in setting the targets and that the variations in actual coverage which emerged from block to block were more accidental than by design. The general understanding of the field personnel also was that the targets for all blocks were uniform. Incidentally, this may also perhaps be one of the reasons for a fairly high percentage of beneficiaries being wrongly identified, i.e. from income levels higher than the ones stipulated for selection, because of the pressures of uniform targets in all the blocks. Then there is another aspect to the coverage which needs to be taken note of. By and large, it is evident from various evaluation studies on IRDP that the success of this programme is relatively greater in comparatively more progressive states. These are states where the growth is comparatively higher and the market relatively more developed. It, therefore, appears logical that in the strategy of implementation of the programme the approach to targeting has to be distinctively different in states and areas with a lower incidence of poverty from those states and areas which have higher incidence of poverty.

21.25 Third, rural banking personnel must enforce normal banking discipline in the choice and supervision of borrowers. This is essential to preserving the integrity of the banking system as well as realising the opportunity of bringing the poor within the pale of responsible entrepreneurship. The virtual lack of involvement of the banks in the choice of participants in the programme, and of the specific activity to be financed for each participant, is having a very deleterious effect not only on the quality of loaning under the programme, but, indeed, on the entire banking culture of their personnel. It has become more important to fulfill quantitative targets of coverage, undoubtedly under constant pressure from governmental agencies on pain of being dubbed as 'non-cooperative', rather than be concerned about the quality and soundness of the loans given. Trends are clearly discernible that a degree of casualness is beginning to creep into the work ethos of the rural branches of commercial banks, with most of them remaining content with 'walk-in' business besides sponsored programmes like IRDP. Populistic measures like 'loan melas' have further aggravated the situation. We would like to give a clear warning that if this decline in responsible banking attitudes is not checked, its adverse effects will fast spill over also to the general developmental business of the banks, in the process imperilling the whole banking system.

21.26 Fourth, many procedural changes must be made in lending practices, from greater emphasis on working capital, to reasonable schedules of repayment, in order to fit the legitimate business needs of the poor in the activity they undertake. The analysis of the Concurrent Evaluation for the period October 1985-September 1986 (Department of Rural Development) indicates that while about 40 per cent of the beneficiaries did not require any working capital, of the balance only about 28 per cent received working capital and the remaining 32 per cent required it but did not receive it. The same Evaluation also indicates that at the national level the cases of loans sanctioned for IRDP for which the repayment period was three years were about 36 per cent of the total and those sanctioned for less than three years were about 26 per cent. According to the programme guidelines, the repayment period of the loan should normally be three to five years. It is obvious that in actual practice the banks had not adhered to these guidelines and had sanctioned loans for repayment period of less than three years. On the basis of the same analysis when we see the State-wise variations in repayment schedules, we observe that the extent of the loan

cases sanctioned for repayment period of less than three years was about 42 per cent in West Bengal, between 30 to 40 per cent in Andhra Pradesh, Kerala, Madhya Pradesh, Tamil Nadu and Punjab, 20 to 30 per cent in Uttar Pradesh, Sikkim, Gujarat, Himachal Pradesh, Assam, Jammu and Kashmir and Maharashtra and 10 to 20 per cent in Orissa, Karnataka, Rajasthan, Bihar, Haryana, Manipur and Tripura. This position seems to have somewhat improved according to Concurrent Evaluation for the period January-December 1987, both at the All-India as well as individual state level. The tight repayment schedule could well be one of the important reasons for non-viability of the schemes financed. The banks should not fix the repayment period less than what has been prescribed in the guidelines.

21.27 Fifth, subsidy to help the poor overcome the special disability which extreme poverty places in the way of entrepreneurship, must be provided in a manner which encourages and facilitates the discipline of financial responsibility. Though there are many evaluation studies on the IRDP and other poverty alleviation programmes, there is no major study to our knowledge specifically focussed on the subsidy element and this has been identified as a gap in the Seventh Plan document also. The Plan document further emphasises that the mechanism of administering the subsidy needs to be reviewed and rationalised with a view to ensuring that leakages are minimised. Nevertheless, in our own field studies and discussions we found that there was general dissatisfaction with administration and utilisation of the subsidy element of assistance. Apart from the inconvenience generally experienced by the borrowers in availing subsidy and the delayed release of payment of subsidy very often by the DRDA to the banks, there was acute criticism of the leakages which were said to occur in the administration of the subsidy. There were widespread complaints that the subsidy amount was not reaching the beneficiary in full and that a sizeable portion of it was being misappropriated by both the Government functionaries and the banks' officials as also some clever borrowers who merely wanted to pocket the subsidy and some middlemen who worked as touts. It is obviously not possible to quantify the exact extent of the leakage, but those who have close contact with the administration of IRDP in the field put the estimate as anywhere from 20 percent and above. This factor itself is bringing the programme into disrepute and is causing resentment among genuine beneficiaries who feel cheated of their full share of assistance.

21.28 Sixth, an integrated view needs to be taken of a self-employment programme like the IRDP and wage-employment programmes like NREP and RLEGP. Data generated by the evaluation and impact studies on IRDP as we have brought out earlier, clearly indicate that those in the 'destitute' and 'very very poor' categories cannot normally be expected to cross the poverty line of Rs.6400, with the level of investment which is being made available under IRDP. The data emerging from the Concurrent Evaluation for the period October 1985 to September 1986, on average assistance to a beneficiary (amount per account in different income groups), is given in table 4 :

Table 4

Average Assistance to Beneficiaries in Different Income Groups

Income Group	(All India Average in Rupees)				
	Less than 2266	2266 to 3500	3501 to 4800	4801 to 6400	More than 6400
Average assistance	2930	3437	3399	4004	4035

21.29 If the average pre-assistance income of a 'destitute' category beneficiary is assumed at Rs.1,500, requiring an incremental income at Rs.4,900 to cross the poverty line, then, illustratively, on the basis of the Incremental Capital Output Ratio (ICOR) which is being adopted in the Seventh Plan, the average capital requirement would be Rs.13,230 for him to cross the poverty line of Rs.6,400. As against this, the average value of asset provided to beneficiaries of this category was only Rs.2,930 and of the 'very very poor' category only Rs.3,437. Such higher levels of investment may not be possible to be provided to the large numbers targeted to be covered, not only because of the resources constraint, but, more importantly, for want of management capability of these persons to handle higher and more sophisticated levels of investment. It seems necessary that the wage and self employment programmes be so consciously coordinated with each other so as to take all the participants above the poverty line.

21.30 Several studies have shown that people far below the poverty line who are burdened, aside from their poverty, with low quality assets, lack of working

capital other than their labour, lack of management skills and with no semblance of entrepreneurial abilities have immense difficulties in crossing the poverty line. We are making a suggestion below that large masses of such people would benefit much more from wage employment programmes than entrepreneurial programmes. However, if these categories of the "destitutes" and "very very poor" are to be assisted under IRDP, it is essential that (i) the quality of assets provided to them becomes a subject of attention; (ii) a well focussed extension programme is provided to assist them with awareness and inputs; (iii) the various leakages in subsidies and loans are plugged and (iv) the package of investments provided for them should match with the skills available within the beneficiary family.

Recommendations

21.31 On the basis of the foregoing analysis on various aspects of IRDP, we now propose to discuss specific recommendations relating to its implementation so that IRDP could graduate into an effective poverty alleviation programme.

Planning Process and Selection of Activities

21.32 We have noted earlier that the selection of economic activities, to be pursued by the beneficiaries under this programme, had been done on an adhoc basis without a careful study of the economic potential of the village/block, or of the essential backward and forward linkages needed. The list of activities which has been circularised by the GOI and the state governments to DRDAs by way really of an illustrative list, has indeed become almost the whole universe of activities and these are being picked up mechanically for financing individual beneficiaries. In other words, the programme was being implemented not within the framework of a well thought out resource-based area development plan but on a scattered family basis. The GOI guidelines, issued in July 1987, laid down that the selection of schemes should be determined in relation to the income gap required to be covered to bring the family above the poverty line with the minimum investment and that while selecting schemes the requirements of infrastructural support and backward and forward linkages available in the area should be kept in view. However, neither we nor our consultants who have made an extensive field survey, found any indications that such an approach was beginning to be extensively adopted. During our discussions with the Depart-

ment of Rural Development, we were told that a significant beginning has been made in this direction and a number of projects focussed on IRDP beneficiaries have lately been developed in some states with appropriate marketing tie-ups. Reference was made by them in this behalf to projects in the field of garment making, gems polishing and cutting, carpet weaving and manufacture of watch parts in U.P., Haryana, etc. with assured marketing of these products contracted with certain large users. We were also told that expert guidance and assistance in planning and management has also been made available to some of these projects. We whole-heartedly welcome this new thrust by the Deptt. of Rural Development. We would, however, like to emphasise that considering the large numbers involved, such project planning would need to be done much more extensively and on a decentralised basis. We strongly recommend that in future implementation of IRDP, this deficiency should be removed and only activities having sufficient potential in the area, based on its resource endowments, market capacity and available infrastructure, should be selected under the programme. The need for building up resource-based local plans has been repeatedly emphasised in the documents of successive Five Year Plans in the past. It seems that this approach will acquire a major thrust during the coming Eighth Five Year Plan, judging from the emphasis which is being placed on district planning by the Prime Minister. While it is difficult for us to anticipate the lines on which such local planning will be done in the coming Plan and the actual shape that this process will take, we are of the view that planning for IRDP need not await the formulation of comprehensive district development plans. When these are available they will form the ideal basis, but meanwhile in the restricted context of IRDP, the emphasis for the present could be on formulation of viable projects in different sectors - primary, secondary and tertiary - for a group of villages or the block or district, depending on the nature of the project, in which the families targeted for assistance under IRDP could be brought in as participants. In other words, what we are recommending is adoption of a project approach, in the real sense of the term, under which technically feasible and economically viable projects and schemes are formulated for a given area and the families from the target group, selected on considerations of their pre-assistance asset base and skills (including traditional skills), their entrepreneurial traits and their own choice, are fitted in these projects. Programmes in the nature of TRYSEM can be meaningfully coordinated with IRDP for imparting or upgrading of skills and for entrepreneurial development

of the participants. With the recent decision of the RBI to allocate specific villages to each branch of the commercial banks/RRBs, to be called its "Service Area", it should indeed be quite feasible to develop the project approach proposed by us with the bank and development staff of the Government working together, taking assistance, of course, of the expertise available to them from their higher levels and from other suitable institutions.

21.33 We also recommend that the preparation of viable projects as proposed above should be a precondition for release of Central assistance for IRDP to the DRDAs. Otherwise, we apprehend that for want of such a discipline the requirement of such project planning may also go the same way as some other guidelines issued by the Government from time to time.

21.34 Like-wise, NABARD should also make such project planning as a precondition to extending its refinance facility. Presently, IRDP lending is considered by NABARD as schematic lending, though in point of fact, it is scattered lending aggregated together to give it the appearance of a scheme.

21.35 A close look also needs to be taken at the existing administrative structure for poverty alleviation programmes. Fuller involvement of the popularly elected local bodies, at village, block and district levels, is called for both in operational planning and implementation of the programme. The nature of their involvement and mechanisms therefore will vary from State to State, because of the considerable diversity in the Panchayati Raj Systems adopted in different States. We can at this stage only emphasise the need to have such mechanisms and operational systems evolved in each State. The involvement, at present, of these bodies with the programme is somewhat perfunctory, if not altogether missing.

Identification of Beneficiaries

21.36 The guidelines issued by the GOI laid down that the initial listing of likely participants in the programme in a village would be done by the block staff on the basis of a survey, and this list will then be placed before the Gram Sabha for approval. The Concurrent Evaluation, October 1985 to September 1986, revealed that Gram Sabha was involved in selection of only 55 per cent of the beneficiaries, whereas 40 per cent were selected by officials. The pattern

varied widely from State to State. The subsequent Concurrent Evaluation, January-June 1987 and January-December 1987 gives the same trend i.e. 59 per cent beneficiaries were selected in the meetings of the Gram Sabha and 37 per cent by block officials. The remaining 4 per cent were selected by various persons including politicians, landlords, employers etc., and this percentage was as high as 32 in case of Jammu and Kashmir and 20 in case of Punjab. As for the involvement of financial institutions in the selection of beneficiaries, the Study conducted by our consultants reveals that, though the guidelines suggested that the bank officials should be invited to Gram Sabha meetings when selection of beneficiaries was to be made, in actual practice they had hardly any involvement in the selection process. Interviews and discussions with bank officials at various levels indicated that the block agencies were not very keen to associate the bank staff in the selection process. The banker must have complete freedom to satisfy himself fully both about the competence of the person whom he finances and also the purpose for which he finances. But in practice, under IRDP the banker is left with no such freedom. In this context therefore we cannot but reiterate that the bank branch concerned must necessarily be involved in the initial process itself of identifying the beneficiaries in conjunction with the block staff. However, we are cognizant of the fact that considering the dimensions of the programme and the large scale on which it is operating, more or less covering all villages, the banks may not have adequate staff for actively participating in the selection process, or even if the bank's staff is able to participate in the meetings of the Gram Sabha where the selection is to be finally made, that participation may be somewhat perfunctory in nature. The banker at that stage will hardly have had the opportunity of assessing a potential beneficiary from the point of view of his capability to implement a scheme of investment. We consider it vital to the success of the whole purpose and thrust of development banking that the banker must have full involvement effectively both in the selection of persons to be assisted from the identified target group and also the purpose for which assistance is to be given.

21.37 In our view the present system of identification needs to be changed altogether. Under the present system, the lists of persons selected from different villages, with or without the participation of the bank's staff in the selection process, are forwarded annually to bank branches for financing them. The process

of selection of potential beneficiaries is generally an annual feature and those selected during the year are proposed to the banks for financing during the year. In other words, the list given during a year to a bank branch becomes the target of coverage for the branch for that year. In fact, not only the names but the economic activity to be financed for each beneficiary is also indicated. This more or less straitjackets the branch altogether in its scope of financing. The system that we propose is that the identification of families below the poverty line should be done at one go for all the villages in a block. This would then become the Master List for the block. The list could be updated, say every three years, to include any changes that may have occurred during this period, though normally not many changes would take place. The advantage of such a Master List would be that it would then be possible for the DRDAs to straight away identify from it those who are best assisted under other programmes e.g. wage-employment programme or social security programme. We are separately recommending later fuller coordination between the self-employment and the wage-employment programmes and in that context the advantage of such a Master List would become clear. The balance, i.e. those who are to be assisted by the banks for self-employment activities, would then be the ones for which the banks and the DRDAs would try to develop economically viable and bankable projects, and cover them in course of time in accordance with annual targets. This will give the needed flexibility to the banks. The concern of the banker is not so much with who are selected as the 'poor' - that can be best done by the State agencies - but with who among those he can meaningfully finance and for what economic activity.

Fixation of Targets

21.38 Much of the faulty implementation of the programme emanates from the targets which get fixed from year to year and which are supposed to be binding on both the financial institutions and the DRDAs. The targets in themselves are unrealistic inasmuch as there is virtual uniformity of targets for all blocks in the State, irrespective of the incidence of poverty and potential of the area. The situation is further compounded by sudden increase in annual targets during the course of the year, often very close to the end of the year, say in January or February, by some State Governments with the intention of showing higher performance of the State in comparison to the other States. Virtually, therefore, it becomes a race among States and among districts/blocks in the State to cover

more and more persons in quantitative terms. The programme is included in the Prime Minister's 20-Point Programme and its physical achievements are being constantly monitored at the GOI level and the comparative performance of the State circularised among all the States periodically. This makes for constant competitive pressure for showing better statistical performance. Of course, budgetary allocation of subsidy sets some outer limits, but this constraint is got over by keeping investment per beneficiary at low enough levels calling for lower matching subsidy and spreading the amount over larger numbers. This, in turn, defeats the purpose of generating incremental income adequate to enable a beneficiary to cross the poverty line. We are of the view that the manner in which targets are being presently fixed is counter-productive and must be given up. We recognise that in a time-bound and object specific programme of this nature it is necessary to have targets, but the targets must be realistic. They must be realistic not only inasmuch as they take into account varying poverty levels in different States (in respect of individual State targets) and in different blocks in a State (in respect of individual block targets); they must also be realistic inasmuch as they take into account the potential of an area which will enable a particular set of targets to be effectively fulfilled. We have mentioned earlier that the findings of various evaluation and impact studies of the programme tend to show that the programme has done relatively better in areas of higher economic growth with a better developed market infrastructure. Merely setting high targets for areas of high incidence of poverty will not be of much avail. Unless these are preceded by well conceived and clearly articulated local development plans, and the needed infrastructural linkages are available, the results will continue to be qualitatively as unsatisfactory as they have been so far, in terms of percentage of persons having actually crossed the poverty line as a result of assistance given under the programme.

21.39 In respect of the targets, therefore, we have the following recommendations to make :

- (i) We do not yet know the basis on which the target of coverage during the VIII Plan would be fixed for the programme. We, however, understand that it would most likely be derived by allocating a certain percentage of families below the poverty line for coverage under this programme, so that the employment and income generating opportunities created by

various other measures contemplated in the Plan along with the residual coverage earmarked for this programme will achieve the poverty eradication target envisaged for the Plan, i.e. not more than 10 per cent families to remain below the poverty line at the end of the Plan. We gathered that the target, therefore, may be close to 30 million beneficiaries. We do not find ourselves in agreement with this approach of targetting. Poverty eradication, more particularly under this programme, does not lend itself to a mere game of numbers. The data and evaluation studies amply show that while a very large number of persons has been assisted, those who have crossed the poverty line are a mere 13 per cent of those; in fact even less if those who were wrongly selected as having higher income (above the poverty line) are excluded. The programme to be meaningful and effective must be based on adequate investment for each beneficiary and the total numbers must be such as can be handled by the banking system effectively both in terms of resources and servicing. Seeing the trends, the investment level per beneficiary (both new and second-dose) even for similar size of units as financed in the past, will in the VIII Plan be considerably higher. Considering the other heavier credit demand for agriculture and allied activities in the VIII Plan and the increasingly emerging demand for non-farm sector, which itself is vital for generating larger employment in rural areas, we foresee that the banking system, both commercial and co-operative, may find it difficult to adequately meet the credit requirements of, and effectively service, an IRD programme of this order. In the circumstances, we suggest that the target of coverage under this programme during the VIII Plan should be retained at the same level as the VII Plan, which will amount to a coverage of 4000 families on an average per block for the five year period, of which half will be new beneficiaries.

- (ii) Targeting for individual blocks should be done in two parts; one a core target to be fulfilled by all blocks and the other variable depending on potential of each block. Coverage of a minimum number of 2000 families per block during the Plan period may be set as the core target uniformly for all blocks i.e. 10 million families during the Plan period.
- (iii) The balance target of 10 million families should then be split up for each block as its additional target for the plan period. This additional

target should be based on specific factors more important among which would be the resource-potential of the block to develop, viable and bankable schemes for the required number of beneficiaries, the capacity of the financing institutions, the availability of required linkages and the incidence of poverty. Higher incidence of poverty need not mean higher additional targets if corresponding potential and other positive factors are not available. It should be quite possible to develop a system of weightages for the above mentioned different factors in order to arrive at a workable formula for determining these variable targets. The basic minimum target as recommended above should take care of the core level of poverty which one could expect prevails in all blocks, with additional targets being given to most blocks in the light of their viability and practicability depending on relevant weighted factors. We believe that this mode of targetting would ensure that while notional minimum target are met by all blocks, many would far exceed those targets as they take advantage of the much larger opportunities for the poor in those blocks, where agriculture is advancing rapidly due to favourable physical, technological and developmental conditions.

Role of Banks

21.40 Though credit is the major plank of the IRDP, the role of financing banks in it has all along been somewhat passive, inasmuch as they have been treated as mere windows for the disbursement of loans. They have had little involvement either in the selection of proposed beneficiaries or in the activities to be financed or, indeed, in assessing the viability and bankability of the activities financed. Theoretically, no doubt, the bank has the right to make its own assessment of all loan cases, and, if necessary, to object to financing a particular activity for a particular beneficiary, but the manner in which the whole system is being operated and the high pressure which is constantly being exercised on the banks by the DRDA and State Government authorities, the bank has neither the time nor the inclination to process the cases sponsored under the programme for their appropriateness and suitability. In the circumstances, if 30 sewing machines or 63 camel carts are financed in one village (these are actual instances), the financing bank, in spite of having the right to question the proposals, is disinclined to do so. Financing of milch animals on an extensive scale in villages which are not on the milk routes of dairy schemes or are far from

consuming centres, making the sale of milk at a remunerative price difficult locally, is far too common a phenomenon in the programme, seriously affecting the viability of such projects. It is our belief that unless the system itself is changed, merely giving a theoretical authority to the banker to appraise each proposal on his own would not do. The system itself has to be such that makes the banker responsible and accountable for every loan sanctioned by him. The financing bank should have no alibi, to be able to say later that both the borrower and the object of borrowing were prescribed by somebody else and therefore he could not be held accountable if the loan turned out to be unsound. As the dimensions of the programme are large, and are continuing to expand, the culture of casualness and permissiveness generated by its existing operational systems, threatens to warp the professional mentality of the bank staff and would no doubt affect the whole work culture of the banks. As development bankers, charged with the task of helping the poor, their challenge should lie in making presently non-viable persons into a viable economic entity and not merely to act as disbursers of loans. This calls for great deal of planning, project formulation and entrepreneurial development. Under the present mode of functioning of the programme, the banker would not be able to fulfil the role expected of him, despite whatever rights and authority he may possess on paper.

21.41 While fully adhering to the objects of the programme, we recommend the following measures which we believe, will facilitate the fulfilment of the objective of the programme and at the same time involve the banks fully and squarely in the task :

- (i) Instead of giving to each bank branch an annual list of proposed beneficiaries which more or less tallies with the annual targets, allowing no leeway to the financing bank, the branch should be given the total list of the identified poor who are required to be assisted by that branch over the entire period of five years of the Plan. This flows from our recommendation made earlier that identification of the poor should be done at one go, instead of piecemeal annually.
- (ii) While sending the list to the bank, no specific economic activity should be proposed for individual beneficiaries.
- (iii) A list of bankable activities should be separately drawn up by the banks in conjunction with the DRDA authorities, which are the most appropriate

and suitable for the area. The projects specifically prepared in the light of the potential of the area as recommended by us earlier, would also form part of this list of activities.

- (iv) The advantage of the above approach will be that the bank branch would then be required to contact the persons in the larger list provided to it and pick out from them those who can be readily fitted in viable projects and who have the ready skills to take up a particular activity immediately, and finance them during the current year. As for the rest, some preparatory work may have to be done either by way of developing skills (TRYSEM) or formulating some new projects or awaiting the creation of some other linkages, and those can be financed in the next year or the year after. Thus, while on the one hand annual targets will have been fulfilled, on the other the banker will have had the needed planning opportunity in the choice of viable activity for each borrower under readily available or developable projects in future. Above all, in this system the banker will have full accountability for the purposes for which financing has been done by him. This system will also give scope to innovative and planning capability of the local branches. They will have to devise projects which are the most viable in the context of local resources and potential.

21.42 One apprehension has been expressed to us that in the 'Master List' approach and the freedom to the bank branch to choose the targeted number of beneficiaries out of it for IRDP assistance, it is likely that the banks may choose only those who are among the upper income range of the poverty scales and ignore the lower poverty deciles. We do not consider this a genuine apprehension, because, firstly, it is neither our case nor that of the bankers that viable projects cannot at all be developed for lower categories of the poor (although recognising at the same time the fact that there will be many in these categories who cannot successfully handle an investment project and are best assisted under a wage employment programme), and secondly, in the constant interface of the bankers and the DRDA which must necessarily follow a programme of this nature it is most unlikely that the bankers would and could ignore the overall social concerns that may be stipulated as a matter of policy. They would still at the same time retain their freedom in the choice of individual beneficiaries based on their bankability.

Administration of subsidy

21.43 We have already brought out earlier that there were widespread complaints of leakages and misuse in regard to the subsidy element of assistance under the programme. We had considerable discussions with a wide cross-section of bankers as well as government officials in this regard. While no one disputes the need for giving subsidy in order to improve the viability of loans to this disadvantaged section, there were a number of persons who felt that the misuse of subsidy would be considerably reduced, if instead of a capital subsidy, the interest were to be subsidised. We have considered both the alternatives and we are of the view that there will be no particular advantage in converting the capital subsidy into interest subsidy. The subsidised interest rate will on the one hand not have the same psychological impact on the poor borrower (it will be another Differential Rate of Interest (DRI) Scheme) and on the other, it will make for considerable increase in the work load of account keeping for both the Government and the banks. Moreover, subsidised interest rates create unhealthy distortions in the interest rate structure and are best avoided. We are of the view that assistance should be given by the Government in the form of capital subsidy only. However, experience has shown that capital subsidy at the initial stage itself, as is being done now, is the main cause of its misuse. Subsidy in the beginning of the project tempts many to diverse manipulations, because it is treated as something by itself, apart from the loan. We, therefore, recommend that instead of adjusting the subsidy to unit cost at the beginning, the same should be retained as a fixed deposit at the normal rate of interest with the bank in favour of the beneficiary, and adjusted towards the last one or two instalments of loan repayments. In other words, the bank will have to extend the full unit cost as loan at the beginning and recover the last instalment(s) from the subsidy-deposit. The following illustration brings out notionally how the modified system of subsidy adjustment towards the last instalment of loan repayment would function for a unit cost of Rs.3,000 repayable over 5 years at ten per cent interest rate.

Present Method			(Rs.)	
Year	Loan	Repayment	Loan	Repayment
1	2000 (Subsidy 1000)	528	3000	540
2		528		540
3		528		540
4		528		540
5		526		465*
		<u>2638</u>		<u>2625</u>

* Balance amount of loan outstanding at the end of fifth year i.e. Rs.1,610 will be adjusted by subsidy deposit of Rs.1,000 made at the beginning whose maturity value will also be Rs.1,610.

21.44 Such a change in procedure will mean that to the extent of the subsidy (which was earlier adjusted towards unit cost), the banks will have to provide additional loans initially. Overall the banking system may have to provide about Rs.2000 crores as additional loans over a five year period. This additional demand, we believe, should be quite possible for the banking system to meet over a five year period. Correspondingly, however, the deposits (subsidy deposit) with the banks would also increase. They would have to maintain the stipulated levels of cash and other reserves, but in the present context CRR and SLR are no longer losing propositions for the banks. Further, since banks would also be eligible for refinance support to the extent of their lending under IRDP, we feel that the overall impact of such a change in procedure on the banking system would only be marginal and well within their capacity to absorb. Under this system the chances of misuse of subsidy will be greatly minimised. Another stipulation which will need to be made would be that, to get the benefit of subsidy deposit for adjustment towards the last repayment instalment (s) the borrower will have to show that the asset for which he had taken the loan was still intact, and if not, for what good reasons. It is also assumed that under the general monitoring systems to be developed, the borrower will have been regularly followed up during the pendency of the loan.

Procedural Aspects

21.45 It is not our intention to go too much into detail into procedural aspects. These are measures which are constantly under review by the authorities concerned and improvements are being gradually made. We would only like to highlight the following specific aspects which are partly in the nature of policy and partly in the nature of practice related to policy :

- (i) Studies have revealed that most beneficiaries financed under IRDP have need for working capital, for purchased inputs including hired labour, e.g. feed for cattle, yarn for handloom etc. Studies have also revealed that only a small percentage of borrowers has actually been financed for such working capital, mostly for some of the items under ISB Sector in which working capital is built into the unit cost itself. We suggest that while sanctioning loan for any unit, the need for working capital should be very specifically assessed and must be financed, otherwise for want of this the entire project may fail.
- (ii) While policy guidelines are that the loan should be for a period of three to five years, in large number of cases the actual repayment schedules stipulated by the banks have been for shorter periods. With the clientele of this nature, we suggest, it will be more prudent to err on the side of liberality rather than strictness and that the repayment schedule should be somewhat easier. In any case, the repayment period should not be less than what has been prescribed in the guidelines. We are happy to note that the latest evaluation study shows some improvement in this respect.
- (iii) The unit costs for different projects have come to acquire a certain rigidity. Though these are fixed by NABARD after considerable interaction with all relevant authorities and are also revised from time to time as costs go up, they are essentially in the nature of standard unit cost. The standard unit cost may have validity as an average cost for a state or even a district, but there could be variations in the actual unit cost from area to area even within a district. There is, therefore, need for a certain degree of flexibility to be allowed to the banks in deviating from the standard unit cost for purposes of financing and subsequent refinancing by NABARD. While it is necessary to lay down standard unit cost as general indicator of the prevailing average, NABARD may examine

as to how and to what extent deviations could be permitted.

Bad Debt Reserves

21.46 Lending to the poor, particularly the poorest, is always fraught with greater risk to the financing bank. IRDP is a Government sponsored programme, with specific targets which the banks have necessarily to fulfil. And, it is a programme which is continuing to grow not only in terms of number of accounts but also in financial involvement of the banks. While a number of recommendations have been made by us, which we believe will improve its implementation, we consider it appropriate and necessary that the Government also should participate and help in building up the Bad Debt Reserve Fund of the financing banks. We recommend that the Government should contribute every year to the Bad Debt Reserve Fund of commercial banks, including RRBs, at the rate of two per cent of the loans disbursed by them under IRDP during the preceding accounting year. This is because the involvement of the commercial banks which was only marginal, now accounts for more than 90 per cent of the total credit given under IRDP. Since 1988, the Government has agreed to give a contribution of six per cent to the risk fund of co-operatives in respect of their term lending under IRDP. But we do not recommend a contribution of six per cent for commercial banks including RRBs since commercial banks are entitled to deduct two per cent of the outstanding advances at rural branches while computing their taxable income. The proposed contribution to Bad Debt Reserve will be in addition to this concession.

Other Poverty Alleviation Programmes

21.47 Apart from IRDP the other major rural Poverty Alleviation Programmes are :

- (i) DWCRA (Development of Women and Children in Rural Area)
- (ii) TRYSEM (Training of Rural Youth for Self-Employment)
- (iii) NREP (National Rural Employment Programme)
- (iv) RLEGP (Rural Landless Employment Guarantee Programme)

Though these programmes do not have a credit component, DWCRA and TRYSEM are closely linked with IRDP. We have discussed other programmes like DRI, SEEU, SEPUP etc., which are primarily implemented by commercial banks in the Chapter III on Commercial Banks and Rural Credit.

Development of Women, Children in Rural Areas

21.48 Despite the stipulation that 30 per cent of beneficiaries under IRDP should be women, it was seen that the benefits under the programme were not flowing to women in adequate measure. Consequently, DWCRA was introduced in Sept. 1982, in 50 blocks on a pilot basis. The major aim of the programme was to increase the income of rural women and provide support services needed to enable them to take up income generating activities. Assistance was given to individual women or to those organised in homogenous groups, to take up economically viable activities. Child care facilities for such women were also provided. The Sixth Plan outlay for the scheme was Rs.15.60 crores in addition to UNICEF assistance of Rs.5.40 crores. During the Sixth Plan (1980-85), in all 3,308 groups covering 52,170 women beneficiaries were organised and the total expenditure was Rs.162.15 lakhs. During the Seventh Plan DWCRA programme was extended to 1,000 blocks. In the first two years of the Seventh Plan, 11,506 groups were formed covering nearly 2 lakh women beneficiaries with a total expenditure of Rs.1,132.75 lakhs. DWCRA continues to be a supportive programme to IRDP during the Seventh Plan. There are very few evaluation studies of DWCRA. It is necessary to make an indepth study of the Programme, in particular, of its credit related aspects.

Training of Rural Youth for Self-Employment

21.49 Started in 1979, TRYSEM aims at providing technical skills to rural youth so that they can take up self-employment in the fields of agriculture and allied activities, industries, services and business activities. The Sixth Plan aimed at training two lakh rural youth every year at the rate of 40 youth per block per annum. The target group was rural youth between the ages of 18 and 35 from families living below the poverty line. It was stipulated that : (i) a minimum of 30 per cent of the trained youth should belong to SC/ST and (ii) a minimum of 1/3 of the rural youth trained should be women. The trainees were given a stipend of Rs.150 per month. In addition, an amount of Rs.75 per month per

trainee was paid to the training institution to meet the training costs. On successful completion of the training, the trainees were provided with a kit of tools costing between Rs.400 to Rs.500, relevant to the trade in which they were trained. Trainees were also entitled to loans from the banks in addition to subsidies on the IRDP pattern. During the Sixth Plan as against the target of 10.05 lakhs, the actual number trained was 10.15 lakhs. Of this, 3.34 lakhs persons (32.91 per cent) belonged to SC/ST and 3.43 lakhs (33.79 per cent) were women beneficiaries. In all, 5.80 lakhs trainees could secure employment i.e. 4.78 lakhs in self-employment and the balance 1.02 lakhs in wage-employment. During the Seventh Plan, it was envisaged that those selected under TRYSEM should be trained according to the actual need and no macro targets were fixed. The cost of training was to be met out of the funds earmarked for 'infrastructure' under IRDP. Evaluation studies of TRYSEM have brought out several weaknesses in the implementation of the programme. The selection of trainees was not always done properly based on their aptitudes. Many trainees treated TRYSEM training period as a short-term employment without paying any serious attention to the training. Training courses in many cases were not relevant to the needs of the area. The training institutes themselves were poorly equipped. There were also complaints of corruption against the training institutes. There was hardly any follow-up of trainees after the training was over.

National Rural Employment Programme

21.50 The NREP was launched in October 1980 and became a regular Plan programme from April 1981. The programme was expected to generate additional gainful employment in rural areas to the extent of 300 to 400 million mandays per annum, create durable community assets and improve nutritional status and living standards of the poor. Creation of durable assets was an important objective of this programme and it had been stipulated that expenditure on materials should be to the extent of 50 per cent of the total project cost. The actual funds made available for the programme during the Sixth Plan were about Rs.1,873 crores i.e. Rs.1,079 crores by the Centre and Rs.794 crores by the States against which the actual utilisation was Rs.1,843 crores. The employment generation objective under NREP has been consistently achieved as can be seen from table 5 :

Table 5

Employment Generation under NREP

<u>Year</u>	<u>(In million man-days)</u>
1980-81	414
1981-82	355
1982-83	351
1983-84	303
1984-85	352
	<hr/>
	1,775
	<hr/>

(Source - Seventh Five Year Plan)

21.51 However, it is not known as to how much of this employment has been directed towards those who are landless and the poorest among the poor. According to the Seventh Plan document, the programme had a substantial impact in terms of stabilisation of wages in rural areas, containing prices of foodgrains and the creation of a wide variety of community assets to help in raising the levels of living of rural people. The broad objectives of the programme remained the same during the Seventh Plan. An outlay of Rs.1,250.81 crores has been provided for NREP in the Central Sector which will be matched equally by the States. A total employment of about 1,445 million man-days would be generated under the programme during Seventh Plan.

Rural Landless Employment Guarantee Programme

21.52 RLEGP was introduced in August 1983, with the primary objective of expanding employment opportunities for the rural landless. The idea was to guarantee employment to at least one member of every landless household upto 100 days in a year. Thus, the programme had a sharper focus on landless labour households. An outlay of Rs.500 crores to be fully financed by the Central Government was provided under the programme during the Sixth Plan. During 1983-85, 320 projects with an estimated cost of Rs.893.05 crores were sanctioned under this programme. As against the target of employment generation in 1983-84 and 1984-85 at 360 million man-days, the actual achievement was 262.81 million man-days. During the Seventh Plan, an outlay of Rs.1,743.78 crores has been provided for RLEGP to be borne by the Centre. A total employment of 1,013

million man-days under RLEGP is likely to be generated during the Seventh Plan.

Linkages of IRDP with other Poverty Alleviation Programmes

21.53 We have already brought out earlier the need to take an integrated view of all anti-poverty programmes, more particularly the wage-employment programmes like NREP and RLEGP and a self-employment programme like the IRDP. The data built up on the basis of the past performance of IRDP clearly indicate that those with a pre-assistance annual income of less than Rs.3,500 cannot generally be expected to cross the poverty line with the level of investment so far being made available under the programme. One approach could be to raise the level of investment, which in other words means raising the unit size, and thereby hope for higher incremental income needed to cross the poverty line of Rs.6,400. We are, however, doubtful of the efficacy of this approach. Such higher levels of investment, particularly for a programme of such huge dimensions, may be quite beyond the capability of the banking system. But what persuades us even more against such an approach is the fact that most, if not all, the beneficiaries of this class, may find it quite outside their pale of capability to handle bigger and more sophisticated units of assets. If they had really been so capable there was no reason why even in the past a large number of them had not opted for higher investments. Even at present the limit is only on subsidy and not on the loan and if one were to take Rs.3,000 as the limit on subsidy (Rs.5,000 in case of tribal beneficiaries), a corresponding loan of Rs.6,000 to Rs.9,000 could have been taken. But the State Government authorities in their wisdom, have fixed the unit sizes at relatively smaller levels in the light of the capability of management of this class of beneficiaries. Of course, a few could with advantage handle higher instalments, i.e. those who have higher entrepreneurial ability, but not the mass in general. Higher level of investment for uninitiated borrowers does not generally succeed. This has been the experience also of Self-Employment Scheme for the Educated Unemployed Youth (SEEUY) (Chapter III) in which the awareness and capability levels of the beneficiaries were believed to be considerably higher than in IRDP. Therefore, while we feel that there is some scope for enhancement of investment per beneficiary, mainly to account for cost escalation, we are not convinced that increasing the unit size with corresponding increase in the investment per beneficiary, as a general policy prescription, would really be desirable or feasible. Yet the object of removal of abject poverty stays, as it must. We believe that

the object set forth by the Government is to bring down the population below the poverty line to five per cent by the year 2000 A.D. Therefore, we have to achieve this objective in a manner which is practical and which will give the best results. This can be done effectively only by suitably dovetailing the various poverty alleviation programmes.

21.54 According to the Seventh Plan estimate, the percentage of population with a consumption standard below the poverty line is expected to come down from an estimate of 36.9 per cent in 1984-85 to 25.8 per cent in 1989-90 and further to less than 10 per cent by 1994-95. In absolute terms, the number of poor persons is expected to decline from 273 million in 1984-85 to 211 million in 1989-90 as shown in table 6 :

Table 6*

<u>Year</u>	<u>Poverty Ratio vis-a-vis Number of Poor</u>					
	<u>Poverty Ratio (per cent)</u>			<u>No. of poor (Million)</u>		
	<u>Rural</u>	<u>Urban</u>	<u>Total</u>	<u>Rural</u>	<u>Urban</u>	<u>Total</u>
1977-78	51.2	38.2	48.3	253.1	53.7	306.8
1984-85	39.9	27.7	36.9	222.2	50.5	272.7
1989-90	28.2	19.3	25.8	168.6	42.2	210.8

21.55 We do not know whether the projections made by the Planning Commission in regard to the total number of poor at the end of the Seventh Plan would turn out to be correct. Perhaps it may turn out to be an underestimate. The latest NSSO Survey figures are not yet available to us. When we look at the two wage employment programmes, viz. NREP and RLEGP, we find that both combined were expected to generate 2,558 million man-days during the Seventh Plan period, which in other words amounts to providing employment for 100 days annually for five years to about 5 million persons. We are not fully aware of the efficacy of these two programmes. A comprehensive evaluation of these programmes is currently under way. Nevertheless, the figures of physical achievements which are available lead us to believe that substantial employment has been generated under these programmes, more or less in conformity with the target. These two programmes have recently been combined and rightly so, and the amalgamated programme designated as Jawahar Rozgar Yojana (JRY) with a considerably enlarged outlay of Rs.2,600 crores during 1989-90. The object

*Source :- Seventh Five Year Plan, 1985-90, Vol.I - Government of India, Planning Commission-Page.33

of JRY is similar to RLEGP. We do not yet know what the outlay and targets for JRY would be during the VIII Plan. Though one should expect a stepping up in the outlay in the VIII Plan, yet even if the annual outlays of this programme remain at the same level as in 1989-90, it would amount to an outlay of Rs.13,000 crores for the five year period 1990-95. Assuming an expenditure of Rs.20-25 on the generation of one man-day of employment, including the materials cost and other incidental costs chargeable to this programme, it should be possible to generate employment for 100 days in the year for five years for approximately 12 million persons. Thus we would have during the VIII Plan notionally about 20 million persons assisted under IRDP (in the light of our recommendation not to increase IRDP coverage beyond 20 million) and about 12 million persons (more, if outlay is stepped up) assisted under the wage employment programme of JRY, with some beneficiaries common to both.

21.56 Following from this, our specific suggestions are as follows :

- (i) We have recommended earlier that a Master List of the poor in each block should be drawn up through a process of identification at one go. After screening out those who have to be assisted only under social security programmes (old, infirm, disabled) the Master List should be made available to each bank branch in respect of its area of operation.
- (ii) Priority in assistance may be given by the bank to those who have some asset base, either of land (small and marginal farmers) or of skill (artisans, or others specially trained in some line of activity). The aim of the bank should be that they should be able to secure enough incremental income through the economic activity financed to be able to go above the poverty line.
- (iii) The remaining ones would be those, mostly belonging to 'destitute' and 'very very poor' categories, who will not be able to cross the poverty line, except in a few cases, with assistance under IRDP alone. For them it will be necessary that they be assisted under both the wage-employment and self-employment programme simultaneously. Of course, there will be some among them who may have no capability altogether of handling an asset of any kind and therefore they will have to be looked after entirely under the wage-employment programme.
- (iv) Generally speaking, the targets for IRDP should be higher in blocks with

better potential and better infrastructure availability, whereas in poorer blocks the targets for wage employment programmes should be comparatively larger. The same applies to states, with less developed states getting larger allocation under wage employment programmes.

- (v) The above recommendations postulate that the selection of beneficiaries under both kinds of programmes will have to be done in a planned and calculated way by the DRDA and banks jointly so that those who are assisted under either or both these programmes do manage to cross the poverty line and are out of the reckoning of poverty. Implementation of these programmes effectively within the broader framework of a growing economy with a dynamic and viable agricultural sector in the next decade should be able to most significantly alter the rural poverty scenario of the country.

PART IX

DEMAND FOR AND SUPPLY OF AGRICULTURAL CREDIT : PROJECTIONS

XXII DEMAND FOR AGRICULTURAL CREDIT: PROJECTIONS

XXIII SUPPLY OF AGRICULTURAL CREDIT : ESTIMATES OF
RESOURCES

XXIV CREDIT FOR AGRO-PROCESSING AND MARKETING :
PROJECTIONS

CHAPTER - XXII

DEMAND FOR AGRICULTURAL CREDIT : PROJECTIONS

Introduction

Looking to the scenario of economic development for the year 2000 AD, against which background the projections for demand and supply of credit are attempted in this and the subsequent chapter, we are confronted with such complex problems as assessment of future rate of inflation, trends in the interest rates structure for agricultural credit, increasing monetisation of the economy that would improve savers' preference for financial instruments and the diversification of agricultural and non-farm economic activities in rural areas that would increase the demand for credit. The demand for credit would also depend on the overall growth in the economy and the pace or level of adoption of new technology. Requirements of credit for integrated production, processing and marketing of high value produce/products of crop - livestock system, crop - livestock - fish production system, and the agro forestry/silvi-horticultural and plantation system could be expected to increase as these systems will assume great significance in the coming years. More importantly, there is likely to be greater prospect in the world trade for horticultural products than for the traditional commodities. Currently, the developed countries account for no less than 80 per cent of the total world import of horticultural products. In fact, world's exports of horticultural products amounted to about US \$ 25 billion or about 11 per cent to 12 per cent of the total world exports of agricultural produce, in the recent years. By supplying adequate finance for production and marketing, and taking into account the bio-technological developments that are emerging in horticulture, India would command a greater share of world market in horticultural products.

22.02 Looking at the other side of the coin, there are certain factors in sight, which might subdue or partly off set the sharply rising demand for credit in the future years. Experience shows that a farmer/borrower delays creation of debt till the time he can manage with his own resources. This concept of fungibility in reverse, using own funds in preference to borrowed funds, particularly when (a) the prices of assets rise higher and higher (b) the output-input ratios become adverse and (c) the borrowers rely more on equity rather than on debt, can somewhat curb the demand for institutional credit.

22.03 On the supply side, the mounting defaults, the poor credit absorption capacity of the credit institutions in underdeveloped areas, and the credit allocation policies and programmes of the government can make considerable difference to the availability of institutional credit. All these variables make it difficult to arrive at a very precise estimate of future demand and supply of credit. To illustrate this phenomenon with an example, when the demand for credit exceeds supply, bankers may prefer to provide more credit to the more viable clients, which could impair the accessibility of small and marginal farmers and the other weaker sections of the rural economy to institutional credit. However, government policies and the poverty alleviation programmes can reverse this trend and accelerate both the broadening and the deepening of rural credit in future.

22.04 Projections of demand and supply in the future, be they of outputs, inputs or credit, are not of the nature of soothsaying. Nor can they be firm forecasts of the future. They depend clearly on the assumptions made about the future behaviour of the many factors which influence demands and supplies. These influencing factors invariably turn out to be many and often intangible and hence not easily forecastable. So the correctness of projections is actually a matter of choice of impinging factors, choice of assumptions and the correctness of assumptions. All that can be said is that, should these factors behind our credit projections be predominantly relevant and the directions and magnitude of the assumptions be basically correct, the projections may come out to be correct. Therefore, with the best of knowledge and feel that one may have about the factors and assumptions, it is best to place a healthy doubt about the possibility of the projections of credit demand and credit supply coming entirely true. On the other hand, insofar as an awareness, a perspective and a feel exist on the part of the projector, these projections cannot be dismissed as irrelevant.

22.05 The second difficulty is that the past behaviours of the projected variables and of the underlying factors, which are some of the key inputs in future projections, are bad guides to the future. In dynamic and growing economies where the structures of demands and supplies are changing and institutional as well as technological changes are the order of the day, the one thing that can be said with confidence is that the future will be different from the past. In that case, the past becomes irrelevant and does not remain a guide to the future;

one cannot project from that kind of a past but has to substitute a different kind of a future. But as there is no experience about the future, one can only go by assumptions.

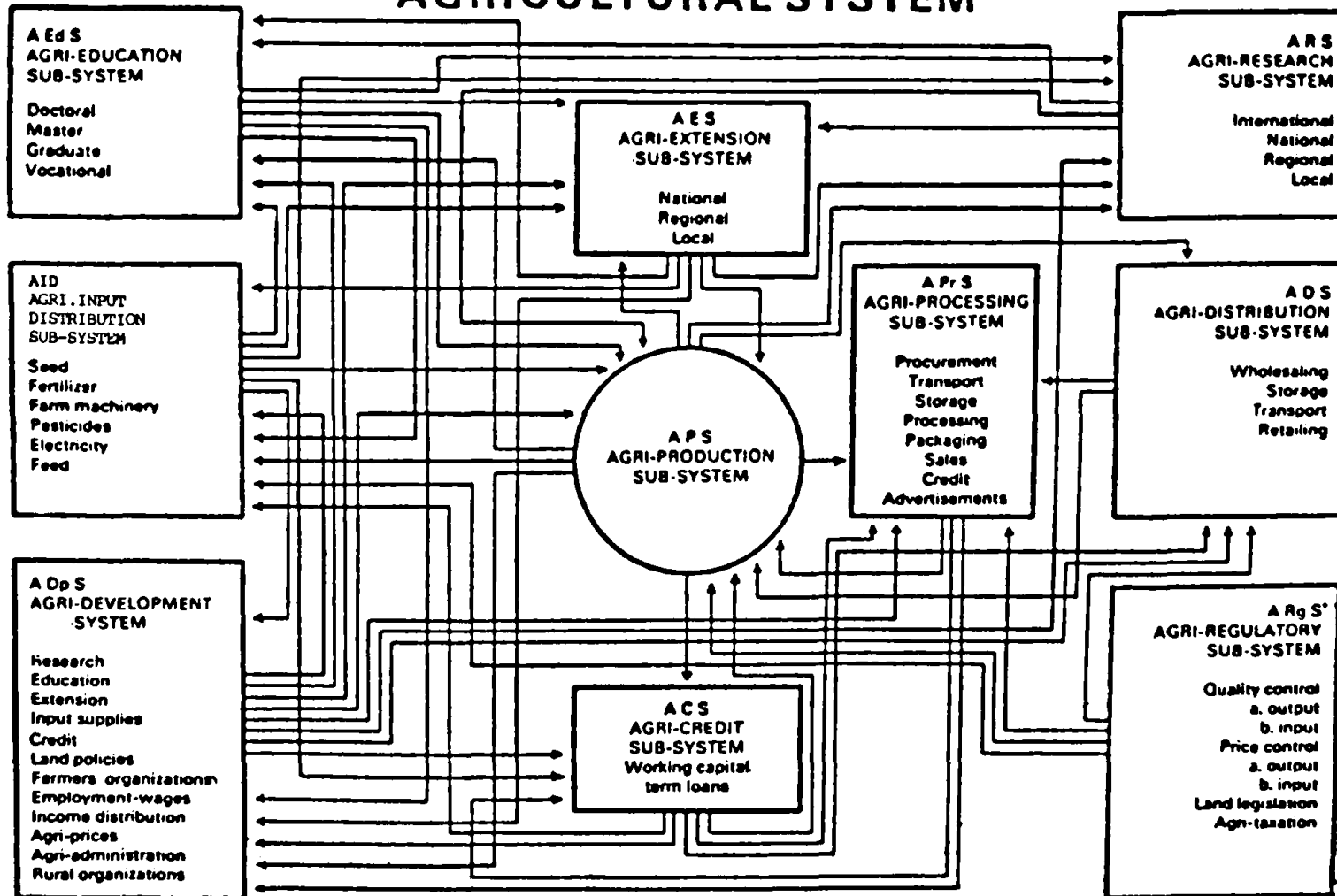
22.06 However, the experience of other economies, during comparable periods of their development and when their structures were substantially comparable, does provide an analogy and can sometimes be used with caution. Even more importantly, there are some laws of economic behaviour which have their roots in logic and have been empirically tested and firmed up over a wide range of experiences, that do provide some guidelines about the factors to be chosen in projections and the assumptions to be made. For instance, it can be stated with confidence that as the Indian economy grows in terms of real income per capita, the projection of demand for cereals to total demand for agricultural products will decline and that the demand for milk and milk products as well as for horticultural products and several others will increase. Similarly it can be stated on the basis of a whole range of empirical observations that a poor economy has a small ratio of stocks to flows over time; that as it grows it has a higher ratio, and that as it grows further and begins to manage its stocks with efficiency and sensitivity to interest rates and other factors, it again has a smaller ratio of stocks to flows. Concomittantly, it can be stated that the credit required for stock building also varies accordingly.

22.07 While such broad behavioural laws and tendencies are known in theory and in practice and can be used in projections, it is obvious that the exact magnitude of the changes again requires assumptions making, and this gives the projections necessarily a semblance of uncertainty. It is in this spirit that our following projections of credit demands and supplies should be viewed.

Agricultural System

22.08 Agricultural system, in the wider sense, includes several supporting sub systems such as agricultural production, agricultural input distribution, agricultural distribution, agricultural processing, agricultural credit, agricultural education, agricultural research, agricultural development, agricultural extension and agricultural regulations. A chart indicating the various sub systems of agriculture is given on the next page.

AGRICULTURAL SYSTEM

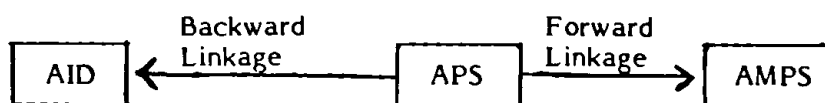


22.09 Each sub system of the agricultural system is inter linked and provides support to other sub systems. Effective development of the agricultural production sub system, which consists of raising of seasonal agricultural crops, horticultural and plantation crops, and the activities allied to agriculture such as livestock (i.e. dairy, poultry, sheep rearing, piggery, etc.) and fishery (i.e. inland and marine), requires a strong back up of agricultural education sub system, agricultural research sub system, agricultural development sub system, agricultural extension sub system and agricultural input distribution sub system, which includes supply of seeds, fertilisers, farm machinery, pesticides, electricity and feed. These sub systems will be backward linkages for effective development of agricultural production sub system.

22.10 With the development of the backward linkages and by providing adequate and timely supply of credit by the agricultural credit sub system, production under the agricultural production sub system will increase. However, for the farmers to realise remunerative prices for the increased produce, a strong agro processing sub system covering, procurement of produce, transport, storage, processing, packaging, etc., will be necessary. Further, the agricultural distribution sub system, covering wholesaling, storage, transport and retailing will have to match the supply with the demand and also increase the demand for certain products by proper advertisement, etc. These are the forward linkages from the perception of agricultural production sub system. For the sustained development of agricultural production sub system, an agricultural regulatory sub system, covering quality control and efficient and effective support price system is also necessary. As the various sub systems of agricultural system are having close linkages with one another, for the proper sustained development of agricultural system, every sub system will have to be strong.

22.11 The backward linkages between agricultural production sub system (APS) and the agricultural input distribution sub system (AID), when realised at an accelerated rate can enhance growth in productivity, production and value added in APS as well as AID. The credit for APS can assist in generating supply of output and thereby creating demand for services from agricultural marketing and processing sub-system (AMPS). This forward linkage between APS and AMPS when achieved at an accelerated rate would provide marketing services, perhaps better price and higher share in value addition through processing to APS. By the same

token, it can enhance growth in productivity, production, and value added in AMPS. This is because what is marketed by APS to AMPS relaxes the latter's raw material constraint and the economy's wage goods constraint. This in turn can lead to higher growth in productivity, production and value added in AMPS and in the rest of the economy. Since the units in AMPS are relatively labour intensive (especially for the basic foods like grains, edible oilseeds, milk and sugarcane processing), and since they produce products whose income elasticity of demand is high, the higher income growth in APS, AMPS and AID would relax the demand constraint for the products produced by AMPS. A diagram indicating the inter relationships of the sub-systems is given below :



22.12 Achieving the backward linkage and the forward linkage cannot be automatic because of several reasons. However, institutional credit, among other policies, can assist achieving these linkages by serving all the three sub-systems and thereby encourage further realisation of potential benefits of new technologies especially in APS and more generally in AID and AMPS. India already has an institutional rural credit policy, which allows the rural financial institutions to extend credit and other services to all the three sub-systems, viz., AID, APS and AMPS.

22.13 In this report, agriculture, more particularly, with reference to the credit needs thereof, assumes the whole range of activities which are eligible for refinance from NABARD. Projections of demand for agricultural credit are accordingly based on this assumption. In this chapter, we have confined our study to the demand for credit upto 2000 AD in respect of agricultural production sub-system and agricultural input distribution sub-system. In a separate chapter we have covered the demand for credit up to 2000 AD for (a) agro-processing industries, (b) storage, transportation and marketing of agricultural produce and (c) export of agricultural produce.

22.14 To start with, the mechanics of working out "Demand Projection" in this report may be briefly stated. Having first clarified what we perceived as the broad canvas of agriculture, and the range of the expanding activities that will be financed, we have traced the progress of institutionalisation of credit in the country since 1951-52. The reason for this is that these institutions not only play a positive role in the demand creation by their developmental activities but also have a critical role on the supply side thereof. We have also furnished

the estimates, of the National Commission on Agriculture, in respect of the credit requirements of agriculture and allied activities for the year 1985 along with the achievements thereagainst, so as to have a comparative view of the agricultural credit-demand projection exercises on the one hand and the actual achievements, on the other. We have also reviewed the targets fixed for agricultural credit during the Sixth Five Year Plan along with the achievements thereunder upto 30th June 1985, as also the targets under Seventh Plan to serve more as the take-off point for our exercise. Against this background we have made our estimates of credit demand for agriculture in its broader sense, both under short-term and long-term requirements, for the years 1989-90, 1994-95 & 1999-2000. As stated earlier these estimates have been made after setting up certain models/assumptions for demand projections. These models/assumptions as well as the methodology followed in respect of each sector coming under agriculture and allied activities, are discussed in the following paragraphs.

Institutionalisation of Rural Credit

22.15 The rural households, especially the cultivators, now depend, as available evidence points to, increasingly on institutional agencies for credit. The percentage of borrowings of the cultivators from institutional agencies to the total debt owed by them has been increasing progressively as will be seen from table I.

Table I

Borrowings of Cultivators from Institutional Agencies

Type of rural households	Year/period	Percentage of borrowings of cultivators from institutional agencies to the total debt.
Cultivators	1951-52	12.3
	30-6-1961	18.4
	30-6-1971	31.7
	30-6-1981	63.3

The share of the cultivators' debt owed to institutional agencies increased progressively from 12.3 per cent in 1951-52 to 63.3 per cent as on 30.6.1981. It will also be observed that the period 30-6-1971 to 30-6-1981 witnessed considerable increase in institutionalisation of credit in the country.

22.16 The non-cultivator households in rural areas had also been borrowing increasingly from institutional agencies as will be seen from table 2.

Table - 2

Borrowings of Non-cultivator Rural Households

Type of rural households	Year/Period	Percentage of borrowings of non-cultivators from institutional agencies to total debt
Non-cultivators	1951-52	12.2
	30-6-1961	10.5
	30-6-1971	10.2
	30-6-1981	36.7

However, the borrowings of non-cultivators in rural areas were very much lower than the borrowings of the cultivators. This can be seen from table 3, indicating the percentage of borrowings of all rural households, (i.e. cultivator households and non-cultivator households), from institutional agencies, to the total debt owed by them.

Table 3

Borrowings of all Rural Households

Type of rural households	Year/Period	Percentage of borrowings of all households from institutional agencies to total debt
All households	1951-52	12.3
	30-6-1961	17.3
	30-6-1971	29.0
	30-6-1981	61.2

Thus the rural households have been increasingly turning to the institutional agencies for their credit needs and this will have a positive influence on "demand" and "supply" of agricultural credit in future.

Source: Reports of All India Rural Credit Survey 1951-52 and All India Debt and Investment Surveys 1961-62, 1971-72 and 1981-82.

Estimates of Credit Requirements for Agriculture and Allied Activities

22.17 The report of the National Commission on Agriculture (NCA) which was submitted on 31st January 1976, contained, among other things, the estimates of credit requirements for agriculture and allied activities for the year 1985.

Methodology adopted by NCA

a) Short-term Credit Requirements for Crop Production

22.18 The credit requirements of crop production by the year 1985, for full programme coverage, were estimated at Rs.600 per hectare for presently irrigated and newly irrigated areas and at Rs.450 per hectare for unirrigated areas. On this basis the credit requirements for crop production by the year 1985 were worked out as indicated in table. 4.

Table 4

Credit Requirements for Crop Production by the year 1985

<u>Class of farmers</u>	<u>Credit requirements (Rs. crores)</u>
i) Marginal and small farmers and agricultural labourers	1,755
ii) Medium and large farmers	5,475
Total	7,230

The total short-term credit requirements for crop production for the year 1985, thus worked out to Rs.7,230 crores.

b) Short-term Credit Requirements for Allied Activities

22.19 The short-term credit requirements under livestock programmes for the year 1985 were worked out on the basis of per unit credit requirement and the number of units expected to be operated by the year 1985. However, it was presumed that no short-term credit (working capital) would be required for milch cattle. The short-term credit requirements for small fishermen were worked out at the rate of Rs.2,200 per hectare and the total coverage under this programme was estimated at one million hectares of water area. The details of credit requirements are given in table. 5.

Table 5
Short-term Credit Requirements for Allied Activities for the year 1985
(Rs. crores)

Particulars of allied activities	Credit requirements for		
	Marginal and small farmers and agricultural labourers	Medium and large farmers	Total
i) Milk Production	-	-	-
ii) Piggery	118	118	236
iii) Poultry	78	78	156
iv) Sheep	20	20	40
v) Fishery	222	-	222
Total	438	216	654

The total short-term credit requirements for allied activities, for the year 1985, thus worked out to Rs.654 crores.

c) **Medium and Long-term Credit Requirements for Land Development and Minor Irrigation**

22.20 The medium and long term credit requirements by the year 1985, for full programme coverage, were estimated on the basis indicated at table 6.

Table 6
Investment Credit - Credit Requirements per hectare

Item	Credit requirements (Rs per hectare)
i) Preparation of land covered under major and medium irrigation (8 Mha)	1,350
ii) Improvements in 5 Mha already developed under major and medium irrigation	200
iii) Improvements in area covered by minor irrigation (1 Mha)	200
iv) Ground water development (9 Mha)	1,000
v) Land development in unirrigated areas, levelling, soil conservation, water harvesting, ponds, etc.	500

The details of credit requirements, worked out on the basis indicated are given in table 7.

Table 7
Medium and Long term Credit Requirements for
Land Development and Minor Irrigation by the year 1985

Category of farmers	Credit requirements (Rs. crores)
i) Marginal and small farmers and agricultural labourers	1,502
ii) Medium and large farmers	5,498
Total	7,000 =====

The total medium and long-term loans for land development and minor irrigation by the year 1985, thus worked out to Rs.7,000 crores.

d) Medium and Long-term Credit Requirements for Allied Activities

22.21 The medium and long-term credit requirements by the year 1985, under livestock programmes were worked out on the basis of unit cost and the number of units expected to be operated by the year 1985. The medium and long term credit requirements for fishery development were worked out on the basis of credit for small fishermen for repairs of existing ponds and brackish water swamps. The details of credit requirements are indicated in table 8.

Table 8
Medium and Long term Credit Requirements for Allied Activities by the year 1985
(Rs. crores)

Particulars of allied activities	Credit requirements for		
	Marginal and small farmers and agricultural labourers	Medium and large farmers	Total
i) Milk production	285	60	345
ii) Piggery	30	30	60
iii) Poultry	90	90	180
iv) Sheep	90	90	180
v) Fishery development	500	-	500
Total :	995	270	1265 =====

The total medium and long-term loans for allied activities, by the year 1985, thus worked out to Rs.1,265 crores.

22.22 The total credit requirements estimated by NCA for agriculture and allied activities by the year 1985, at the full programme coverage amounted to Rs.16,549 crores. The details are indicated in table 9 below.

Table 9
Total Credit Requirements by the year 1985

		(Rs. crores)		
		Marginal and small farmers and agricultural labourers	Medium and large farmers	Total
		_____	_____	_____
<u>Short-term credit</u>				
i)	Crop production	1,755	5,475	7,230
ii)	Allied activities	438	216	654
	Total	2,193	5,691	7,884
=====				
<u>Medium and long term loans</u>				
i)	Land development and minor irrigation	1,502	5,498	7,000
ii)	Allied activities	995	270	1,265
	Total	2,497	5,768	8,265
=====				
Total of short-term and medium and long term loans		4,690	11,459	16,149
Plus credit requirements for machinery and implements				400
			Grand Total	16,549
=====				

[The statistical information indicated in respect of the estimates is based on Appendix 55.9 (pages 101 to 108) of Part XII of the Report by the National Commission on Agriculture]

22.23 For the purpose of working out more realistic estimates of credit requirements for the year 1985, to be met by institutional sources, NCA adopted graduation in respect of short-term credit for crop production and for medium and long term credits for land development and minor irrigation. The details are given in table 10.

Table 10

Basis of Graduation of Full Requirements

	(Per cent)	
	<u>Marginal and small farmers</u>	<u>Medium and large farmers</u>
a) Areas already irrigated or to be irrigated :		
(i) Short-term loans :		
Coverage by 1985	100	100
Scale of financing	100	50
(ii) Long & medium term loans:		
Coverage by 1985	100	100
Scale of financing	100	100
b) Unirrigated areas :		
(i) Short-term loans :		
Coverage by 1985	50	50
Scale of financing	100	60
(ii) Medium and long term loans		
Coverage by 1985	50	50
Scale of financing	100	60

22.24 In the case of livestock and fishery development programmes, no graduation was considered necessary by NCA since the programme coverage envisaged was the minimum. Due deductions were made from medium and long term credit requirements, for subsidy element to which small and marginal farmers and the agricultural labourers were eligible under the then SFDA and MFAL programmes. The graduated requirements were worked out at Rs.9,400 crores. The details are given in table 11.

Table 11

Graduated Requirements of Credit for 1985

	(Rs. crores)		
	Short-term	Medium and long-term	Total
Marginal and small farmers	1,766	2,022	3,788
Medium and large farmers	2,242	3,003	5,245
Total :	4,008	5,025	9,033
Machinery and implements say	-	400	400
	4,000	5,400	9,400

The estimates made by NCA in respect of short-term credit requirements related to the year 1985. The medium and long-term credit requirements estimated related to the cumulative disbursements during the period 1976 to 1985.

Credit Estimates by NCA and the Achievements

22.25 The graduated requirements of short-term credit for agriculture and allied activities by the year 1985 were estimated by NCA at Rs.4,000 crores. As against this estimate, the short-term loans issued during the year 1984-85 by primary agricultural credit societies and commercial banks including regional rural banks for agriculture and allied activities amounted to Rs.3,489.9 crores. The short-term loans outstanding as on 30-6-1985 amounted to Rs.5,006.2 crores (Source : Report on Currency and Finance 1986-87, Volume I, Table - VII - 41, page 216).

22.26 As against the graduated requirements of medium and long term loans for agriculture and allied activities, estimated to be issued during the years 1976 to 1985 by financial institutions at Rs.5,400 crores, the actual disbursements during the period 1975-76 to 1984-85 amounted to Rs.12,646.7 crores and far exceeded the estimate by NCA. This was mainly due to the very low credit requirements per hectare, assumed by NCA in respect of the various activities related to irrigation and land development and due to the impact of inflation on the cost of inputs for the various investment activities. The credit requirements per hectare assumed by NCA are given at table 6 in paragraph 18. The details in respect of the medium and long term loans issued during the period 1975-76 to 1984-85 are given in table 12.

Table 12
Medium and Long-term Loans Issued During the Period 1975-76 to 1984-85

<u>Year</u>	(Rs. crores) <u>Loans issued during the year</u>
1975 - 76	497.7
1976 - 77	668.2
1977 - 78	667.8
1978 - 79	849.5
1979 - 80	1,081.5
1980 - 81	1,388.8
1981 - 82	1,555.6
1982 - 83	1,593.1
1983 - 84	1,909.0
1984 - 85	2,435.5
Total :	12,646.7

The medium and long-term loans for agriculture and allied activities outstanding as on 30th June 1985, at the financing institutions, amounted to Rs.8,667 crores.

(Source : Reports on Currency and Finance for various years)

22.27 It will be observed from the foregoing paragraphs that the projections were made by NCA, in respect of short-term credit requirements for crop production and the medium and long term credit requirements for land development and minor irrigation, on per hectare basis, for the broad categories of such areas, as irrigated, unirrigated, etc., on all India basis. Further, in respect of the short-term and the medium and long term credit requirements for livestock, the credit requirements were worked out on per unit basis, on all India level. Thus the estimates were made by NCA at macro level, based on the same unit cost for a particular type of activity, for the whole of India, without taking into account the regional variation in costs. It will be observed from the succeeding paragraphs that we have, in this study, estimated the future credit requirements at first at micro level and thereafter aggregated these requirements both at state and national level.

Targets of Agricultural Credit for Sixth Five Year Plan

22.28 Sixth Five Year Plan targets for institutional finance for agriculture and allied activities and the achievements are indicated in table 13.

Table 13
Targets of Agricultural Credit for VI Plan and Achievements
(Rs. crores)

Nature of credit	Targets-level to be reached in the year 1984-85	Achievements	
		Loans issued during the year 1984-85	Outstanding as on 30-6-1985
Short-term	4,000.0	3,489.9	5,006.2
Medium and long term loans	1,415.0	2,435.5	8,667.0
Total	5,415.0	5,925.4	13,673.2

(Source : Sixth Five Year Plan document - Table 9.2 at page 110 and Report on Currency and Finance 1986-87 - Table VII - 41, page 216)

It will be observed that the short term loans issued during the terminal year, i.e., 1984-85, fell short of the target by about Rs.500 crores. However, the outstanding as on 30.6.1985 exceeded the level of short term loans to be reached in the year 1984-85 by about Rs.1000 crores. In respect of the medium and long term loans, the amount of loans issued during the terminal year, i.e.1984-85, exceeded the target for that year by about Rs.1,000 crores.

Targets of Agricultural Credit for Seventh Five Year Plan

22.29 The targets of Seventh Five Year Plan for institutional finance for agriculture are indicated in table 14.

Table 14
Targets of Agricultural Credit for VII Plan

Nature of credit	(Rs. crores)
	Target - level to be reached by the year 1989 - 90
Short-term loans	8,040
Medium and long term loans	4,530
	<u>12,570</u>

(Source : Seventh Five Year Plan Document - Table 1.12, Page 18 of Volume II)

Growth of Direct Agricultural Credit

22.30 The compound rate of growth of direct agricultural credit by institutional agencies, over the period of 11 years, viz. 1974-75 to 1984-85, has been worked out by the consultants for Study I. This rate of growth for a fairly long period would take care of the fluctuations occurring in the in between years. The compound rate of growth of direct agricultural credit by co-operative institutions and commercial banks for the period 1974-75 to 1984-85 is indicated in table 15.

Table 15

Growth of Direct Agricultural Credit During the Period 1974-75 to 1984-85

	<u>Compound rate of growth - per cent per annum</u>	
A. <u>Short-term credit</u>		
Primary Agricultural Credit Societies (PACSS)		11.84
Scheduled Commercial Banks (CBs)		19.63
Total		14.17
B. <u>Medium and long-term credit</u>		
Primary Agricultural Credit Societies (PACSS)		26.43
Land Development Banks (LDBs)		9.45
Scheduled Commercial Banks		21.75
Total		20.41
C. <u>Total Direct Agricultural Credit</u>		
	<u>Loans issued</u>	<u>Loans outstanding</u>
PACSS, LDBs and CBs	16.28	16.53
Total		

22.31 The overall rates of growth for loans issued as well as the outstandings are more or less the same i.e. 16.28 per cent and 16.53 per cent, respectively. The shares of cooperative institutions and commercial banks in credit dispensation have been changing over a period of time. There has been a consistent increase in the share of commercial banking system, both in the short-term and the medium and long-term credit, in the flow (i.e. loans issued) as well as in the stock (i.e. outstandings). The changing shares of the credit institutions in the flow and the stock for the years 1974-75, 1980-81 and 1984-85 are indicated in table 16.

Table 16
Share of Credit Institutions in the Flow and the Stock of Credit
(Percentage)

Category	1974-75		1980-81		1984-85	
	Co.op.	Comm/ RRBs	Co.op.	Comm/ RRBs	Co.op.	Comm/ RRBs
Short-term loans	83.69 (78.61)	16.31 (21.39)	68.70 (60.00)	31.30 (40.00)	64.15 (56.65)	35.85 (43.35)
Medium and long-term loans	69.27 (79.80)	30.73 (20.20)	45.60 (57.42)	54.40 (42.58)	29.68 (40.74)	70.32 (59.26)

(Figures in brackets relate to share in stock, i.e. outstanding)

22.32 It will be observed from the foregoing paragraphs that in respect of the short-term loans, the growth rate during the period 1974-75 to 1984-85 was higher in respect of scheduled commercial banks as compared to PACSs, mainly because of the low base of the former in 1974-75. Similarly, in the case of medium and long term loans, the growth rate of term loans by the PACSs was higher than that of commercial banks for the same period, mainly due to the lower base of term loans advanced by the PACSs. In the case of LDBs the growth rate of term loans stood low, owing to the high level of overdues and the consequent constraint in disbursement of fresh loans.

Financial Requirements and the Demand for Credit - Projections upto 2000 AD

22.33 To begin with, we distinguish clearly the total requirements of agricultural credit from the demand for agricultural credit. The former is an all-

pervasive concept indicating what will be the credit needs if all farmers obtained from the sources of credit all that is needed for full agricultural operations according to prevailing norms. Credit requirements thus obtained are a blown-up projection and indicate the maximum possible credit needs that are conceivable. Effective credit demand, on the other hand, is what the agriculturists may actually wish to borrow from the institutional and non-institutional sources after taking into account what they would not borrow, considering their own resources and various constraints on demand. Credit demand then is a much more limited and more realistic concept than the credit requirements.

22.34 The future demand for agricultural credit will depend to a large extent on the agricultural development. This will among other things, involve estimating the growth of agriculture in its widest sense in the different parts of the country, keeping in view, among others, the regional variations, technological developments in agriculture and government's strategies and specific programmes for agricultural development in different regions of the country. Recognising that credit absorption capacity varies from area to area, we have taken this factor into account while estimating credit requirements of different states. The areas with poor credit absorption capacity are generally those where infrastructural facilities such as all weather roads, communication facilities, micro-watershed development, irrigation, flood control, drainage, water management, power extension services, agricultural inputs supply, processing, storage and marketing, are not well developed. The financial requirements for agricultural activities, therefore, need to be based on the projected growth of agriculture. An account will also have to be taken of the own resources of the farmer, the credit likely to be obtained from non-institutional agencies as well as the efforts for progressive institutionalisation of agricultural credit.

22.35 In projections of rural credit needs, several caveats must be kept clearly in mind. First and most important, rural development is a dynamic process in which technological change and shifting demand structures are key elements. While for each of these, the past experience provides a rough base for estimating the future, it is not closely predictable. In particular, both new technology and shifting demand will have very different effects depending on the interaction of the specifics of technology and the demand changes as they interact with the widely varying agro-ecological background and with socio-economic forces. Speci-

fically a new technology or new demand will cause one area to leap ahead today and quite another tomorrow. Thus, while our projections give a broad indication of the large demands to be placed on the rural credit system, they cannot be taken to indicate the precise level of that demand in individual regions.

22.36 Secondly, the very technological changes that stimulate and expand the cereals sector provide the basis for accelerated growth in the other elements of rural demand and thus create new credit extension opportunities. As credit use expands production of the basic commodities of a region, the resultant higher incomes expand demand for livestock and horticultural commodities which in turn will require additional financing. Thus, within a region the expansion of one sector will stimulate growth in others and in particular offer opportunity for the labour-intensive activities which are most helpful in poverty alleviation. It should be clear that while agriculture continues to be so very large in the Indian economy, it must play a major stimulative role with respect to other sectors. A very high proportion of the growth in employment in India must come in the non-agricultural sub-sectors of the rural sector. These opportunities require a linking of credit with a whole range of new opportunities.

22.37 Thirdly, it should be made clear that the tremendous growth in livestock and dairy production will require substantial increase in cereals production as a source of concentrate feeds. Concentrate feed use is highly elastic with respect to the growth rate in the livestock sector. We are already beginning to see this take effect in India. There must be rapid growth in the cereals sector to allow that. As cultivable land is running out of supply, this additional cereal production both for people and animals would have to come out of the increased efficiency, that is increased productivity per acre in the cereals sector. And if this happens, additional acreage could become available for use in the newly growing sub-sectors of the agricultural economy with high value commodity and labour-intensive operations generating employment.

22.38 Our projections of the demand for credit can of course be affected, among other things, by different degrees of participation in the credit demand system by the marginal, the small, the middle and the large farmers. The participation of the marginal and the small farmers category in credit is known from

various sources of data, and amounted to 50.2 per cent of the short-term agricultural loans outstanding as on 30 June 1985, though they held only about 27.5 per cent of the total area of the operational holdings.* The data of borrowings by the middle farmers and the large farmers are not available separately. We, therefore, do not have full awareness of participation of these categories of farmers in credit.

22.39 While estimating the projected demand for credit for the years 1989-90, 1994-95 and 1999-2000, we have estimated the balance outstanding (i.e. stock) of advances as at the end of the year and not the amount of loans expected to be issued (i.e. flow) during the year. This procedure has been adopted to enable easy comparison of the demand for credit with the resources that will be available with banks for financing agriculture and allied activities. The resources that will be available for financing agriculture and allied activities have been worked out as a percentage of the estimated total outstanding advances (i.e. stock). Hence for purposes of comparison, the estimates of demand for credit and the supply of credit have to be made in terms of outstandings.

22.40 The demand for credit for short-term requirements from institutional sources is essentially for

- i) crop production
- ii) livestock production
- iii) fisheries and
- iv) input distribution

Similarly, the demand for medium and long-term credit will mainly consist of credit for crop and livestock production, including that for horticulture and plantation, land development, irrigation, implements and machinery. Another major segment of production for which medium and long-term credit will be required is in respect of fisheries and fishery development works. We have estimated the requirements of credit for short-term and for medium and long-term. The projections so made and the basis and assumptions thereof are set out in paragraphs below.

*Source : Report on Currency and Finance 1986-87, published by Reserve Bank of India.

Short-term Credit for Crop Production

a) The Basic Assumption

22.41 The basic assumption made in respect of the estimation of short-term credit requirements for crop production, is that there is a relationship between the value of output of a crop and the cost of cultivation for production of that crop. The relationship between the value of output of a crop and the cost involved for its production, varies from crop to crop, and for the same crop it varies from season to season, from state to state and within the same state from area to area, depending on the agro-climatic conditions. The relationship between the value of output of a crop and the cost of its production varies according to the technology and practices for cultivation adopted. The input output relationship in those areas which have experienced rapid technological development, is likely to rise as they are reaching the production plateau. However, large areas of the eastern and the north-eastern regions and some other parts of the country will be taking up more and more to the improved methods of production, and these areas will be experiencing more favourable output input relationship. Considering these developments, we have used the input output relationship worked out by the consultants for the purpose, on all India level, and this relationship is assumed to remain the same for the next 10 to 15 years.

b) Financial Requirement - The Model used

22.42 The model adopted for our estimate is based on the above assumptions. The production cost itself has two major components viz. the labour cost and the cost of materials. Under labour cost, the man and woman days required are worked out separately as certain agricultural operations are done by men alone and certain agricultural operations are done by women alone. Further, the daily wages paid to a man and a woman are different. The labour cost for each crop, for each season, on hectare basis, for a particular area, is worked out on the basis of man/woman days required for each type of agricultural operation like preparatory tillage, preparation of land for sowing, where necessary, sowing, application of fertilisers, mulching, weeding, irrigation, application of pesticides, harvesting, threshing, etc. These man/woman days are converted to cash equivalent (wherever there is opportunity cost of labour), based on the normal daily wages for man/woman agricultural labourer. This labour cost, together with the cost per hectare for materials such as seeds, fertilisers and pesticides,

and the cost of electricity/diesel for irrigation, hire charges for bullocks/tractors for tillage, etc., will constitute the total cost for the agricultural operations, per hectare, for producing the output.

22.43 It is observed that in the model used, the total cost of production includes labour cost, i.e. the cost of hired labour and the imputed value of family labour, wherever there is opportunity cost for labour, and the cost of materials used for the production of the crop. This total expenditure for production, is deemed as the short-term financial requirement for raising the particular crop, per hectare, for that season, for that area.

c) **The Notations used in the Model**

22.44 Before attempting the projection of short-term financial requirements for crop production, it is necessary to spell out, at the outset, the notations used in the model so that the model itself is clearly understood. Since there are regional variations in costs, the cash and kind expenditure, with and without the imputed value of family labour, for each crop for each state and for all states in India, have been arrived at. These figures, have been arrived at, using the following notations. The notations contain the following abbreviations :

- Y = the value of output
- i = crop
- j = state
- t = period/year
- y = quantity output per hectare
- p = farm harvest price
- v = the value of output per hectare
- V = the value of output of the crop
- c1 = cash and kind expenditure per hectare
- c2 = C1 + imputed value of family labour for all crops

- i) Y_{ijt} denotes the value of output for the crop i in the state j and for the period t .
- ii) y_{ijt} denotes quantity of output per hectare of crop i in the state j for the period t .
- iii) p_{ijt} denotes farm harvest price of crop i in the state j for the period t .
- iv) v_{ijt} denotes the value of output per hectare of the crop i in the state j for the year t . This is obtained by multiplying y_{ijt} by p_{ijt} .
- v) V_{ijt} denotes the value of output of the crop i in the state j for the year t .
- vi) c_{ijt} denotes cash and kind expenditure per hectare of crop i in the state j for the year t . This includes purchased items such as seeds, fertilizers, insecticides, electricity, diesel oil and others, $c2_{ijt}$ denotes c_{ijt} plus the imputed value of family labour.
- vii) K_{ijt} is the ratio of c_{ijt} to v_{ijt} and $K2_{ijt}$ is the ratio of $c2_{ijt}$ and v_{ijt} .
- viii) C_{ijt} denotes the cash and kind expenditure for crop i in the state j for year t . This is obtained by multiplying Y_{ijt} by K_{ijt} , and $C2_{ijt}$ denotes C_{ijt} plus the imputed value of family labour.
- ix) $\sum Y_{ijt}$ denotes the value of all crops in the state j for the year t .
- x) $\sum Y_{jt}$ denotes the value of all crops for all states in India for the year t .
- xi) $\sum C_{ijt}$ denotes the cash and kind expenditure for all crops in the state j for the year t .
- xii) $\sum C2_{ijt}$ denotes the cash and kind expenditure plus the imputed value of family labour for all crops in the state j for the year t .
- xiii) $\sum C_{1jt}$ denotes cash and kind expenditure for crop production for all the states in the country for the year t and called $C1$.
- xiv) $\sum C2_{jt}$ denotes cash and kind expenditure plus the imputed value of family labour for crop production for all the states in the country for the year t and called $C2$.

22.45 After working out the financial requirements of the two types, i.e. $C1$ and $C2$, they are broken down according to the size of holdings in proportion to the area held by them.

- (a) L_s denotes proportion of area operated by small and marginal holdings to total area of all holdings.
- (b) L_m denotes proportion of area operated by medium holdings to total area of all holdings.
- (c) L_l denotes proportion of area operated by large holdings to total area of all holdings.

22.46 In this model the financial requirements are related to the value of output. To determine the values of output for the future, say by 1990, 1995 and 2000 AD, the future growth rates are worked out. The projected growth rates in respect of value of crops are worked out on the basis of the data of value of crops for a period of 15 years from 1970-71. The projections are made at current prices and also at constant prices. We have worked out the projections of the probable growth rates for the periods 1984-85 to 1990, 1991 to 1995 and 1996 to 2000 AD and based on these growth rates and the technological developments for productivity enhancement, the scope for area expansion due to availability of irrigation facilities and other improvements in the states, the demand for the crop products in the country and the export possibilities. The data obtained from the sample survey of 1920 respondents, carried out by our consultants, have also been taken into account while forming our judgement. The survey results give an idea of the level of use of technology, the crop yields, the fertiliser use and the extension work being done in various regions of the country. Detailed discussions were also held with research personnel and the officials of the agricultural departments of various states.

22.47 The projections in respect of the compound growth rate and the value of output of each major crop, are based on 1970-71 prices. While making these projections, the compound growth rate is worked out in respect of each major crop, separately for the major producing states. Further, the projections on All India basis have also been indicated in respect of each crop. The main crops for which separate projections are made, are rice, wheat, other cereals, gram, other pulses, groundnut, other oilseeds, cotton, sugarcane and potato. The details are given in tables 17 to 26.

Table 17

**Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Rice in Major Producing States :**

RICE

State.	1970 - 71 to 1984 - 85	1986 to 1990	1991 to 1995	1996 to 2000
Andhra Pradesh	3.47	4	5	6
Bihar	- 1.56	1	2	3
Karnataka	0.88	1.5	2.5	3.5
Madhya Pradesh	0.95	1	2	3
Orissa	1.38	1.5	2.5	3.5
Punjab	15.56	15	12	10
Tamil Nadu	3.13	3	4	5
Uttar Pradesh	2.94	3	4	5
West Bengal	0.24	2	3	4
All India	2.33	2.5	4	5

Table 18
Estimated Compound Growth Rates of Value of Output
(at 1970-71 price) of Wheat in Major Producing States :

WHEAT

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000AD
Gujarat	7.84	6	8	10
Haryana	7.33	5.5	6	6.5
Madhya Pradesh	4.70	2	3	4
Punjab	5.88	5	6	6
Rajasthan	6.91	6	7	8
Uttar Pradesh	1.75	5.5	6	6.5
All India	5.15	5	6	6.5

Table 19
Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Other Cereals :

OTHER CEREALS

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000AD
Andhra Pradesh	0.76	1.5	2	2.5
Madhya Pradesh	-	1.5	2	2.5
Maharashtra	8.76	8	9	10
Gujarat	1.91	1.5	2	2.5
Rajasthan	3.59	- 2	- 1	- 0.5
Uttar Pradesh	1.17	- 3.5	- 3	- 2.5
All India	1.86	1.5	2	3

Table 20

**Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Gram in Major Producing States :**

GRAM

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000AD
Haryana	- 5.06	- 5.00	- 4.00	- 3.00
Madhya Pradesh	2.89	2.00	3.00	4.00
Rajasthan	1.81	2.00	3.00	4.00
Uttar Pradesh	- 1.95	- 2.00	- 1.50	- 1.00
All India	- 0.34	2.00	3.00	4.00

Table 21

**Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Other Pulses in Major Producing States :**

OTHER PULSES

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000AD
Andhra Pradesh	3.10	3	4	5
Bihar	1.61	1.5	2	3
Gujarat	13.01	8	8	6
Madhya Pradesh	NA	2	3	4
Maharashtra	- 2.06	- 1	1	1.5
Orissa	1.51	2	3	4
Rajasthan	NA	2	3	4
Uttar Pradesh	NA	2	3	4
All India	2.00	2	3	4

Table 22

Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Groundnut in Major Producing States :

GROUNDNUT

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000AD
Andhra Pradesh	- 0.37	1.5	2.5	3
Gujarat	3.36	5	6	7
Karnataka	- 0.04	1	1.5	2
Maharashtra	2.38	2.5	4	5
Orissa	10.34	10	8	6
Tamil Nadu	- 0.91	1	1.5	2
All India	0.53	2.5	3.5	4.5

Table 23

Estimated Compound Growth Rates of Value of Output
(at 1970-71 price) of Other Oil Seeds in Major Producing States :

OTHER OIL SEEDS

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000AD
Andhra Pradesh	3.03	3	4	5
Gujarat	14.35	10	8	6
Haryana	13.75	10	8	6
Karnataka	0.25	1.5	2.5	3.5
Madhya Pradesh	6.64	6	7	8
Maharashtra	18.58	10	8	6
Orissa	8.56	8	6	5
Rajasthan	6.48	6	5	4
Tamil Nadu	- 5.80	- 2	1	1.5
All India	2.73	4	5	6

Table 24

**Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Cotton in Major Producing States :**

COTTON

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000
Andhra Pradesh	NA	2.5	3.5	4.5
Gujarat	- 0.49	2	2.5	3.5
Haryana	8.72	5	6	7
Karnataka	NA	6	7	8
Maharashtra	3.28	3	4	5
Punjab	1.93	5	6	7
Rajasthan	5.01	8	9	10
Tamil Nadu	1.71	3	4	5
All India	2.42	4	5	6

Table 25

**Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Sugarcane in Major Producing States :**

SUGARCANE

State	1968-69 to 1980-81 *	1986 to 1990	1991 to 1995	1996 to 2000AD
Andhra Pradesh	0.01	1	1.5	2
Karnataka	3.25	3	4	5
Maharashtra	6.01	6	5	4
Tamil Nadu	4.40	4.5	5	5.5
Uttar Pradesh	1.83	2	3	4
All India	2.40	3	3.5	4

* Growth rate pertains to physical production.

Table 26

Estimated Compound Growth Rates of Value of Output
(at 1970 - 71 price) of Potato in Major Producing States

POTATO

State	1970-71 to 1984-85	1986 to 1990	1991 to 1995	1996 to 2000AD
Assam	7.8	3	5	7
Bihar	- 1.17	1	1.5	2
Himachal Pradesh	- 1.84	1	1.5	2
Maharashtra	- 1.51	1	1.5	2
Uttar Pradesh	13.36	7.5	9	10
West Bengal	5.37	3.5	4.5	6

22.48 The estimated compound growth rates of physical output, value of physical output at constant price (1970-71) and current prices of various crops in major producing states in different agro-climatic zones in India are given in table 27.

Table 27

Estimated Compound Growth Rate of Physical Output, Value of Physical Output at Constant Price (1970-71)
and Current Prices of Various Crops in Major Producing States in Agro-Climatic Zones in India

Zone No.	State		Rice	Wheat	Coarse Cereals	Gram	Other Pulses	Ground-nut	Other Oil seeds	Sugar-cane	Cotton	Potato	Other Crops	All Crops	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	15	
I	Jammu & Kashmir	p	-	-	-	-	-	-	-	-	-	-	-	-	
		r	-	-	-	-	-	-	-	-	-	-	-	0.97	3.79
		n	-	-	-	-	-	-	-	-	-	-	-	9.55	11.81
	Himachal Pradesh	p	-	-	-	-	-	-	-	-	-	-	-	-	-
		r	-	-	-	-	-	-	-	-	-	-	- 1.84	0.39	0.80
		n	-	-	-	-	-	-	-	-	-	-	2.72	5.17	7.42
II	West Bengal	p	0.87	-	-	-	-	-	-	-	-	-	-	-	-
		r	0.24	-	-	-	-	-	-	-	-	-	5.37	1.96	1.96
		n	6.85	-	-	-	-	-	-	-	-	-	12.98	11.24	8.43
	Assam	p	-	-	-	-	-	-	-	-	-	-	-	-	-
		r	-	-	-	-	-	-	-	-	-	-	7.80	0.86	1.12
		n	-	-	-	-	-	-	-	-	-	-	14.63	10.42	9.22
III	Other States [®]														
IV	Punjab	p	18.09	4.86*	-	-	-	-	-	-	4.40*	-	-	-	
		r	15.56	5.86	-	-	-	-	-	-	1.93	-	-	5.48	
		n	24.35	12.14	-	-	-	-	-	-	8.31	-	-	12.55	
	Uttar Pradesh	p	3.57	5.53	- 3.67*(c)	-	-	-	-	1.83*	-	-	-	-	
		r	2.94	1.75	1.17	-1.95	-	-	-	-	-	-	13.36	-	1.89
		n	9.68	6.80	5.88	7.67	7.22	-	-	9.32	-	-	19.07	-	8.73

	1	2	3	4	5	6	7	8	9	10	11	12	13	14	15
Bihar	p		0.65	5.20*	-	-	-	-	-	-	-	-	-	-	-
	r		-1.56	3.53	-	-	1.61	-	-	-	-	-	-1.17	-	0.21
	n		5.10	8.27	-	-	9.17	-	-	-	-	-	4.23	-	6.88
V Orissa	p		-0.79	-	-	-	-	-	-	-	-	-	-	-	-
	r		1.38	-	-	-	1.51	10.34	8.58	-	-	-	-	-	3.65
	n		7.72	-	-	-	14.03	20.07	17.92	-	-	-	-	-	11.45
Andhra Pradesh	p		4.12	-	1.13*	-	-	-0.35	-	0.01	-	-	-	-	-
	r		3.47	-	0.76	-	3.10	-0.37	3.03	-2.00	-	-	-	-	2.18
	n		9.59	-	5.87	-	12.04	8.36	11.43	4.92	-	-	-	-	9.59
VI Haryana	p		-	5.50	-	-	-	-	-	-	-	5.06	-	-	-
	r		-	7.33	-	-5.06	-	-	-	-	-	8.72	-	-	5.81
	n		-	13.10	-	4.25	-	-	-	-	-	12.18	-	-	12.21
Rajasthan	p		-	6.36*	-4.19(b)	-	-	-	-	-	-	8.74*	-	-	-
	r		-	6.91	3.59	1.81	-	-	6.48	-	5.01	-	-	-	2.93
	n		-	12.46	6.02	11.58	6.22	-	14.89	-	11.09	-	-	-	9.89
Gujarat	p		-	6.14*	0.96(b)	-	-	4.68*	-	-	-	1.62*	-	-	-
	r		-	7.84	1.91	-	13.01	3.36	-	-	-	-0.49	-	-	3.15
	n		-	12.01	6.84	-	21.75	11.54	-	-	-	5.89	-	-	10.45
VII Madhya Pradesh	p		-0.09	-2.19*	-0.11(a)	-	-	-	-	-	-	-	-	-	-
	r		0.95	4.70	-	2.09	-	-	6.64	-	-	-	-	-	2.47
	n		7.13	10.23	8.29	12.14	8.94	-	15.47	-	-	-	-	-	8.97
Maharashtra	p		-	-	9.26(a)	-	-	0.59	-	6.01*	2.90*	-	-	-	-
	r		-	-	8.76	-	-2.05	2.38	-	-	3.20	-1.51	-	-	5.31
	n		-	-	15.37	-	15.78	11.25	-	11.16	9.70	2.08	-	-	12.93

1	2		4	5	6	7	8	9	10	11	12	13	14	15
VIII	Karnataka	p	0.79	-	-	-	-	0.41	-	3.25*	5.76*	-	-	
		r	0.88	-	-	-	-	-0.04	0.25	-	-8.43	-	-0.90	0.29
		n	6.99	-	-	-	-	8.61	9.66	6.89	5.80	-	8.85	7.89
	Kerala	p	-	-	-	-	-	-	-	-	-	-	-	-
		r	-	-	-	-	-	-	-	-	-	-	-	-4.47
		n	-	-	-	-	-	-	-	-	-	-	-	3.53
	Tamil Nadu	p	0.97	-	-	-	-	0.53	-	4.40*	2.07	-	-	-
		r	3.13	-	-	-	-	-0.91	-5.80	-	1.71	-	1.05	1.52
		n	9.66	-	-	-	-	7.14	2.44	7.53	6.74	-	9.31	8.71
	All India	p	2.19*	5.13*	2.76	-	-	1.08*	-	2.40*	2.93*	-	-	-
		r	2.33	5.15	1.86	0.34	2.00	0.53	2.73	2.66	2.24	6.51	1.20	2.33
		n	9.00	10.50	6.98	8.19	10.69	9.04	11.63	9.29	8.74	12.38	10.28	9.60

(c) Estimates of Zone III (viz. Sikkim, Arunachal Pradesh, Tripura, Nagaland, Manipur, Mizoram, Meghalaya and Andaman Nicobar) are not worked out on account of non-availability of requisite data.

<u>Zone</u>	<u>Description</u>
I	- Humid Western and Himalayan Region
II	- Humid Bengal and Assam Basin
III	- Humid Eastern, Himalayan Region and Bay Islands
IV	- Sub-humid Sutlej and Ganga Alluvial Plains
V	- Sub-humid to humid Eastern and South/Eastern Uplands
VI	- Arid Western Plains
VII	- Semi-arid Lava Plateaus and Central Highlands
VIII	- Humid to semi-arid Western Ghats and Karnataka Plateaus

- p** - Growth rate of physical output (1968-69 to 1980-81)
- r** - Growth rates at constant price of 1970 - 71 (1970 - 71 to 1984 - 85)
- n** - Growth rates at current price of 1984-85 (1970-71 to 1984-85)
- a** - For jowar
- b** - For bajra
- c** - For maize
- *** - Significant at 5 per cent level

Source : S. D. Sawant, Investigation of the hypothesis of Declination of Indian Agriculture.

22.49 Since the growth rates of 'other crops' are not readily available separately for each crop, it has been assumed that the approximate growth rate of these crops, for different periods, will be the average of the growth rates of the main crops for which separate projections have been made.

22.50 The value of output of various crops for various years is converted at the base year prices i.e. at 1984-85 prices. The projections worked out on the above basis in respect of crop-wise financial requirements at All India level for the years 1989-90, 1994-95 and 1999-2000 AD are given in table 28.

Table 28

Crop-wise Financial Requirement at All India Level for Different Years

		(Rs. crores)							
Sr. No.		1984-85		1989-90		1994-95		1999-2000	
		C1	C2	C1	C2	C1	C2	C1	C2
1	Rice	7778 (27)	9236 (26)	8000 (25)	10450 (25)	10706 (26)	12714 (26)	13664 (28)	16226 (27)
2.	Wheat	3325 (11)	3903 (11)	4243 (12)	4987 (12)	5679 (14)	6666 (13)	7780 (16)	9134 (15)
3	Other Cereals	2015 (7)	2671 (8)	2171 (6)	2878 (7)	2397 (6)	3177 (6)	2779 (6)	3683 (6)
4	Gram	802 (3)	1069 (3)	885 (3)	1181 (3)	1026 (3)	1369 (3)	1249 (3)	1665 (3)
5	Other Pulses	1114 (4)	1540 (4)	1230 (4)	1709 (4)	1425 (4)	1982 (4)	1734 (4)	2411 (4)
6	Sugarcane	1766 (6)	1972 (6)	2048 (6)	2286 (5)	2432 (6)	2715 (5)	2959 (6)	3303 (6)
7	Groundnut	1827 (6)	2112 (6)	2067 (6)	2390 (6)	2455 (6)	2839 (6)	3059 (6)	3537 (6)
8	Other Oil Seeds	1466 (5)	1941 (5)	1845 (5)	2442 (6)	2434 (6)	3221 (7)	3257 (7)	4311 (7)
9	Cotton	1220 (4)	1440 (4)	1484 (4)	1752 (4)	1895 (5)	2236 (5)	2535 (5)	2992 (5)
10.	Jute & Mesta	318 (1)	461 (1)	369 (1)	535 (1)	438 (1)	635 (1)	533 (1)	772 (1)
	Potato	421 (1)	488 (1)	512 (2)	594 (1)	653 (2)	757 (2)	874 (2)	1014 (2)
	Other Crops	7412 (25)	9164 (25)	8503 (26)	10543 (26)	9027 (21)	11272 (22)	8933 (16)	11276 (18)

13 All Crops	29464 (100)	36011 (100)	34156 (100)	41747 (100)	40567 (100)	49582 (100)	49356 (100)	60324 (100)
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C1 - Cash and Kind Expenditure

C2 - Cash and Kind Expenditure plus imputed value of family labour.

Figures in the brackets are percentage to the total.

It will be observed from the table that in respect of crop-wise financial requirements for the period 1984-85 to 2000 AD, rice has the highest share (25 - 28 per cent), followed by wheat (11 - 16 per cent) and the lowest share is that of jute and mesta (one per cent). The share of 'other crops' which include plantation and horticulture crops, varies between 17 and 25 per cent of the total financial requirements.

22.51 The details of statewise financial requirements for all crops are given in table 29 :

Table 29
Statewise Financial Requirements for All Crops

State	(Rs. Crores)							
	1984-85		1989-90		1994-95		1999-2000	
	C1	C2	C1	C2	C1	C2	C1	C2
1 Jammu & Kashmir	207 (a)	259 (a)	252 (1)	315 (1)	314 (1)	392 (1)	400 (1)	501 (1)
2 Himachal Pradesh	128 (a)	159 (a)	135 (a)	167 (a)	145 (a)	180 (a)	160 (a)	198 (a)
3 West Bengal	2605 (9)	3270 (9)	2738 (9)	3436 (8)	2950 (3)	3702 (3)	3256 (7)	4087 (7)
4 Assam	799 (3)	1099 (3)	840 (2)	1155 (3)	905 (3)	1244 (3)	999 (2)	1374 (2)
5 Punjab	2424 (8)	2890 (8)	3168 (9)	3778 (9)	4240 (10)	5055 (10)	5309 (11)	6926 (11)
6 Uttar Pradesh	2941 (11)	3802 (11)	3247 (11)	4197 (11)	3674 (9)	4749 (10)	4259 (9)	5505 (9)
7 Bihar	1693 (6)	2023 (6)	1779 (5)	2127 (5)	1917 (5)	2291 (5)	2117 (4)	2529 (4)
8 Orissa	2077 (7)	2529 (7)	2467 (7)	3004 (7)	3002 (7)	3654 (7)	3741 (8)	4554 (7)
9 Andhra Pradesh	2550 (9)	2894 (9)	2816 (8)	3195 (8)	3186 (8)	3615 (7)	3693 (7)	4190 (7)
10 Haryana	1450 (5)	1910 (5)	1941 (6)	2556 (6)	2659 (7)	3502 (7)	3729 (8)	4911 (8)

Sr. No.	State	1984-85		1989-90		1994-95		1999-2000	
		C1	C2	C1	C2	C1	C2	C1	C2
11	Rajasthan	1312 (4)	1869 (5)	1520 (4)	2167 (5)	1806 (4)	2573 (5)	2197 (4)	3131 (5)
12	Gujarat	2043 (7)	2533 (7)	2426 (7)	3009 (7)	2952 (7)	3660 (7)	3768 (8)	4672 (8)
13	Madhya Pradesh	2169 (7)	2712 (8)	2454 (7)	3068 (7)	2845 (7)	3557 (7)	3379 (7)	4224 (7)
14	Maharashtra	2697 (9)	3193 (9)	3442 (10)	4075 (10)	4607 (11)	5453 (11)	6461 (12)	7648 (13)
15	Karnataka	1418 (5)	1666 (5)	1490 (4)	1751 (4)	1605 (4)	1886 (4)	1773 (4)	2083 (3)
16	Kerala	373 (1)	466 (1)	432 (1)	540 (1)	514 (1)	642 (1)	625 (1)	781 (1)
17	Tamil Nadu	2235 (8)	2575 (7)	2408 (7)	2774 (7)	2658 (7)	3063 (6)	3008 (6)	3465 (6)
	Total	29121	35849	33555	41314	39979	49218	49374	60778
	All India	29464 (100)	36011 (100)	34156 (100)	41747 (100)	40567 (100)	49582 (100)	49356 (100)	60324 (100)

C1 - Cash and Kind expenditure

C2 - Cash & Kind expenditure plus imputed value of family labour

Figures in brackets are percentage to the total.

(a) - Less than one per cent

There are some differences between the estimates of cropwise financial requirements at All India level given at table 28 and the statewise financial requirements for all crops given at table 29. This is on account of the fact that the value of output of all crops estimated for different years (1990, 1995 and 2000 AD) are independently worked out on the basis of the growth rates and they are not aggregate of all crops at the state level. Hence C1 and C2 values estimated from the values of output at All India level would not exactly tally with the aggregate value of C1 and C2 at the state levels.

(d) Short-term Credit Needs - Alternatives for Credit Estimation

22.52 We now proceed to work out the credit requirements primarily based on the financial requirements as already estimated by us.

The short-term credit requirements for crop production from institutional agencies are estimated separately according to the different size groups of land holdings and based on four alternatives.

22.53 The proportion of area operated by different size groups of holdings during the years 1970-71, 1976-77 and 1980-81 and the projections made for the year 1989-90 are indicated in table 30.

Table 30
Area Operated by Different Size Groups of Holdings and Projections
(Percentage)

Year	Small and Marginal Farmers		Medium Farmers		Large Farmers	
	No.	Area	No.	Area	No.	Area
1970-71	69.89	20.87	26.21	48.25	3.90	30.88
1976-77	72.64	23.52	24.37	50.24	2.99	26.24
1980-81	74.54	26.27	23.05	50.92	2.41	22.81
1989-90		28.96		52.03		19.01

While it is true that over a period of time there will be an increase in the total area of the land holdings of the small and marginal farmers and the medium farmers, and a decline in the total area of the land holdings of the large farmers, we have assumed the same proportions as estimated for the year 1989-90 for the years 1994-95 and 1999-2000 in view of the difficulties in estimating the respective proportions of the operative holdings for the years 1994-95 and 1999-2000.

22.54 The consultants have considered four alternative assumptions for estimating the short-term credit requirements for crop production.

Alternative I

22.55 Credit is to be made available to farmers on a differentiated basis according to the size of holdings, as indicated below.

- (i) Credit to the full extent of cash and kind expenditure plus the imputed value of family labour (C2ijt) to be incurred for the production of a crop for the small and marginal farmers. This gives a preferential treatment to small and marginal farmers. It would

cover also a part of the consumption credit needed by the small and marginal farmers equivalent of imputed value of family labour.

- (ii) Credit to the full extent of cash and kind expenditure (C1ijt) incurred for the production of a crop, for the medium farmers.
- (iii) Credit to the extent of 50 per cent of cash and kind expenditure (C1ijt) incurred for the production of a crop for the large farmers. This is based on the assumption that large farmers would be able to finance crop production to a considerable extent, from their own savings, without substantial help from the credit institutions.
- (iv) Credit facilities would be available for all crops and the cash and kind component and family labour component per unit of area of a crop would be fixed by the credit institution operating in the area.

Alternative II

- 22.56 (i) Credit for the cash and kind expenditure plus the imputed cost of family labour for production of a crop (C2ijt) in respect of cereals other than rice and wheat, all pulses and oilseeds. The basic assumption is that these crops are mostly grown in dry farming areas which need special attention. Moreover, there is a need for giving special treatment to pulses and oilseeds which are lagging behind in production and productivity.
- (ii) Credit for the cash and kind expenditure only (C1ijt) for production of rice and wheat. These crops have an advantage over other crops of having the technological breakthrough and a substantial portion of area under these crops is irrigated.
 - (iii) Credit to the extent of fifty per cent of the cash and kind expenditure only (C1ijt) for production of cotton, jute and mesta, potato, and other crops including tobacco, fruits and vegetables and plantation crops. These are cash crops. The basic assumption is that

the producers of these crops would have larger savings than other producers and hence they can finance these crops without substantial help from credit institutions.

- (iv) Credit for respective crops would be available on the basis of the cash and kind component and family labour component fixed by the credit agency operating in the area.

Alternative III

22.57 Credit for all farmers on the basis of cash and kind expenditure (C_{ij}t) for production of all crops.

All the three alternatives assume that there would be an overall shortage of credit resources. The short-term credit will have to be rationed to some extent.

Alternative IV

22.58 Credit for all farmers on the basis of cash and kind expenditure plus the imputed value of family labour (C_{2ij}t) for production of all crops. In this alternative, the assumption is that credit would be provided to all farmers, without discrimination, and would cover partly the consumption needs.

22.59 Using the notations discussed earlier, the credit requirement of crop production of a state would be as follows under each of the four alternatives.

Alternative I

$$\text{Credit requirement} = \sum_i C_{2ij}t \times L_s + \sum_i C_{ij}t \times L_m + 0.5 \sum_i C_{ij}t \times \sum_i L_i$$

Alternative II

$$\text{Credit requirement} = \sum_i C_{ij}t \text{ where } i \text{ stands for all cereal crops other than wheat and rice, all pulses and}$$

oilseeds + $\frac{1}{2}$ C1ijt where i stands for rice and wheat + 0.5 $\frac{1}{2}$ C1ijt where i stands for cotton, jute and mesta, potato and other crops.

Alternative III

Credit requirement of a state = $\frac{1}{2}$ C1ijt

Alternative IV

Credit requirement of a state = $\frac{1}{2}$ C2ijt

22.60 The projected credit requirements for the years 1989-90, 1994-95 and 1999-2000, under the alternatives, with details such as the credit requirements by small, medium and large farmers are given in table 31.

It will be observed from the table that the highest estimate of credit requirements is under Alternative IV, followed by Alternative III. The lowest estimate of credit requirements is under Alternative II.

22.61 Among the various alternative assumptions, Alternative IV assumes that credit is to be provided to all farmers for their entire financial requirements, i.e. cash and kind expenditure plus imputed value of family labour, for crop production, without any discrimination among the farmers based on the size of land holdings. We consider this as a mere academic exercise in view of the fact that neither all the farmers would be borrowing nor would all of them borrow to the full extent of the financial requirements and secondly in view of the constraints on resources of the financial institutions. Alternative III differs from Alternative IV only to the extent that in Alternative III, the farmers will not get finance in respect of imputed value of family labour. Alternative III also suffers from the same drawbacks indicated in respect of Alternative IV. Alternative II is quite restrictive in respect of credit. Under this alternative, the small and marginal farmers may have to approach other sources of credit, including money-lenders, for meeting the full financial requirements of crop production. Hence this alternative is also not realistic. Under Alternative I, however, the assumption is that the small and marginal farmers would get the entire financial

Table 31
Credit Requirements According to Different Alternatives

(Rs. crores)

Year	T	S			M			L
<u>ALTERNATIVE I</u>								
1984-85	27,824	9,460	(34.00)	15,003	(53.92)	3,361	(12.08)	
1989-90	33,108	12,090	(36.52)	17,771	(53.68)	3,247	(9.80)	
1994-95	39,322	14,359	(36.52)	21,107	(53.68)	3,856	(9.80)	
1999-2000	47,842	17,470	(36.52)	25,680	(53.68)	4,692	(9.80)	
<u>ALTERNATIVE II</u>								
1984-85	25,783	6,773	(26.27)	13,129	(50.92)	5,881	(22.81)	
1989-90	30,101	8,717	(28.96)	15,662	(52.03)	5,722	(19.01)	
1994-95	36,196	10,482	(28.96)	18,833	(52.03)	6,881	(19.01)	
1999-2000	44,968	13,023	(28.96)	23,397	(52.03)	8,548	(19.01)	
<u>ALTERNATIVE III</u>								
1984-85	29,464	7,740	(26.27)	15,003	(50.92)	6,721	(22.81)	
1989-90	34,156	9,492	(27.79)	18,071	(52.91)	6,593	(19.30)	
1994-95	40,567	11,748	(28.96)	21,107	(52.03)	7,712	(19.01)	
1999-2000	49,356	14,293	(28.96)	25,680	(52.03)	9,383	(19.01)	
<u>ALTERNATIVE IV</u>								
1984-85	36,011	9,460	(26.27)	18,337	(50.92)	8,214	(22.81)	
1989-90	41,747	12,090	(28.96)	21,721	(52.03)	7,936	(19.01)	
1994-95	49,582	14,358	(28.96)	25,798	(52.03)	9,426	(19.01)	
1999-2000	60,324	17,470	(28.96)	31,386	(52.03)	11,468	(19.01)	

Figures in bracket indicate per cent to total of each year.

T = Total S = Small and marginal farms M = Medium farms
L = Large farms.

requirements for raising crops, including the imputed value of family labour. This would cover a part of the consumption credit needed by the small and marginal farmers. The medium farmers will get credit to the full extent of cash and kind expenditure incurred for production of crops. However, the medium farmers would not get credit to cover the imputed value of family labour. The large farmers would get credit to the extent of 50 per cent of cash and kind expenditure incurred for production of crops. Thus; Alternative I gives relatively higher share of the total credit to small and marginal farmers than under any other alternative. Further, Alternative I provides a much lower share to the large farmers as compared to the share under other alternatives. The medium farmers will get slightly better share under Alternative I as compared to the other alternatives. Taking into account the feasibility of the proposal and the need for social justice, Alternative I is considered by the consultants as more acceptable than the rest. However, estimates in all the four alternatives presume that 100 per cent of the farmers would require credit for raising of crops. This presumption, in our view, is not realistic. Further, in Alternative I, which is considered by the consultants as more acceptable than the other alternatives, there is a presumption that the medium farmers would require credit to the full extent of the cash and kind expenditure incurred for production of crops, and that no amount of the financial requirements for raising of crops would be met out of their own savings. This presumption also does not appear to be realistic.

22.62 In view of the limitations in each of the alternatives, we have estimated the demand for credit based on the following assumptions, rather than using any of the four alternatives. However, for working out the demand for credit, we have accepted the financial requirements for raising crops, estimated by the consultants under Alternatives III and IV. The Alternative III relates to the financial cost based on cash and kind expenditure while Alternative IV relates to the financial cost based on cash and kind expenditure plus the imputed value of family labour. At first, we have worked out the demand for credit from all sources, i.e. institutional and non-institutional. For this purpose, we have assumed that the small and marginal farmers will require credit to the full extent of the cash and kind expenditure for crop production and fifty per cent of the imputed value of family labour. The small and marginal farmers may not, generally, have their own resources to meet even a part of the expenditure for raising crops. Further, a portion of the imputed value of family labour, taken into account for estimation of credit requirements, would cover a part of the consumption credit needed by such farmers. In respect of the medium and the large farmers, we have assumed

that 25 per cent and 50 per cent respectively of the cash and kind expenditure for raising crops could be met by them out of their own savings. Hence the demand for credit requirements from the medium and large farmers will amount to 75 per cent and 50 per cent respectively, of the cash and kind expenditure. No credit will be required by such farmers to cover the imputed value of family labour. On the basis of these assumptions, the demand for credit from all sources would work out as indicated in table 32.

Table 32
Demand for Short-term Credit for Crop Production

<u>Category of farmer</u>	(Rs. crores)	
	<u>Demand for short-term credit for crop production from all sources by the year</u>	
	<u>1994-95</u>	<u>1999-2000</u>
<u>Small and marginal farmers</u>		
(a) 100 per cent of the cash and kind expenditure	11,748	14,293
(b) 50 per cent of the imputed value of family labour	1,306	1,589
Sub-total	<u>13,054</u> =====	<u>15,882</u> =====
<u>Medium farmers</u>		
75 per cent of the cash and kind expenditure	15,398	19,260
<u>Large farmers</u>		
50 per cent of the cash and kind expenditure	3,856	4,692
Total	<u>32,808</u> =====	<u>39,834</u> =====

22.63 After estimating the demand for short-term credit for crop production, from all sources, we have estimated the demand for the short-term credit on institutional agencies on the following assumptions. Several medium and large farmers may not approach institutional credit agencies as they are getting finance from non-institutional sources such as friends and relatives. In this connection, it may be stated that a sample study conducted by the Consultants for Study II, revealed that the borrower farmers were also resorting to private sources for meeting their borrowing needs to the extent of 35 to 50 per cent of their production

expenditure. Taking all these aspects into account, we have assumed the percentage of demand for credit that will be called upon to be met by institutional credit agencies as indicated in table 33.

Table 33

**Percentage of Short-term Credit for Crop Production
to be met by Institutional Credit Agencies**

Category of farmers	Percentage of short-term credit for crop production that would be required to be met by institutional credit agencies by the year	
	<u>1994-95</u>	<u>1999-2000</u>
Small and marginal farmers	60	75
Medium farmers	40	50
Large farmers	40	50

On the basis of the above assumptions the demand for credit from institutional agencies has been worked out. The details are given in table 34.

Table 34

**Demand for Short-term Credit for Crop Production
to be met by Institutional Credit Agencies**

(Rs. crores)

Category of farmers	Demand for short-term credit for crop production to be met by institutional credit agencies by the year (at 1984-85 prices)	
	<u>1994-95</u>	<u>1999-2000</u>
Small farmers	7,832	11,912
Medium farmers	6,359	9,630
Large farmers	1,542	2,346
	----- 15,733 =====	----- 23,888 =====

22.64 The amounts of demand for short-term credit for crop production, thus estimated for the years 1994-95 and 1999-2000 are the total requirements of short-term credit for those years and are not necessarily the 'flow' of short term credit during those years. The actual flow of credit for those years will depend on, among other things, the overdues, at the end of the previous year/

season. The short-term loans are normally repayable within a year. Since only the non defaulters are issued fresh loans, the amount of loans issued (i.e. flow) during a year and the balance outstanding at the end of the year (i.e. stock) may be different. In the short-term credit requirements projected by us, the total short-term credit requirements for a year, irrespective of defaults by some borrowers are indicated under the demand for credit. The demand will, therefore, include not only the actual disbursements (i.e. flow) during the year, but also the overdues. Hence the estimates of demand for credit indicated in table 34 are the outstandings, as at the close of the year, and not the disbursements during that year.

22.65 It will be observed from the projection of demand for short-term loans for crop production from institutional agencies, that the short-term loans outstanding will increase from Rs.5,006 crores as at the end of June 1985 to Rs.15,733 crores as at the end of June 1995. Thus, the short-term loans for crop production are expected to increase at a compound rate of 12.1 per cent per annum during the above period. At this growth rate, the short-term loans for crop production outstanding as at the end of June 1990 will amount to Rs.8,861 crores.

22.66 During the period 1974-75 to 1984-85, the short-term loans for crop production increased at a compound rate of 14.2 per cent per annum. The compound rate of growth of the short term loans may decline to 12.1 per cent per annum during the period 1985-86 to 1994-95. This does not mean any decline in the actual amount of loans to be issued each year during this period, since the decline in the growth rate is on account of a higher base reached in 1984-85. Having reached a still higher base by 1994-95, the compound rate of growth is likely to decline to around 8.7 per cent per annum during the period 1995-96 to 1999-2000. It may however be stated that though the compound rate of growth is estimated to decline during the period 1995-96 to 1999-2000 as compared to the period 1984-85 to 1994-95, the average increase per annum in the quantum of the short-term credit for crop production, will be higher by about Rs.558 crores during the period 1994-95 to 1999-2000 at Rs.1,631 crores, compared to Rs.1,072.70 crores during the period 1985-86 to 1994-95.

Short-term Credit for Livestock Production

22.67 For estimating the short-term credit requirements for livestock production, we have followed the same assumption as was adopted for estimating the

credit requirements of crop production, i.e. there is a relationship between the value of output and the cost involved for its production. The data of the value of output of the livestock sector, both at current and constant prices, have been collected for the period 1970-71 to 1984-85. The data included item-wise break-up into milk and milk products and other livestock products. The milk and milk products formed 68 per cent of the total value of livestock production in 1970-71 and remained at the level of 66 per cent in 1984-85. The details are given in table 35. The growth rates of value of output for different periods viz 1970-71 to 1978-79, 1978-79 to 1984-85 and 1970-71 to 1984-85 at current and constant prices are indicated in table 36.

Table 35
Value of Output of Livestock

Items	(Rs. crores)					
	1970-71		1978-79		1984-85	
	Current	Constant	Current	Constant	Current	Constant
Milk & Milk Products	2167 (68)	2167 (68)	5281 (67)	2847 (68)	10538 (64)	3345 (66)
Meat & Meat Products	294 (9)	294 (9)	753 (10)	355 (9)	1742 (10)	466 (9)
Hides & Skins	73 (2)	73 (2)	163 (2)	78 (2)	307 (2)	93 (2)
Eggs & Poultry	212 (7)	212 (7)	620 (8)	339 (8)	1467 (9)	512 (9)
Wool & Hair	20 (1)	20 (1)	52 (1)	23 (1)	95 (1)	31 (1)
Dung	320 (10)	320 (10)	728 (9)	391 (9)	1539 (9)	409 (8)
Others	111 (3)	111 (3)	267 (3)	144 (3)	816 (5)	238 (5)
Total	3197 (100)	3197 (100)	7864 (100)	4177 (100)	16504 (100)	5094 (100)

Constant prices = 1970-71 prices.

Figures in brackets indicate the percentage to the value of output of the livestock sector.

Table 36
Compound Growth Rates of Output of Livestock

Item	(in percentage)					
	Current Price			Constant Price		
	1970-71	1978-79	1970-71	1970-71	1978-79	1970-71
	to	to	to	to	to	to
	1978-79	1984-85	1984-85	1978-79	1984-85	1984-85
Milk & Milk Products	11.78	10.31	11.12	3.47	2.33	2.94
Meat & Meat Products	12.47	12.73	12.59	2.38	3.96	3.12
Hides & Skins	10.56	9.47	10.05	0.83	2.54	1.63
Eggs & Poultry	14.36	13.09	13.76	6.04	6.07	6.05
Wool & Hair	12.69	8.99	10.95	1.76	4.36	2.96
Dung	10.82	11.29	11.04	2.54	0.65	1.65
Others	11.54	17.39	14.23	3.31	7.44	5.22
Total	11.91	11.17	11.56	3.40	2.88	3.15

Based on these growth rates we have assumed the growth rates of the value of output of the total livestock production for the period 1986 to 1990, 1991 to 1995 and 1996 to 2000 AD at 4, 5 and 6 per cent per annum respectively.

22.68 On the basis of the sample survey (in 32 districts) the proportion of purchased inputs to the value of livestock production has been arrived at by the consultants for different types of farms viz. large, medium, small and marginal. The details are given in table 37.

Table 37
Proportion of Purchased Inputs to the Value of Livestock Production

Type of farm	Production per farm (Rs.)	Expenditure per farm for inputs (Rs.)	Proportion of Expenditure to Production
Large	10,939	3,993	0.36
Medium	6,862	3,063	0.45
Small	5,746	2,147	0.37
Marginal	5,116	1,660	0.32
Average	7,015	2,651	0.38

The average proportion of the expenditure on purchased inputs to the total value of production amounted to 0.38. It is presumed that in future the proportion of purchased inputs to the value of livestock production would increase from 0.38 to 0.40, mainly because of the expected increase in expenditure on concentrates.

22.69 After working out the value of output and the financial requirements of livestock for future i.e. for the years 1989-90, 1994-95 and 1999-2000, the credit requirements have been worked out by the consultants on the assumption that 30 per cent of the financial requirements will be necessary as credit requirements. Apart from milk sold through Government/Co-operative dairy schemes, a substantial quantity of milk is sold through private sector on credit basis. The milk producers have to incur cash expenditure on concentrates etc. In view of these our consultants have considered that the credit requirements be assessed at 30 per cent of the financial requirements. The projections made by the consultants in respect of the financial requirements, short-term credit requirements etc., for livestock are indicated in table 38.

Table 38

Credit Requirements of Livestock Estimated by the Consultants

	(Rs. crores)			
	1984-85	1989-90	1994-95	1999-2000
Value of Output	16,504	19,307	23,468	29,628
Proportion of Cash and Kind Expenditure to the Value of output	0.38	0.40	0.40	0.40
Financial Requirements	6,106	7,723	9,387	11,851
Credit Requirements	1,832	2,317	2,816	3,555

Note : Prices at 1984 - 85

22.70 The assumption made by the consultants that the short-term credit requirements will amount to 30 per cent of the financial requirements, seems in our view to be on high side. At present short-term credit is normally not provided for meeting the recurring expenditure for livestock. About 80 per cent of the value of production from livestock is from milch cattle and poultry. In respect of poultry, the cost of feed for the first batch of one day old chicks till they become layers, (i.e. till they start laying eggs), is capitalised and term loan is given, including the above cost of feed. A farmer will be getting income from sale of eggs, atleast once a fortnight. In respect of milch cattle also the farmer gets income from sale of milk atleast once a fortnight. Further, in respect of very poor farmers, the feed cost for one month could be capitalised and included in the investment cost. The minimum unit of milch cattle financed is expected to be two animals, the second animal being financed 6 to 8 months from the date of purchase of the first animal, so that atleast one animal will be in lactation at any time. However, in practice, the requirement of minimum unit is not observed in large number of cases.

22.71 Though at present no short-term credit is normally given for meeting the recurring expenditure of milch cattle or poultry, it is desirable to provide some short term credit, not exceeding the cost of feed for one month, so that the farmers' liquidity position is not affected adversely immediately on investment. Feed cost for one month will amount to 8.33 per cent of the cost of feed per year. The milch cattle and poultry account for about 80 per cent of the value of production under livestock. In respect of the other animals under livestock viz. sheep, goats, pigs, etc., it may be desirable to give a slightly larger proportion of the cost of purchased feed as short-term credit. Taking the above aspects into account, the short-term credit for livestock is considered appropriate at 10 per cent of the financial requirements (i.e. cost of purchased inputs) as against 30 per cent of the financial requirements presumed by the consultants. We, therefore, estimate the short-term credit requirements for livestock for the years 1989-90, 1994-95 and 1999-2000 at Rs.772 crores, Rs.939 crores and Rs.1,185 crores respectively. As in the case of the short-term loans for crop production, the credit requirements estimated for the above years are the outstandings as at the end of the year and not the flow during that year.

Short-term Credit Requirements for Fisheries

22.72 The short-term credit requirements for fisheries, per annum, are estimated on an approximate basis, at five per cent of the total fixed capital investments for fisheries. The projections so estimated for the years 1989-90, 1994-95 and 1999-2000 are indicated in table 39.

Table 39
Short-term Credit Requirements for Fisheries

Particulars	(Rs. crores)		
	1989-90	1994-95	1999-2000
<u>Investments :</u>			
Marine fisheries	300	600	1,000
Inland fisheries	900	1,800	3,000
Total	1,200	2,400	4,000
	=====	=====	=====
Short-term credit requirements			
Marine fisheries	15	30	50
Inland fisheries	45	90	150
Total	60	120	200
	=====	=====	=====

As in the case of short-term loans for crop production, the short-term credit requirements for fisheries estimated for the above years also represent the outstandings as at the end of the year and not the flow during that year. The details about the investments in fisheries are given in a later paragraph on the estimates of medium and long-term credit requirements for fisheries.

Short-term Credit for Input Distribution

22.73 The rationale for institutional credit for inputs distribution business arises mainly due to (a) the need to stock inputs ahead of the time when farmers demand them, (b) lack of synchronisation between the cash inflows and outflows for the input distributors and (c) length of the period for which the supplier may give credit to the distributors.

22.74 The estimates of credit requirements for input distribution have been worked out on the following basis. The credit outstanding for distribution of ferti-

lisers, pesticides and agricultural equipment and machinery by the commercial banks formed 1.34 per cent of the total credit outstanding. In the case of co-operatives, the credit outstanding reported under other agricultural purposes, including distribution of input, formed 3.66 per cent of the total short-term credit. On this basis, the estimated credit requirement for input distribution, excluding agricultural equipment and machinery, will be about 2 per cent of the total short-term credit requirements for crop production. The rough estimates of short-term credit requirements for input distribution for the years 1989-90, 1994-95 and 1999-2000 are worked out, based on the projected short-term credit requirements for crop production. The details are given in table 40.

Table 40
Short-term Credit Requirements for Input Distribution

<u>Year</u>	<u>Short-term credit requirements for crop production</u>	(Rs. crores) <u>Short-term credit requirements for input distribution (at 2 per cent)</u>
1989-90	8,861	177
1994-95	15,733	315
1999-2000	23,888	478

The above short-term credit requirements for input distribution will have to be met by the co-operative and the commercial banks. As in the case of short-term loans for crop production, the short-term credit requirements estimated for input distribution for the above years are the outstandings as at the end of the year and not the flow during that year.

22.75 At present the input distributors stock only small quantities of the various inputs required for crop production in view of several bottlenecks in supplies and the high rate of interest currently charged by banks for financing input distribution. It is suggested that a concessional rate of interest may be charged for input distribution, to enable the input distributors to stock adequate quantities for crop production. This will enable the farmers to get the required quantity of inputs, at the proper time. Incidentally it may be stated that if the rate of interest on short-term credit for input distribution is reduced, the demand for short-term credit for input distribution is likely to exceed the estimates indicated in table 40.

Term Credit for Crop and Livestock Production

(a) Methodology

22.76 The methodology adopted for assessing the term credit requirements is based on the hypothesis that the credit requirement is dependent on the private gross capital formation (GCF) in agriculture. The data of GCF in agriculture have been obtained from the statistics published by the Central Statistical Organisation (CSO) for the year 1970-71 to 1984-85. These include capital formation in agriculture for both private and public sectors. The data of public sector GCF as well as inventory are deducted to obtain the private gross capital formation.

22.77 The data on capital formation by the private sector include farm investments on items such as land development, irrigation works, orchards, plantations, agricultural implements and machinery and livestock. Hence they cover crop production and livestock sector of the agricultural production sub system. These series are in terms of current as well as constant prices (1970-71). However, they do not give statewise or itemwise break-up. We have, therefore, worked out the statewise and itemwise break-up of private gross capital formation.

22.78 The details in respect of distribution of value of gross capital formation, according to different purposes, at 1984-85 prices are given in Table 41. The estimated growth rates of GCF for the periods 1985-86 to 1990, 1991 to 1995 and 1996 to 2000 AD, at constant prices (1970-71 prices) for different purposes, are given in table 42.

Table 41
Distribution of Value of Gross Capital Formation (GCF) according to
Different Purposes at Current Price of 1984-85

Item	Percentage distribution	Value of GCF (Rs.crores)
1. Land development	3.62	156
2. Irrigation(wells, tubewells, etc.)	18.07	781
3. Implements and machinery	28.75	1,242
(a) Tractors and power driven implements	8.33	360
(b) Oil-engines, electric pumps and other implements	20.42	882
4. Livestock	49.56	2,141
(a) Cross-bred animals	4.95	214
(b) Other animals	44.61	1,927
Total Gross Capital Formation	100.00	4,320

Table 42

Estimated Growth Rates of Different Items of Gross Capital Formation
In Agriculture at Constant Price (1970-71)

Item	1970-71 to 1984-85	1985-86 to 1990	1991 to 1995	1996 to 2000
1. Land development		3.00	3.00	3.00
2. Irrigation (wells, tubewells, etc)		3.00	3.00	3.00
3. Implements and machinery				
(a) Tractors and power driven implements and machinery	9.45 a 9.40 b 20.78 c	9.00	8.00	7.00
(b) Oil-engines, electric pumps and other implements (irrigated area)	3.57 d	3.00	4.00	5.00
4. Livestock				
(i) Cross-bred cows		10.00	15.00	15.00
(ii) Other animals		3.00	4.00	5.00
Total Gross Capital Formation	3.39	5.86	6.25	6.77

On the basis of the growth rates at constant prices and the value of purpose-wise GCF of the base period 1984-85 (at current prices), the values of GCF, purposewise, for the years 1989-90, 1994-95 and 1999-2000 are obtained. The details are given in table 43.

Table 43**Distribution of Value of Gross Capital Formation at Current Price of 1984-85**

Item	(Rs. crores)			
	1984-85	1989-90	1994-95	1999-2000
1. Land development	156	182	211	244
2. Irrigation (wells, tubewells, etc.)	781	904	1,099	1,401
3. Implements and machinery	1,242	2,083	3,060	4,292
a) Tractors and power driven implements and machinery	360	604	887	1,244
b) Oil-engines, electric pump sets and other implements	882	1,479	2,173	3,048
4. Livestock	2,141	2,579	3,407	4,855
a) Cross-bred cows	214	345	692	1,391
b) Other animals	1,927	2,234	2,718	3,469
Total	4,320	5,748	7,777	10,792

b) Relationship of Purposewise Gross Capital Formation with Term Credit Supply

22.79 After working out the GCF of different items, for the year 1984-85, they are compared with the purposewise supply of credit through all sources, such as commercial banks, regional rural banks and co-operatives. The details in respect of the purposewise breakup of the gross capital formation as compared to the purposewise credit supply for the year 1984-85 are given in Table 44.

Table 44
Relationship between Credit Supply and GCF in 1984-85

(Rs. crores)			
Item	Value of GCF 1984-85	Credit supply	Percentage of Col.3 to Col.2
1.	2.	3.	4.
1. Land development	156	121	77.56
2. Irrigation (wells, tubewells, etc)	781	300	38.41
3. Implements and machinery	1,242	896	72.14
(a) Tractors and power driven implements	360	NA	NA
(b) Oil-engines, electric pumps and other implements	882	NA	NA
4. Livestock	2,141	920	42.97
(a) Cross-bred animals	214	NA	NA
(b) Other animals	1,927	NA	NA
Total Gross Capital Formation	4,320	2,237	51.78

N.A. - Not Available

It will be observed from the table that the performance in supply of credit for implements and machinery and for land development is very good. However, more efforts are needed to provide increasing credit for minor irrigation and livestock.

c) Term Credit Projections

22.80 We have projected the term credit requirements in two ways as under:

i) Projections based on the assumption that the government would like to encourage minor irrigation, development of cross bred animals and other livestock and land development in preference to tractorisation, keeping in view the overall emphasis on capital formation. This is called Case I.

ii) Projections based on the assumption that the government would like to encourage rapid growth of gross capital formation per

hectare particularly in states which are below the national average. This is called Case II.

22.81 According to the first assumption (Case I), we have worked out the percentage of GCF to be covered by institutional credit for various purposes during the years 1989-90, 1994-95 and 1999-2000. The details are given in table 45.

Table 45

Assumed Percentage of GCF to be Supplied by Institutional Credit and Credit Requirement According to Different Purposes during Different Years

Purpose	1984-85	1989-90	1994-95	1999-2000
1. Land development	77.56	80	80	80
2. Irrigation (wells, tubewells, etc)	38.41	50	60	70
3. Implements and machinery	72.14			
a) Tractors and power driven implements		75	70	60
b) Oil-engines, electric pumps and other implements		50	60	70
4. Livestock	42.97			
i) Cross-bred animals		60	75	80
ii) Other animals		50	60	70
Total Credit Requirement :	51.78	54.14	63.04	70.38

The term credit to GCF (percentage) for oil engines, electric pumps and agricultural implements and also in respect of construction of wells and tube wells is expected to increase from 50 to 70 during the period 1990 to 2000 AD, due to the emphasis on development of minor irrigation. In respect of cross bred animals, the percentage of term credit to GCF will increase from 60 to 80 during the period 1990 to 2000 AD. However, in respect of tractors and power driven

implements, the percentage of term credit to GCF will decline from 75 to 60 during the period 1990 to 2000 AD. The purposewise term credit requirement estimated for the years 1989-90, 1994-95 and 1999-2000 are given in table 46.

Table 46

Purposewise Term Credit Requirement in Different Years in India

Purpose	(Rs. crores)			
	1984-85	1989-90	1994-95	1999-2000
1. Land development	121	146	169	195
2. Irrigation (wells, tubewells, etc.)	300	452	659	981
3. Implements and machinery	896	1,192	1,925	2,880
a) Tractors and power driven implements		453	621	746
b) Oil-engines, electric pumps and other implements		739	1,304	2,134
4. Livestock	920	1,322	2,150	3,539
i) Cross-bred Animals		207	519	1,113
ii) Other Animals		1,115	1,631	2,426
Total Credit Requirement :	2,237	3,112	4,903	7,595

22.82 In terms of the second assumption (Case II), the statewise term credit requirements are worked out. In states such as Assam, Gujarat and West Bengal where the percentage of term credit supply to GCF is low, the percentage has been increased keeping the future developments in view. In states such as Bihar, Orissa, Karnataka, Kerala and Tamil Nadu, where the percentage of term credit supply to the GCF is about 80 or more., it has been fixed at 80 per cent for future years. In the states where the current credit coverage of GCF varied between 35 to 70 per cent, the assumed percentage is increased in such a way that it varies between 60 and 80 per cent by the year 2000 AD. The details are given in table 47.

Table 47

**Assumed Percentage of GCF to be supplied by Institutional Credit
According to Different States**

Zone/State	Year			
	1984-85	1989-90	1994-95	1999-2000
I J & K	48	50	60	75
H.P.	63	70	75	80
II Assam	29	35	40	45
W.B.	31	40	50	60
III Other States				
IV Punjab	46	50	55	60
U.P.	37	45	50	60
Bihar	85	80	80	80
V Orissa	100	80	80	80
A.P.	56	60	70	80
VI Rajasthan	35	40	50	60
Gujarat	29	35	45	55
Haryana	70	70	75	80
VII M.P.	43	50	60	70
Maharashtra	47	55	65	75
VIII Kerala	79	80	80	80
Karnataka	81	80	80	80
Tamil Nadu	88	80	80	80
All India :	52	54.53	60.47	67.72

The state-wise credit requirements for the years 1989-90, 1994-95 and 1999-2000 on the basis of the assumed percentage of GCF to be supplied by institutional credit, are given in table 48.

Table 48

Term Credit Requirement According to Different States for Different Years

Zone/State		(Rs. Crores)		
		Year		
		1989-90	1994-95	1999-2000
I	J & K	16	28	51
	H.P.	21	24	33
II	Assam	16	24	35
	W.B	47	62	85
III	Other States			
IV	Punjab	244	326	545
	U.P.	443	659	1,058
	Bihar	120	146	186
V	Orissa	46	61	86
	A.P.	274	428	665
VI	Rajasthan	147	234	376
	Gujarat	126	188	280
	Haryana	152	198	270
VII.	M.P.	154	210	284
	Maharashtra	345	520	783
VIII	Kerala	126	135	150
	Karnataka	266	308	374
	Tamil Nadu	253	307	392
All India :		2796	3858	5653

22.83 The summary of the estimates of credit requirements according to Case I and Case II are given in table 49.

Table 49

Credit Requirements for Crop and Animal Husbandry Sector in India

(Rs. crores)

Year	Case I		Case II	
	Based on purposewise estimation of GCF	Percentage Growth rate	Based on state estimation of GCF	Percentage Growth rate
1984-85	2,237	6.83	2,237	4.56
1989-90	3,112	9.52	2,796	6.65
1994-95	4,903	9.15	3,858	7.94
1999-2000	7,595		5,653	

The term credit requirement estimated for the year 1999-2000 varies between Rs.5,653 crores and Rs.7,595 crores. It appears that the GCF calculated on the existing methodology gives an under estimation of the actual GCF. Hence, estimates of credit requirements, based on GCF, are also likely to indicate under-estimated figures in respect of credit requirements. In view of this, out of the two estimates, the credit requirements according to Case I, which indicates the higher figure at Rs.7,595 crores for 1999-2000 is considered reasonable and realistic. The subsidy provided by Government to certain term borrowers viz. small and marginal farmers, scheduled castes and scheduled tribes and other weaker sections, for certain purposes, will not affect the above estimate, if the scale of subsidy remains the same upto the year 2000 A.D. The term credit requirements for the years 1989-90, 1994-95 and 1999-2000 are estimated at Rs.3,112, crores Rs.4,903 crores and Rs.7,595 crores respectively.

22.84 To convert the term loans issued during a particular year, to stock as at the end of that year, we have examined the relationship between the term loans issued during a year and the balance outstanding as at the end of that year. The details are given in table 50.

Table 50

Term Loans Issued during a Year and
the Balance Outstanding as at the end of the Year

(Rs. crores)

Year (July-June)	Term loans issued during the year (a)	Balance outstanding at the end of the year (b)	Ratio of (a) to (b)
1975-76	497.7	1,771.5	1:3.56
1976-77	668.2	2,159.9	1:3.23
1977-78	667.8	2,519.6	1:3.77
1978-79	849.5	2,908.4	1:3.42
1979-80	1,081.5	3,568.0	1:3.30
1980-81	1,388.8	4,289.1	1:3.09
1981-82	1,555.6	4,843.4	1:3.11
1982-83	1,593.1	5,995.2	1:3.76
1983-84	1,909.0	7,185.1	1:3.76
1984-85	2,435.5	8,667.0	1:3.56
Average for 10 years			1:3.46

Source : Reports on Currency and Finance for various years.

22.85 Using the above ratio of 1:3.46, the outstandings in respect of term credit requirements for the years 1989-90, 1994-95 and 1999-2000 have been worked out. The details are given in table 51.

Table 51

Term Loans for Crop and Animal Husbandry Sector

(Rs. crores)

Year	Term credit estimated for the year	(At 1984-85 prices) Balance outstanding as at the end of the year
1989-90	3,112	10,768
1994-95	4,903	16,964
1999-2000	7,595	26,279

Term Credit for Forestry

22.86 The forestry projects can be divided into three main categories, viz. social forestry, wasteland development and agro-forestry. The main aim of social forestry is to recreate village forests, if land is available, and to raise fuel wood and fodder trees along vacant strips of land on either side of roads, canals, rail tracks and also in village common lands. Under the project, individual farmers are also encouraged to raise trees in part of their holdings and along their field boundaries, so that they may become self sufficient in respect of their requirements of fuelwood, fodder and small timber. In this programme, plantations of economic importance are being established in degraded forests and marginal lands. Besides increasing the forest coverage, such a programme will attract local employment and boost industrial development by making available raw materials in rural areas. In arid and semi-arid areas, tree crops will ensure greater stability of income than the annual crops.

22.87 The Wasteland Development Board formulates perspective plans and programmes for the management and development of wastelands in the country. It is difficult to promote massive afforestation programmes on private lands, as it requires heavy investments and as most of such lands are with the poor people. The Consultants for Study I have stated that the Gujarat Energy Development Agency has done an experiment to develop plantations in 1,000 hectares of wasteland in Abdasa taluka of Kutch district in Gujarat state. The experiment showed that in shallow, depleted and saline soils with scanty and erratic rainfall and brackish underground water, it was possible to grow select species of eucalyptus, prosopis, acacia, casurina and leucena. An analysis of the economic returns from the 1,000 hectares of fuelwood plantations and 1,000 hectares of crop lands of similar type, showed that the plantations were far more profitable than the agricultural crops.

22.88 Agro-forestry is a generic term which includes agri-sylviculture, sylvi-pastoral system, agri-sylvi-pastoral system and the multipurpose forest trees production system. Agri-sylviculture is a conscious and deliberate use of land for the concurrent production of agricultural crops (including tree crops) and forest crops. In the sylvi-pastoral system, forests are managed for the production of wood and the rearing of domesticated animals. The agri-sylvi-pastoral system

refers to the management of land for concurrent production of agricultural and forest crops and also for rearing of domesticated animals. In fact, it is the combination of the first two systems. In the multipurpose forest trees production system, the forest tree species are regenerated and managed for their ability to produce not only wood, but leaves, and for fruits that are suitable for food and/or fodder.

22.89 The major problem in forestry projects is the low productivity of the existing forest area. It is estimated that the existing forest areas yield about 13.5 million cubic meters of wood, giving an average of only 0.2 cubic meter of wood per hectare. Thus, the present productivity is very low and therefore efforts are needed to increase the productivity of the forest area.

22.90 Due to the Government budgetary allocation for the forest development, there was very little involvement of financial institutions in forestry. However, with the strategy of establishing forest development corporations, introduction of social forestry and wasteland development programmes and the encouragement given for agro-forestry, the involvement of financial institutions would increase in future. At present, there are only scanty data to project the credit requirements for forestry development. However, attempts are made to provide rough estimates of the credit requirements.

22.91 At present there are about 10 million hectares under forest, needing immediate attention. A number of forest development corporations are established to develop particularly the degraded forest areas. It is assumed that by the year 2000 AD, the forest development corporations would undertake the programme of developing about 25 per cent of the degraded forest area i.e. about 2.5 million hectares under bankable projects. Further out of the total culturable wasteland of about 32 million hectares, the area available for social forestry, is estimated to be about 16 million hectares. In addition, another one million hectares of land is available on roadsides, drains, rail lines, etc. for tree planting. Thus the total area that would be covered under social forestry and wasteland development would amount to 17 million hectares. By the year 2000 AD, it is estimated that about 25 per cent of this area i.e. about 4.25 million hectares, would be covered by the bankable projects. The unit cost of developing one hectare area under tree plantation varies considerably. However, for the rough estimate, the average unit cost has been taken at Rs.3,000 per hectare. The details of the investment required

for forestry development through various forest corporations, social forestry and wasteland development board, and the credit requirements, worked out at 80 per cent of the total financial requirements, are indicated in table 52.

Table 52
Credit Requirements for Forestry Development Programmes

(Area in million ha.)
(Rs. crores)

Item	1989-90	1994-95	1999-2000
1. Area to be developed by Forest Development Corporations	0.50	1.00	1.00
2. Social forestry programme and programmes of the Wasteland Development Board	1.25	1.50	1.50
Total :	1.75	2.50	2.50
3. Investment required	525	750	750
4. Term credit required	420	600	600

22.92 The term credit requirements indicated for the years 1989-90, 1994-95 and 1999-2000 are the cumulative requirement of term credit for five years ending those years. Hence we have to estimate the cumulative credit requirements in terms of outstandings, or in other words convert into stock. To convert the cumulative term credit requirements for five consecutive years to stock as at the end of the fifth year, we have examined the relationship between the cumulative total of term loans issued for five years and the balance outstanding (stock) as at the end of the fifth year. The details are given in table 53.

22.93 Using the ratio of 1:0.93, the outstandings in respect of term credit requirements for forestry for the years 1989-90, 1994-95 and 1999-2000 have been estimated. The details are given in table 54.

Table 53

**Cumulative Total of Term Loans Issued for 5 Years
and the Balance Outstanding as at the end of the 5th Year**

(Rs. crores)			
Year (July-June)	Cumulative total of term loans issued for 5 years ending the year (a)	Balance outstanding at the end of the year (b)	Ratio of (a) to (b)
1979-80	3,764.7	3,568.0	1: 0.95
1980-81	4,655.8	4,289.1	1: 0.92
1981-82	5,543.2	4,843.4	1: 0.87
1982-83	6,468.5	5,995.2	1: 0.93
1983-84	7,528.0	7,185.1	1: 0.95
1984-85	8,882.0	8,667.0	1: 0.98
		Average.	1: 0.93

Table 54

Term Loans for Forestry Development

(Rs. crores)		
(At 1984-85 prices)		
Year	Term credit requirements for five consecutive years ending the year	Balance outstanding as at the end of the year
1989-90	420	391
1994-95	600	558
1999-2000	600	558

Term Credit for Fishery

22.94 A detailed study of the marine and inland fisheries, including the proposed developments of fisheries upto the year 2000 AD, has been conducted. According to the study, the total financial requirements in the fishing sector, in the year 2000 AD, will be as indicated in table 55.

Table 55

Total Financial Requirements for Fishery

	(Rs. crores)
<u>Sub-sector</u>	<u>Amount</u>
i) Marine Fisheries	830
ii) Inland Fisheries	1,875
iii) Seed Hatcheries	135
iv) Brackish Water Culture	1,000

Total :	3,840
	=====

Say Rs.4,000 crores.

22.95 Presently the fishery development programmes are being financed to a considerable extent by budgetary sources. However, as the fishing activities become more and more bankable, the financing of this programmes is likely to be undertaken by the credit institutions on a larger scale. We have, therefore, assumed that by the year 2000 AD, at least 50 per cent of the financial requirements of the long term nature of the fishery sector will be met by credit institutions. Accordingly the term credit requirements of the fishery sector by the year 2000 AD would be as indicated in table 56.

Table 56

Term Credit Requirements for Fishery by the year 2000

	(Rs. crores)
<u>Sub-sector</u>	<u>Term credit requirements</u>
i) Marine Fisheries	415
ii) Inland Fisheries	938
iii) Seed Hatcheries	67
iv) Brackish Water Culture	500

Total	1,920
	=====

(Say Rs.2,000 crores)

22.96 Based on the financial requirements and the term credit requirements for the year 2000 AD, we have interpolated the financial requirements and

the term credit requirements for the years 1989-90 and 1994-95. The details are given in table 57.

Table 57
Term Credit Requirements for Fishery Development

<u>Item</u>	(Rs. crores)		
	(At 1984-85 prices)		
	<u>1989-90</u>	<u>1994-95</u>	<u>1999-2000</u>
<u>Investments</u>			
(a) Marine Fishery	300	600	1,000
(b) Inland fishery	900	1,800	3,000
Total :	1,200	2,400	4,000
Incremental investment	1,200	1,200	1,600
Term credit requirements	600	600	800

22.97 The term credit requirements for fishery development indicated for the year 1989-90, 1994-95 and 1999-2000 are the cumulative requirements of term credit for five years ending those years. However, in order that there may be the same base for comparison in demand as well as supply projection, it is necessary to estimate the outstandings, or in other words convert the flow in terms of stock. To so convert the cumulative credit requirements for five years to stock as at the end of the fifth year, we have adopted the methodology, used in respect of the term credit requirements for forestry, indicated at table 53. The details are given in table 58.

Table 58
Term Loans for Fishery Development

Year	(Rs. crores)	
	(At 1984-85 prices)	
	Term credit requirements for 5 consecutive years ending the year	Balance outstanding as at the end of the year
1989-90	600	558
1994-95	600	558
1999-2000	800	744

Summary of Demand for Credit

22.98 The projected demand for credit from institutional agencies for Agricultural Production sub system (APS) and the Agricultural Input Distribution sub system (AID) has been briefly summed up at table 59.

Table 59

Summary of Demand for Credit (outstandings or in otherwords, stock) for Agricultural Production sub system (APS) and the Agricultural Input Distribution sub system (AID) @

Particulars	(Rs. crores)								
	1989-90			1994-95			1999-2000		
	S.T.	Term	Total	S.T.	Term	Total	S.T.	Term	Total
APS									
Crop Production (S.T)	8,861	-	8,861	15,733	-	15,733	23,888	-	23,888
Live stock Production (S.T.)	772	-	772	939	-	939	1,185	-	1,185
Crop production and Livestock production (Term)	-	10,768	10,768	-	16,964	16,964	-	26,279	26,279
Forestry	-	391	391	-	558	558	-	558	558
Fisheries	60	558	618	120	558	678	200	744	944
	<u>9,693</u>	<u>11,717</u>	<u>21,410</u>	<u>16,792</u>	<u>18,080</u>	<u>34,872</u>	<u>25,273</u>	<u>27,581</u>	<u>52,854</u>
AID									
Agricultural Input Distribution	177	-	177	315	-	315	478	-	478
Total (APS + AID)	9,870	11,717	21,587	17,107	18,080	35,187	25,751	27,581	53,332

● - At constant prices (1984-85 prices)

S.T. - Short-term credit

Term - Medium and long-term credit

22.99 The above projections are made at 1984-85 prices. It will, however, be erroneous to presume that there will be no price rise (input prices) at all during the next decade or so. At the same time, no estimate of the inflation rate or its impact on agricultural input prices can be reasonably made for a period extending over 10 years. We have, for the purpose of this exercise, assumed

the inflation impact on demand for credit at 5.0 per cent per annum, and worked out the credit requirements. The details are given in table 60. In this connection it may be stated that the rate used here should not be presumed to be the annual inflation rate during the next ten to fifteen years, but represents only the assumption of the impact of inflation during that period on the demand for credit.

Table 60 .

Brief Summary of Demand for Credit (i.e. outstandings, or stock) for APS and AID, Assuming Increase in Credit Requirements at 5.0 Per cent per Annum on Account of Increase in Prices

(Rs. Crores)								
1989-90			1994-95			1999-2000 AD		
<u>S.T.</u>	<u>Term</u>	<u>Total</u>	<u>S.T.</u>	<u>Term</u>	<u>Total</u>	<u>S.T.</u>	<u>Term</u>	<u>Total</u>
12,597	14,954	27,551	27,866	29,450	57,316	53,534	57,339	1,10,873

S.T. - Short-term credit
 Term - Medium and long-term credit
 APS - Agricultural Production sub system
 AID - Agricultural Input Distribution sub system

The credit requirements of (a) agro-processing industries, (b) storage, transportation and marketing of agricultural produce and (c) export of agricultural produce are indicated in a separate chapter.

CHAPTER XXIII

SUPPLY OF AGRICULTURAL CREDIT : ESTIMATES OF RESOURCES

Assets and Liabilities of Rural Households

Savings in the form of financial assets, which include deposits with institutional credit agencies, would grow over the years in the rural areas, with the greater monetisation of the economy, rapid institutionalisation of savings and the improvement in the levels of income in the rural areas. As the financial assets constitute a part of the total assets, the position of the total assets owned by the rural households is indicated in the following paragraphs.

23.02 The average value of all items of assets owned by a rural household as on 30th June 1981, amounted to Rs.36,090 and was lower than that owned by an urban household at Rs.40,573. The average value of assets owned by a cultivator household amounted to Rs.44,524 and was nearly five times that for a non-cultivator household. The non-cultivator households cover agricultural labourers, village artisans and other non-cultivator households. The average value of total assets per rural household registered more than three-fold increase from Rs.11,311 to Rs.36,090 over the decade ended 30th June 1981. The compound growth rate in the average value of the total assets of rural households during the decade was 12.3 per cent per annum in nominal terms (i.e. current prices).

23.03 The percentage share of assets owned by selected proportions of cultivators and the Gini-co-efficient of Concentration (CR), which summarises inequalities in the overall distribution pattern, as on 30th June 1981 and 30th June 1971 are indicated in table I.

Table I

Percentage Share of Assets Owned by Selected Proportions of Cultivators

Reference point	CR value	Proportion of assets (per cent) owned by				
		Lowest			Top	
		10 per cent	25 per cent	50 per cent	25 per cent	10 per cent
1	2	3	4	5	6	7
30th June 1981	0.5848	0.6	2.8	12.0	70.0	46.7
30th June 1971	0.5847	0.6	2.9	12.0	68.4	45.3

Source : Report of All India Debt and Investment Survey, 1981-82 - Assets and Liabilities of Households as on 30th June, 1981 - Table 9.5 on page 132 - Published by Reserve Bank of India in September 1987.

It would be observed that as on 30th June 1981, while the lowest 25 per cent of the cultivator households held only 2.8 per cent of the total assets, the top 25 per cent of the cultivator households held 70.0 per cent of the total assets.

23.04 The flow of funds in rural areas shows a high correlation with the average value of assets per household. The rural households with larger assets got larger share of their total borrowings from the institutional agencies, while the rural households with small assets got only a small percentage of their total borrowings from the institutional agencies. The percentages of cash dues of rural household, outstanding by asset groups, from all institutional agencies, as on 30th June 1981 are indicated in table 2.

Table 2

All Rural Households - Asset Groups and Credit From Institutional Agencies

Asset group in Rupees	Percentage of credit from institutional agencies (all rural households)
Upto 1,000	9.1
1,000 - 5,000	28.2
5,000 - 10,000	32.6
10,000 - 20,000	45.7
20,000 - 50,000	55.0
50,000 - 1 lakh	58.1
1 lakh - 5 lakhs	76.4
5 lakhs and above	<u>95.0</u>
Total for all rural households	<u>61.2</u>

Source : Report of All India Debt and Investment Survey 1981-82. Assets and Liabilities of Households as on 30th June 1981 - Table 4.2.2 on page 51.

As the table makes it clear, rural households with assets less than Rs.10,000 got 9.1 per cent to 32.6 per cent only, of their total borrowings, from institutional agencies, while the households having assets of Rs.1 lakh and above got 76.4 per cent to 95 per cent of their total borrowings, from institutional agencies.

23.05 The position is not much different in respect of cultivator households in the rural areas. The percentages of cash dues of such households, outstanding by the various asset groups, from all institutional agencies, as on 30th June 1981 are indicated in table 3.

Table 3

Cultivators - Asset Groups and Credit From Institutional Agencies

<u>Asset group in Rupees</u>	<u>Percentage of credit from institutional agencies (rural areas - cultivators)</u>
Upto 1,000	4.6
1,000 - 5,000	30.4
5,000 - 10,000	33.2
10,000 - 20,000	47.0
20,000 - 50,000	55.6
50,000 - 1 lakh	58.4
1 lakh - 5 lakhs	76.3
5 lakhs and above	<u>94.8</u>
Total for all cultivator households	<u>63.2</u>

Source : Report of All India Debt and Investment Survey 1981-82
- Assets and Liabilities of Households as on 30th June 1981 - Table 4.2.3 on page 52.

It will be seen that the cultivator households holding assets less than Rs.10,000 got 4.6 per cent to 33.2 per cent only, of their total borrowings, from institutional agencies, while the households with assets of Rs.1 lakh and above got 76.3 per cent to 94.8 per cent, of their total borrowings, from institutional agencies.

The poor credit absorption capacity of the rural households with very low level of assets, appeared to be the main reason for the low level of credit obtained by them from the institutional agencies. However, due to the special emphasis given by institutional credit agencies for financing marginal and small farmers, the short term agricultural loans outstanding from such farmers constituted 50.2 per cent of the short-term agricultural loans outstanding as on 30th June 1985, though they held only about 27.5 per cent of the total area of the operational holdings.

23.06 In view of the direct relationship of the size of the assets of the rural households, to the credit obtained from institutional agencies, the composition of assets of rural households has been analysed, and the details are given in table 4.

Table 4
Assets of Rural Households

		(Per cent)
Item	As on 30th June 1981	
1.	Productive assets	70.9
	of which	
	a) land	62.1
	b) livestock and poultry	5.0
	c) implements and machinery	3.8
2.	Building	20.7
3.	Consumer durables	7.1
4.	All financial assets	1.3
	Total	100.0

(Source : All India Debt and Investment Survey 1981-82 - Assets and Liabilities of Households as on 30th June 1981 - Published by Reserve Bank of India in September 1987).

It may be noted that land was the most important item which constituted about three-fifth of the total value of assets, followed by building which accounted for another one-fifth.

23.07 The details about institutionalisation of rural credit are indicated in the preceding chapter. It would be observed therefrom that in respect of rural households, the percentage of borrowings from institutional agencies to the total debt, increased from 12.3 per cent in 1951-52 to 61.2 per cent as on 30th June 1981. The details about the savings and the mobilisation of resources by various agencies are indicated in the subsequent paragraphs.

Macro Dimensions - Savings

23.08 The gross domestic product (GDP), the gross domestic savings, the rate of domestic savings and the rate of investments for the periods 1979-80 and 1984-85 and the projected figures for the years 1989-90 and 1999-2000 are indicated in table 5.

Table 5

Gross Domestic Product, Savings and Investment

		(Rs. crores)			
<u>Item</u>	<u>1979-80*</u>	<u>1984-85**</u>	<u>1989-90**</u>	<u>1999-2000**</u>	
i) Gross domestic product (GDP)	1,08,546	2,17,762	2,81,945	4,68,082	
ii) Gross domestic savings	23,055	50,738	68,997	1,20,540	
iii) Rate of domestic savings (as percentage of GDP)	21.2	23.3	24.5	25.8	
iv) Rate of investment (as percentage of GDP)	21.8	24.5	25.9	26.4	

* At 1979-80 prices

** At 1984-85 prices

The rate of savings increased from 21.2 per cent during the year 1979-80 to 23.3 per cent during the year 1984-85 and is expected to increase to 25.8 per cent by the year 1999-2000. The rate of investments is estimated at slightly higher rate than the rate of savings, the difference representing external assistance.

23.09 The relative shares of the different sectors in the aggregate domestic savings during the year 1984-85 and the projections in respect of the year 1989-1990 are indicated in table 6.

Table 6

Shares in Aggregate Domestic Savings

		(Rs. crores at 1984-85 prices)	
<u>Item</u>		<u>1984-85</u>	<u>1989-90</u>
i) Public sector		9,364	14,443
ii) Private corporate and co-operative sector		3,737	6,514
iii) Household sector		<u>37,637</u>	<u>48,040</u>
	Total :	50,738	68,997

(Source : The Sixth Five Year Plan and the Seventh Five Year Plan documents.)

The share of the household sector to gross domestic savings which amounted to 74.2 per cent during the year 1984-85 would decline to 69.6 per cent by the year 1989-90. The shares of public sector and the private corporate and co-operative sector, to gross domestic savings, are estimated to increase from 18.4 per

cent and 7.4 per cent respectively during the year 1984-85 to 20.9 per cent and 9.5 per cent respectively by the year 1989-90.

23.10 The savings of the households and institutions are mobilised by Unit Trust of India, Life Insurance Corporation of India, Government agencies, non-banking companies and by institutional credit agencies. These agencies compete with one another for mobilisation of savings. The Consultants for Study I have conducted a detailed study on mobilisation of resources by various types of agencies. The study, however, does not cover mobilisation of resources by companies by issue of share capital and debentures. The findings by the consultants, in brief, are indicated below.

**Mobilisation of Resources by various Agencies,
other than the Institutional Credit Agencies**

a) **Unit Trust of India (UTI)**

23.11 The value of sale of units, the percentage of this value to GDP and to the household sector savings are indicated in table 7.

Table 7

Year	<u>Value of Sale of Units</u>		
	UTI Sale	Per cent to GDP	Per cent to Household Sector Savings
1970-71	18.00	0.048	0.37
1975-76	21.50	0.032	0.20
1980-81	52.10	0.045	0.24
1981-82	157.37	0.121	0.66
1982-83	166.90	0.080	0.63
1983-84	330.16	0.192	1.02
1984-85	756.19	0.400	2.05
1985-86	896.00	0.433	2.06

The resources mobilised in respect of sale of units had increased from Rs.18 crores in 1970-71 to Rs.896 crores in 1985-86. Thus the sales increased by nearly 50 times during the above period.

b) **Life Insurance Corporation of India (LIC)**

23.12 The total life insurance business in force as on 31st March 1987, as reported in the Annual Report of LIC for the year 1986-87, amounted to Rs.60,795 crores, under 298.80 lakh policies. During the year 1986-87 new business in rural areas amounted to Rs.2,916.04 crores under 14.82 lakh policies, constituting 32.16 per cent of the total new business during that year. As on 31st March 1987, LIC's investment in public sector amounted to Rs.10,259.31 crores and constituted 80.1 per cent of its total investments. As on that date, LIC's investments in co-operative sector and in the private and joint sectors amounted to Rs.1,058.63 crores and Rs.1,494.93 crores respectively and constituted 8.3 per cent and 11.6 per cent respectively of its total investments.

c) **Non-banking Companies**

23.13 The growth of deposits in the non-banking corporate sector, during the period March 1977 to March 1986 is indicated in table 8.

Table 8

Growth of Deposits in the Non-Banking Corporate Sector

End of March	No. of accounts in thousands	Amount (Rs. crores)
1977	4646.2	1,734.9
1978	4914.0	2,062.5
1979	2332.0	2,636.1
1980	3413.5	3,453.6
1981	3923.3	4,188.0
1982	5914.2	5,491.8
1983	7511.9	9,194.3
1984	8897.1	11,124.1
1985	12414.7	16,140.4
1986	15899.7	18,072.1

The total deposits in the non-banking corporate sector thus increased from Rs.1,734.9 crores as at the end of March 1977 to Rs.18,072.1 crores as at the end of March 1986. The deposits in the non-banking corporate sector, it will be seen, increased by more than ten times during the nine years ended March 1986.

(Source : Growth of deposits with non-banking companies, 1985-86 - Reserve Bank of India Bulletin - November 1987)

d) **Government Schemes**

23.14 Besides the above, financial savings are mobilised also under the small savings schemes by Government of India. The Government of India launches from time to time special schemes which offer attractive returns to the investors, with special tax concessions. The household savings in small savings instruments increased from Rs.2,936 crores in 1984-85 to Rs.3,318 crores in 1985-86 and further to Rs.4,575 crores in 1986-87.

(Source : Report on Currency and Finance 1986-87, Volume I, pages 12 and 13)

23.15 The data in respect of the various small savings schemes of Government of India are given in table 9.

Table 9

Small Savings Schemes of Government of India

			(Rs. crores)
Name of Scheme	Rate of Interest per cent per annum	Amount outstanding as on March 31, 1987	
1.	Post Office Savings Bank Accounts	5.50	3,126
2.	7 Year National Savings Certificates II Issue	6.50	448
3.	Public Provident Fund Accounts	12.00	655
4.	National Savings Scheme	9.00	-
5.	6 Year National Savings Certificates VI Issue	11.30	10,696
6.	6 Year National Savings Certificates VII Issue	11.00	1,134
7.	10 Year Social Security Certificates	11.30	18
8.	Post Office Time Deposit Accounts	Between 9.50 and 11.00	6,468
9.	Post Office Recurring Deposit Accounts (Period 5 years)	11.00	1,257
10.	Indira Vikas Patra	13.43	835
11.	Total (1 to 10)	-	24,637

The total amount outstanding as at the end of March 1987 in respect of the various small savings schemes of Government of India amounted to Rs.24,637 crores.

(Source : Report on Currency and Finance, 1986-87 Vol. II, Page 135)

23.16 Mobilisation of resources by the various agencies other than the institutional credit agencies, mentioned in the foregoing paragraphs, compete with the institutional credit agencies in mobilisation of resources. The performance of credit agencies, as discussed below, against such a background is commendable.

**Mobilisation of Deposits by
Institutional Credit Agencies**

- a) **Commercial Banks including Regional Rural Banks**
(i) **Branch Expansion**

23.17 There has been considerable increase in the number of branches of commercial banks, since the nationalisation of 14 major commercial banks with effect from 19th July 1969. The increase in the number of offices can be seen from table 10.

**Table 10
Offices of Commercial Banks**

<u>As at the end of June</u>	<u>Number of Offices</u>	<u>Percentage of rural offices to total offices</u>
1969	8,262	22.4
1979	30,203	44.1
1980	32,420	46.6
1981	35,707	49.4
1982	39,177	52.1
1983	42,079	53.9
1984	45,332	56.0
1985	51,978	55.4
1986	53,265	55.8

(Source : Reports on Trend and Progress of Banking in India)

The number of offices increased from 8,262 as at the end of June 1969 to 53,265 as at the end of June 1986. The number of offices of commercial banks increased at a rapid rate during the period 1969-70 to 1978-79. The compound rate of growth of offices during the 10 year period ended June 1979 amounted to 13.8 per cent per annum. However, the rate of growth of offices declined thereafter

and during the period 1979-80 to 1985-86, the compound rate of growth of offices of commercial banks amounted to only 8.5 per cent per annum.

23.18 An important feature in the growth of offices of commercial banks is the high rate of growth of rural offices. A rural centre is defined as a place with a population upto 10,000. The percentage of rural offices to the total offices increased from 22.4 as at the end of June 1969 to 55.8 as at the end of June 1986. This rapid increase in the number of rural offices helped in spreading banking to the relatively under developed areas.

(ii) Deposit Mobilisation

23.19 Deposits constitute the major portion of the resources of commercial banks. The position of deposits of commercial banks, including regional rural banks (RRBs), for the 10 year period ended June 1987 is indicated in table 11.

Table 11
Deposits of Commercial Banks Including RRBs

<u>Year</u>	<u>Deposits as at the end of June</u>	(Rs. crores) <u>Percentage growth of deposits during the year</u>
1976-77	18,903	19.7
1977-78	23,313	23.3
1978-79	28,671	23.0
1979-80	33,377	16.4
1980-81	40,549	21.5
1981-82	46,128	13.8
1982-83	54,039	17.2
1983-84	64,620	19.6
1984-85	77,075	19.3
1985-86	91,828	19.1
1986-87*	1,07,345*	16.9

* (provisional figure)

(Source : Reports on Trend and Progress of Banking in India)

During the ten year period ended June 1987, the deposits increased by 5.679

times. This amounted to a compound rate of growth of 18.97 per cent per annum for the ten year period. The compound rate of growth of deposits for the last five years ended June 1987 was slightly lower at 18.40 per cent per annum.

23.20 The growth of deposits during the year 1986-87 amounted to 16.9 per cent only. The decline in growth rate may be due to the diversion of savings of the household sector into the new issues in the capital market and the new financial instruments produced during the last couple of years. The aggregate deposits on the last Friday of June 1988 were provisionally placed at Rs.1,25,234 crores.

(iii) Projections of Future Deposits

23.21 In view of the above and due to the restrictive policy adopted in respect of branch licensing, we may estimate the growth rate of the deposits for the period 1987-88 to 1989-90 at a compound rate of 17.0 per cent per annum. Further, in view of the competition from a wide range of alternative saving instruments including those in the capital market, and in view of the restrictive policy for branch licensing, the compound growth rate of deposits during the years 1990-91 to 1994-95 may be at a lower rate of 15 per cent per annum. The growth rate of deposits is likely to decline further during the period 1995-96 to 1999-2000 A.D., in view of the high level of deposits that would have been reached by the year 1994-95. The compound rate of growth of deposits during this period is, therefore, estimated at 12 per cent per annum only.

23.22 The consultants for Study I had based their estimates of deposits on the study conducted by Balaiah Donta, Kamaiah Bandi and Nachane D.M., of the National Institute of Bank Management and published in Prajnan Vol.XVI, April-June 1987 issue. The comparative position of the rate of growth of deposits, as estimated by us, and as estimated by the consultants, is indicated in table 12.

23.23 The deposits as at the end of June 1990, 1995 and 2000 A.D., as projected by us and as projected by the consultants are indicated in table 13.

Considering that the deposits of scheduled commercial banks grew at 5.679 times during the ten years period ended 30.6.1987, the growth of 3.543 times during

Table 12

Deposits of Commercial Banks - Estimated Rate of Growth

<u>As estimated by us</u>		<u>As estimated by the consultants</u>	
<u>Period</u>	<u>Compound rate of growth - per cent per annum</u>	<u>Period</u>	<u>Compound rate of growth - per cent per annum</u>
1987-88 to 1989-90 (3 years)	17	1985-90	9.70
1990-91 to 1994-1995 (5 years)	15	1990-2000	6.85
1995-96 to 1999-2000 (5 years)	12		

Table 13

<u>Estimated Deposits of Commercial Banks including RRBs</u>			(Rs. crores)
<u>Year (as at the end of June)</u>	<u>According to our estimate</u>	<u>According to consultants' estimate</u>	
1990	1,71,967	1,31,253	
1995	3,45,826	1,84,972	
2000	6,09,345	2,38,441	

the years 1990 to 2000 estimated by us is quite realistic and reasonable. The consultants' projection is, therefore, considered very much on the lower side. This is evident by the fact that on last Friday of June 1988 the deposits had already reached a level of Rs.1,25,234 crores, which amounted to a compound rate of growth of 17.6 per cent per annum during the period July 1985 to June 1988, as against the compound rate of growth of 9.7 per cent per annum estimated by the consultants. According to the compound growth rate estimated by the consultants, the deposits of commercial banks would have reached the level of Rs.1,01,750 crores only by the end of June 1988, as against the actual level of deposits reached by the end of June 1988 at Rs.1,25,234 crores. Thus the compound rate of growth assumed by the consultants is very low not only in comparison with the actual rate of growth till June 1988 but appears lower still

during the period 1990-2000. The consultants have not explained the reasons for their accepting such lower rates except that they were based on a study by NIBM published in 1987 as stated in para 23.21 above. In the circumstances, we have not accepted the estimates of deposits made by the consultants, as they are much on the lower side.

b) **Co-operative Credit Institutions**

(i) **Deposit mobilisation**

23.24 The position of entire deposits of State Co-operative Banks (SCBs), District Central Co-operative Banks (DCCBs) and the Primary Agricultural Credit Societies (PACSs), for the ten year period ended June 1987 is indicated in table 14.

Table 14

Deposits of Co-operative Credit Institutions

	(Rs. crores)	
As at the end of June	Total of entire deposits of SCBs, DCCBs & PACSs	Percentage growth of deposits during the year
1977	2,131	17.0
1978	2,546	19.5
1979	3,111	22.9
1980	3,652	17.4
1981	4,398	20.4
1982	4,976	13.1
1983	5,682	14.2
1984	6,786	19.4
1985	7,812	15.1
1986	8,889	13.8
1987	10,456	17.6

(Source : Reports on Trend and Progress of Banking in India)

It will be observed that during the ten year period ended June 1987, the deposits increased by 4.907 times. This amounted to a compound rate of growth of 17.2 per cent per annum. However, the growth rate of deposits during the five years ended June 1987 amounted to only 16 per cent per annum.

23.25 It needs to be stated however, that the deposits of SCBs would include a part of deposits of DCCBs with SCBs and the deposits of DCCBs would include a part of deposits of PACSs with DCCBs. There may thus be an element of double counting in deposits of co-operative credit institutions, which may appear to inflate the resources. On an analysis of the working of co-operative credit societies and the provisions of the Co-operative Societies Acts of various states, it will be observed that certain reserves like statutory reserve fund, building fund which is not invested in bank building, special bad debt reserve, etc., which are built out of profits or from grants from government, are required to be kept mainly as deposits with higher financing agency. These deposits will be held with the higher financing agency, even if no other deposits are kept. These deposits cannot, therefore, be reckoned for double counting. The deposits of PACSs are very low. They constituted only 6.8 per cent of the total deposits of SCBs, DCCBs and PACSs as on 30th June 1987. The case studies conducted in a few states as a part of this review, revealed that the deposits of DCCBs kept with the concerned SCB, varied from about 17 per cent to 33 per cent of the deposits of the DCCBs. These deposits are inclusive of a part of their statutory liquidity requirements (SLR) and the deposits representing the investments of statutory reserve fund, building fund, special bad debt reserve fund, etc. Excluding the investments of these reserves, in deposits with the higher financing agency, the deposits of DCCBs with the concerned SCB would be of the order of about 10 to 25 per cent of the deposits of DCCBs and mainly represented their statutory liquidity requirements.

23.26 But as against the element of double counting in deposits of co-operative banking system indicated above, the federal structure of co-operatives and the statutory liquidity requirements enable the system to release a considerable portion of the amount involved in double counting, for the purpose of lending. For example, if a DCCB receives Rs.100 from PACSs as deposits, about Rs.30 will be kept apart for statutory liquidity requirement. The balance of Rs.70 will be available for lending, etc. by the DCCB. If the entire statutory liquidity requirement is kept by the DCCB with the concerned SCB, the deposits of the SCB will increase by Rs.30/-. The statutory liquidity requirement of the SCB, in respect of the deposit of Rs.30/-, will be about Rs.9/-, and Rs.21/- will be available for lending etc. by the SCB. In other words, as against the original deposit of Rs.100/-, the system releases about Rs.91/- for lending business.

The amount available for lending will further go upto Rs.94/- or to 94 per cent of the original deposit, if the National Co-operative Bank of India is set up as proposed. In the circumstances, we have ignored the element of double counting for the purpose of estimation of resources of the co-operative credit institutions.

(ii) **Projections of Future Deposits**

23.27 We estimate that the compound rate of growth of deposits of co-operatives during the period 1987-88 to 1994-95 would slightly decline to 15 per cent per annum. Further, in view of the high level of deposits that would have been reached by the year 1994-95 we estimate that the compound growth rate of deposits of co-operatives during the period 1995-96 to 1999-2000 is likely to decline to 13 per cent per annum. Based on these assumptions, the deposits of co-operatives have been projected as at the end of June 1990, 1995 and 2000. The details are given in table 15.

Table 15

Estimated Deposits of Co-operative Credit Institutions

(Rs. crores)

<u>As at the end of</u>	<u>Amount of deposits</u>
June 1990	15,902
June 1995	31,985
June 2000	58,930

However, it is possible that with the implementation of the various measures suggested in this report to strengthen the co-operative credit system, the actual growth of deposits of co-operatives may exceed the growth rate assumed by us.

(c) **Aggregate Deposits of Institutional Credit Agencies**

23.28 The projections made in the preceding paragraphs, in respect of deposits of institutional credit agencies, are summarised in table 16.

The deposits of institutional credit agencies which amounted to Rs.1,00,717 crores as at the end of June 1986, are expected to increase to Rs.6,68,275 crores by the end of June 2000 A.D. This means a compound growth rate of 14.5 per cent per annum.

Table 16

Projected Deposits of Institutional Credit Agencies

(Rs. crores)

Institutions	Deposits as at the end of June			
	1986	1990	1995	2000
Commercial Banks (including RRBs)	91,828	1,71,967	3,45,826	6,09,345
Co-operatives (SCBs, DCCBs and PACSs)	8,889	15,902	31,985	58,930
Total	1,00,717	1,87,869	3,77,811	6,68,275

23.29 After projecting the deposits of institutional credit agencies, we have made assessment in the following paragraphs as to what extent the institutional credit agencies would be able to finance the credit requirements for agriculture and allied activities upto the year 2000 A.D., which are expected to be met by such agencies, as assessed in the previous chapter. Incidentally, it might be mentioned that at the end of June 1986, the total direct finance (outstanding) by all institutional credit agencies to the agricultural sector aggregated Rs.16,410 crores. Of this outstanding amount, Rs.4,262 crores were overdue from the ultimate borrowers. Thus 25.97 per cent of the resources deployed by the credit agencies for the agricultural sector were locked up in overdues and were not available for recycling. For quick reference, the credit requirements for the years 1989-90, 1994-95 and 1999-2000, that are expected to be met by the institutional credit agencies are indicated in table 17.

Table 17

Brief Summary of Demand for Credit for APS and AID

(Rs. crores)

S.T.	1989-90		1994-95			1999-2000			
	Term	Total	S.T.	Term	Total	S.T.	Term	Total	
(a)	At 1984-85 prices								
	9,870	11,717	21,587	17,107	18,080	35,187	25,751	27,581	53,332
(b)	Assuming increase in credit requirements at 5.0 per cent per annum on account of increase in prices								
	12,597	14,954	27,551	27,866	29,450	57,316	53,534	57,339	1,10,873

- S.T. - Short term loans
- Term - Medium and long term loans
- APS - Agricultural production sub-system
- AID - Agricultural input distribution sub-system

23.30 The above estimates of demand for credit, however, do not include the demand for credit for (a) agro-processing industries, (b) storage, transportation and marketing of agricultural produce and (c) export of agricultural produce. The demand for credit for these sectors has been estimated in a separate chapter.

23.31 After determining the amount of credit for agricultural and allied activities that may have to be supplied by the institutional credit agencies, in future, we have analysed the practicability of this, by assessing the resources of the credit institutions that would be available for financing agriculture and allied activities. The details are given in the succeeding paragraphs.

Assessment of Resources of Commercial Banks including RRBs, for Financing Agriculture and Allied Activities

23.32 For assessing the availability of resources for financing agriculture and allied activities, at first, the credit deposit ratios for 10 year period ended June 1986, have been analysed. Thereafter projections in respect of future credit deposit ratios are estimated. As the deposits for future years have already been estimated, the credit deposit ratios will enable us to arrive at the total resources that will be available for lending for future years. Thereafter, the percentage of credit for agriculture and allied activities to total credit has been projected for future years. By using this ratio, the resources that will be available for lending for agriculture and allied activities by commercial banks, upto the year 2000 AD have been assessed. The details are given below.

Credit Deposit Ratio of Commercial Banks

23.33 The credit deposit ratios for the 10 year period ended June 1986 are given in table 18.

It would be observed that the credit deposit ratio declined from 71.4 per cent as at the end of June 1977 to 62.3 per cent as at the end of June 1986. In view of the declining trend of the credit deposit ratio, we estimate that the

Table 18

Commercial Banks - Credit Deposit Ratio

<u>As at the end of June</u>	<u>Credit deposit ratio</u> (Percentage)
1977	71.4
1978	68.9
1979	68.7
1980	66.1
1981	65.5
1982	65.4
1983	66.6
1984	67.5
1985	66.1
1986	62.3

(Source : Reports on Trend and Progress of Banking in India)

credit deposit ratio would further decline to about 58 per cent, 55 per cent and 52 per cent as at the end of June 1990, 1995 and 2000 AD respectively. We have thereafter assessed the share of credit for agriculture and allied activities to the total credit outstanding, and have made projections for future, as indicated below.

Level of Advances for Agriculture and Allied Activities

23.34 Reserve Bank of India had stipulated that the direct agricultural advances of scheduled commercial banks should reach a level of 16 per cent of the total outstanding credit by March 1987. The direct advances of commercial banks outstanding as at the end of December 1986 amounted to Rs.8,876 crores and constituted 16.24 per cent of the total advances outstanding as on that date. Thus by the end of December 1986, the scheduled commercial banks had already crossed the target required to be achieved by March 1987. The total advances (i.e. including the indirect advances) of commercial banks, for agriculture and allied activities, outstanding as at the end of December 1986, amounted to Rs.10,138 crores and constituted 18.56 per cent of the total advances outstanding as on that date. It is estimated that the advances for agriculture and allied activities (including indirect advances) might reach the level of 20 per cent of the total outstanding advances by the end of June 1990. The share of advances

for agriculture and allied activities to the total outstanding, as we see it, would however, decline marginally to 18 per cent by June 1995 and remain around that level up to June 2000, due to the high base that would be reached by June 1990 and due to the competing claims on credit from agro-processing industries, marketing and storage of agricultural produce and agricultural exports, which are the forward linkages of the agricultural production sub system. The share of these sectors to the total outstanding advances by the end of June 1995 may amount to about 10 per cent. Though the advances to these sectors may increase in absolute amounts, the share of these sectors to the total outstanding advances may remain at about 10 per cent level upto June 2000. The details are given in the chapter titled 'Credit for Agro-processing and Marketing: Projections'

Projection of Resources of Commercial Banks

23.35 Based on the credit deposit ratios of 58 per cent, 55 per cent and 52 per cent as at the end of June 1990, 1995 and 2000 AD respectively, and the resources that would be available for financing agriculture and allied activities at 20 per cent of the total outstanding advances, as at the end of June 1990, and 18 per cent each at the end of June 1995 and 2000, the resources available for financing agriculture and allied activities would amount to 11.60 per cent, 9.90 per cent and 9.36 per cent of the deposits as at the end of June 1990, 1995 and 2000 AD respectively. The projections in respect of deposits have already been made in this chapter. Based on the projections in respect of deposits, the resources that will be available for financing agriculture and allied activities by commercial banks will work out as indicated in table 19.

Table 19

As at the end of June	Deposits	Resources that will be available for financing agriculture and allied activities
1990	1,71,967	19,948
1995	3,45,826	34,237
2000	6,09,345	57,035

Assessment of Resources of Co-operative Credit Institutions

23.36 In respect of co-operatives, the SCBs and DCCBs will have to maintain cash reserve and liquid assets at 3 per cent and 25 per cent respectively of the deposits. The PACSs will also have to maintain liquid resources. These, together with cash in hand, may amount to about 35 per cent of the total deposits. Hence about 65 per cent of the deposits will be available for loans and advances for agriculture and allied activities and for non-agricultural purposes. Presuming that 10 per cent of deposits will be required for agro-processing industries, marketing, storage etc. activities and based on the projections of deposits of co-operatives already made, the deposit resources available for financing agriculture and allied activities will be 55 per cent of the deposits, and will be as indicated in table 20. It does not follow from this that all co-operatives will invest 55 per cent of their deposit resources in agricultural lending. The extent of their involvement in agricultural lending will depend upon the return obtainable on such involvement. However, we expect that with implementation of our recommendations on interest rates later in the Chapter on "Interest Rates, Costs and Margins", the disincentive to invest own resources in agricultural lending by co-operatives will disappear to a large extent. To the extent the co-operative banking system fails to invest 55 per cent in agricultural lending, the draft on refinance from NABARD may increase.

Table 20

Co-operative Credit Institutions - Resources for Agricultural Finance

As at the end of June	Deposits	(Rs. crores) Resources that will be available for financing agriculture and allied activities
1990	15,902	8,746
1995	31,985	17,592
2000	58,930	32,412

Relative Shares of the Commercial Banks and the Co-operatives

23.37 The relative shares of the commercial banks and the co-operative banks in financing agriculture and allied activities have been indicated at paragraph 22.31 of the chapter titled 'Demand for Agricultural Credit: Projections'. It will be observed therefrom that the share of commercial banks in the total short

term and the medium and long-term advances for agriculture and allied activities, outstanding as at the end of June 1975, amounted to only 21.39 per cent and 20.20 per cent respectively. However, there has been an increasing trend in the share of commercial banks in the total advances for agriculture and allied activities. As at the end of June 1985, the share of commercial banks in the total short, medium and long-term loans outstanding for agriculture and allied activities amounted to 43.35 per cent and 59.26 per cent respectively. We estimate that the share of commercial banks in the short-term credit on the one side and the medium and long-term loans outstanding for agriculture and allied activities on the other, will increase to 50.0 per cent and 65.0 per cent respectively by the year 1989-90 and may well stabilise at the level. This would mean that the declining trend in the share of co-operatives will be arrested as a result of the series of measures suggested towards institutional strengthening, democratisation of co-operatives and the greater involvement of the members in managing the societies. The summary position of the shares of commercial banks and the co-operatives in the loans outstanding for agriculture and allied activities during the years 1974-75 and 1984-85 and the estimated shares in future are indicated in table 21.

Table 21

Estimated Shares of Commercial Banks and the Co-operatives in the Loans Outstanding

<u>Type of institutional agency</u>	(Percentage)					
	1974-75		1984-85		1989-90 to 1999-2000	
	<u>S.T.</u>	<u>Term</u>	<u>S.T.</u>	<u>Term</u>	<u>S.T.</u>	<u>Term</u>
Commercial Banks	21.39	20.20	43.35	59.26	50.00	65.00
Co-operatives	78.61	79.80	56.65	40.74	50.00	35.00

S.T. - Short-term loans

Term - Medium and long-term loans.

23.38 Based on the shares of the commercial banks and the co-operatives as estimated, the credit requirements to be met by the commercial banks as at the end of June 1990, 1995 and 2000 AD have been worked out and indicated in table 22.

Table 22

Projected Credit Requirements from Commercial Banks

(Rs. crores)

	1989-90			1994-95			1999-2000		
	S.T.	Term	Total	S.T.	Term	Total	S.T.	Term	Total
a)	<u>At 1984-85 prices</u>								
	4,935	7,616	12,551	8,554	11,752	20,306	12,876	17,928	30,804
b)	<u>Assuming increase in credit requirements at 5.0 per cent per annum on account of increase in prices</u>								
	6,299	9,720	16,019	13,933	19,143	33,076	26,767	37,270	64,037

S.T. - Short-term credit

Term - Medium and long-term credit.

23.39 A brief summary, of the credit requirements for agriculture and allied activities from commercial banks and the resources of the commercial banks that will be available for financing agriculture and allied activities, is given in table 23.

Table 23

Brief Summary of Credit Requirements from Commercial Banks and the Resources Available

(Rs. crores)

Year	Credit Requirements		Resources available at current prices
	At 1984-85 prices	Assuming increase in credit requirements at 5.0 per cent per annum	
1989-90	12,551	16,019	19,948
1994-95	20,306	33,076	34,237
1999-2000	30,804	64,037	57,035

23.40 It will be observed from the foregoing analysis that there may not be any appreciable constraint of resources in the commercial banking system, at 1984-85 prices to finance the projected credit requirements to be met by the commercial banks upto the year 1999-2000. However, at 5.0 per cent increase per annum in the credit requirements, on account of increase in prices, which seems likely, there will be constraint of resources for financing the agricultural

credit requirements. Thus as against the credit requirements of Rs.64,037 crores for the year 1999-2000 to be financed by commercial banks, the resources available for the purpose will be only Rs.57,035 crores.

23.41 The overdues under agricultural loans of commercial banks, excluding RRBs, increased from Rs.200 crores as on 30th June 1976 to Rs.1,744 crores as on 30th June 1986. The overdues as on 30th June 1986 constituted 43 per cent of the demand for the year 1985-86. In respect of RRBs, the overdues under agricultural loans increased from Rs.54.22 crores as on 30th June 1981 to Rs.413 crores as on 30th June 1986. The overdues as on 30th June 1986 constituted 51 per cent of the demand for the year 1985-86. During the year 1985-86, 84 per cent of the RRBs had only restricted eligibility for refinance from NABARD for schematic lending. Therefore, the flow of credit will depend to a considerable extent on the recovery position. The steps required to be taken for improving the recovery position of institutional credit agencies are discussed in a separate chapter.

23.42 Based on the share of the co-operatives in the outstanding loans for agriculture and allied activities, estimated and indicated in table 21, the credit requirements to be met by co-operatives as at the end of June 1990, 1995 and 2000 AD have been worked out. The details are given in table 24.

Table 24

<u>Projected Credit Requirements from Co-operatives</u>								
(Rs. crores)								
1989-90			1994-95			1999-2000		
<u>S.T.</u>	<u>Term</u>	<u>Total</u>	<u>S.T.</u>	<u>Term</u>	<u>Total</u>	<u>S.T.</u>	<u>Term</u>	<u>Total</u>
a)	<u>At 1984-85 prices</u>							
4,935	4,101	9,036	8,553	6,328	14,881	12,875	9,653	22,528
b)	<u>Assuming increase in credit requirements at 5.0 per cent per annum on account of increase in prices</u>							
6,298	5,234	11,532	13,933	10,307	24,240	26,767	20,069	46,836
S.T.	-	Short-term credit.						
Term	-	Medium and long-term credit						

23.43 A brief summary of the credit requirements for agriculture and allied activities from co-operatives and the resources of the co-operatives that will

be available for financing agriculture and allied activities, is given in table 25. Incidentally, it may be stated that the resources of the co-operatives estimated, are of the short-term co-operative credit structure comprising PACSs, DCCBs and SCBs. The long-term co-operative credit structure comprising PLDBs and SLDBs, do not raise resources by mobilising deposits.

Table 25
Brief Summary of Total Credit Requirements from
Co-operatives and the Resources Available

Year	Credit requirements		Resources available at current prices	(Rs. crores)
	At 1984-85 prices	Assuming increase in credit requirements at 5.0 per cent per annum		Deficit (Col.3 less Col.4)
(1)	(2)	(3)	(4)	(5)
1989-90	9,036	11,532	8,746	2,786
1994-95	14,881	24,240	17,592	6,648
1999-2000	22,528	46,836	32,412	14,424

Deficit in resources as above, by the co-operatives would have to be met from out of refinance from NABARD. In other words NABARD's refinance to the co-operative system would need to be continued.

23.44 The co-operatives at present depend on NABARD in an appreciable measure, for long-term finance. The resources for long-term lending by the Land Development Banks are raised mainly by flotation of special debentures, subscribed by NABARD, Central and state governments and by issuing of ordinary debentures. However, in respect of short-term loans, a substantial portion of the resources is from the internal resources of the co-operatives.

23.45 The aggregate position of demand for credit (outstandings) for the APS and AID as well as supply of resources by the commercial banks and co-operatives is given in table 26.

Table 26

Demand for Credit for APS and AID and Supply of Resources

		(Rs. crores)		
		<u>1989-90</u>	<u>1994-95</u>	<u>1999-2000</u>
<u>A - Demand</u>				
i)	At 1984-85 prices	21,587	35,187	53,332
ii)	At increased input prices of 5 per cent per annum	27,551	57,316	1,10,873
<u>B - Resources</u>				
(a)	Commercial Banks	19,948	34,237	57,035
(b)	Co-operatives	8,746	17,592	32,412
Total		28,694	51,829	89,447
<u>Surplus (+)</u>				
<u>Deficit (-)</u>		+ 1,143	- 5,487	- 21,426

Conclusion

23.46 The position of demand for credit for agriculture, estimated by us at constant (1984-85) prices and the resources available (table 23) indicate that there may be no difficulty for the commercial banks to meet in full, the demand for agricultural credit. With the increase in credit requirements at 5.0 per cent per annum, on account of increase in input prices, which we consider very likely, the commercial banks would face constraint in resources for financing in full the agricultural credit demand in 2000 A.D. though not earlier in 1994-95 or 1989-90. This position is, however, subject to our assumptions, based on which the demand for credit and the supply of resources are worked out, not getting vitiated by external factors operating in the economy of the country during the next 10 years or so. If, however, the demand for credit increases and/or the growth of deposits lags behind, because of such reasons as new measures by Government and other financial institutions to attract the savings of the community, there could be a resource crunch under both the scenarios. In the case of co-operatives they have resource deficit for all the years under the second scenario i.e. credit requirements increasing at 5.0 per cent per annum. They would, as we see it, continue to depend on refinance from NABARD as hitherto though on a declining scale in the case of short-term loans. In both

the credit systems, however, they will have to take effective steps for recovery of dues to enable the smooth flow of funds. The various steps to be taken for effective recovery of dues are indicated in another chapter. The suggestions for bridging the gap between the demand for credit for agriculture and allied activities from the institutional credit system and the resources available with the credit system for such advances, are discussed in the chapter titled 'National Bank for Agriculture and Rural Development : Role, Organisation and Management'.

CHAPTER XXIV

CREDIT FOR AGRO-PROCESSING AND MARKETING : PROJECTIONS

In an earlier chapter, the demand for credit for the agricultural production sub-system (APS) and the agricultural input distribution sub-system (AID) was projected upto the year 1999-2000 AD. With the increase in production of agricultural produce, the forward linkages such as (a) agro-processing industries, (b) storage, transportation and marketing and (c) export of agricultural produce, will have to be strengthened, to enable the farmers to realise remunerative prices for the increased produce. Hence, in this chapter, the demand for credit for these sub-sectors is projected upto the year 1999-2000 AD.

(A) Agro-Processing Industries

24.02 There are two concepts commonly used to classify industrial units as agro-processing industries. One concept is based on the value of agricultural raw materials used and the other is based on the value of such raw materials and the value added by processing. We are concerned in the exercise attempted in this chapter, with the value added concept in view of the fact that credit requirements in India, for any given area of activity, need to be viewed in the context of the overall resource constraint and the consequent prioritisation involved. Accordingly, the agro-processing industries would be those, which use not less than 50 per cent of the raw materials from agriculture and where the value added as a result of the processing undertaken is not more than 50 per cent of the final value of output. This concept is relatively a more restrictive approach and gives greater emphasis on the agricultural raw materials used. Hence, for the estimation of demand for credit, the term agro-processing industries is used in this sense. The details of demand for credit for such industries, based on the projections made by our consultants, are indicated in this chapter.

24.03 The agro-processing industries can be grouped under three broad heads, viz. the industries based on (i) crop production, (ii) wood, and (iii) the livestock production. The agro-processing industries based on crop production can be sub-divided into six main heads viz., the industries based on foodgrains, oilseeds, sugarcane, fruits and vegetables, fibre crops and plantation crops. The details

about the projected demand for credit in respect of various agro-processing industries are indicated below.

a) **Agro-processing industries**

Foodgrains

i) **Paddy processing**

24.04 Paddy processing in India is carried out by hullers, shellers, shellers-cum-hullers and modern rice mills. A study of the value added due to the paddy processing revealed that when the price of paddy was Rs.1,940 per tonne, the values of products after paddy processing were, rice (720 kgs) worth Rs.2,160, husk (200 kgs) worth Rs.50 and bran (80 kgs) worth Rs.136. The total value of all outputs was Rs.2,346. The value added was Rs.406 per tonne of paddy. The raw material formed 82.7 per cent of the final product. The value added would increase considerably when rice bran is processed further, to obtain rice-bran-oil and de-oiled cake, and the rice husk is processed to obtain activated carbon, briquettes, etc.

24.05 In agro-processing industries in general and rice milling in particular, the under utilisation of capacity is a well known phenomenon. Looking to the trend of modernisation in rice industry, it can be assumed that the existing under-utilisation of hullers and sheller mills would continue and perhaps the under-utilisation would increase as it would be uneconomical to operate such mills. The modern rice mills would increase in the areas where rice production increases and slowly replace the huller and sheller mills. The financial institutions may have to encourage in setting up modern rice mills and in modernisation of the existing sheller mills. In order to make the projections for the additional modern rice mills required for the years 1989-90, 1994-95 and 1999-2000, the following assumptions have been made.

- (i) Fifty per cent of the existing huller mills would be scrapped by the year 1989-90 and the rest would operate at the same level as in 1984-85.
- (ii) In the year 1999-2000 the remaining 50 per cent of the huller mills would be scrapped.
- (iii) Fifty per cent of sheller and the huller-cum-sheller mills would be scrapped by the year 1999-2000 and the remaining would operate at the same level of 1984-85.

(iv) If there is any shortfall in milling capacity, new modern rice mills would be established.

(v) By the year 2004-5 all sheller and the huller-cum-sheller mills would be scrapped.

The state-wise projections of rice production for the years 1989-90, 1994-95 and 1999-2000 are given in table 1. On the basis of the projections of rice production, the quantities of paddy available for processing, after deducting the requirements of seeds, wages and home consumption are given in table 2.

Table 1
Statewise Estimates of Rice Production

State	1989-90	1994-95	1999-2000
West Bengal	9.51	11.03	13.42
Punjab	8.17	14.41	23.20
Uttar Pradesh	6.68	8.12	10.36
Bihar	5.75	6.57	7.61
Orissa	4.73	5.35	6.36
Andhra Pradesh	7.02	8.96	11.98
Madhya Pradesh	3.25	3.59	4.16
Karnataka	2.51	2.84	3.37
Tamil Nadu	9.59	11.66	14.89
All India	66.02	80.32	102.51

Note : (i) One million = 10 lakhs

(ii) Rice production can be converted into paddy production, assuming 66 per cent turnout of rice from paddy.

24.06 The investment costs for establishing the processing units, for processing the additional paddy have been estimated by our consultants at Rs.9.5 crores, Rs.53.0 crores and Rs.120.0 crores, by the years 1989-90, 1994-95 and 1999-2000 respectively.

24.07 It is observed that generally the paddy season starts in November and extends upto May, particularly in the areas where kharif paddy is predominant.

Table 2
Statewise Estimates of Paddy Available for
Processing by Commercial Units

(in million tonnes)

State	1989-90		1994-95		1999-2000	
	Paddy Prod.	Available Prod. for processing	Paddy Prod.	Available Prod. for processing	Paddy Prod.	Available Prod. for processing
W. Bengal	14.41	10.41	16.71	12.07	20.33	14.69
Punjab	12.38	8.74	21.83	15.77	35.15	25.39
Uttar Pradesh	10.12	7.31	12.30	8.80	15.76	11.34
Bihar	9.81	6.51	9.95	7.19	11.53	8.33
Orissa	7.17	5.18	8.11	5.86	9.64	6.96
Andhra Pradesh	10.64	7.68	13.58	9.81	18.15	13.11
Madhya Pradesh	4.92	3.55	5.44	4.72	6.30	5.58
Karnataka	3.80	2.74	4.30	3.10	5.11	3.69
Tamil Nadu	14.53	10.50	17.66	12.76	22.56	16.30
All India	100.00	72.26	121.70	87.72	155.32	112.20

The full swing of procurement is only for two months, viz. January and February. It is during these two months that the arrivals are the largest. The major part of the mills' requirements will have to be procured during the months of peak arrivals. The relationship between the value of paddy purchased for the whole year and the value of capital locked up in stock of paddy showed that about two months inventory needs to be kept for the continuous processing. Hence the working capital required for the inventory would be 1/6th or about 17 per cent of the purchase value of paddy. In addition, the processing and other costs will have to be provided for. The processing and other costs amounted to about 17 per cent of the purchase value of paddy. The working capital requirements for processing and other costs will be about 1/6th of the processing costs per year or it would amount to about 3 per cent of the purchase value of paddy. Thus the total working capital required would be about 20 per cent of the estimated purchase value of paddy. The details about the estimated purchase value of paddy are indicated in table 3 and the estimated working capital requirements for the years 1989-90, 1994-95 and 1999-2000 are indicated in table 4.

Table 3
Estimated Purchase Value of Paddy

Particulars	1989-90	1994-95	1999-2000
Paddy available for processing (million tonnes)	72.26	87.72	112.20
Purchase value of paddy for processing at 1984-85 farm harvest price (Rs. crores)	12,269	14,922	19,067

Table 4
Working Capital Requirements

Particulars	1989-90	1994-95	1999-2000
Purchase value of paddy for processing	12,269	14,922	19,067
Working capital requirements at 20 per cent of the purchase value of paddy	2,454	2,984	3,813

24.08 The credit requirements for long-term investments would be based on the requirement of margin. It is assumed that the financial institutions would require 40 per cent of the investment cost as margin for the term loans. Further, the financial institutions would require 50 per cent margin for the working capital advances. On this basis the credit requirements for long-term loans for investment and for short-term loans for working capital requirements for the rice processing industries have been worked out. It is assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions like the State Financial Corporation and the balance amount will

be financed by banks. The details are indicated in table 5.

Table 5

Term loans and short-term loans required for paddy processing

Particulars	Year		
	1989-90	1994-95	1999-2000
Additional investment required	9.5	53.0	120.0
Term loans-requirements	6	32	72
Of the above, term loans from banks	3	16	36
Working capital requirements	2,454	2,984	3,813
Short-term loans for working capital	1,227	1,492	1,906

ii) **Wheat processing**

24.09 In India wheat is purchased as whole grain by the households and then it is converted into wheat flour by getting the required quantity ground on custom basis at the nearby small wheat flour mills. Hence the quantity of wheat processed at larger wheat roller mills forms only a small proportion of the total wheat production. However, as urbanisation increases, the habits of consumers also change. The sale of packaged wheat flour and other wheat products is increasing. The number of flour mills increased from 232 in the year 1975-76 to 454 in the year 1984-85. The percentage of wheat processed to the total production of wheat, increased from about 5 per cent in the year 1974-75 to about 10 per cent in the year 1984-85. This indicates that in future the trend would be towards increased quantity of wheat getting processed by the modern roller mills.

24.10 The phenomenon of under-utilisation of installed capacity, which was observed in rice processing, is also prevalent in wheat processing. However, the utilisation of roller mills increased from about 25 per cent in the year 1974-75 to about 51 per cent in the year 1984-85. The total wheat processing capacity in wheat zones and other zones formed about 41 per cent and 59 per cent respectively, of the total processing capacity in the country. The utilisation of installed capacities shows that it was utilised less in the wheat zones as compared to the other zones. This indicates that wheat processing facilities have at present some locational advantages in consumption centres than in production centres. The details of the projections made by our consultants in respect of wheat production,

quantity of wheat to be processed, additional installed capacity required for processing, etc. are given in table 6.

Table 6

Projection for Additional Wheat Processing Capacity Required (Roller Mills)

S.No.	Item	('000 tonnes)		
		1989-90	1994-95	1999-2000
1.	Wheat production	58,019	77,642	1,06,377
2.	Percentage of wheat production processed	10	15	20
3.	Quantity of wheat to be processed	5,802	11,646	21,275
4.	Installed capacity existing	8,915	8,915	15,489
5.	Installed capacity required	7,717	15,489	28,296
6.	Additional installed capacity required (5-4)	-	6,574	12,807

24.11 It is assumed that (a) the utilisation of installed capacity, which was about 51 per cent in the year 1984-85 would increase to about 75 per cent of the existing capacity by the year 1989-90 and would remain at that level thereafter; (b) the utilisation of installed capacity of new mills would also be about 75 per cent and (c) the quantity of wheat processed which was about 10 per cent of the total wheat production in the year 1984-85, would continue upto the year 1989-90. It is also assumed that the wheat processed would increase to 15 per cent and 20 per cent of the total wheat production in the years 1994-95 and 1999-2000 respectively as a result of the changing habits of consumers. On the basis of the investment required per thousand tonnes of wheat processed, the additional investments required for the years 1989-90, 1994-95 and 1999-2000 have been worked out. The working capital required for wheat processing has been worked out on the basis of the relationship of working capital and the fixed investment. It is assumed that the margin money required for term loans for fixed investment would be 40 per cent and for working capital, 50 per cent. On this basis the term loans and the short term loans for wheat processing for the years 1989-90, 1994-95 and 1999-2000 have been worked out and it is assumed that 50 per cent of the term loan requirements will be met by the specialised term lending institutions like the State Financial Corporations, and the balance

amount will be financed by banks. The details are given in table 7.

Table 7

Projections for Investment, Working Capital and Credit Requirements

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000
Additional installed capacity of wheat processing required ('000 tonnes)	-	6,574	12,807
Additional investment required at 1984-85 prices	-	167	326
Working capital required	58	159	343
Term loans-requirements	-	100	196
Of the above, term loans from banks	-	50	98
Short-term loans for working capital	29	80	172

iii) **Pulse processing**

24.12 In India about 70 per cent of the total pulse produced is consumed in the form of dal obtained from various dal making processes, ranging from home processing to organised milling industry. There are more than 10,000 organised dal mills of varying capacities scattered all over the country. No information is, however, available about the number of small scale processors. The average yield of dal from pulse grain is about 70 per cent to 72 per cent. As the husk content of common pulses forms about 11 per cent to 15 per cent, the yield of the dal can be increased to over 80 per cent, if the losses in processing are prevented.

24.13 It is difficult to project the investment and the credit requirement for pulse processing, as detailed data about dal milling industry are not available. However, according to our consultants, a dal mill with the annual capacity of 9,000 metric tonnes would cost about Rs.60 lakhs. As there is an overall shortage of pulses, which are consumed mostly in the form of dal, it is assumed that there would be enough dal milling capacity up to the year 1989-90. It is therefore also assumed that additional investments would be required for dal milling for

additional pulse production for the years 1994-95 and 1999-2000. On the assumption that 70 per cent of pulse production would be converted into dal and that the additional investment in dal milling will be at the rate of Rs.60 lakhs for the capacity of 9000 metric tonnes, the total additional investment requirements for the years 1994-95 and 1999-2000 have been worked out. As no information is readily available on the relationship of the working capital to the value of raw material, it has been assumed that the pulse mills will have the same relationship as oil mills. In respect of edible oil mills, the working capital forms 7.68 per cent of the value of raw material. Applying this proportion to the value of pulse processed by dal milling, the working capital requirements have been projected. The credit requirements are estimated on the assumption that the margin money required for term loans for fixed investment would be 40 per cent and for short term loans for working capital would be 50 per cent. It is assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions like the State Financial Corporation, and the balance amount will be financed by banks. The details of the projections made by our consultants in respect of pulse production, the quantity to be converted into dal by dal mills, the investment and the working capital requirements and the term loans for investment and the short-term loans for working capital requirements are indicated in table 8.

Table 8

Investment and Credit Requirements in Dal Milling Industry

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000
Pulse production	13,002	15,075	18,337
Value	5,107	5,921	7,203
Additional pulse production	1,226	2,073	3,262
Total quantity to be converted into dal (70 per cent)	9,101	10,553	12,836
Value	3,549	4,116	5,006
Additional investment required	-	97	152
Working capital (at 7.68 per cent of the value of raw material)	273	316	384
Term loans-requirements	-	58	91
Of the above, term loans from banks	-	29	46
Short-term loans for working capital	137	158	192

Oil-seeds

iv) Edible oil industry

24.14 It is estimated that on an average 30 per cent oil is recovered and 45 per cent oil cakes are produced from edible oilseeds. The remaining portion of the oilseeds comprises waste. The oil cakes produced in the expeller process contain 7 to 8 per cent oil. About 55 per cent of the total expeller oil cakes is used as cattle feed, whereas the remaining 45 per cent is processed by solvent extraction plants. This process gives 6 per cent oil, 92.2 per cent oil cake, and 1.8 per cent wastage.

24.15 The statistics of 2401 units operating in the edible oil industry revealed that the total investment was of the order of Rs.271 crores. The raw material utilised was worth Rs.1,437 crores. This shows that the ratio of value of raw material to investment was 5.3 : 1. The capacity utilisation of edible oil industry is not readily available. Further, the ratio of the value of raw material processed to the value of production of edible oil seeds on all India basis is also not available, though the ratio for all oilseeds is available. The value of raw material processed constituted 20 per cent of the production of all oilseeds in the year 1984-85. Assuming the same ratio for edible oilseeds for the year 1984-85 and a five percentage points increase during every five year period subsequently up to 1999-2000, the values of raw material to be processed in those years have been worked out.

24.16 On the basis of the relationship of the investment in fixed capital and the raw material processed, the investment required for the raw material to be processed in the years 1989-90, 1994-95 and 1999-2000 has been worked out by our consultants. The working capital requirements have been worked out on the basis of the relationship of working capital and the value of raw material processed. The percentage of the working capital to the value of raw material was 7.68. The credit requirements have been estimated on the assumption that the margin money required for term loans for fixed investment would be 40 per cent and for short-term loans for working capital would be 50 per cent. It is assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions like the State Financial Corporations, and the balance amount will be financed by banks. The details about the

projections in respect of the value of output of oilseeds, the value of raw material to be processed, investment in fixed capital required, working capital required, and the credit requirements for term loans for investment purpose and short term loans for working capital are indicated in table 9.

Table 9
Credit Requirements of Edible Oil Industry

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000
Value of output of oilseeds	8,665	10,995	14,360
Per cent of raw materials to be processed to the value of output of oilseeds	25	30	35
Value of raw material to be processed	2,164	3,298	5,026
Investment in fixed capital required	408	622	948
Addl. investment required	137	214	326
Working capital required (at 7.68 per cent of the value of the raw material)	166	232	386
Term loans-requirements	82	128	196
Of the above, term loans from banks	41	64	98
Short-term loans for working capital	83	116	193

24.17 The projection of 25 million tonnes of oilseeds production by the year 1999-2000 is not likely to meet the demand of raw materials of edible oil industry and the vanaspati industry. Our consultants have, therefore, assumed that not much additional capacity needs to be added for vanaspati upto the year 1999-2000.

Sugarcane

v) Sugar industry

24.18 In 1983-84, there were about 339 sugar factories in the country. About 25 million cultivators were engaged in sugarcane cultivation. Out of the 339 factories, 127 were in private sector, 43 in public sector and 169 were in co-operative sector. The average number of days for which the sugar factories worked during

a year varied between 86 and 173. The total investment in the 339 sugar factories in 1983-84 was about Rs.2,700 crores. The average quantity of sugarcane crushed per factory during the year was 177.26 thousand tonnes. The average sugar production per factory was 18.12 thousand tonnes.

24.19 The value of output of sugarcane for the years 1989-90, 1994-95 and 1999-2000 has been projected at 1984-85 prices. Although the quantity of sugarcane crushed for sugar production depends on the sugar policy and the relative prices of sugar, gur and khandsari, it is assumed that in future 50 per cent of sugarcane production would be available for sugar production. On the basis of the projection of sugarcane production, the quantity of sugarcane to be crushed for sugar production and the installed capacity required have been worked out. The additional capacity required is then worked out and the requirement of fixed investment has been calculated. However, instead of creating new additional factories, if the existing factories are allowed to expand their capacities, it is observed that the incremental investment could be reduced to about 25 per cent of the new investments.

24.20 The working capital of 339 sugar factories in 1983-84 amounted to Rs.5,571.8 crores. This gave an average of Rs.16.4 crores per sugar factory. The short-term credit requirements for working capital have been assumed at about 20 per cent of the working capital. In respect of incremental investment required, the long term credit requirement is estimated at 60 per cent of the investment cost, on the assumption that the margin money required for term loans for fixed investments would be 40 per cent.

24.21 The details about the sugarcane production, sugarcane to be crushed, additional installed capacity required, investment required if additional capacity has to be created by installation of new factories, investment required if additional capacity is to be achieved by allowing the existing factories to expand, the working capital required and the term loans required for investment purposes for the years 1989-90, 1994-95 and 1999-2000, estimated by our consultants, are given at table 10. It is assumed that the entire term loan requirements will be met by specialised term lending institutions, while the entire short-term loan requirements will be met by banks.

Table 10

Credit Requirements for Sugar Industry

(Sugarcane and capacity in million tonnes, Rs. crores)

Item	1989-90	1994-95	1999-2000
Sugarcane production	198	235	286
Sugarcane to be crushed	99	117	143
Installed capacity	110	130	159
Additional installed capacity	44	20	29
Investment required	a) 1,958 b) 489	890 222	1,290 322
Working capital required	9,595	11,429	14,086
Term loans-requirements (to be met by specialised term lending institutions)	a) 1,175 b) 293	534 133	774 193
Short-term loans for working capital	1,919	2,286	2,817

Note :

a = New investments, by establishing additional factories

b = Incremental investments, if the existing factories are allowed to expand.

vi) **Processing industries based on fruits and vegetables**

24.22 India is considered the home of many of the finest tropical and sub-tropical fruit trees. Unfortunately the statistics of area and production under different fruit trees and vegetables are not yet on a sound footing. However, the official statistics showed that the area under fruits and vegetables increased from 1.2 million hectares in 1976-77 to 5.9 million hectares in 1982-83. The value of output of fruits and vegetables formed 9.8 per cent of the total value of all crops in 1983-84. Although the value of output increased from Rs.3,416 crores in 1977-78 to Rs.6,419 crores in 1983-84, its share in the total value of output of all crops declined from 11.6 per cent to 9.8 per cent during that period. This is because the growth of fruits and vegetables has not been able to keep pace with other crops.

24.23 The major portion of fruits and vegetables is sold as fresh. Hence the

post harvest treatment to fruits and vegetables is important. The application of metabolic inhibitors which reduce sprouting of onions and potatoes during the storage, the growth promoters which prolong the shelf-life of vegetables and the ripening hormones, is picking up.

24.24 Canning is the most widely used technique employed to conserve fruits and vegetables. The canning process includes blanching, filling, exhausting and sealing, heat processing and subsequently cooling and storage. Fruits and vegetables can be protected by processing them into more durable products like juices, jams, jellies, chutneys, soups, powders, chunks and discs. Juicy drinks are the most favoured products. The juices are of different types such as juice without any alteration (pure juice), juice which has undergone alcoholic fermentation (fermented beverages), clarified sweetened juice (cordial), clarified juice artificially flavoured and juice squash consisting of moderate quantities of pulp with cane sugar added for sweetening.

24.25 In 1983-84, there were 199 units in the country engaged in canning and preservation of fruits and vegetables. The raw material used by these units was worth Rs.88.87 crores. The value of final products of these units was Rs.128.46 crores, giving the value added of Rs.39.59 crores. The raw materials formed 69.18 per cent, of the value of final products. The installed capacity of 199 units was 107.9 tonnes per annum, but the utilization was only 46 per cent in 1983-84.

24.26 The relationship between the value of the raw material and investment in fixed capital was 1.56 : 1. The working capital of 199 units in 1983-84 was Rs.21.5 crores. The requirement of working capital depends on the quantity and value of raw material processed. The percentage of working capital to the value of raw material processed worked out to 24.2.

24.27 The data in respect of fruits and vegetables industry using different techniques of preservation are not readily available, except in respect of canning. The value of raw material processed formed only 2 per cent of the value of fruits and vegetables in 1983-84. It is assumed that in future, fruits and vegetables processing industry will grow at a much faster pace. It is therefore assumed that in the years 1989-90, 1994-95 and 1999-2000 the value of raw material

processed, would form 3, 5 and 10 per cent respectively of the total value of fruits and vegetables.

24.28 At present the installed capacity is utilised to the extent of about 46 per cent only. It is assumed that the installed capacity would be used at the levels of 50 per cent, 60 per cent and 75 per cent in the years 1989-90, 1994-95 and 1999-2000 respectively. On the basis of this utilisation, the required installed capacities are worked out. The additional installed capacities required to be created in different years are then worked out. On the basis of the investment required to process the raw materials in 1983-84, the total investment required for the installed capacity is worked out by our consultants for the years 1989-90, 1994-95 and 1999-2000. On the basis of the relationship between the working capital and raw material processed, the requirements of working capital for different years have been worked out. It is assumed that the term loans for investment would be available with the margin of 40 per cent and the short term loans for working capital with the margin of 50 per cent. On this basis the credit requirements for term loans for investment and short term loans for working capital have been projected for the years 1989-90, 1994-95 and 1999-2000. It is assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions, and the balance amount will be financed by banks.

24.29 The details in respect of the value of output of production of fruits and vegetables, the value of raw material to be processed, the additional installed capacity required, the additional investment required, the working capital required and the projections in respect of term loan requirements for investment and short term loan requirements for working capital for the years 1989-90, 1994-95 and 1999-2000 are given in table II.

Fibre crops

vii) Cotton ginning and pressing

24.30 Cotton textile is one of the most important agro-processing industries in India. According to the definition adopted for agro-processing industry for this study, only the cotton processing stage upto ginning and pressing has been taken into account for the purpose of projections in respect of credit requirements.

24.31 In the year 1983-84 there were 3,106 units in various stages engaged in cotton processing. The value of cotton processed by these units amounted to Rs.490 crores. The capacity utilisation was about 70 per cent.

Table 11
Projections for Additional Processing Capacity Required and
Credit Requirements - Fruits and Vegetables

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000
Value of output of production of fruits and vegetables	8,881	10,655	12,782
Percentage of production processed	3	5	10
Value of raw material processed	266	533	1,278
Utilisation of capacity (%)	50	60	75
Installed capacity required (value)	532	888	1,703
Additional installed capacity	202	356	815
Additional investment required	79	139	318
Working capital required (at 24.2% of the value of raw material)	64	129	309
Term loans-requirements	47	83	191
Of the above, term loans from banks	24	42	96
Short-term loans for working capital	32	64	155

Note: The installed capacity required has been worked out by our consultants on value terms, as it will be difficult to work out the installed capacity on tonnage basis, in view of the different types of fruits involved in processing.

24.32 It is assumed that all cotton production will be processed upto the ginning and pressing stage. The cotton production for the years 1989-90, 1994-95 and 1999-2000 has been projected. On this basis the additional investment required for ginning and pressing has been worked out. The working capital required is about 16 per cent of the value of cotton. On this basis the working capital requirement has been projected. The credit requirements for term loans for investment purpose and short term loans for working capital requirement have been projected on the assumption that the margin requirement for these purposes

would be 40 per cent and 50 per cent respectively. It is assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions, and the balance amount will be financed by banks. The details about the cotton production, additional investment required, working capital required and the term loans and short term loans required for the years 1989-90, 1994-95 and 1999-2000 estimated by our consultants, are indicated in table 12.

Table 12
Additional Investment and Credit Requirement for Cotton Ginning and
Pressing Industry

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000
Cotton production in 1000 tonnes	1,759	2,245	3,005
Value of cotton production	2,969	3,789	5,071
Additional investment required	75	165	470
Working capital required (at 16% of the value of cotton)	475	606	811
Term loans-requirements	45	99	282
Of the above, term loans from banks	23	50	141
Short-term loans for working capital	238	303	405

viii) **Jute and Mesta Pressing and Baling Industry**

24.33 Similar to cotton textile industry, in jute industry also we have restricted projections to the stage of pressing and baling for being included as an agro-processing industry. The production of jute increased from 8 lakh tonnes in 1975-76 to about 12 lakh tonnes in 1984-85, whereas the production of mesta fluctuated between 2.21 lakhs and 3.40 lakhs tonnes during the same period. The value of output of jute and mesta increased from Rs.158 crores in 1974-75 to Rs.795 crores in 1984-85. The percentage contribution of the jute and mesta, to the value of all crops varied between 0.36 and 0.79 during 1975-76 to 1984-85.

24.34 The relationship between the fixed capital and the value of output worked out to 1 : 7.28. The ratio between fixed capital and raw material processed was 1 : 6.49. The working capital required formed 10.5 per cent of the value of raw material.

24.35 The production of jute and mesta has been projected for the years 1989-90, 1994-95 and 1999-2000. It is assumed that all the jute and mesta production would go through the processing upto pressing and baling before trade transaction. In 1984-85 about 72 per cent of the installed capacity of this industry was utilised. The utilisation of installed capacity is assumed to increase to 80 per cent, 90 per cent and 90 per cent for the years 1989-90, 1994-95 and 1999-2000, respectively. The details about the production of jute, additional investment required, working capital required and the credit requirements for term loans for investment purpose and short term loans for working capital required for the years 1989-90, 1994-95 and 1999-2000, estimated by our consultants, are given in table 13. It is assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions, and the balance amount will be financed by banks.

Table 13
Projections of Investment and Credit Requirements of Jute and Mesta
Pressing and Baling Industry

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000 AD
Production of jute and mesta (Quantity in '000 tonnes)	1,626	1,931	2,349
Value of production	922	1,095	1,332
Installed capacity for pressing and baling (value)	1,152 (80)	1,215 (90)	1,478 (90)
Investment required	158	167	203
Additional Investment	6	9	36
Working capital (at 5 per cent of the value of raw materials)	97	115	140
Term loans-requirements	4	5	22
Of the above, term loans from banks	2	3	11
Short-term loans for working capital	48	57	70

Note : Figures in brackets show percentage utilisation of capacity.

Plantation crops

ix) Tea processing

24.36 India commands a premier position as the largest producer, consumer and exporter of tea with the phenomenal growth of over 60 per cent in the last two decades. In 1984, Indian tea production reached a level of 645 million kgs. from the level of 487 million kgs. in 1975. The domestic consumption of tea reached the level of 400 million kgs. in 1984. India will have to produce 1,000 million kgs. of tea by the year 2000 AD in order to maintain its share of 28 per cent in the world market.

24.37 The costs of modernisation and expansion of factories and other items by the year 1989-90 were assessed by the Tea Board at Rs.347 crores. It is assumed that term loan requirements will be about 60 per cent of the investment cost. Thus the total term loan requirement by the year 1989-90 would be Rs.208 crores. No further investment in the years 1994-95 and 1999-2000 is envisaged. It is assumed that the term loan requirements of tea processing units will be met by the specialised term lending institutions. The short-term credit requirements for tea processing units for the years 1989-90, 1994-95 and 1999-2000 are estimated at Rs.400 crores, Rs.440 crores and Rs.485 crores respectively, at 1984-85 prices.

x) Cashew processing industry

24.38 Cashew is one of the important foreign exchange earning agricultural commodities in India. The country had often depended on imports of raw nuts from East African countries and processed them in India. Up to mid 1960's, India imported 70 to 75 per cent of the total requirement of raw nuts and produced about 25 to 30 per cent domestically. During the period 1965 to 1978 the import of raw nuts dwindled from 160 thousand tonnes per year to 20 thousand tonnes per year. Since then domestic production has picked up. By 1983-84 about 210 thousand tonnes of raw nuts were produced in the country. The contribution of cashew crops to the total value of all crops varied between 0.13 and 0.85 per cent.

24.39 The processing of cashewnuts involves drying of raw nuts, roasting,

shelling, heating, peeling, grading and packing. The bye-products of cashew industry are the cashewnut shell liquid, tannins, acids and cashew apple products. Among the bye products, only cashewnut shell liquid is commercially exploited.

24.40 The investment in fixed capital of cashew processing units was about Rs.11 lakhs per unit in 1983-84. The installed capacity of these units could process 273 thousand tonnes of raw cashew kernels. More than one lakh workers are employed in this industry, with women constituting about 94 per cent of the work force.

24.41 The ratio of fixed capital to the value of raw material processed was 1 : 1.23. The value added by cashewnut processing was 38 per cent of the value of the finished product. Thus the value of raw material formed 62 per cent of the value of finished product. the working capital formed 20 per cent of the value of raw material.

24.42 It is assumed that (a) the share of cashewnut to the value of all crops would increase from 0.18 per cent in 1984-85 to 0.50 per cent in 1989-90, 0.75 per cent in 1994-95 and 1.0 per cent in 1999-2000, (b) there will be no imports of raw nuts in future and all domestic production will be processed and (c) the utilisation capacity of the factories would increase to 90 per cent by 1989-90 and would continue to operate at that level upto 1999-2000. The credit requirements for term loans for investment activity and short term loans for working capital requirements have been projected on the assumption that the margins at the rate of 40 per cent and 50 per cent respectively would be required. It is also assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions and the balance amount will be financed by banks. The details of the projections made by our consultants in respect of the value of raw cashewnuts, additional investment required, working capital required and credit required for investment activity and for working capital, for the years 1989-90, 1994-95 and 1999-2000 are given in table 14.

xi) **Rubber processing industry**

24.43 Although natural rubber forms more than 50 per cent of the raw material utilised in the industry, the value added to natural rubber, in the value of final

Table 14
Additional Investment and Credit Requirements for
Cashewnut Processing Industry

Items	(Rs. crores)		
	1989-90	1994-95	1999-2000 AD
Cashewnut - Raw material (value)	380	676	1,097
Installed capacity (value)	422	750	1,218
Required investment	309	547	889
Additional investment	199	239	342
Working capital (at 20 per cent of the value of raw material)	76	135	219
Term loans-requirements	119	143	205
Of the above, term loans from banks	60	72	103
Short-term loans for working capital	38	67	110

products, is more than 50 per cent. Hence we have not included this industry in agro-processing industries.

b) Agro processing industries based on wood

xii) Wood based industries

24.44 For the purpose of this study, only those wood based industries which fall under our definition of agro-based industries have been selected. These industries can be divided into the following five heads.

- (1) Manufacture of veneer, plywood and their products.
- (2) Sawing and planing of wood, other than plywood.
- (3) Manufacture of wooden and cane-boxes, crates, drums, barrels and other wooden containers, baskets and other ratten, bamboo, reed and willow wares made entirely or mainly of cane ratten, reed, bamboo and willow.
- (4) Manufacture of structural wooden goods (including treated timber) such as beams, posts, doors and windows.
- (5) Manufacture of wooden industrial goods, such as bobbins, logs, handles, sadding and similar equipments and fixtures.

24.45 The total number of wood-based factories in 1984-85 in the above list

amounted to 3,243. All of them were small units. The raw material utilised by these units was valued at Rs.261 crores. This formed only 7 per cent of the gross domestic product of the forestry sector. The working capital required by these units was Rs.101 crores.

24.46 It was observed that the gross domestic product of the forestry sector, both at constant and current prices, was declining. In the next 15 years, this trend will have to be reversed. If the gross domestic product (GDP) of forestry increased at the rate of 2 per cent per annum up to 1989-90, 3 per cent per annum during 1990-91 to 1994-95 and 5 per cent per annum during 1995-96 to 1999-2000, the value of G.D.P. of forestry would be Rs.3,930 crores, Rs.4,556 crores and Rs.5,815 crores during 1989-90, 1994-95 and 1999-2000 respectively, at 1984-85 prices. Assuming that the value of raw material of the wood-based industries formed 10 per cent of the value of G.D.P. of forestry, the value of raw materials to be processed by the wood-based industries during the years 1989-90, 1994-95 and 1999-2000 would be Rs.393 crores, Rs.456 crores and Rs.581 crores respectively. Based on the value of raw materials to be processed, the investments required for the years 1989-90, 1994-95 and 1999-2000 have been projected. The working capital requirements amounted to 39 per cent of the value of raw material. On this basis, the working capital requirements for the future years have been projected. It is assumed that the margin requirement would be 40 per cent and 50 per cent in respect of the term loans for investment purposes and short term loans for working capital requirement respectively. It is also assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions, and the balance amount will be financed by banks. On this basis the future credit requirements have been projected. The details of the projections made by our consultants, in respect of the investment required, working capital required and the term loans for investment purpose and short-term loans for working capital requirement, for the years 1989-90, 1994-95 and 1999-2000 are given in table 15.

c) **Agro processing industries based on livestock**

xiii) **Milk processing**

24.47 The annual milk production in India has more than doubled in the last 26 years from about 20.4 million tonnes in 1960-61 to 43.9 million tonnes in

Table 15
Credit Requirements for Woodbased Industries

Items	(Rs. crores)		
	1989-90	1994-95	1999-2000 AD
Investment required	130	150	192
Working Capital (at 39 per cent of the value of raw material)	153	178	226
Term loans-requirements	78	90	115
Of the above, term loans from banks	39	45	58
Short-term loans for working capital	76	89	113

1986-87. There are 250 milk processing units, in the public and co-operative sectors, with an installed capacity of processing of about 16 million litres of milk per day. They process about 12.4 million litres of milk per day. The capacity utilisation is about 77 per cent. The pattern of milk utilisation in India has not changed much during the last 35 years, except that the share of liquid milk has increased from 39 per cent in 1950-51 to 46 per cent in 1985-86 while that of ghee declined from 39 per cent in 1950-51 to 29 per cent in 1985-86.

24.48 At present, so far as the organised dairy is concerned, the financial requirements for investments are met from budgetary source, donations and their own resources. From the budgetary source, an amount of Rs.500 crores was provided in Seventh Five Year Plan. A portion of the amount gets invested in the infrastructural facilities for milk production. It is assumed that the budgetary provisions for the years 1994-95 and 1999-2000 would increase in proportion to the milk handled by the organised dairy sector.

24.49 On the basis of the trend in the pattern of milk utilisation, projections have been made by our consultants for the years 1989-90, 1994-95 and 1999-2000. The details are given in table 16.

Table 16
Pattern of Milk Utilisation in 1989-90, 1994-95 and 1999-2000 in India

Item	(Percentages)		
	1989-90	1994-95	1999-2000
Milk Procurement by organised dairies	10	15	25
Home consumption	25	25	25
Milk sold through unorganised sector	65	60	50
(a) as liquid Milk	30	28	23
(b) Sold as milk products	35	32	27

24.50 Using these patterns, the value of milk to be converted into milk products through the unorganised sector for different years has been estimated. It is assumed that this milk will be handled by the private sector. In order that credit can be given to these unorganised sectors, milk processing activities will have to become bankable enterprises. It is assumed that in future a substantial portion of milk handled by the unorganised sector will be covered by the bankable enterprises. The credit requirement for term loans for these investments has been worked out on the basis of margin money of 40 per cent. As processed milk will be sold immediately, no short-term credit may be required. The details in respect of the value of milk to be converted into milk products through unorganised sector, the value of milk products to be processed through organised bankable enterprises, the investment required and the term loans required, for the years 1989-90, 1994-95 and 1999-2000 are given in table 17.

Table 17

Investment and Credit Requirement for Milk and Milk Products

Items	(Rs.crores)		
	1989-90	1994-95	1999-2000
Value of output of livestock	19,307	23,468	29,628
Value of milk and milk products (66 per cent of above)	12,743	15,489	19,554
Value of milk to be converted into milk products through unorganised sector	4,460	4,956	5,280
Value of milk to be processed by small units in private sector, through bankable enterprises (at percentages indicated in the bracket)	1,115 (25)	1,487 (30)	2,112 (40)
Investment required for above (10 per cent of the value of milk)	112	149	211
Incremental investment required	23 (approx)	37	62
Term loans required	14	22	37

xiv) **Poultry processing**

24.51 The poultry processing is more or less an integrated business. No separate data are available for investment for poultry processing. As processing is integrated with production, the estimates of credit requirements for poultry could be construed to include credit requirements for processing. As the credit requirements for poultry have been included under the head titled credit requirements of

livestock in the projections made in an earlier chapter on demand for agricultural credit no separate estimates have been made in respect of credit requirements for poultry processing.

xv) **Leather industry**

24.52 In India the raw material for leather industry comprises hides and skins. According to a survey recently carried out by the Central Leather Research Institute (CLRI) Madras, about 22 million cattle hides, 16 million buffaloe hides, 75 million goat skins and more than 31 million sheep skins were produced in 1986. Out of the total production, 50 per cent of the bovine hides (cattle and buffaloes) represent fallen category, recovered from dead animals and mobilised from villages scattered all over the country.

24.53 One of the major constraints of leather industry relates to the lack of reliable information on vital aspects such as installed capacity and the actual capacity utilisation in tanning, footwear and leather product sectors. The working capital formed 16.37 per cent of the value of raw material processed.

24.54 Assuming that the proportion of value of hides and skins to the value of livestock would remain the same as in 1984-85, the value of output of hides and skins for the years 1989-90, 1994-95 and 1999-2000 has been worked out. On the basis of these projections, additional investments required have been estimated. The credit requirements for term loans for investment and short-term loans for working capital have been estimated on the assumption that the margin requirement would be 40 per cent and 50 per cent respectively. It is assumed that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions, and the balance amount will be financed by banks. The details of the projections made by our consultants, in respect of the additional investment required, working capital required and the credit required for the years 1989-90, 1994-95 and 1999-2000 are given in table 18.

xvi) **Wool cleaning, baling and pressing industry**

24.55 As in the case of cotton textiles, in the woollen textiles also, the stages upto the level of cleaning, baling and pressing alone have been included in the agro-processing industry. In 1983-84 the units dealing with these processes

for which data were available, were only 33. The installed capacity was utilised to the extent of 45 per cent only. The value added by the industry was 39.4 per cent. The ratio of the value of raw material to the fixed capital was 0.86. The proportion of the working capital to the value of raw material processed was 0.41.

Table 18
Additional Investment Required and the Credit Requirement for
Leather Tanning Industry

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000
Value of output of livestock sectors	19,307	23,468	29,628
Value of hides and skins (9 per cent of above)	1,738	2,112	2,666
Investment required	1,121	1,362	1,720
Additional investment required	163	241	358
Working capital (at 16.37 per cent of the value of raw material)	284	346	436
Credit requirements :			
Term loan requirements	98	145	215
Of the above, term loans from banks	49	73	108
Short-term loans for working capital	142	173	218

24.56 Assuming that the contribution of the value of output of wool and hair would remain the same in the years 1989-90, 1994-95 and 1999-2000, as in the year 1984-85, the value of output of wool and hair for these years was estimated from the projections of the value of output of livestock sector. Assuming again that margin of 40 per cent and 50 per cent will be required for term loans for investment and short-term loans for working capital requirements respectively, the credit requirements have been projected for the years 1989-90, 1994-95 and 1999-2000 AD. A further assumption made is that in respect of the term loan requirements, 50 per cent will be met by the specialised term lending institutions

and the balance amount will be financed by banks. The details of the projections made by our consultants, relating to the value of wool and hair, additional investment required, working capital required and the credit requirements for the years 1989-90, 1994-95 and 1999-2000 are given in table 19.

Table 19
Additional Investment in Wool Processing Industry and Credit Requirements

Item	(Rs. crores)		
	1989-90	1994-95	1999-2000
Value of output of livestock sector	19,307	23,468	29,628
Value of wool and hair (1 per cent)	193	235	296
Installed capacity	386	391	423
Utilisation of capacity (per cent)	50	60	70
Investment required	449	455	492
Additional investment required	23	6	37
Working capital (at 41 per cent of the raw material used)	79	96	121
Term loan requirements	14	4	22
Of the above, term loans from banks	7	2	11
Short-term loans for working capital	40	48	60

xvii) **Fish processing**

24.57 As very little processing is involved in respect of fish, both for domestic and export markets, the projections in respect of credit made for investments for marine and inland fishery for the years 1989-90, 1994-95 and 1999-2000, in an earlier chapter, would be adequate to take care of the credit needs for processing and marketing of fish. Hence no separate estimates are made for credit requirements for processing and marketing of marine and inland fishery.

24.58 The summary of credit requirement of agro-processing industries is given in table 20.

24.59 The term credit requirements estimated for the years 1989-90, 1994-95 and 1999-2000 are the cumulative requirements of term credit for five years ending those years. It will be necessary to work out the 'stock' position of

Table 20
Summary of Credit Requirements of Agro-Processing Industries

Agro-Processing Industries	(Rs. crores)								
	1989-90			1994-95			1999-2000		
	Term Loan	Short Term	Total	Term Loan	Short Term	Total	Term Loan	Short Term	Total
1. Paddy Processing	3	1,227	1,230	16	1,492	1,508	36	1,906	1,942
2. Wheat Processing	-	29	29	50	80	130	98	172	270
3. Pulse Processing	-	137	137	29	158	187	46	192	238
4. Edible Oil Industry	41	83	124	64	116	180	98	193	291
5. Sugar Industry	-	1,919	1,919	-	2,286	2,286	-	2,817	2,817
6. Fruits & Vegetables Processing	24	32	56	42	64	106	96	155	251
7. Cotton Ginning & Pressing	23	238	261	50	303	353	141	405	546
8. Jute Pressing & Baling	2	48	50	3	57	60	11	70	81
9. Tea Processing	-	400	400	-	440	440	-	485	485
10. Cashewnut Processing	60	38	98	72	67	139	103	110	213
Agro-Processing based on Crop Production (Sub-Total)	153	4,151	4,304	326	5,063	5,389	629	6,505	7,134
11. Agro-Processing based on Wood	39	76	115	45	89	134	58	113	171
12. Milk Processing	14	-	14	22	-	22	37	-	37
13. Leather Industry	49	142	191	73	173	246	108	218	326
14. Wool Processing	7	40	47	2	48	50	11	60	71
Agro-Processing based on Livestock Production (Sub-Total)	70	182	252	97	221	318	156	278	434
Total of Agro-Processing Industries	262	4,409	4,671	468	5,373	5,841	843	6,896	7,739
Food Processing Industries (Sub-Total)@	142	3,465	3,607	295	4,263	4,558	514	5,545	6,059
Non-Food Processing Industries (Sub-Total)@@	120	944	1,064	173	1,110	1,283	329	1,351	1,680

@ Sub-total of Sr. Nos. 1 to 6, 10 and 12.

@@ Sub-total of Sr. Nos. 7, 8, 9, 11, 13 and 14.

Note : The projections are made at constant prices (1984-85 prices).

the cumulative term credit requirements for five consecutive years as at the end of the fifth year. For this purpose we have adopted the same methodology for arriving at outstandings, as in the case of the term credit requirements of forestry, indicated in table 53 at paragraph 22.92 in the chapter titled 'Demand for Agricultural Credit : Projections'. The details are given at table 21.

Table 21
Term Loans for Agro-Processing Industries - Stock (Outstanding)

(Rs. crores)
(At 1984-85 prices)

Year	Term credit requirements for five consecutive years ending the year	Ratio for conversion of (2) to stock (outstanding)	Balance outstanding as at the end of the year
(1)	(2)	(3)	(4)
1989-90	262		244
1994-95	468	1:0.93	435
1999-2000	843		784

(B) Storage, Transportation and Marketing

24.60 In this analysis, the credit requirements of the wholesale trade, in the private sector, in agricultural commodities, for marketing (including transportation) and storage, for the years 1989-90, 1994-95 and 1999-2000 have been projected. This analysis covers the credit requirements of the private wholesale trade in foodgrains (i.e. rice, wheat, pulses and other cereals), cotton, raw jute and mesta and sugar.

i) Food grains

24.61 In assessing the financial requirements of the private wholesale trade in foodgrains, it is necessary to look into the cost of marketing and the time pattern of marketing. This analysis is confined to the movement of foodgrains from their arrival into the wholesale market to the point of reaching the retail trader for distribution to the consumers or for export. As a first step, the cost incurred by the wholesale traders for different commodities has been estimated. The cost includes purchase price of the produce, cost of handling, packaging, transporting, grading, storage, etc. Only very scanty data are available on marke-

ting cost of foodgrains in the country. The Market Research and Planning Cell of the Directorate of Marketing and Inspection had undertaken a study on marketing costs and margins of major commodities in the country, at the instance of the Food and Agricultural Organisation of the United Nations. The study data related to the year 1982-83. For the purpose of this analysis, the costs estimates for various stages of trade channels of selected commodities have been brought to the level of 1984-85 prices, by using the wholesale price index of the concerned commodity. The details are given in table 22.

Table 22
Marketing Price and Cost of Selected Commodities

(Value in Rupees)								
Commodity	Year	Price of Commodity+	Transport cost	Storage cost	Physical losses	Others (Loading, unloading, fixed cost etc.)	Total cost	Total purchase price
Wheat	1982-83	1,745	78.4	15.0	5.6	94.2	193	1,938 (1,897)
Rice	1982-83	2,638	50.3	3.1	5.0	41.0	100	2,738 (2,913)
Total Pulses	1984	2,635					142	2,777
Jowar	1984	1,550.7						
Bajra	1984	1,517.1					103	1,637

Figures in the bracket give 1984 prices for the respective commodity.

Note : + Local assembling traders' selling price to wholesaler.

* Other cereals.

Source : Market Research and Planning Cell, Directorate of Marketing & Inspection, Ministry of Rural Development, Government of India.

24.62 Most of the wholesale traders in private sector deal in more than one commodity, so as to spread out their storage and establishment costs. The lean period of one commodity will coincide with the peak period of another commodity. By the time wheat and pulses purchases are likely to taper off, the rice purchases will commence in a peak way. The concept of peak and lean seasons is likely to wane with increase in multiple cropping and also due to the increase in the waiting capacity of the producers. A part of the storage problem has now shifted from the procurer to the producer.

24.63 It is assumed that the role of public agencies in procurement, for building up buffer stocks and for moderating the price fluctuations through public distribution system, would decrease gradually. The projections in respect of the share of private trade have been made for the years 1989-90, 1994-95 and 1999-2000 AD, based on the projections of estimated production of the various commodities. The details are given in table 23.

Table 23
Projected Private Trade in Foodgrains Production

Commodities	('000 tonnes)			
	1984-85 Base period	1989-90	1994-95	1999-2000
Wheat	(8.4)	(12) 6,749	(15) 11,291	(20) 20,627
Rice	(19.30)	(25) 16,504	(30) 24,095	(35) 35,875
Pulses	(34.73)	(35) 4,551	(40) 6,030	(45) 8,252
Other Cereals	(11.22)	(12) 4,031	(15) 5,563	(20) 8,599

Note : Figures in brackets relate to the share of private trade.
1984-85 - Figures of share are based on actual position.
For rest of the years they are according to the projections made.

24.64 The trade in foodgrains is subject to selective credit control by the Reserve Bank of India. The stipulations of the conditions vary from time to time depending upon the contingencies. The short-term credit requirements of the private trade have been assessed at one month's financial requirements. The details in respect of the financial requirements and the short-term credit requirements, as estimated by our consultants, for the years 1989-90, 1994-95 and 1999-2000 are given in table 24.

24.65 For meeting the needs of additional handling on account of increase in the share of private trade, it would be necessary to create additional storage capacity. The storage capacity created in villages has become handy for the producers in spreading the market arrivals over a longer period, thereby earning better prices. The producers have thus taken a part of the storage cost portion

Table 24

Projected Financial and Short-Term Credit Requirements of Private Trade

Commodities	(Rs. crores)					
	1989-90		1994-95		1999-2000	
	Financial requirements	Credit requirements (1 month)	Financial requirements	Credit requirements (1 month)	Financial requirements	Credit requirements (1 month)
Wheat	1,280	107	2,142	178	3,913	326
Rice	4,808	401	7,019	585	10,451	871
Pulses	1,264	105	1,674	139	2,291	191
Other Cereals	660	55	911	76	1,408	117
Total	8,012	668	11,746	978	18,063	1,505

from the traders. The traders are also increasingly utilising the storage capacity available in public sector. The details about commoditywise quantum to be stored are given in table 25.

Table 25

Quantum of Stocks (Private Trade) to be Stored

Commodities	('000 tonnes)		
	1989-90	1994-95	1999-2000
Wheat	3,043	4,542	9,336
Rice	5,243	7,591	11,783
Pulses	462	1,479	2,222
Other Cereals	533	1,532	3,036

24.66 The investment requirements towards the additional storage capacity are worked out on the basis of Rs.500 per metric tonne in terms of 1984-85 prices. The requirement for the additional storage capacity is kept at 75 per cent of the trade requirements, assuming that 25 per cent of the provision for storage would be made by hiring public storage capacity. The credit requirements for investment are worked out at 60 per cent of the investment costs, based on margin of 40 per cent to be borne from own resources of the traders. The projected term credit requirements work out to Rs.208 crores, Rs.340 crores and Rs.593 crores for the years 1989-90, 1994-95 and 1999-2000 AD respectively. The details, including the cropwise break-down, as estimated by our consultants, are given in table 26.

Table 26
Financial/Credit Requirements for Storage Capacity by Private Trade

Commodities	(Rs. crores)					
	1989-90		1994-95		1999-2000	
	Financial requirements	Credit requirements	Financial requirements	Credit requirements	Financial requirements	Credit requirements
Wheat	114	68	170	102	350	210
Rice	196	118	284	170	442	265
Pulses	17	10	55	33	83	50
Other Cereals	20	12	58	35	114	68
Total	347	208	567	340	989	593

ii) **Cotton and kapas**

24.67 There are three types of agencies operating in cotton trade, viz., the Cotton Corporation of India (CCI), co-operatives and the private trade. In Maharashtra, there is monopoly procurement of cotton, through the State Co-operative Cotton Growers' Federation. The proportion of private trade in cotton, to the total trade in cotton, amounted to 66.63 per cent for the 10 year period ended 1984-85. It is assumed that the share of private trade in cotton will increase to 70, 75 and 80 per cent in 1989-90, 1994-95 and 1999-2000 AD respectively.

24.68 The financial requirements of the private trade have been estimated on the basis of the total purchase price (i.e. purchase price plus marketing costs). After projecting production of cotton for the years 1989-90, 1994-95 and 1999-2000 and based on the share of private agencies in the total cotton trade, as estimated earlier, the financial requirements have been projected. The credit requirements have been worked out on the basis of 45 per cent margin. The details of financial requirements and credit requirements for the years 1989-90, 1994-95 and 1999-2000, estimated by our consultants are given in table 27.

Table 27
Projected Financial and Short-Term Credit Requirements
for Private Trade in Cotton

Year	(Rs. crores)	
	Financial requirements	Credit requirements with 45 per cent margin
1989-90	787	433
1994-95	1,077	592
1999-2000	1,538	846

iii) **Jute**

24.69 Most of the jute growers are small farmers. The regulated markets for raw jute have not been developed in the jute producing areas. The private trade accounted for about 90 per cent of the total trading in jute. The Jute Corporation of India Ltd. (JCI) accounts for only about 10 per cent of the total trading in jute.

24.70 In view of the non-availability of detailed data, the purchase price and marketing costs of the commercial operations of JCI have been adopted for arriving at the financial requirements. The financial requirements for the jute trade for the years 1989-90, 1994-95 and 1999-2000 have been projected on the basis of the projected production of jute and the share of private trade at 90 per cent. The credit requirements have been projected with 60 per cent margin requirement. The details in respect of financial requirements and the short term credit requirements for 1989-90, 1994-95 and 1999-2000, as estimated by our consultants, are given in table 28.

Table 28
Projections of Short-term Credit Requirements for Private Trade in
Raw Jute/Mesta

Year	Financial Requirements	(Rs. crores)
		Credit Requirements with 60 per cent margin
1989-90	486	194
1994-95	576	230
1999-2000	702	281

iv) **Sugar**

24.71 Since sugar is an essential commodity, the government has imposed number of conditions and restrictions on the private trade in sugar. As a matter of government policy, private trade in sugar is restricted to the free sale component. The share of private trade in sugar for the years 1980-81 to 1984-85 amounted to 35 per cent of the production of sugar. It is assumed that the free sale of sugar will increase to 60 per cent, 70 per cent and 75 per cent of the total production of sugar by the years, 1989-90, 1994-95 and 1999-2000 respectively. It is assumed that the production of sugar would increase at 3 per cent,

3.5 per cent. and 4 per cent per annum (i.e. at the same growth rate as that of sugarcane), for the periods 1984-85 to 1989-90, 1990-91 to 1994-95 and 1995-96 to 1999-2000 respectively. On these assumptions and based on the cost of sugar (purchase price plus handling charges), the financial requirements have been projected. The credit requirements have been projected on the assumption that margin requirement would be 45 per cent. The details of the projections made by our consultants in respect of financial requirements and credit requirements for the years 1989-90, 1994-95 and 1999-2000 are given in table 29.

Table 29
Projected Short-term Credit Requirements

Year	Financial requirements	Credit requirements with 45 per cent margin
1989-90	1,578	868
1994-95	2,187	1,203
1999-2000	2,854	1,570

24.72 A summary of credit requirements for marketing and storage is given at table 30.

24.73 The short-term credit requirements estimated for the years 1989-90, 1994-95 and 1999-2000 are the total requirements of short-term credit for those years. Hence the requirements as indicated in table 30 are outstandings and not the disbursements during that year.

24.74 The term credit requirements estimated for storage for the years 1989-90, 1994-95 and 1999-2000 are the cumulative requirements of term credit for five years. To express the cumulative credit requirements in terms of outstandings, we have adopted the same methodology used in respect of term loan requirements for agro-processing industries. The details are given at table 31.

(C) Export of Agricultural Produce

24.75 Looking to the scenario of world trade, the performance of agricultural exports from India for the period 1970-71 to 1980-81 has been reviewed. The details about India's share in world exports in respect of food articles and raw materials are given in table 32.

Table 30
Summary of Credit Requirements for Marketing and Storage

Commodity	1989-90	1994-95	1999-2000
(Rs. crores)			
A. Short-term credit requirements			
1. Foodgrains			
i) Rice	401	585	871
ii) Wheat	107	178	326
iii) Pulses	105	139	191
iv) Other Cereals	55	76	117
Sub Total	668	978	1,505
2. Cotton	433	592	846
3. Raw Jute and Mesta	194	230	281
4. Sugar	868	1,203	1,570
Sub Total	1,495	2,025	2,697
Total	2,163	3,003	4,202
B. Term Credit Requirements			
Storage	208	340	593

Table 31
Term Loans for Storage

Year	Term credit requirements for five consecutive years ending the year	Ratio for conversion of (2) to stock (outstandings)	Balance outstanding as at the end of the year
(1)	(2)	(3)	(4)
1989-90	208		193
1994-95	340		316
1999-2000	593		551

Table 32
India's Share in World Exports as Percentage

	1970-71	1975-76	1980-81
Food			
Tea	28.19	28.47	27.88
Coffee	0.96	1.68	2.22
Sugar	0.94	5.00	0.18
Rice	0.46	0.39	3.25
Pepper	24.16	20.14	16.82
Cashew Kernels	69.03	62.71	NA
Raw Materials			
Tobacco	3.29	4.71	3.91
Raw Cotton	0.22	0.51	1.65
Raw Jute	4.11	3.27	4.43
Oil Cakes	7.74	5.03	3.45

Source : FAO Trade Year Book - Different Issues.

24.76 It will be observed from the above that India still occupies a predominant position in three commodities, viz., cashew kernels, tea and pepper, though the shares are falling over a time. Though coffee and rice occupied very low position initially, there has been a substantial increase in their shares. Among the raw materials, the share of tobacco has been fairly stable. The share of oil cakes has been showing a declining trend.

24.77 The most fundamental factor that determines the volume of exports is the quantity of its domestic production. The quantity of export also depends on the level of domestic consumption, i.e. the ratio of consumption to domestic production. This determines the pull of domestic market. Domestic consumption of food items is assumed to be governed by domestic real income and is expected to increase according to the income elasticities of respective items. Similarly, domestic use of raw materials is assumed to depend on the domestic production activity using the raw material as an input.

24.78 The details about the share of agricultural exports in total exports over a time are given in table 33.

Table 33
Share of Agricultural Exports in India's Total Exports

Year	Export of Selected Agricultural Commodities	Total Exports from India	(Rs. crores)
			Share of Agricultural Export to Total Exports
1965-66	335	806	41.6
1970-71	565	1,535	36.8
1971-72	585	1,609	36.4
1972-73	751	1,971	38.1
1973-74	1,007	2,523	39.9
1974-75	1,401	3,329	42.1
1975-76	1,685	4,042	41.9
1976-77	1,890	5,142	35.0
1977-78	2,000	5,408	37.0
1978-79	1,903	5,725	33.2
1979-80	2,238	6,418	34.9
1980-81	2,376	6,683	35.5
1981-82	2,623	7,806	33.6
1982-83	2,643	8,803	30.0
1983-84	2,819	9,771	28.9

Source : Monthly Statistics of Foreign Trade of India, Vol. I & II, Department of Commercial Intelligence and Statistics, Calcutta.

It will be observed from the table that agricultural exports are slowly losing ground to non-agricultural exports in value terms.

24.79 The details about the classification of the agricultural exports into two broad categories, viz., food articles and non-food articles are given at table 34.

Table 34
Classification of Agricultural Exports

	(Rs. crores)		
	1974-75	1979-80	1983-84
Food articles	989 (70.55)	1,512 (70.15)	1,956 (69.38)
Non-Food articles	413 (29.45)	677 (29.85)	863 (30.62)

Source : Directorate of Economics & Statistics, Agriculture in Brief, 21 Edition, Department of Agriculture and Co-operation, Ministry of Agriculture, New Delhi.

24.80 It will be observed from the table that the composition does not show much variation over a period (1974-75 to 1983-84). It may be mentioned that among the food articles, the traditional exports, viz., coffee, tea, cocoa and spices continue to have the major share. The shares of non-traditional items like meat and meat preparations, dairy products and eggs, fish and fish preparations, fruits and vegetables are also substantial and in most of the cases consistently increasing. Among non-food or raw material groups, the major share is that of feed stuff for animals, textile fabrics, dyeing, canning and colouring materials.

24.81 For the purpose of these projections, the export of agricultural commodities has been confined to 11 commodities, viz., tea, coffee, sugar, rice, black pepper/spices condiments, cashew kernels, processed food and vegetables, tobacco, raw cotton, raw jute and marine products.

24.82 For working out the value of export component, the wholesale price of the concerned commodity for the base year (i.e. 1984-85) was used. The value of projected exports of the 11 commodities has been worked out, by our consultants, by projecting the value of production of those commodities and applying the export component in the production of each of these commodities. The details in respect of value of projected exports are given in table 35.

24.83 The projected value of agricultural exports for the different years can be construed as the total short-term credit requirements for export of agricultural commodities for those years. It may be incidentally mentioned that in respect of commodities for which marketing credit is projected, if a part of those commodities is exported, there may be overlapping in respect of marketing credit projected and the export credit projected. However, the value of overlap will be negligible as compared to the total projected amount.

24.84 The summary of projections, in respect of credit requirements for agro-processing industries, marketing and storage and export of agricultural produce, is given in table 36.

Table 35

Projected Credit Requirements for Exports of Selected Agricultural Commodities

Commodity	(Rs. crores) (At 1984-85 prices)		
	1989-90	1994-95	1999-2000
Tea	206	220	220
Coffee	218	233	234
Sugar	16	19	23
Rice	169	205	262
Other spices & condiments	781	833	836
Cashewnuts	57	61	61
Tobacco	204	218	219
Cotton	183	233	312
Raw Jute	218	259	315
Processed Fruits & Vegetables	123	290	695
Marine Products	400	458	517
Total	2,575	3,029	3,694

Table 36

Summary of Projection of Demand for Credit in Respect of Certain Sectors Related to Agriculture

Sector	(Rs. crores) (At 1984-85 prices)								
	1989-90			1994-95			1999-2000		
	S.T.	Term	Total	S.T.	Term	Total	S.T.	Term	Total
Agro-processing Industries	4,409	244	4,653	5,373	435	5,808	6,896	784	7,680
Marketing (including transportation) and storage	2,163	193	2,356	3,003	316	3,319	4,202	551	4,753
Agricultural exports	2,575	-	2,575	3,029	-	3,029	3,694	-	3,694
Total	9,147	437	9,584	11,405	751	12,156	14,792	1,335	16,127

S.T. = Short-term credit

Term = Medium and long-term credit.

24.85 These projections have been made at 1984-85 prices. The credit requirements are likely to increase on account of the increase in prices. Hence we

have attempted to work out the estimates of the credit requirements at current prices also. We have, for the purpose of this exercise, assumed the inflation impact on demand for credit at 5.0 per cent per annum and worked out the credit requirements. The details of the projections are given in table 37. It may, however, be added that the rate used here should not be presumed to be the annual inflation during the next ten to fifteen years, but represents only the assumption of the impact of inflation during that period on the demand for credit. It will be observed that the total credit requirements by the end of June 2,000 in respect of the sectors related to agriculture will increase from Rs.16,127 crores at 1984-85 prices to Rs.33,527 crores, assuming increase in credit requirements at 5.0 per cent per annum. The credit requirements of these sectors will be met, mainly by the commercial banks and partly by the co-operative banks, out of their resources for non-agricultural advances.

Table 37
Summary of Projection of Demand for Credit in respect of Certain Sectors Related to Agriculture, Taking into Account the Increase in Prices

Sector	(Rs. crores)								
	1989-90			1994-95			1999-2000		
	S.T.	Term	Total	S.T.	Term	Total	S.T.	Term	Total
Assuming increase in credit requirements at 5.0 per cent per annum on account of increase in prices									
Agro-processing Industries	5,627	311	5,938	8,752	709	9,461	14,336	1,630	15,966
Marketing (including transportation) and storage	2,761	246	3,007	4,892	515	5,407	8,736	1,145	9,881
Agricultural exports	3,286	-	3,286	4,934	-	4,934	7,680	-	7,680
Total	11,674	557	12,231	18,578	1,224	19,802	30,752	2,775	33,527

S.T. = Short-term credit

Term = Medium and long-term credit

24.86 In the chapter on 'Supply of Agricultural Credit : Estimates of Resources', the deposits and the credit deposit ratios of commercial banks, as at the end of June 1990, 1995 and 2000 have been projected. Based on these, the total outstanding advances of commercial banks would be as shown in table 38.

Table 38
Commercial Banks - Projected Total Advances

As at the end of June	Deposits	Credit deposit ratio (Per cent)	(Rs. crores)
			Advances (Outstanding)
1990	1,71,967	58	99,741
1995	3,45,826	55	1,90,204
2000	6,09,345	52	3,16,859

24.87 Presuming that the entire demand for credit for agro-processing industries, marketing and storage and the agricultural exports, summarised in tables 36 and 37, is to be met by commercial banks alone, the shares of these sectors in the total outstanding advances as at the end of June 1990, 1995 and 2000 would be as indicated in table 39.

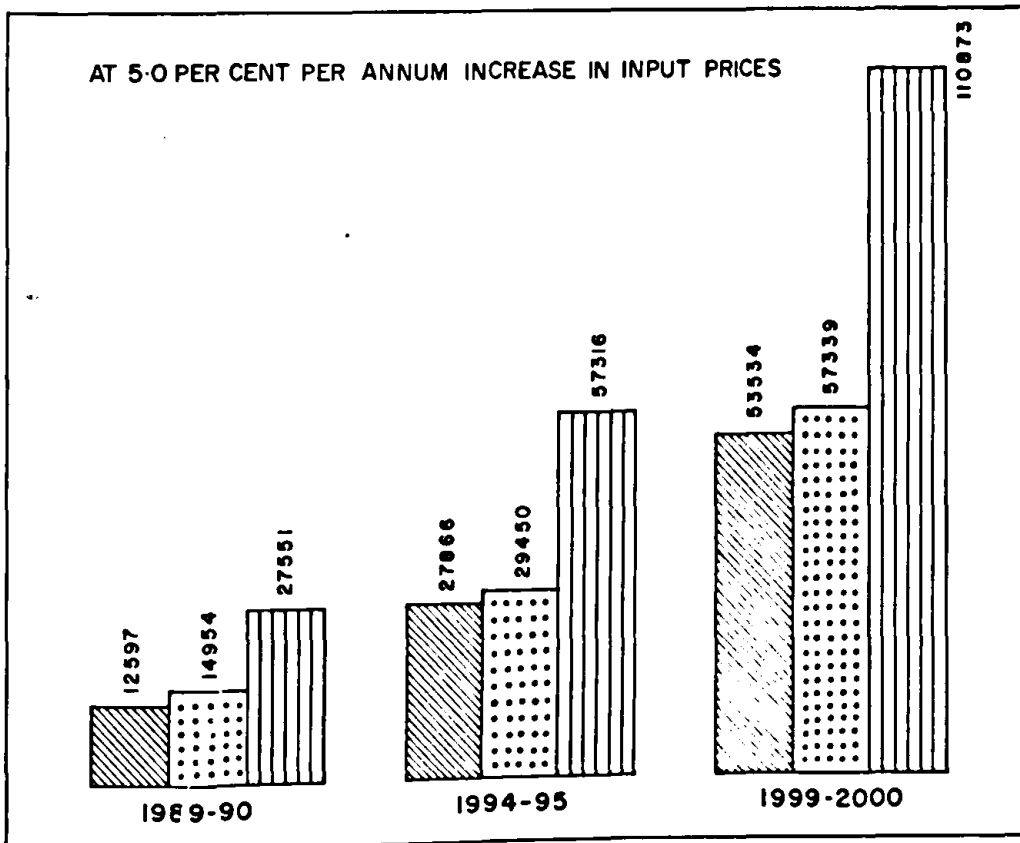
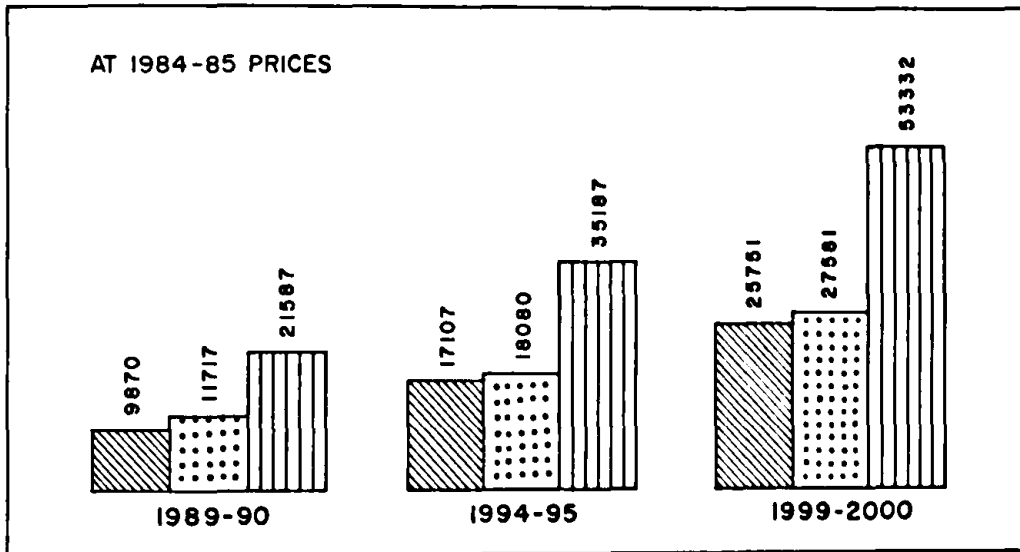
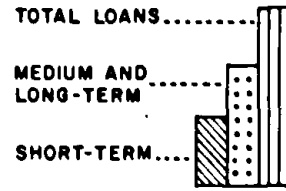
Table 39
Commercial Banks - Percentage Share of Agro-processing, Marketing and Agricultural Exports in the Total Advances Outstanding

Sector	At 1984-85 prices			Assuming increase in credit requirements at 5.0 per cent per annum on account of increase in prices		
	As at the end of June			As at the end of June		
	1990	1995	2000	1990	1995	2000
Agro-processing industries	4.67	3.05	2.42	5.95	4.97	5.04
Marketing (including transportation) and storage of agricultural produce	2.36	1.75	1.50	3.02	2.84	3.12
Agricultural exports	2.58	1.59	1.17	3.29	2.59	2.42
Total	9.61	6.39	5.09	12.26	10.40	10.58

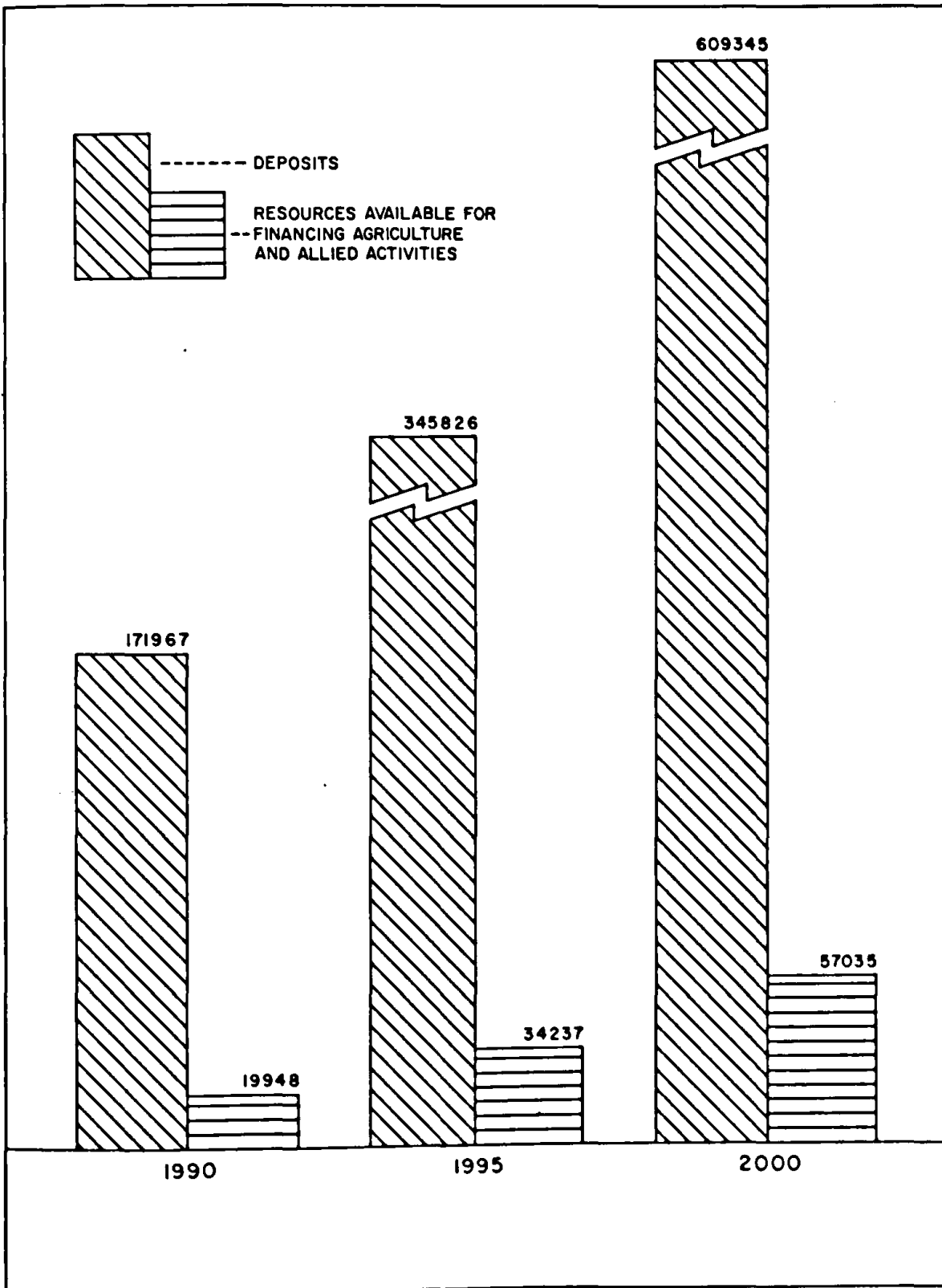
24.88 It will be observed from table 39 that the shares of the agro-processing industries, marketing and storage of agricultural produce and the agricultural exports, in the total outstanding advances of commercial banks would not be

unreasonably high at 10.58 per cent as against 18 per cent assumed for agriculture. These two sectors together will account for about 29 per cent of the commercial banks' total loans and advances, as at the end of June 2000, leaving a little over 71 per cent for other loans and advances including trade, commerce, industry and other priority sectors. Further, it may be mentioned that the actual share of these sectors relating to the forward linkages of agricultural production, in the total outstanding advances of commercial banks would be lower, as the demand for credit by these sectors would be met partly by the co-operative banks.

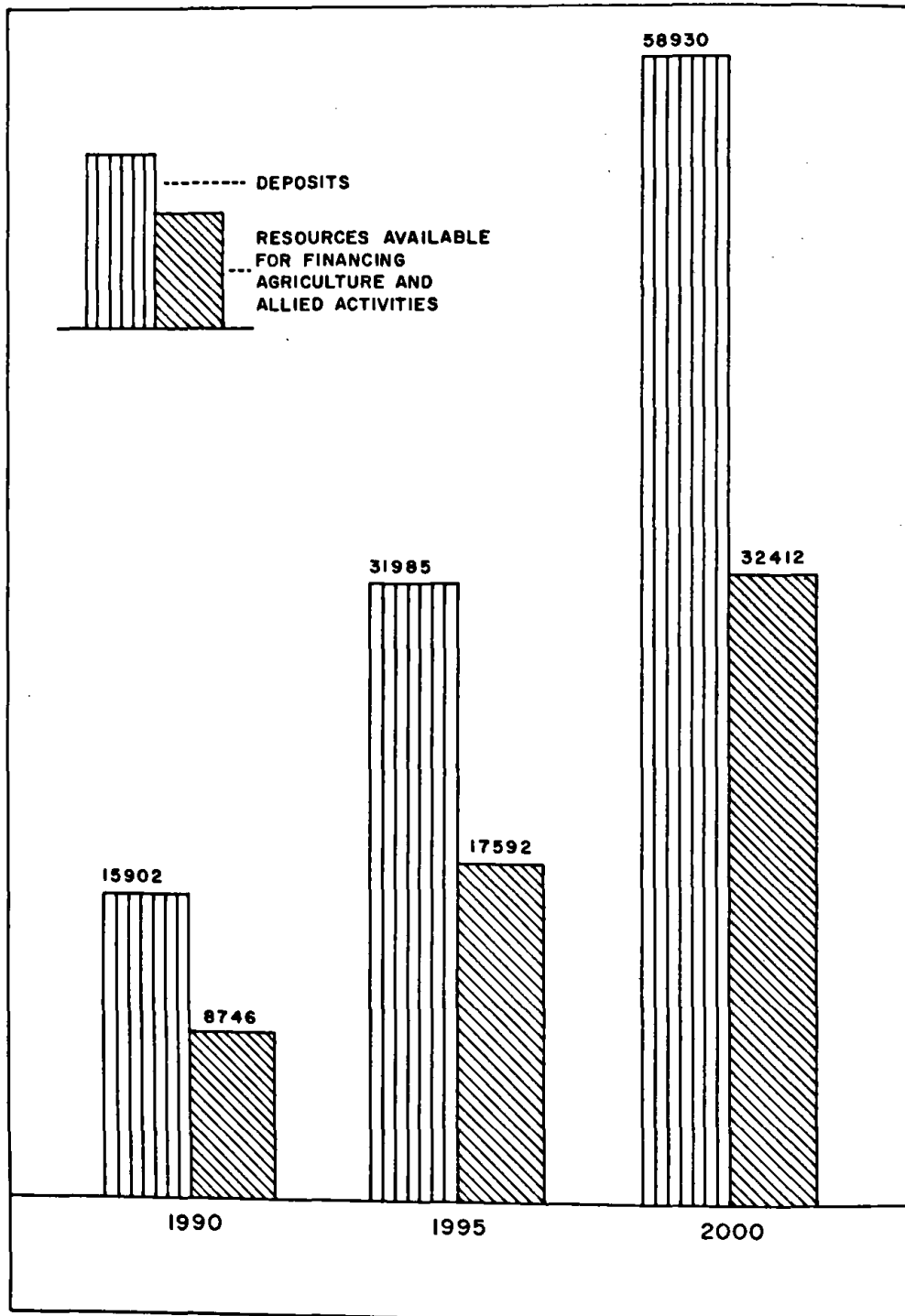
**DEMAND FOR CREDIT FOR
AGRICULTURAL PRODUCTION SUB-SYSTEM
AND AGRICULTURAL INPUT
DISTRIBUTION SUB-SYSTEM**
(RS.CRORES)



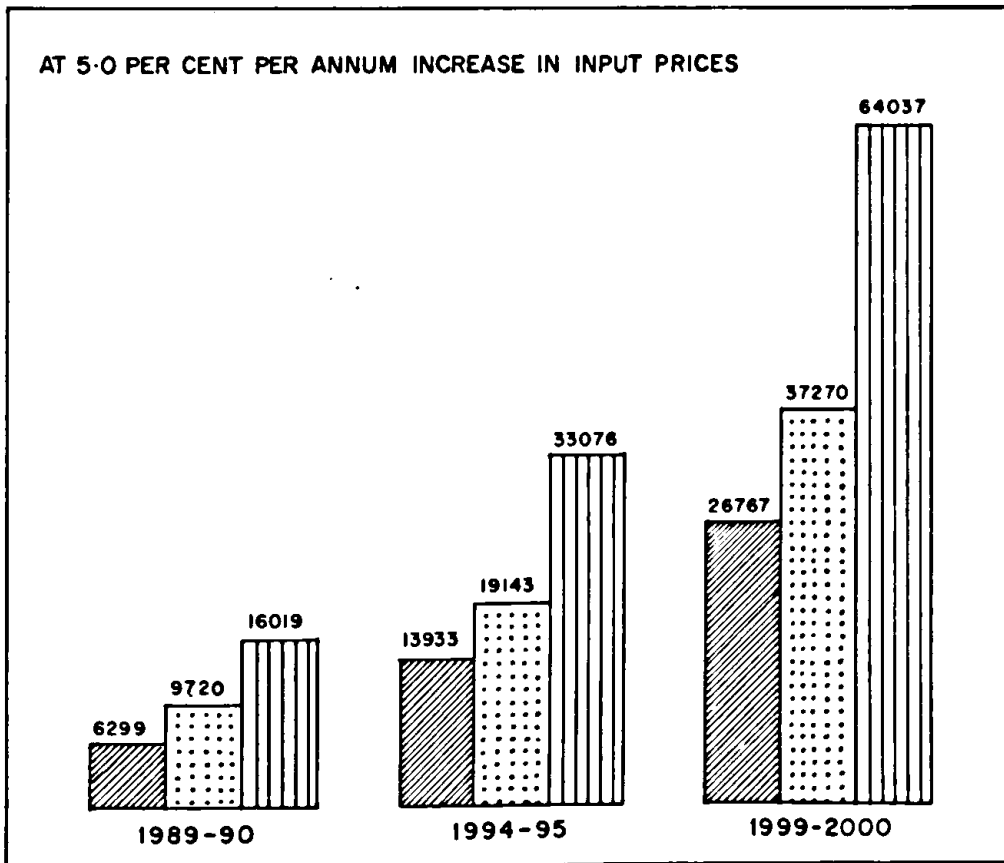
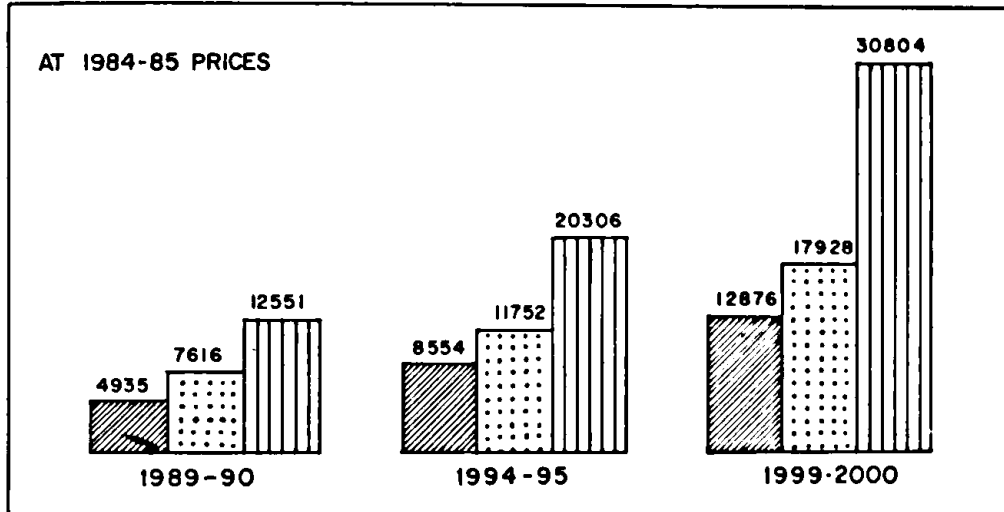
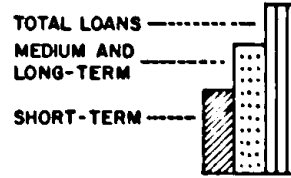
DEPOSITS OF COMMERCIAL BANKS AND THE RESOURCES AVAILABLE FOR FINANCING AGRICULTURE AND ALLIED ACTIVITIES
(AS AT THE END OF JUNE) (Rs. CRORES)



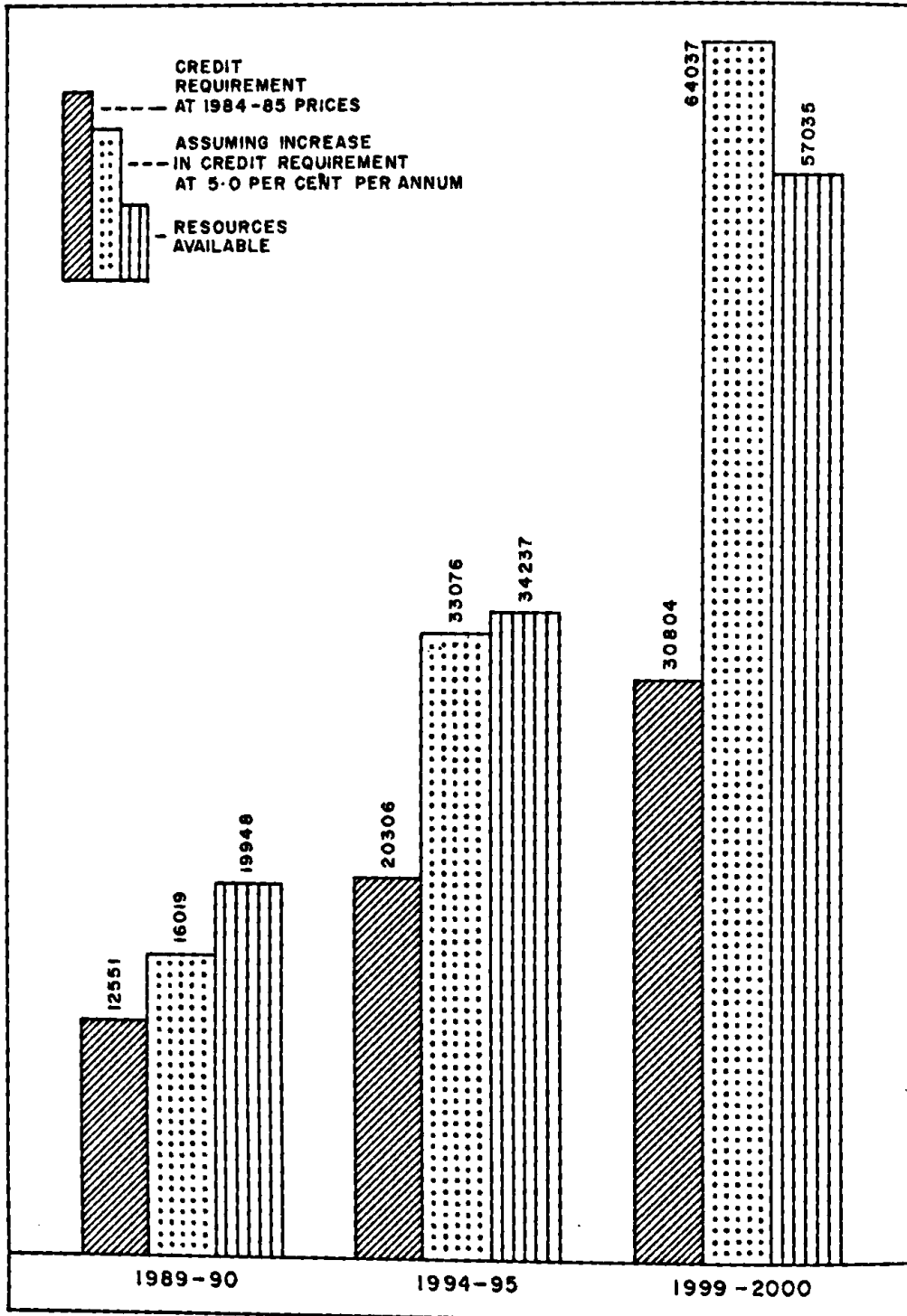
DEPOSITS OF CO-OPERATIVE CREDIT INSTITUTIONS
AND THE RESOURCES AVAILABLE FOR FINANCING
AGRICULTURE AND ALLIED ACTIVITIES
(AS AT THE END OF JUNE) (RS. CRORES)



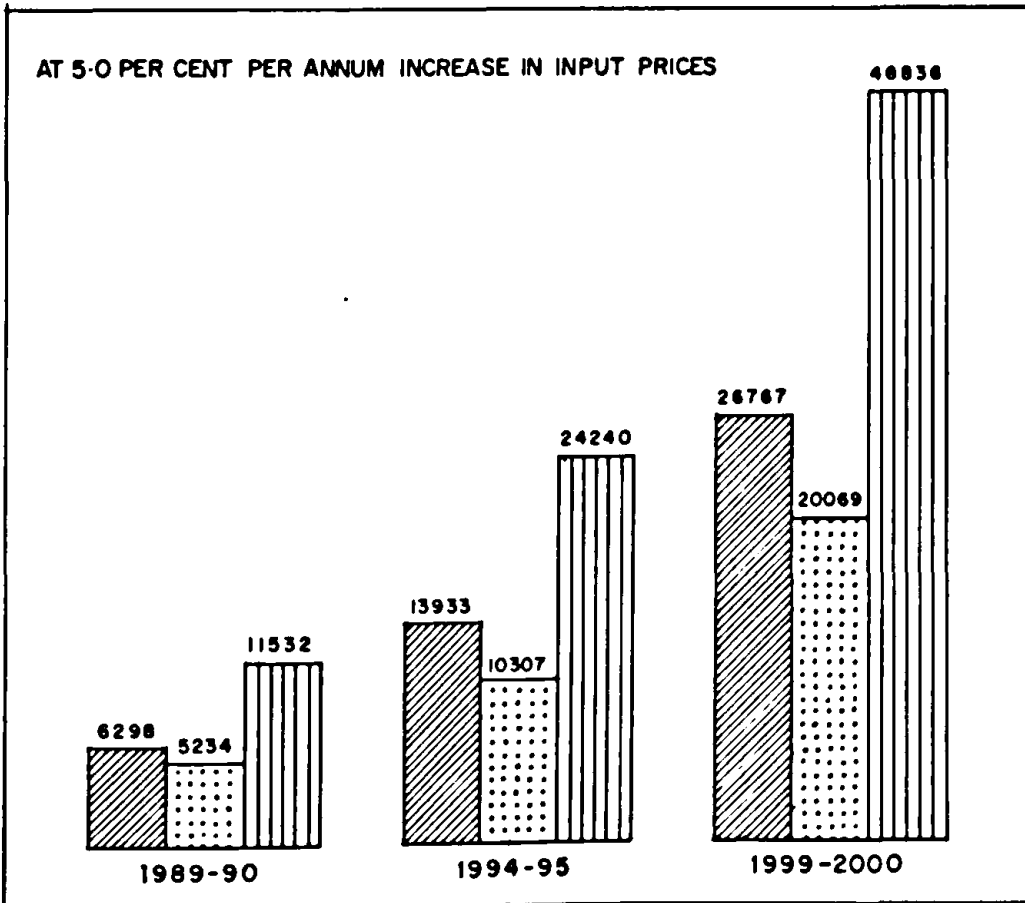
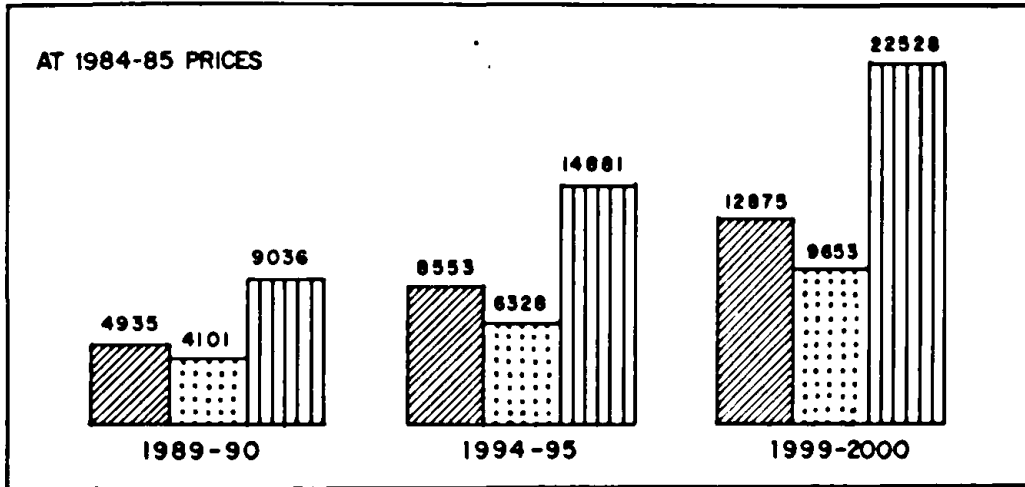
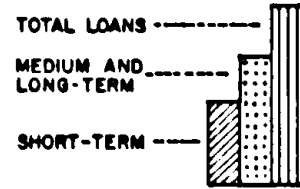
PROJECTED DEMAND FOR CREDIT
FROM COMMERCIAL BANKS
FOR FINANCING AGRICULTURE AND
ALLIED ACTIVITIES
(APS AND AID)
(RS. CRORES)



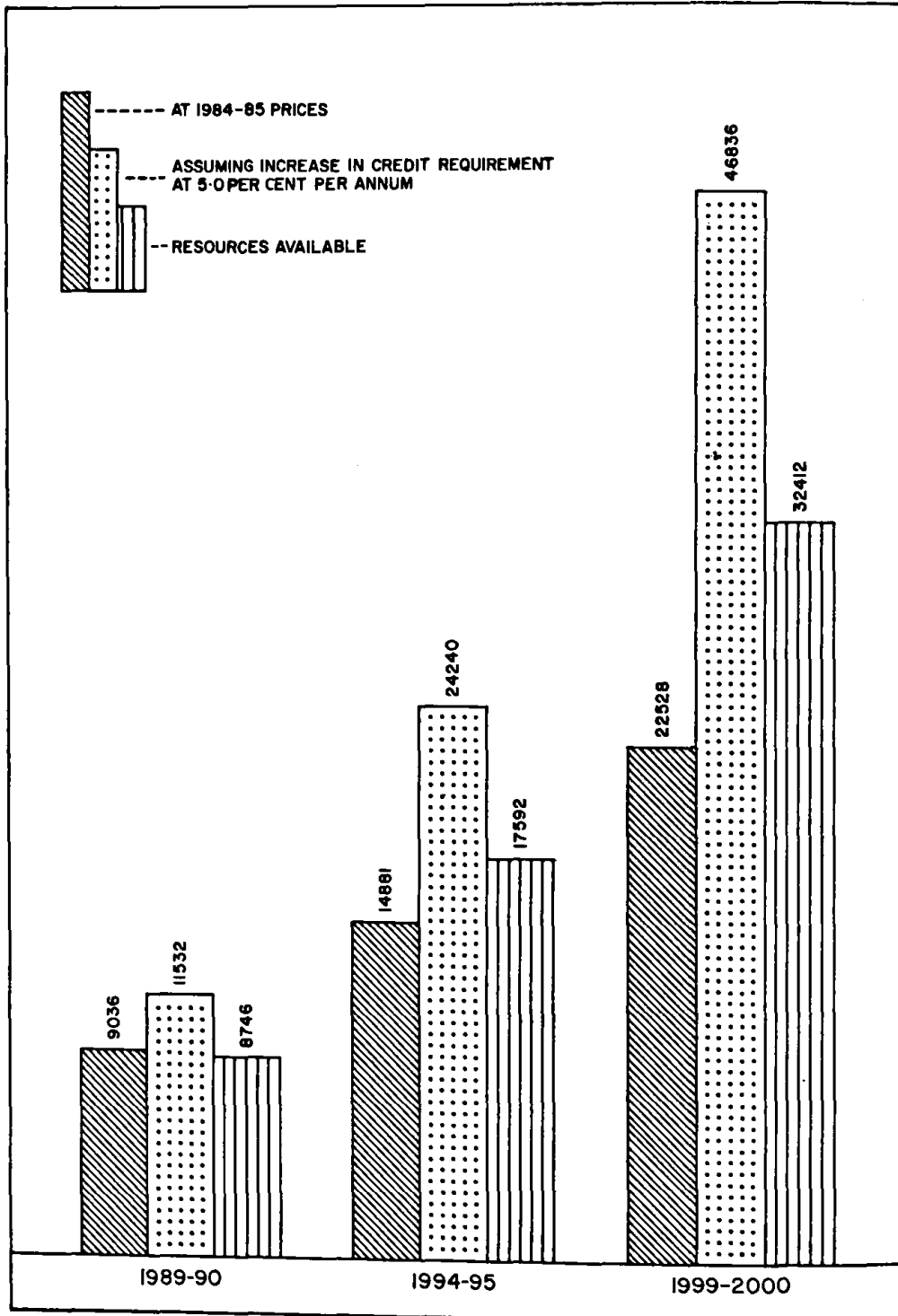
PROJECTED DEMAND FOR CREDIT AND AVAILABLE
RESOURCES OF COMMERCIAL BANKS FOR
FINANCING AGRICULTURE AND ALLIED
ACTIVITIES (APS AND AID)
(Rs. CRORES)



PROJECTED DEMAND FOR CREDIT
FROM CO-OPERATIVE CREDIT INSTITUTIONS
FOR FINANCING AGRICULTURE AND
ALLIED ACTIVITIES
(APS AND AID)
(RS. CRORES)



PROJECTED DEMAND FOR CREDIT AND AVAILABLE
RESOURCES OF CO-OPERATIVE CREDIT INSTITUTIONS
FOR FINANCING AGRICULTURE AND ALLIED ACTIVITIES (APS AND AID)
(Rs. CRORES)



PART X

SUMMARY AND RECOMMENDATIONS

A SUMMARY OF THE REPORT

ACTION POINTS ON THE RECOMMENDATIONS

APPENDIXES

A SUMMARY OF THE REPORT

Chapter I : The Report - An Overview

1. The problems of Indian rural financial market, the key messages of the report, and suggestions for systemic improvements are briefly summarised in this chapter.
2. The emerging agricultural technologies and the secular shifts in the agricultural sub-sectors in favour of commercially oriented agriculture are expected to create in the coming decades, a robust agricultural economy in India. It is to these changes and the associated problems that the rural credit system will have to effectively respond and gear itself. (Paras 1.03- 06)
3. Earlier reviews on rural credit in India had emphasised institutionalisation of rural credit to wean away the poor peasantry from the money lenders. Judging from the steep increase in the quantum of institutional credit over the last two decades and its coverage of rural population this object of policy makers can be said to have been by and large achieved although the credit pattern that emerged in the process is more skewed in favour of larger and smaller farmers to the neglect of medium ones. The future thrust has, therefore, to be on preserving the vitality of the credit structures which have shown signs of atrophy in the very process of quantitative expansion. There is no need for a major structural reorganisation as the basic foundations of the credit systems have been found sound and well suited to Indian conditions. The only two structural changes visualised are the merger of the RRBs with their SBs and the creation of a national apex co-operative bank of India. A comprehensive crop insurance scheme and a separate Corporation to administer this as well as Agricultural and Rural Development Corporations in certain states with a view to correcting the regional imbalances have also been recommended. These are meant to reinforce the existing two systems of credit delivery. (Paras 1.42 - 1.45, 1.61 - 1.68)
4. A socially tempered market system for rural credit where a larger segment responding to the market forces operates side by side with a smaller social segment has been envisaged. The social component has to be within the absorbable capacity of the total system as otherwise it would be counter-productive for the social component itself. (Para 1.08 - 1.12)
5. In a poverty ridden economy, financial institutions do have a responsibility towards weaker sections, but it is essential to recognise the limitations

of credit as the principal instrument of poverty alleviation. It is necessary to have a sharper focus on the selection of beneficiaries to avoid leakages and greater transparency of concessions and subsidies if only, to know who is paying for whom.

6. The vitality of the rural financial institutions depends on the vitality of the economy and the activities pursued by the borrowers. Recognising this inter-linkage, a better co-ordination between development planning and credit planning through a graduation of the present 'service area scheme' into a more comprehensive 'development area scheme' is necessary. The existing 'Multi-agency approach' should be sharpened where CBs and co-operatives supplement and support each other. Relative freeing of interest rates, a new and greater thrust on deposit mobilisation, more effective lending and recovery etc. as recommended are meant to make the credit system more responsive to the emerging developmental needs. (Paras 1.50 to 1.52)

7. All these could be achieved only if there is greater autonomy to the credit institutions. The growing inroads into the commercial banking system through excessive directions and controls and interference with the democratic management of co-operatives which debilitated these systems over the years are disturbing trends. There is need to reverse this trend. (Paras 1.85 to 1.87)

8. The rural credit problems in the Indian context could be summed up as "credit well delivered will be well accepted - Credit can be well delivered only by well conceived institutions".

Chapter II : Emerging Scenario in Agricultural Economy

9. Agriculture still remains the mainstay of the Indian economy; one per cent increase in agricultural growth is co-related with an increase of 0.7 per cent in national income. The share of agriculture in the net domestic product is estimated to decline to about 32 per cent in 1990-91 and to about 25 per cent by 2000-2001. The proportion of the population dependant on agriculture has, however, declined slowly from 70 per cent in 1950-51 to 65.5 per cent in 1984-85. Further, Indian agriculture is characterised by small farmers and high population density. (Paras 2.002 to 2.005)

10. The index of agricultural production as also the food-grains production rose by over 50 per cent during the period 1969-70 to 1985-86 but Indian agriculture has still not moved away from the cyclical pattern of peaks and troughs. This pattern has to give way for a sustained and stabilized growth pattern for accelerated development. Supply and demand pattern in respect of inputs, needs corrective steps to avoid mismatches. Higher levels of public and private investments are needed to correct imbalances between the supply and demand. Further, land reforms should get the top priority to boost productivity of investments in agriculture. (Paras 2.006 to 2.023)

11. Among the constraints on extending production are : i) the declining size of farms due to a continuous process of sub-division of holdings, ii) over exploitation of water in the green revolution areas where paddy and wheat are grown by rotation, year after year, iii) the energy constraint persisting as a critical factor in spite of large public investment going into the energy sector. (Power generation growth is limited to no more than 10 per cent when atleast 15 per cent reliable growth was needed.) These constraints have operated more severely in underdeveloped regions than in the better developed regions of the country. (Paras 2.024 to 2.035)

12. Economic development can be accelerated when all the supporting systems work in harmony. The price policy and the terms of trade should also be favourable to the agricultural sector since the capital formation in agriculture is becoming increasingly costly. For sustained agricultural development, more attention has to be paid to resource conservation research, soil and water conservation, better water management, conservation of flora and fauna and conservation of post-harvest food losses in quantity as well as quality. (Paras 2.036 to 2.042)

13. Now that the food situation has become somewhat comfortable, the emphasis has shifted to diversification of agriculture, correction of regional imbalances, promotion of more labour intensive technological improvements and improving farm systems. Also, a pattern of regional specialization will have to be evolved so as to produce cereals, processed food, marine products, etc. on a cost effective basis and compete in exporting these products outside India. Strong technological developments are necessary in livestock farming,

fisheries, farm forestry, social forestry and horticulture etc. which operate as agricultural sub-systems. Another sub-sector which needs special attention is edible oils, as the per capita domestic production has been declining over the years as against the rising trend in per capita consumption. A more pragmatic approach will have to be adopted in formulating and implementing support prices which will go a long way to help the country to achieve self-sufficiency. Further, high priority to dry land farming has to be accorded with a view to raising productivity of unirrigated land and reducing unemployment in agricultural sector. Conscious policy decisions will have to be taken to strengthen agricultural research and extension education institutions with an added thrust to evolve and adapt new cost effective technological knowledge and associated inputs. (Paras 2.043 to 116)

14. In sum, it can be said that Indian agriculture will experience larger growth by the turn of the century. It can also be expected to be a scene of relative sub-sectoral shift. This will need agricultural development programmes in different states being strongly supported by financial institutions to make agricultural and rural economies more viable, productive, progressive and profitable. (Para 2.117)

Chapter III : Commercial Banks and Rural Credit

15. Until late sixties, the commercial banks with the exception of State Bank of India were largely confined to urban areas. However, with the introduction of social control in 1967 and subsequently, the nationalisation of major commercial banks in July 1969, these banks started playing a substantive role in dispensing rural credit and to this end began opening branches in rural areas. During the period from June 1969 to December 1986, priority sector advances of 28 public sector banks (which account for more than 90 per cent of the total business of all scheduled commercial banks) increased from Rs.441 crores to Rs.23,811 crores and their branches from 6,596 to 36,265. The total number of branches increased over five times, and rural branches eleven times. The growth in deposits and loans during this period was about 23 times and 19 times respectively. Thus, after nationalisation, rural people have come to be served quite extensively by commercial banks. (Paras 3.01 to 3.06)

16. The commercial banks are mandated to achieve certain targets and sub-targets under priority sector lendings. Forty per cent of the total credit is thus required to be channelled to identified priority sectors such as agriculture, small-scale industry, small business, etc. Direct finance to agriculture and allied activities is to reach a level of 17 per cent of net bank credit and credit for weaker sections 10 per cent. All these targets were achieved by the banks by March 1988. (Paras 3.07 and 3.09)

17. One of the objectives of nationalisation of commercial banks was to increase the flow of credit to weaker sections. The commercial banks' involvement in various poverty alleviation programmes such as IRDP, Differential Rate of Interest Scheme, Self-Employment Scheme for Educated Unemployed Youth and Self-Employment Programme for Urban Poor, increased substantially after nationalisation. During the Sixth Plan, the share of commercial banks in IRDP (16.6 million beneficiaries were provided term-credit of Rs.3,210 crores by all agencies) was about 49 per cent of the amount. This share of commercial banks in IRDP loans has since gone up to 69 per cent, as against 23 per cent in the case of RRBs and eight per cent in the case of co-operatives. (Paras 3.13 to 3.18)

18. There has been a sharp increase in the branches of commercial banks in all states and regions of the country. As against 8321 branches at the time of nationalisation, the commercial banking system (including RRBs) had 54,736 branches as at the end of December 1987. As at the end of 30 June 1969 rural branches (22 per cent) and semi-urban (40 per cent) accounted for 62 per cent of total branches. While at the end of 1987, these branches accounted for 76 per cent of the total branches i.e. 56 per cent rural and 20 per cent semi-urban branches. As regards population coverage, as against an estimated 65,000 served by a commercial bank branch in 1969, coverage in December 1986 was 13,000 per branch. Since the main objective of branch expansion has to a large extent been fulfilled in the last decade and half since nationalisation, there has lately been a shift in policy from further expansion to consolidation and from quantitative to qualitative improvement. (Paras 3.09, 3.20, 3.23 and 3.25)

19. With the rapid expansion of commercial bank branches in the rural

areas, it was thought necessary to emphasise deployment of deposits mobilised by rural branches locally in the rural areas. The banks were, therefore, advised to achieve a credit-deposit ratio of at least 60 per cent in their rural and semi-urban branches. It was not, however, envisaged that this ratio should be achieved separately for each branch, district or region although banks were asked to avoid any wide disparity between different states and regions. Commercial banks as a whole could achieve these targets in respect of their rural branches, although not in respect of semi-urban branches. As at the end of December 1986, CD Ratio of public sector commercial banks was 60.5 for their rural branches and 51.3 for semi-urban branches. An analysis of the regional distribution of commercial bank deposits and advances showed a marked variation in the deployment of credit and mobilisation of deposits. Perhaps this is only to be expected considering the widely prevailing regional differences in resource endowments and infrastructural facilities in the country. Certain measures to reduce regional imbalances have been suggested elsewhere in this Report. (Paras 3.27 to 3.33)

20. The commercial banks have found sanctioning and monitoring of large number of small advances in their rural branches, time consuming and manpower intensive and consequently a high cost proposition. Partly because of this the banks have been found reluctant in posting sufficient supervisory and other staff in rural branches. Consequently, supervision of rural advances has come to be neglected. Also the staff in rural branches of commercial banks lack sufficient motivation to work in rural areas for various reasons. If commercial banks are to expand in the rural areas, they should have the right staff, properly trained and motivated to man these rural branches. Incentives both monetary and non-monetary are necessary for these staff. (Paras 3.34 to 3.37)

21. The overall recovery of commercial banks in respect of their direct advances to agriculture as at the end of June 1987 was 57.4 per cent. Their recovery under IRDP was relatively less at 45.3 per cent. There has however, been variations in the recovery statewise and bankwise. Whenever commercial banks geared up their organisational structure, adopted schematic lending, improved pre-lending appraisal of schemes and launched recovery drives, the recoveries have improved. (Para 3.38)

22. Under the Lead Bank Scheme started in 1969, the Lead Bank was mainly intended to act as a consortium leader for co-ordinating the efforts of all credit institutions in the allotted districts for branch expansion and for meeting the credit needs of the rural economy. The various machineries created under Lead Bank Scheme have, no doubt, created an awareness for better understanding of the problems at the ground level. However, many of these committees under the LBS have tended to become more ritualistic than functional. To tone up the quality of rural lending by the commercial banks, a new approach known as the 'service area scheme' was initiated by RBI from April 1989. The crucial element of the scheme is the preparation of the branch credit plan taking into account the financial support and infra-structural facilities available in the area. Credit planning for a village or for that matter any area, will be more meaningful only if all the credit agencies in the area effectively coalesce in the preparation of the credit plan and each agency is given a task to perform in its implementation. It is necessary to have better collaboration between bankers and development planners in this effort. We would prefer to modify this 'service area approach' into 'development area approach' especially because it emerges out of the development plan and development linked credit plan. (Paras 3.39 to 3.51)

23. The overall profitability of the commercial banks has been under strain for some time due to rise in the cost of deposits, declining yield on advances, rise in establishment expenses, etc. However, in recent years there has been some improvements in the absolute net profits of commercial banks. Losses on account of rural business of commercial banks have been contributing to their overall losses. Low interest rates on agricultural advances, lendings under IRDP, relatively poor deposit mobilisation in rural branches, lower staff productivity etc. have contributed to the poor profitability of rural business. As rural lending has been found contributing to losses compared with the rest of the business necessitating cross-subsidisation, commercial banks have been rather reluctant to expand their rural business and post further staff to support these lendings. (Paras 3.52 to 3.59)

24. As of now, the commercial banks are in a position to absorb the losses of their rural branch operations through earnings from their more profitable business. Although an increase in the share of weaker section lendings, which

carry lower interest rates, puts strain on their overall profitability, commercial banks, as a whole, do make profits. The basic point is that if lendings to rural and weaker sections are to be at concessional rates, there has to be some cross-subsidisation and only a system like commercial banks has, in the Indian context, the capacity for such a cross-subsidisation. The emphasis on the continuance of commercial banks as an important channel for rural credit stems from this consideration. (Para 3.59)

25. Although the primary object of bank nationalisation i.e. increased credit flow to weaker sections and rural areas has been achieved, it has created some strain in the system due to rapid expansion and diversification. Several measures have been initiated to tone up and consolidate the commercial banking system. In this context it has been thought to increase the capital base of public sector banks to a level of two per cent of their assets by the year 1990, three per cent by 1995 and further to around four per cent by 2000 as against the current level of 1.77 per cent (Paras 3.61 to 3.64)

26. Initially commercial banks were rather hesitant to enter the field of rural finance but today they have forged ahead of co-operatives in extending rural credit. One of the problems of such rapid expansion has been the deterioration in the quality of scheme preparation, particularly under the anti-poverty programmes. Such deterioration in the quality of lending was also due to heavy workload of day-to-day housekeeping, without commensurate increase in the supporting staff. Over-dependence on standard norms without adequate flexibility in individual cases, under provision of production finance in support of investment finance, fixation of shorter repayment schedules than what is warranted, lending under poverty alleviation programmes without assessing the realistic potentials, etc. were certain other deficiencies in their rural lending. There was a tendency to rely more on walk-in-business or sponsored loan applications by the branch managers. Too many detailed instructions on several aspects of rural lending have led to a decline in the professionalism of rural branch managers. It is necessary to give them sufficient discretion so that credit decisions are taken within the overall framework of guidelines and for which they can be made accountable. (Paras 3.66 to 80)

27. If commercial banks are to emerge as a strong system to be able

to purvey credit effectively and efficiently in rural areas in the years to come, they should tackle several issues such as reduced staff productivity, increase in overdues, lower staff motivation, etc. They should be accorded greater autonomy in their functioning. Their rural branches need to be strengthened. They should be allowed to have a higher margin and their equity base should be fortified. The targets for financing weaker sections and the rural poor should be reasonable such as the system can bear. They should also be in a position to protect the interest of depositors with adequate cover to the depositors. The Committee would like to sound a note of concern in this behalf. Unless urgent action is taken on these lines to put the house in order, the magnificent edifice of commercial banks which has been built over time, would not be able to meet the emerging challenges in financing the rural sector. (Paras 3.81 to 3.83)

Chapter IV : Regional Rural Banks

28. The Working Group on Regional Rural Banks set up by the Government of India in 1975, recommended the formation of RRBs to supplement the efforts of the commercial banks and co-operatives in extending credit to weaker sections of the rural community. The intention in having these new banks was that there should, in the Indian context, be an institutional device which combined the local feel and familiarity with the rural problems which the co-operatives possessed and the degree of business organisation and modernised outlook which the commercial banks had, with a view to reaching the rural poor more extensively. Partnered by GOI, State Government and sponsor bank in the equity in the ratio 50, 15 and 35, these new banks were conceived as low cost district banks exclusively to meet the credit needs of the target group i.e. small and marginal farmers, agricultural labourers, artisans and other rural residents of small means. (Paras 4.01 to 4.09)

29. Between 1975 and 1986 the RRBs increased their number from 6 to 194, their branches from 17 to 12,838 and districts covered from 12 to 351. During the same period, their deposits increased from Rs.0.20 crore to Rs.1,715 crores and lendings from Rs.0.10 crore to Rs.1,785 crores. Admittedly, the RRBs have achieved considerable degree of success in taking the banking services to the very remote areas which had hitherto remained unbanked, and making available institutional credit to the weaker sections in these areas. (Paras 4.10 to 4.14)

30. These indices of fast progress, however, do not reveal the whole story. The various Working Groups on RRBs had brought out the deficiencies in their working and in particular their inability to operate on a viable basis. A closer look on their performance to evaluate their impact on the rural credit structure reveals that RRBs have developed some serious organisational problems. These critical areas relate to their steep decline in profitability, poor recoveries and problems relating to management and staff. The number of RRBs working at loss increased from 14 in 1976 (incurring an annual loss of Rs.2.55 lakhs) to 148 in 1986 (incurring an annual loss of Rs.3,355 lakhs). The accumulated losses in respect of 157 RRBs at the end of December 1986 amounted to Rs.9,431 lakhs and these losses had wiped out the entire share capital of 117 RRBs as on that date. (Paras 4.15 to 4.17)

31. The major factors which had contributed to the erosion of RRBs' profitability were their lendings exclusively to weaker sections, low interest rate margins and high operating cost involved in handling small loans. Even those 46 banks which were in profit during 1986 earned their profits primarily from sources other than by way of interest on lending. With the financial cost of 7.80 p.a. and transaction cost of 8.65 p.a. if RRBs have to break even, they have to charge interest on their advances at least 16.45 p.a. Since RRBs have to cater to the weaker sections, this is obviously not possible. Also, in the absence of loans which could yield higher returns, they do not have any scope for cross-subsidisation. (Paras 4.18 to 4.20)

32. As on June 1986, the recovery of RRBs was 49 per cent of demand; recovery of dues in respect of 81 RRBs was 50 per cent or less of the demand. Wilful defaults, misuse of loans, lack of follow-up, wrong identification of borrowers, extension of berami loans, staff agitations, etc. contributed to the poor recovery in the RRBs. (Paras 4.21 to 4.22)

33. Although weaknesses such as poor recovery, bad management and proliferation of unsound loans are common to the other institutional structures in the credit system, what really places RRBs on a different footing is their built-in non-viability. Experience has shown that the objective of serving the weaker sections effectively could be achieved only by self-sustaining credit institutions. RRBs, structured as they are, are not institutions which could fulfil this role. (Para 4.24)

34. The logic and rationale which justified or perhaps even necessitated the setting up of the RRBs do not any longer exist. The changes which the last few years have witnessed in the rural credit scene have been qualitatively different from what had been experienced in the past and the RRBs have belied the basic assumptions of the 1975 Working Group. In particular, the commercial banks expanded in rural areas much faster than what was anticipated. To cope with this expansion, they could also induct staff with technical qualifications and aptitude in rural lending. There have been near-parity in pay scales between commercial banks and RRBs and this and other factors have made the loans transaction costs in RRBs at times even higher than in rural branches of commercial banks. The local feel thought to be brought in RRBs through their staff was not found to be the same as in co-operatives. (Paras 4.28 to 4.33)

35. An analysis of these factors shows that weaknesses of RRBs are endemic to the system and non-viability is built into it. The RRBs would not be able to serve the interests of the target group in the manner expected of them. Hence, there can be no place for the RRBs in the country's rural credit system for the future and they should be merged with the sponsor banks. (Paras 4.34 to 4.37)

36. The possibilities of letting the RRBs continue with certain improvements such as enlargement of their share capital, provision of bad debt reserves, providing somewhat large access to more resilient customers and even giving them a subsidiary status to the commercial banks have been examined. But on close examination, these alternatives were found to be unsatisfactory and did not solve the problems of effective service to the rural poor. The question of tackling the existing RRBs is only of secondary concern; the major concern is the building of a mechanism which would effectively perform the function which the RRBs were expected to do i.e. financing of the weaker sections on an increasing scale. (Paras 4.36 to 4.39)

37. Under the circumstances, the only feasible alternative to achieve this end would be to merge the RRBs and their branches with the concerned sponsor banks by making necessary amendments to the existing law. No major hurdles are seen in such a merger arrangement. As such, the public sector

commercial banks are involved in a much larger way in lending to the rural areas as well as to the weaker sections. The share of RRBs (which account for 32 per cent of the total number of rural and semi-urban branches of the banking system) in rural lending is barely nine per cent and in total business 6.4 per cent, whereas the commercial banks (which accounted for the balance of 68 per cent of the branches) have as much as 91 per cent of the share of rural lending and 94 per cent of the total business. (Paras 4.40 to 4.42)

38. Thus, a merger would not only leave no void but on the other hand the commercial banks which are stronger institutions may be in a position to step up their share in rural lending so far catered to by the branches of RRBs. Under such a merger arrangement, the sponsor banks will not only be able to strengthen their delivery system but also enhance their deposit raising capability. The 'service area concept' could be implemented more effectively with such a merger. More important than all this, the scope for internal cross-subsidisation would be widened and losses on account of having to serve the weaker sections could be offset by earnings from the higher interest yielding loan portfolio of sponsor banks. (Paras 4.43 to 4.44)

39. The merger recommendation does not mean any dilution of the concern for the small man. On the contrary, the intention is to give the small man a stronger institution to serve his needs more efficiently. Our objective is to ensure service to the poor and not poor service. Hence, after merger it is not only imperative that the banks' volume of credit given to the weaker sections in the erstwhile RRBs be maintained but that the past growth rate of lending to the poor should also be adhered to. To ensure increased lendings to weaker sections after merger of RRBs, the current stipulation of lending to weaker sections by commercial banks at 10 per cent is to be raised to 15 per cent of the net bank credit. (Paras 4.46 to 4.48)

40. The proposed merger would involve the question of absorption of the accumulated losses of the RRBs. The net loss of each RRB should be shared between GOI, sponsor bank and State Government in the same proportion as their shareholdings. The current profit position of the sponsoring commercial banks is adequate to absorb their share in such losses. But as accumulated losses are steeply increasing year by year, there is a sense of urgency in giving effect to the proposal on merger. (Para 4.49)

41. The merger of RRBs with commercial banks will offer a solution to the problem of insolvency and the in-built non-viability of the majority of RRBs. The merger would also solve the problem of accumulated losses of the RRBs. Further, by providing the structural arrangement, it will have a built-in self-strengthening and internal cross-subsidisation capability and would remove the innate weaknesses of RRBs. The emerging system will be able to achieve the goal of creating a strong viable credit system in which the interests of the small man would be better served. (Para 4.54)

Chapter V : Co-operative Banking System - An Overview

42. Promotion of credit co-operatives in the later part of 19th century was a pioneering effort among many measures taken by government in institutionalising provision of credit in rural areas. To begin with, it was essentially to solve the problem of indebtedness, usury and a stagnant rural economy, with a large peasantry. (Para 5.01)

43. The co-operative credit system had by the nineteen twenties, become the principal institutional agency for the provision of agricultural credit, both for production and investment. However, as a result of the economic depression of the thirties the movement suffered a serious setback. But, with the Second World War, which saw a period of economic recovery, the co-operative banking system acquired a place of importance in the Indian Banking System by the late forties. The Rural Banking Enquiry Committee (1950) made special reference to the role of the Provincial (now State Apex) Co-operative Banks as well as the District Level Central Co-operative Banks. It came to the conclusion that a sound and satisfactory co-operative banking system had come to stay though it had developed then in some states only, but they noted that in other states also the structure was in the process of reorganisation, consolidation and rehabilitation. It was of the view that in regard to functions as well as clientele, there could be a broad division of labour between commercial banks and co-operative banks. (Paras 5.02 to 5.05)

44. Various expert committees have opined that from the point of view of structural appropriateness, there is no alternative to co-operatives at the village level for provision of agricultural credit. The Rural Credit Survey

Committee, which was set up by the RBI in 1951, summed up its findings in the celebrated dictum that "co-operation has failed, but co-operation must succeed". It diagnosed certain failures of co-operatives in purveying agricultural credit and made many recommendations, to correct the position, which among others, included state partnership, effective integration of credit with marketing and processing and management through trained personnel. The Committee also recommended a greater role for the State Bank of India in providing the needed credit support for the commercial transactions of co-operatives. The RBI was required to constitute certain funds to provide financial strength and make the co-operative structure commercially viable. (Paras 5.06 and 07)

45. The All India Rural Credit Review Committee reported that for various reasons the performance of the co-operatives had not measured upto the expectations and it came to the conclusion that there was need for some supplementary effort, so that agricultural production did not suffer. It therefore, recommended a multi-agency approach to rural credit. With the establishment of the regional rural banks commencing from 1975, one more institutional device was added to the banking structure. (Paras 5.08 and 5.09)

46. While the refrain of all committees and working groups had been that the co-operatives have not done as well as they should have, the experience of commercial banks and RRBs has shown that the weaknesses which were earlier considered as those peculiar to the co-operative system in fact arise from such deficiencies as relate to the structure of agricultural production itself. (Para 5.10)

47. Numerically, in terms of membership, the co-operatives have spread widely in the country. By 1985-86, they covered 65 per cent of the rural population. The ST and MT credit recorded an increase from Rs.22 crores in 1950-51 to Rs.3140 crores in 1985-86, while the long-term credit increased from Rs.12 crores in 1960-61 to Rs.533 crores in 1985-86. Other areas in which co-operatives have made an indelible impression are fertiliser distribution, milk production, sugar production, cold storages and distribution of consumer goods. (Para 5.13)

48. However, while in some states like Punjab and Kerala, the system is strong, in many others it continues to operate at much below the desired level of expectation. (Para 5.14)

49. It has been said of co-operation that it has failed in India because it has been both state sponsored and state patronised. With the excessive government intervention in the affairs of the co-operatives, effective non-official leadership along with democratic management disappeared altogether. (Para 5.15)

50. The basic requirement for all the tiers working as a cohesive system is the mutuality of support among various tiers. There must be a system of mutual accountability and obligations among the higher and the lower tiers. The higher tier should exercise an effective leadership role through an efficient system of supervision, training and management guidance by professionally skilled personnel. There must also be a commonly shared interest in deposit mobilisation and in profits and reserves. (Para 5.17)

51. The organisational set up for the S.T. credit consists of three tiers - SCB, DCCBs and PACSs - the lower tiers being members and shareholders of the next higher tier. The higher tier while having the right to exercise supervision over the performance of the lower tiers must also share in their losses, extend legal and other help, provide refinance and management assistance. For sharing the losses of primary level organisations, a Fund to be built up by regular contributions from SCB and DCCBs needs to be created. (Para 5.18)

52. A major weakness of the co-operative system has been the neglect of the base level institutions and the tendency of the higher level institutions to look after their own interests often at the cost of the primaries. The co-operative credit system has woefully neglected its basic responsibility towards mobilising deposits, with the lower tiers looking up to the higher tiers for refinance at all levels. (Para 5.22)

53. Organisational and financial ties in the co-operative system have to be so designed that each tier strengthens the other. Only in such a cohesive

structure can the co-operative credit system be rebuilt as a sound system. (Para 5.24)

54. The essence or basic features of co-operative banking system must be a larger reliance on resources mobilised locally and a lesser and lesser dependence on higher credit institutions. Heavy dependence on outside funds has, on the one hand, made the members less vigilant, not treating these funds as their own, and on the other led to greater outside interference and control. Overall, this has made the co-operatives a mediocre, inefficient and static system. (Paras 5.27 to 5.29)

55. There is a distinct change now in the savings scenario. The rate of savings in India has steadily risen over the years to as much as 23 per cent. Larger rural savings are now available. The mobilisation of local resources will reduce the dependence of the co-operatives on higher institutions/government. Further with higher dependence on deposits, the members would be more concerned about the safety of their deposits and will keep a critical eye on lending and recovery. (Paras 5.30 and 5.32)

56. The powers which vest in the government under the co-operative law and rules are all-pervasive. Compounded further by their lack of self-reliance and their dependence on higher tiers and the government, the state has come to gain almost total financial and administrative control over the co-operatives, in the process stifling their growth. This trend must be reversed. Progressively, the powers which lie with the Registrar today should be vested in the higher tier organisations in respect of its lower tier. (Paras 5.36 to 5.38)

57. Some of the unhealthy results of politicisation are interference in recovery of co-operative dues or promise to write off the dues if elected to power, and determination of interest rates on considerations other than financial returns i.e. with an eye on populist appeal. Such actions generate a general psychology of non-repayment, vitiating the recovery climate and jeopardising the financial interest of credit agencies. Besides, mass super-sessions are resorted to on political consideration. Another lever for greater politicisation has been the incorporation of certain undesirable provisions in the Co-operative Societies Acts and Rules of various states. Paradoxically,

state partnership which was conceived, as an effective measure for strengthening the co-operative credit institutions has paved the way for ever-increasing state control over co-operatives, culminating in virtually depriving the co-operatives of their democratic and autonomous character. The time has come to reverse this process. (Paras 5.40 to 5.45)

58. Progressive officialisation and politicisation have caused damage to the co-operative system. This phenomenon has now reached such immense proportions that unless this trend is reversed, the agricultural credit system in general, and the co-operative system in particular, will get seriously jeopardised. (Para 5.46)

59. The net outcome of all the above factors has been to impart a great deal of inefficiency, high costs, low or negative profitability, inefficient service and lack of self-reliance in the co-operative organisations, especially at the level of the PACSs. It is thus necessary that the country recaptures the spirit of co-operation, its culture, its discipline and above all its ethos. This can only be achieved with a cohesive structure based on a strong foundation at the primary level deriving inspiration from the higher tiers which are professionally managed under a dynamic and motivated leadership. (Para 5.47)

Chapter VI : Short-term Co-operative Credit Structure

60. The short-term co-operative credit structure has at its base, the primary agricultural credit societies (PACSs) of all types, all federated into DCCBs at district level which in turn are federated into SCBs at state level. As on 30th June 1986, there were 92,408 PACSs, 352 DCCBs and 31 SCBs of which a few functioned as DCCBs as well. (Para 6.001)

61. The concept of three tier hierarchy in the short-term co-operative credit structure has been accepted as the appropriate pattern following the AIRCSC (1954) recommendations and we do not see any advantage in abolishing any one of the tiers. In fact there are positive advantages in continuing with the three tier structure as it exists. (Para 6.045)

62. Though the co-operatives ceased to be the sole purveyor of agricultural credit with the entry first of commercial banks and later, of RRBs, the

co-operatives still continue to occupy a leading position in the disbursement of production finance for agriculture. In 1985-86, the PACSs issued loans of Rs.3140.37 crores as against only Rs.1,023.44 crores in 1975-76. While, however, their performance in the issue of loans was commendable, the performance in deposit mobilisation and recovery of dues was rather disappointing. (Paras 6.001 - 6.002)

63. The profitability of the co-operatives has been a matter of considerable concern. At the end of 1984-85 for which data was available, only 51878 or 56.5 per cent societies worked at profit. The programme of reorganisation of PACSs on the basis of viability norms has not been completed in some states. Unsatisfactory recovery of dues, low margins and the non-viable nature of many societies are important factors affecting the working of PACSs in the country. 23,525 PACSs did not have even a full-time paid secretary. Where the societies had full-time paid secretaries, 50 per cent of them were not trained. (Paras 6.014 - 6.018)

64. The position of DCCBs and SCBs was slightly better though at the end of 1985-86, 173 of the 352 DCCBs were classified as weak banks. The number of SCBs under rehabilitation at the end of 1984-85 was nine. The low level of deposits and high level of overdues (37.8 per cent of demand in 1985-86), predominance of agricultural finance earning lower margins with little scope for non-agricultural loans (earning higher margins) were important factors affecting working results of many banks. (Paras 6.020 - 6.031)

65. The progress of short-term co-operative credit structure has been uneven in most states. Thus while notable progress has been achieved in Kerala, Punjab and Tamil Nadu in deposits mobilisation at PACS level, the problem and weaknesses which beset the structure continue to be substantially the same as were identified by the AIRCS Committee in 1954 and the AIRCR Committee in 1969. Certain structural weaknesses, failure to mobilise adequate deposits, the mounting overdues and lack of properly trained staff, are factors responsible for the failure of co-operatives to measure up to expectations. (Paras 6.040 - 6.044)

66. Measures suggested for removing the weaknesses of PACSs and strengthe-

ning them so as to enable them carry out their functions effectively are grouped under (i) viability; (ii) strengthening of share capital; (iii) mobilisation of deposits; (iv) improving lending policies and procedures; (v) management; (vi) office premises and godowns; (vii) loans for non-productive purposes; (viii) allocation of repayments; and (ix) audit of PACSs. Paras 6.047 - 6.102)

67. The minimum criterion of viability of a PACS can be summed up as its ability to (a) appoint a full-time paid secretary; (b) set up a regular office in a building either owned or hired; (c) contribute to statutory and other reserves on the scales considered necessary; and (d) pay a reasonable dividend. Accordingly RBI had laid down certain guidelines on the basis of which the societies were to be reorganised. (Para 6.046)

68. This process of reorganisation has been completed in all states except Maharashtra, Gujarat and Jammu & Kashmir, but inspite of such reorganisation, a large number of societies continued to have low borrowing membership, low business volume and high level of overdues resulting in accumulation of losses. It is therefore necessary that a determined and clearly programmed effort is called for to upgrade the level of functioning of such PACSs. (Para 6.047)

69. The following are the recommended lines of action :

(a) Firstly, an action programme, not extending over more than five years, should be drawn up for each PACS. All PACSs which have not reached a loaning business of Rs.10 lakhs should be taken up for specific attention. The programme of development for each PACS should deal with increasing loan business, enlarging its package of profitable non-credit activities, augmentation of resources (deposits) and reduction in overdues. The VIII Five Year Plan should, infact, become the plan for the revival of PACSs. The programme will have to be closely monitored and necessary guidance provided from time to time by the higher tiers and the state governments. The states of Maharashtra, Gujarat and Jammu & Kashmir must also undertake the programme or reorganisation at the earliest. (Para 6.048)

(b) Secondly, each PACS must come to have atleast one full-time paid

official, properly trained, who can handle the business activities on a regular basis. He needs to be paid reasonably well. A two-part salary structure has been recommended by us for the Secretary. (Para 6.049)

- (c) Thirdly, the process of reorganisation should not stop short at what had been prescribed by RBI more than a decade ago but be flexible, in tune with the dynamics of economic development. It is however, not the intention to recommend another state sponsored programme of reorganisation of PACSs (except in the three states already referred to). Further, reorganisation should come through voluntary effort. (Para 6.050)

70. The share capital of PACSs in many cases needs strengthening to meet the growing responsibilities and challenges devolving on them and to play their roles effectively. It is, therefore, recommended that :

- (a) The NABARD should provide the minimum essential requirement of share capital loan to state governments in the light of the action programme irrespective of overdues level.
- (b) The ratio of share linking at the DCCB level for PACSs may be fixed at five per cent so that they are able to retain with them a part of the share capital received from their members.
- (c) The ratio of share linking in respect of cash credit to PACSs be reduced from two and half per cent to one per cent. (Paras 6.051 - 6.053)

71. Most of the PACSs at present are totally dependent on finance provided by DCCBs and consequently, if DCCBs are weak, the PACSs are starved of finance. While the branches of commercial banks and RRBs are able to mobilize rural savings, the PACSs by and large have failed in this area, with some exceptions such as those in states like Kerala and Punjab. The fault is not entirely theirs. They were looked upon by the state authority as mere channels of refinance and in due course therefore became mere post offices for routing of refinance. This culture must change and a realization must dawn that without own resource mobilization, the scope and size

of agricultural lending by PACSs will continue to be small and inadequate. There would undoubtedly be many difficulties for PACSs in making a beginning in deposit mobilization as many of them do not have the essential wherewithal for handling deposits. The weak PACSs have a poor image and credibility. Nevertheless, deposit mobilization is absolutely vital for the future growth and strength of PACSs and, therefore, all necessary measures will have to be taken and support given to achieve this object. (Para 6.054)

72. The SCB/DCCB could help in building up infrastructural facilities like banking counters etc. As recommended by CRAFICARD earlier, the SCBs/DCCBs should create a co-operative development fund without delay to provide assistance to PACSs for acquiring banking counters, safes, etc. (Para 6.055)

73. The deposits of commercial banks, RRBs and also of DCCBs/SCBs in most cases are insured by DICGC. Appreciating the need to provide insurance cover for the deposits of PACSs but recognizing the difficulties therein we recommend that to start with the SCBs in co-ordination with their state governments should formulate suitable schemes for insuring deposits of PACSs in their states. (Para 6.056)

74. The PACSs should preferably mobilize low cost deposits such as savings bank deposits. The PACSs should maintain 15 per cent (of deposits) liquidity with DCCBs in a special account (Para 6.057 - 6.058)

75. The crop loan system for financing short-term agriculture requirements is in operation for over two decades. In the light of experience gained so far, certain modifications in some aspects/areas are considered necessary.

(a) At present for financing crop loans, fixed short-term loans are granted for a period not exceeding 12 months. It is felt that the cash credit system may be introduced in areas where perennial irrigation is available and multiple cropping is in practice; it may be premature to introduce it in other areas where only one crop is grown during the year and agricultural practices do not require frequent operations on the loan account. (Para 6.066)

- (b) The normal credit statements which take considerable time to prepare and lead to delays in loaning, are presently required to be prepared every year for fixing individual crop loan limits of members of PACSs, may be prepared once in three years subject to certain precautions to ensure that any subsequent changes in the crop acreages of members are duly taken note of. (Para 6.068)
- (c) Initially according to crop loan system it was insisted that inputs component of the crop loan should be disbursed in kind only. This stipulation is no longer considered necessary in areas where fertiliser/pesticide use is well-established, and if the DCCB so decides, PACSs may not insist on disbursing the input part of the loan in kind. (Para 6.069)
- (d) The crop loan system stipulates that the Kharif loans taken during the period May to September be repaid by March end next year and Rabi finance taken from October to March next be paid by the end of June. It is felt that the due date for rabi repayments be changed to 31st August from the present one of 30th June. This will allow two more months for the farmers to market their produce at better prices. (Para 6.074)
- (e) The present scales of finance fixed by District Level Technical Committees of DCCBs and accepted by commercial banks are generally found to be inadequate, even falling short by about 50 per cent of farmers' requirements in certain cases. This could have happened possibly because of the resources crunch experienced by one or the other tier of the credit structure. In our view, the resources crunch should not be a determinant factor in fixing the scales of finance and that the scales should be fixed strictly according to the provisions of the crop loan manual. Where due to shortage of resources, it becomes necessary to reduce the quantum of crop loans fixed in this manner, the remedy should lie not in tinkering with the recommended scales of finance but in adopting a prioritisation approach to different classes of borrowers, with larger farmers getting less but the smaller ones getting their full credit requirements. (Para 6.077)

76. A major area of weakness of the PACSs is the quality of their management. There is urgent need to provide at least one full time trained official (secretary) to each and every PACS. (Para 6.078)

77. The cadre system devised by the state governments for this purpose has generally failed to fulfil the desired results. The power to appoint a secretary must fully vest in the concerned PACS. The existing cadre system may, therefore, be given up and the PACSs allowed to recruit their own secretaries. The SCB should only prescribe qualifications, selection procedure to ensure objectivity in the scales of pay, in consultation with the RCS. (para 6.079)

78. To provide suitable promotion opportunities to these secretaries a two-way approach is suggested. Firstly, the DCCB should inform all incumbent secretaries of PACSs in lower business classification when a higher business PACS intends to recruit a secretary so as to enable them to compete for the post. Secondly, a specific quota of appropriate posts may be reserved in the DCCB to which recruitment may be made from the secretaries of PACSs only. (Para 6.081)

79. To ensure payment of prescribed salary to the secretaries by all PACS - presently half the PACSs are in loss-arrangement in the nature of a District Fund at the level of DCCB will have to be made till all PACSs reach a reasonable level of viability. This fund will provide assistance to the needy societies to the extent of deficit in their capability to pay the full salary. The contribution to this fund will be made by SCB, DCCBs, PACSs and state government. The PACSs may be classified on a set criteria into very good, good and weak, and the weak societies may also contribute a small amount. Though the respective contributions to the Fund will be decided by SCB/DCCB in each state, illustratively for the DCCB and SCB, 1/4 per cent and 1/8 per cent respectively of their loan outstandings as contribution to this fund is suggested. The deficit, if any, may be made good by the state government which has a vital stake in well being of all PACSs. (Para 6.082)

80. As most PACSs at present will not be able to pay adequate salary to the Secretary, a two-part salary structure is suggested - one, a reasonable

fixed salary decided by the society in a scale of pay, and the other, a variable payment based on increased performance, for which guidelines should be laid down by the SCB in consultation with others concerned. Illustratively, the incentive may be thought of for four major areas of work viz. recovery, deposits, additional loan business generated and additional non-credit business undertaken. The incentive for each of the specified areas of work should more appropriately be in terms of additional remuneration by way of percentage of the basic salary. (Para 6.084)

81. Lastly, but not less importantly, the managing committees of PACSs must play an important role. They determine the overall policy, appoint, support and supervise the secretary, decide on loans and credits and are accountable to the general body of the society for management of all its affairs. The managing committees must be motivated to play their roles effectively. For this purpose, the training of the managing committee members should be arranged through orientation programmes and educational programmes by DCCBs. The DCCB should evolve a regular system of meetings with the PACSs.- say twice a year at which chairman, directors, and executives of the DCCB will interact with chairmen, managing committee members and secretaries of PACSs, in the matter of mutual interests and problems. (Para 6.086)

82. It is necessary for all PACSs to have proper office premises and godown space to conduct their activities as multi-purpose societies. The PACSs should look like banks if they are to attract depositors. Presently NCDC operates certain assistance schemes to enable the PACSs to have office-cum-godowns. The Government of India should extend this scheme to all viable societies. The NCDC could also consider granting exemption on the eligibility criteria in individual cases viz. financial viability and recovery percentage of not less than 55 upto 10 per cent of the project in any state. (Paras 6.087, 6.088 & 6.093)

83. The various measures suggested above should be implemented as a total package since one part of the package is relatively ineffective without the others. (Para 6.094)

84. We recommend that PACSs should also be allowed to give credit out of their own resources for non-productive purpose, e.g. consumption loans, upto certain prescribed limits but against tangible security only. They may be allowed to grant loans upto 20 per cent of their deposits against the security of gold and silver ornaments (Jewel loans) at a rate of interest higher than that on crop loans. This will provide added viability to PACSs. If the Nehru Rozgar Yojana authorities guarantee repayment from wages earned by such a borrower, this should be accepted as security for such loans. This will greatly help the poor who need occasional consumption loans. (Para 6.095-096)

85. The present system of first allocating all recoveries (principal + interest) towards interest due by the higher tier, has in the federal structure of co-operatives created unfavourable imbalance in outstanding loans against lower tier. It is adversely affecting the PACSs in particular. It appears desirable that the principal and interest collected by the PACS from the members should be adjusted towards principal and interest in the same manner at the DCCBs. However, as the issue has many implications for DCCBs and SCBs, it is suggested that this change in procedure may first be examined by a group of experts to see how it can be best implemented. (Paras 6.098 - 101)

86. The audit of the PACSs may be done by the RCS free of cost or at a nominal fee only. (Para 6.012)

87. The following areas are critical to the overall development of state co-operative credit structure (i) development of the leadership role of higher tiers, (ii) greater deposit mobilisation, (iii) development of project formulation and investment planning capability for better and diversified project lending and (iv) rehabilitation of weak banks. (Para 6.103)

88. The need for the development of the co-operative credit system into a functionally integrated organisational structure has been brought out earlier. At present, the pervading ethos is that of each one for itself "rather than one for all and all for one" which is the basic philosophy of co-operative

movement. It appears necessary that a two way system of obligations and rights must come about among the institutions at different levels. Thus the DCCB in relation to PACSs and SCB in relation to DCCBs should have their mutual obligations and rights, to enable the system to function as a cohesive whole. The rights will include authority to issue directives to secure better management and obligations will mean responsibility to assist, train and supervise the lower level institutions. (Para 6.104)

89. The deposit mobilisation efforts of co-operative banks have fallen way behind those of commercial banks in rural areas. The problem has two aspects viz. (i) the efforts that the co-operative banks must make to improve deposit mobilisation and (ii) policy constraints which demotivate them from greater effort. (Para 6.106)

90. In regard to efforts to collect more deposits there is no set prescription except that each one must make the needed efforts in the context of local conditions, competition, etc. Suitable publicity and trained staff for the purpose will help the efforts. (Para 6.107)

91. As for constraints which demotivate DCCBs/SCBs, their genuine problems must be recognised and ways found to mitigate them. Larger deposits must not mean larger losses. Under the present conditions DCCBs are not permitted to lend to individuals and non-co-operative institutions. This, though theoretically justifiable yet if applied rigidly proves counter productive. We, therefore, recommend that DCCBs should be permitted to lend to non-members also whether individuals or institutions, to the extent of not more than 20 per cent of their deposits, at remunerative rates to provide opportunities to cross-subsidise the losses on agricultural finance. This relaxation is not recommended for SCBs. (Paras 6.109 - 111)

92. Each SCB must set up a technical cell with trained staff to formulate schemes for financing and help DCCBs in this area. Most SCBs may be able to meet the entire costs of the cell but if need be, NABARD may assist them to build such a capability. (Para 6.114)

93. Besides credit planning and project formulation, there is need also

to develop expertise at least at SCB level to advise DCCBs on better financial management and investment/portfolio management. (Para 6.115)

94. The programme of improving the working of weak DCCBs and weak SCBs under two-tier structure was launched by RBI in 1971 and has since then been implemented by RBI and NABARD. Though the programme envisaged action on many fronts, attention was more concentrated on overdues and reducing them to a much lower level. The programme envisaged full assistance from the state governments both in financial terms and manpower or organisational levels but this was not made available adequately in many cases. Therefore, the programme, though in operation for over 18 years, has not been able to make any serious impact on working of the weak banks. From a study initiated by NABARD on the rehabilitation programmes in several states, it appears that not much attention is paid to providing the weak banks with adequate resources for financing the non-defaulting and new members of PACSs as well as to rehabilitate the non-wilful defaulters. Unless a multi-pronged attempt at providing finance adequately to eligible borrowers, intensive deposit mobilisation, recovery of overdues and current dues, strengthening of PACSs, etc. is made simultaneously, it may not be possible to make an impact on the functioning of the weak DCCBs. An improvement in the present rehabilitation programme has been suggested in Chapter XII and the revised/modified programme is named "Institutional Strengthening Programme". (Paras 6.116 - 121)

Chapter VII : Long-term Co-operative Credit Structure

95. The LDB structure is not uniform in the country. In some states, it is unitary and in some other states, it is federal and in two states, it is both unitary and federal. At the end of June 1986, the long-term credit structure consisted of SLDBs in 19 states and union territories with 2447 PLDBs/branches of SLDBs all over the country. In the federal structure, the PLDBs are located either at the district level or sub-divisional/taluk level with some having branches at lower levels. The overall performance of LDBs in reaching the plan targets had been satisfactory and their progress in lending steady. However, after the adoption of multi-agency approach in agricultural lending and the entry of commercial banks in the field in a big way, the performance of LDBs has shown a declining trend in respect of

their share in agricultural lending. Increasing overdues resulting in restricted eligibility for lending, reduced scope for minor irrigation, etc. are some other reasons for this declining trend. (Paras 7.06 & 7.04)

96. Starting with pure land mortgage banking in 1919, the LDBs have now become Agricultural and Rural Development Banks, required to cater not only to the investment needs of agriculture and allied activities but also in some cases to the credit needs of the rural cottage industries and small enterprises in rural areas, i.e. non-farm activities. As a consequence of the changing role of the LDBs, the legal frame of the Co-operative Societies Acts, and the bye-laws of the banks in many states require changes. The state governments, should, without any delay, initiate necessary action for amending the Co-operative Societies Acts and Rules suitably. (Paras 7.02 & 7.21)

97. Like the short-term co-operative credit structure, this structure is also facing some problems that have so far defied solution. These are -

- (i) problems of overdues, the percentage of overdues of PLDBs being 44.1 per cent of the demand during 1985-86;
- (ii) restricted lending eligibility of units with only 32.3 per cent of the total number of PLDBs/branches of SLDBs having unrestricted lending eligibility during 1985-86;
- (iii) inability of banks to become viable because of restricted lending (30 per cent of the total number of PLDBs/branches of SLDBs were deemed not viable as on 30.6.1986);
- (iv) consequent deterioration of the profitability of the banks;
- (v) high cost of raising ordinary debentures and lower margins available on non-schematic lending;
- (vi) external interference and government intervention in management, etc. (Para 7.67)

98. To obviate these difficulties, certain suggestions have been made for tackling the problem of overdues, provision of higher margins to the PLDBs and adoption of viability criterion in place of eligibility criteria for being able to obtain adequate refinance from NABARD. Even with the recommended interest margins, the LDBs to work as viable institutions will have to make every effort to increase their volume of business with such diversification of activities as may be feasible. (Paras 7.68 - 69)

99. Another problem the banks have been facing for long, is the uneconomical cost of interim finance required for issue of loans before debentures are floated. It is, therefore, recommended that NABARD should provide adequate interim finance at a concessional rate of interest. (Para 7.28)

100. Issue of ordinary debentures for non-schematic lending for productive purposes is at present a loss making proposition as the ordinary debentures carry higher rates of interest than the rates at which loans are issued by them. To overcome this problem, institutional and government support for this programme is recommended which may be limited to not more than ten per cent of the total lending programme, at concessional rate of interest. (Para 7.31)

101. The floatation of special development debentures in respect of schematic lending refinanced by the NABARD involves elaborate paper work which leads to delays and causes loss of interest to the SLDBs. It is recommended that NABARD should provide refinance by way of term loans instead of by contribution to special development debentures. In states where the legal provisions for raising resources by SLDBs in the form of term loans do not exist, the necessary legal provisions may be made. With this change in the mode of refinance by NABARD, the need for interim finance will also be substantially obviated. (Para 7.29)

102. In the case of most land development banks there is no definite policy in regard to recruitment, appointment, career planning and development of the staff. LDBs should have a policy for recruitment, appointment, promotion and training of the staff and for manpower development for meeting future needs and thus develop professional management, rather than depend on

transitory deputationists. The state government must allow them to do so. In the case of most of SLDBs the Chief Executives are either officers belonging to IAS or to the co-operative departments. LDBs should have their own staff and taking of government staff on deputation should be resorted to only in exceptional cases. (Para 7.45)

103. Housing finance activity may be taken up by LDBs only on an agency basis with reasonable agency commission. Co-operative Acts/Bye Laws of LDBs may suitably be changed for this purpose. (Para 7.40)

104. One of the major issues which has been frequently debated is the question of integration of the structure with the short-term structure. Starting with the emphasis on the need for effective functional co-ordination between the two structures, the debate subsequently centred round full-fledged Integration, following the recommendations of the Hazari Committee on Integration (1976) in favour of integrating the two structures. The subsequent committees, CRAFTICARD being the latest, have not found integration of the two wings desirable. The opinion, not only among the co-operators but also among the experts is sharply divided. This question has been examined again in-depth and it is strongly felt that the PACSs in their present weak state cannot undertake long-term lending effectively and efficiently. What is needed is the strengthening of both the structures. There is at present no need for a structural integration. The well managed and viable PACSs should, however, be allowed to grant long-term loans where necessary. There is also need to have effective co-ordination between the two agencies to complement the efforts of each other. (Paras 7.47 to 7.63)

Chapter VIII : Bridging The Systemic Gap in Co-operative Credit : The National Co-operative Bank of India.

105. The organisation of the co-operative credit system in India has followed the traditional pattern of a federal multi-tier (two or three as the case may be) structure. On the Indian law relating to co-operatives (1904) undergoing changes in 1912 to provide for organisation of non-credit societies also and subsequently in 1919 it becoming a State subject, the higher tiers came to be organised at district and state levels only. In course of time, the non-credit co-operatives especially those engaged in the manufacture of

agricultural inputs, marketing of agricultural inputs, etc. have either federated themselves at the national level as well or enlarged their area of operation to cover the whole country in order to secure the benefit of wider national market. The state apexes in the credit sector and the other larger co-operative banking systems with all-India jurisdiction have, however, yet no national level bank of their own to function either as a national balancing centre of the surpluses of the state systems or the national level non-credit co-operative systems or the larger co-operative enterprises; these functions are today done in some areas perfunctorily and in others (such as deposit holders), effectively by the commercial banks. Nor has the co-operative banking system an institution at the national level which would be the spokesman and leader of the credit co-operatives in the country and provide a forum for the central and state governments, RBI and NABARD to discuss major issues, and pursue programme, relating to the co-operatives. Further, in the absence of a national bank, the co-operative banking system has been a two way loser. On the one hand, it loses out to the commercial banks, in the form of deposits of co-operative surpluses and on the other, the better and more profitable clientele involving large business. This void or the systemic gap at the national level has prevented the state systems to function more effectively as parts of a total cohesive national system. Only a national apex co-operative bank could fill the systemic gap and hopefully help build the systemic strength and cohesiveness which stems from a union of the state apexes. It is in this context, that the establishment of a National Co-operative Bank of India (NCBI), is recommended. (Paras 8.01 to .09)

106. It has sometimes been argued that the NABARD functions as the national level organisation for the co-operative system. NABARD is a refinancing and co-ordinating body at the national level for the entire rural credit system and not meant as apex solely for the co-operatives. Further, NABARD is an organisation external to the co-operative system. However, for the purpose of routing of refinance, the present arrangements in this regard will continue and no change is proposed. The proposed National Co-operative Bank will work with its own resources and, therefore, the apprehension if any that it might add another tier in the co-operative hierarchy is totally misplaced. Therefore, the NCBI's responsibilities in no way overlap or conflict with the role of the NABARD. (Paras 8.11 & 13)

107. The NCBI is expected to provide the much and long needed agency at the national level for retaining and balancing the resources of the co-operatives within the co-operative movement. To start with, it is envisaged that alongwith its responsibilities as a national balancing centre for state apexes, it will, being a bank itself, function as an effective spokesman of the co-operative banking system in the bankers' and other forums. (Paras 8.13 & 14)

108. The question of establishing a national co-operative bank was raised for the first time by the Committee on Co-operation (1965). Though this Committee recommended the establishment of a national co-operative bank, the position was subsequently reviewed by some of the later committees. For various reasons, the idea of establishing such a national bank was not favoured by these committees. Nevertheless the Rural Credit Review Committee did recognise that there was a need for a national level organisation to be the spokesman of the co-operative banking system but felt that the two federations of state co-operative banks and state land development banks would serve the purpose. But not being banks, they do not have a place in the bankers forum nor have they been able to effectively fulfil the function of spokespersonship. (Paras 8.16 & 22)

109. The reservations of the earlier committees in rejecting the proposal which had largely centred round (a) the apprehension that its main work will be routing of refinance to the state apexes and thereby adding one more tier making credit costlier and (b) the lack of worthwhile surpluses with the co-operative system. The situation has, however, changed considerably and the present position is that surpluses do exist in the co-operative banking system. With the implementation of measures recommended for the enlargement of deposits and other resources of the co-operative banks, sizeable growth in deposits on the one hand and the expansion of the co-operative credit system on the other is anticipated which would eventually generate even more surpluses. Without in anyway disturbing the existing funding arrangements for agriculture and rural development through NABARD, the NCBI will facilitate the use of the surpluses for the benefit of the co-operatives themselves. (Para 8.19)

110. The question of NABARD itself being either converted into the National Co-operative Credit Bank at the apex of the co-operative banking sector and alternatively forming a new corporate shell for the NCBI with transfer to it, either wholly or substantially, the financial and other resources including personnel of NABARD was considered and not found feasible. (Paras 8.23 to 26)

111. The NCBI will be a national body, functioning as a bank owned and operated by the co-operative credit system. It will be a bank for the co-operatives and does not in any way, as already stated, overlap with the role of the NABARD. On the other hand, it will be of great assistance to NABARD in its vital role of institution building in the co-operative sector. (Para 8.20)

112. NCBI will be the national apex institution for all co-operatives and would primarily provide leadership in the area of banking operations to the state apexes and would largely operate as a balancing centre at the national level. It would function as a consortium of the co-operative banking system besides mobilising deposits at the all India level which the state systems are not in a position to do. It will do all types of banking business including foreign exchange, make loans and advances, act as an apex co-operative bank at the national level and provide leadership in all matters of co-operative interest, including developmental and promotional activities, evolving and administering an efficient national system of training exclusively for the co-operative banking personnel. It will also be appropriate for NCBI, as part of its responsibilities, to function as a national data clearing centre for the co-operative system. (Paras 8.24 & 36)

113. The NCBI will have a Board of Directors elected by its members grouped into electoral colleges separately consisting of SCBs and SLDBs, urban banks and the national level co-operative institutions. The bank will have a managing director as the chief executive officer who will be a highly competent professional banker. (Para 8.38)

114. NCBI will be the repository of surplus resources of the co-operative system which each of the systems are not able to use themselves. It is envi-

saged that the SCBs will keep a part of their SLR and all member-institutions will keep their statutory Reserve Fund and other reserves required to be invested outside their business (presently even outside the movement) as deposits with NCBI. The bank will have the same status as that of any scheduled bank and it would be eligible for such concessions and facilities as are available to a scheduled co-operative bank in terms of provisions of RBI Act/B.R. Act. (Paras 8.29, 30 & 39)

115. Taking into account the cost of raising the resources and the return expected in the deployment of the funds, it should be possible for the NCBI to meet its establishment and other operating expenses and leave sufficient balance to pay a reasonable dividend on its share capital. Apart from creating the normal reserves, the NCBI, should establish a Development Fund by appropriation from profits. This Fund is to be utilised for assisting the SCBs and SLDBs in the overall development of co-operative banking system particularly at the grass root level. Any higher margin earned in the deployment of its resources will be shared with the State apexes in conformity with the co-operative principle. (Paras 8.45 & 46)

116. In order to give it an appropriate status as a national apex bank and to get over the procedural hurdle in registering it as a co-operative society, it is proposed that the NCBI be established by an Act of Parliament. (Para 8.37)

117. A national system with the proposed NCBI at the top for the credit co-operatives and its horizontal relationship with the other national apexes of the non-credit co-operatives, as a receptacle of their surplus funds and provider of credit support to them would help build the required degree of mutualism and federalism which are the essence of any co-operative system and add to the systemic cohesiveness. (Para 8.48)

Chapter IX : National Bank for Agriculture and Rural Development - Role, Organisation and Management

118. In pursuance to the recommendations of CRAFTICARD, NABARD was established in July 1982 for giving undivided attention and purposeful direction to integrated rural development. The NABARD was visualised as a centre-

piece for the entire rural credit system at the national level and as a provider of supplemental funding to rural credit institutions. The institution operates within the policy framework of RBI and GOI. Apart from providing financial assistance to NABARD, RBI has continued to maintain close links with it. (Paras 9.001 - 003)

119. NABARD was formed by the merger of ARDC, ACD and RPCC in RBI. NABARD's functions are an amalgam of activities inherited from these parent organisations rather than those of a unified apex institution. Several deficiencies in the organisational structure have been examined by the Consultants and they have made several recommendations. These may be adopted with such modifications as NABARD may consider appropriate. Similarly, Consultants have made several recommendations on recruitment, promotions and transfer policies, etc. NABARD may tackle these issues taking into account the need for a change in its image and identity which can be brought about only through better employee motivation and performance. Suggestions of consultants regarding delegation of authority, preparation of operating manuals, induction of change in the organisational culture and manpower development etc. may be considered in this light. (Paras 9.009, 050 - 065)

120. The three main functions of NABARD are refinancing, institutional development and inspection of client banks. On evaluation of these functions, it seems that the refinance function has attracted relatively more attention and resources over the years. If NABARD has to fulfil its leadership role, it has necessarily to enlarge its activities much beyond those of refinance. The NABARD should emerge as the primary source of inspiration, of conceptual guidance, of information and research in all matters relating to credit for rural development. (Paras 9.004 - 007)

121. Two aspects of NABARD's role in future need to be emphasised. One relates to its role in institution building, particularly in the promotion of viable co-operatives. A strong directing hand from NABARD with necessary support from the state governments and RBI is necessary to revitalise the co-operative system. Secondly, NABARD should give greater attention to non-farm business and agro-processing activities than what it has so far done. (Para 9.008)

122. NABARD provides assistance by way of refinance or otherwise at concessional rates of interest to client banks. While refinance for term investment credit is available to all the client banks, short-term credit for production and marketing purpose and medium-term for investment and for conversion of short-term loans are confined to SCBs and RRBs. Agency-wise, the share of commercial banks in investment credit has been progressively increasing as compared with that of the SLDBs. Over 50 per cent of NABARD's refinance for term loans has been granted for minor irrigation, land development and farm mechanisation. NABARD has also ear-marked a sizeable portion of refinance for the benefit of the weaker sections. In addition, it has also strongly supported IRDP with about 30 per cent of its long-term refinance. In future NABARD's new thrust areas would include rainfed farming, non-farm sector, social forestry and waste land development. (Paras 9.010 - 018)

123. NABARD sanctions annual credit limits, out of a general line of credit from RBI, to SCBs and RRBs for seasonal agricultural operations. Over the years the co-operatives have been meeting increasingly the crop loan needs out of their own resources. However, there has been a reversal of the trend, following an increase in NABARD's support for crop loans during the last 2-3 years on account of large requirements of some special programmes such as NODP, SFPP etc. launched by GOI. (Paras 9.019 - 020)

124. Following the reduction in the ultimate lending rates on crop loans announced in the 1988-89 budget, NABARD, in consultation with RBI evolved a formula for compensating SCBs and DCCBs for the consequent losses by reduction in the refinance rates and facilitating cross-subsidisation. RBI itself reduced its rate of interest on refinance from 6 per cent to 3 to 5 per cent and NABARD agreed to charge the same rate on its refinance to SCBs thus foregoing its own earlier margin of 1 per cent. Rates of refinance from NABARD to SCBs sanctioned on behalf of CCBs would, according to the new arrangement depend on the extent of CCB's own involvement in crop loans. There has been a further reduction in the interest rates in March 1989. The NABARD would therefore need to review the entire position again. While doing so the recommendations made in the Chapter XVIII may be taken into account. (Para 9.024)

125. A lack of co-ordination amongst various activities together with the absence of monitoring and evaluation of the effects of NABARD's refinance activity upon the credit system, has made the operating cycle of refinance work less effectively. NABARD has initiated several remedial measures and has started what is called potential - linked credit plans for the districts. The adoption of these plans should help hasten the process of upgrading the 'Service Area Approach' to the suggested 'Development Area Approach'. (Paras 9.024 - 027)

126. NABARD has started the process of decentralisation of powers to the Regional Offices. ROs are being delegated more powers in the matter of scrutiny, appraisal of schemes and sanction of loans. Close monitoring of the ROs would be necessary in order to ensure that the delegated powers are being in fact exercised.

127. NABARD should build up the capacity of its client banks so that the latter can satisfy themselves about the financial and technical viability of the schemes, on the basis of guidelines furnished by NABARD. This will help NABARD improve its own project scrutiny and sanctioning process. (Paras 9.028 - 030)

128. NABARD could resort to direct lending under special circumstances in the wider interest of regional or sectoral development, especially in respect of the proposed Development Corporations in the eastern and north-eastern states. Such selective direct lending would not detract NABARD from its efforts in strengthening the credit institutions. (Paras 9.031 - 032)

129. NABARD has taken several initiatives for the development of selected PACSs, CCBs and PLDBs. Under these rehabilitation schemes, financial assistance from NABARD is available for a variety of promotional purposes. The 15 point pilot programme to strengthen PACSs, 12 point time-bound action programme for the rehabilitation of CCBs and 10 point action programme for PLDBs etc initiated by NABARD come under this category. (Paras 9.033 - 035)

130. NABARD Act requires it to undertake the responsibility for institutional

development and accordingly it uses the lever of refinance as an instrument for this purpose. However, at present NABARD's activities in institutional development are primarily reactive rather than proactive in nature. NABARD should undertake a more effective role in institutional development, particularly with regard to co-operative development. The various components of the institutional strengthening programme and NABARD's role in it have been spelt out separately in Chapter XII. NABARD's role should be one of policy planning and review, besides extension of necessary financial assistance. A greater degree of professional management has to be brought about in the co-operatives by NABARD. (Paras 9.030 - 041)

131. NABARD is empowered to conduct periodic statutory inspections of SCBs, DCCBs and RRBs. Though these inspections by and large fulfil the statutory requirements, they suffer from several deficiencies. The inspection function is not integrated with refinancing and institutional development function. NABARD should redefine the purpose and objectives of inspections to facilitate such integration. For improving the process of inspection, several proposals have been made by the Consultants for Study V. (Paras 9.042 - 049)

132. As the apex for rural credit institutions, NABARD is required to collect and analyse information not only for its own use, but also for providing information to GOI, client banks and other institutions for facilitating co-ordination of policies and programmes at all levels. Regarding monitoring and evaluation the Consultants have stated that there is a need to exercise a major overhaul in the way information is collected, collated, analysed, evaluated and used. Similarly, according to the Consultants, the present management information system does not measure up to the needs of the senior management and requires to be streamlined. NABARD can provide computerised support to activities which are repetitive, involving non-judgemental work and in processing of quantitative information. The Consultants have made several recommendations relating to information and evaluation which may be considered by NABARD. (Paras 9.066 - 080)

133. The NABARD has to play a positive role in training its own staff as well as training of the client bank staff. The management of training of

NABARD's own staff should be separated from that of client banks. As regards its own staff, NABARD should undertake a detailed analysis of training needs at all levels, develop a co-ordinated approach for training and improve the design and delivery of the training programme. Regarding training of the client bank staff, the needs of these banks have to be assessed first. The Consultants have made several recommendations to improve the role of NABARD in imparting training to staff of client banks. While NABARD should fill the gap wherever the training institutions of client banks are under-developed, such direct training by NABARD should be gradually phased out as the client institutions develop their own training capabilities. (Paras 9.081 - 094)

134. R & D fund is expected to support studies on agriculture and rural development in order to develop innovative approaches and schemes as also to strengthen the client banks. NABARD should extend liberal assistance from the fund on a priority basis to client banks, particularly the co-operatives, in strengthening their monitoring, evaluation and inspection systems and procedures. R & D fund should be used much more imaginatively and aggressively to identify, evaluate, develop and promote new and practical initiatives in rural development. (Paras 9.095 - 100)

135. NABARD has to find resources to meet its client banks' demand for short-term and investment loans. As far as short-term loans are concerned, it is not envisaged that CBs would seek refinance from NABARD, as they have their own resources. As far as the co-operatives are concerned, their dependence on refinance from NABARD has been declining gradually except during the last two/three years, and this trend is expected to continue in future. By 2000 NABARD may have to provide refinance to the co-operatives to the extent of roughly 10 per cent of the base level outstandings. This amount at around Rs.2,700 crores could be met from the general line of credit from RBI. As far as the investment credit is concerned NABARD will have to provide refinance support in an increasing measure in the next 10-12 years. The projections show an increase in loans outstanding of Rs.8,248 crores by 1994-95 and Rs.11,310 crores by 1999-2000, over the refinance level of Rs.6,831 crores in 1989-90. NABARD can raise the required additional resources to meet these commitments roughly 50 per cent through

its own profits, and RBI contribution to national rural credit funds, and balance through market operations, and borrowings from RBI/GOI, at concessional rate. In the context of the resources crunch NABARD will have to gear itself to raise resources from the market in the coming years on an increasing scale. (Paras 9.104 - 116)

136. NABARD commenced its operations with highly favourable debt-equity ratio due to initial share capital of Rs.100 crores and the National Agricultural Credit funds of the RBI to the extent of Rs.1390 crores. However, with the present lending and borrowing rates of NABARD most of its loans if funded through borrowings, will result in its making losses. If NABARD expands its operations in future based on market borrowings at the current rates, its profitability will decline and even result in losses. The situation has further worsened due to recent reduction in NABARD's lending rates to member institutions for short-term loans. If NABARD has to expand its operations, either its equity base has to be strengthened or low cost borrowings resorted to. Consultants have recommended RBI/GOI to provide free resources on a larger scale to countervail this impact. Recognising the various limitations in this regard, we have proposed to substitute it with increased borrowings from GOI/RBI at a concessional rate of 5 1/2 per cent. (Paras 9.117 - 124)

137. If NABARD has to emerge as a strong development bank for rural re-generation, it has to take certain fresh initiatives. It should concentrate more on the building up of the co-operatives, improve its functional capabilities in project identification, preparation, appraisal and monitoring, forge a better linkage between inspection and development function, pay greater attention to the non-farm sector and staff training and extend its net-work to the district level. NABARD will have to play its part in open market borrowing also, so that it could meet its refinance commitments. The present lack of control over its member institutions should be rectified by developing necessary clout with the help of and in co-ordination with RBI. In course of time, however, NABARD will have to evolve its own image to enforce the required discipline among member banks. (Paras 9.125 - 127)

Chapter X : Development Plans and Credit Planning

138. In a credit system which is becoming increasingly sophisticated, credit

planning assumes crucial importance. Such credit planning has to be undertaken at different levels of the financial institutions. Despite several blue-prints evolved in this regard, we observe that credit planning has not yet made any serious dent at the level of implementation. Several deficiencies have been noticed in the existing district credit plans. (Para 10.01)

139. The key point is that a district credit plan must emerge from the district development plan and a block credit plan from the block development plan. In our view, credit planning to be effective, needs to be backward-linked with such development plans in physical terms and forward linked via credit disbursement agencies with the credit using agents. In the current state of availability of data and information at the village and block levels, the development planning should begin at the district level and the district plans so drawn should be split into block plans and village plans, meanwhile commissioning the accumulation and analysis of the data at the grassroot levels. When such base level data are available on a regular basis, grassroot level planning could start effectively. (Paras 10.05 - 07)

140. The district development plan should concern itself with the targeting of output and investment both for private and public functionaries unlike the National or the state plans which have so far concerned themselves only with planning of output and investment by Central and state governments and public enterprises, leaving private sector planning only to broad guidelines and indications. (Para 10.10)

141. The objectives of a district development plan are to obtain a set of physical targets of output and investment for different activities over the stipulated period. The objective of a district credit plan then is to convert these physical targets of output and investment in each activity into their credit equivalents and to pursue their achievements and implementation. While converting district development plan into a district credit plan, availability of projects, resources with the Government and resources within the banking system would have to be taken into account. In the absence of district development plans prepared by the state governments, district credit plans cannot be formulated on a realistic basis. (Paras 10.15 - 17)

142. The District Credit Planning Committee should convert the development plan into a credit plan for different activities and sub-sectors identifying specific schemes and projects. Once such a district credit plan is evolved separately in terms of investment targets for the government and the credit targets for private investment as well as production activities in different sub-sectors the credit plan will have to be split into separate sub-totals for each block by the District Credit Planning Committee.(Para 10.18)

143. The Block Planning Committee should take over the block part of the district development plan as well as the block part of the district credit plan along with the activity targets for production and investment credit in different sub-sectors of the block economy. Credit targets at the block and district levels for each sub-sector should be considered as only indicative targets and suitable revision should be allowed depending upon the emergence of actual demand. Economic development planning to be meaningful should have an economic content, an administrative/organisational content, a social content and an input of popular wishes and aspirations. In this new scheme the Lead Bank acquires a key role and the Lead Bank Officer emerges as a key functionary in the district credit planning exercise. (Paras 10.24 - 26)

144. The RBI should continue to be in-charge of Rural Credit Planning at different levels under the new Development Area Approach suggested by us. There is however, a need for more active collaboration of NABARD in credit planning exercises at different levels i.e. district, state and national. At the district level a designated officer of NABARD should associate himself with the various machineries created for credit planning at that level. (Para 10.27)

145. While the 'service area scheme' recently evolved by the RBI with a view to strengthening the rural lending operations of the commercial banks is to be welcomed, it seems necessary to somewhat widen the scope of the existing scheme. The scheme should encompass a reordering of the branch net work of commercial banks, inclusion of the co-operative banking system as a partner in the scheme and keep in view the total development of the command area. In other words, the 'service area approach' should be graduated

into a 'development area approach' and in the process bring about also a rationalisation of the branches of the commercial banks so as to avoid wastage of resources and efforts. (Para 10.28)

146. The token presence of several commercial banks in a block often with one or two sparse and isolated branches, is a disturbing commentary on the somewhat irrational expansion of commercial banking in the country. It was a detraction from the efficacy of the multi-agency system. There is a need for homogenisation in the branch spread of commercial banks. As each village is allotted to a commercial bank branch under 'service area approach', a block will have to be allotted to one commercial bank instead of many under the proposed 'development area approach'. Each block should be allotted to that commercial bank which already has a larger presence through its many branches. Other banks may be asked to move out of the blocks not allotted to them gradually in finite length of time, say three years. Such rationalisation can substantially reduce the cost of supervision, improve the quality of monitoring and would also be beneficial to the customers. (Paras 10.30 - 34)

147. In such a developmental approach, emphasis shifts on the one hand to effective savings mobilization through new techniques and on the other to effective lending. The banker enlarges the credit cycle continuously by canvassing new schemes and projects, tying credit with inputs, inputs with outputs, outputs with repayments and repayments with new lending. A banker is judged not so much by how much he lent, how well he kept the accounts and how thoroughly he followed the rules and procedures, but by how much he succeeded in changing the economy of the customer and the socio-economic face of the region. In other words, an audit becomes not an audit of accounts but an audit of development performance. We envisage Indian commercial banking to develop on these lines. (Para 10.36)

Chapter XI : Regional Imbalances - Some Corrective Measures

148. Substantial development has taken place in the past two to three decades in the agricultural sector, but such development has been uneven as between different regions/states. Apart from imbalances in natural endowments, such as pattern of land holdings, irrigation facilities, etc. there are wide

variations, region-wise/and state-wise, in the productivity of major crops. The performance of the credit agencies whether commercial banks or the co-operatives has also been relatively better in agriculturally advanced areas. Thus, both in development of agriculture as also in the deployment of credit, Southern, Western, Northern and Central regions are relatively well developed whereas the Eastern and North-Eastern regions have remained undeveloped. (Para 11.11)

149. Apart from peculiar problems pertaining to land tenure system, mountainous terrains and problems of transport, etc. the Eastern and North-Eastern regions suffer from lack of backward/forward linkages and inadequate support services. The result is that there is very little scope for bringing about agricultural development through individual investments with the help of institutional credit. Development of agriculture in these regions could however be possible through programmes/schemes financed partly or wholly through public funding. It is equally necessary to develop infrastructural support also to be funded through the public exchequer. (Para 11.28)

150. For bringing about a meaningful departure from the existing system of agricultural lending, establishment of an Agricultural and Rural Development Corporation (ARDC) is considered necessary and has been recommended for each of the three eastern region states viz. Bihar, Orissa and West Bengal and one for all the North-Eastern region states. (Para 11.29)

151. Each ARDC may be jointly sponsored by the central and state governments. The main task of these corporations would be to adopt a bolder strategy for increasing the tempo of agricultural lending. Each corporation would initiate action for building up necessary backward and forward linkages and supporting services, take up area-wise potential studies, formulate location-specific projects, for accelerating transformation of agriculture and arrange for funding of these projects through public exchequer where and to the extent individual investments are not feasible. (Paras 11.29 to 31)

152. The success of the proposed corporations calls for the government assuming far greater degree of responsibility in developing appropriate policies, evolving mechanism and machinery for infrastructural development, etc. in these regions. (Para 11.33)

Chapter XII : Programme for Institutional Strengthening

153. This chapter deals with 'Eligibility Criteria' (EC) governing refinance from NABARD for project lending and the 'Programme for Institutional Strengthening' (ISP). (Para 12.01)

154. Studies conducted by the consultants have brought out the adverse impact of EC on LDBs. In PLDBs/branches of SLDBs with restricted eligibility, there is a general decline in fresh lending and profitability and in the long-run these banks slowly wither away. In commercial banks, RRBs, SCBs/CCBs on the other hand, the impact of EC is more on their profitability since NABARD refinance to which they have access is cheaper. The statistical evidence on the impact of EC in enhancing the recovery performance of client banks is scanty. On the contrary, recoveries have deteriorated in the case of banks with restricted eligibility on account of EC. The most undesirable feature of EC is that overdues become the sole determinant of eligibility for refinance, resulting in new and potential borrowers being denied fresh finance. In the ultimate analysis, EC has done more harm than good both to borrowers and the credit system. (Para 12.13)

155. It is therefore, considered necessary that the discipline of 'Eligibility Criteria' is replaced by a new discipline known as "Viability Criteria" (VC) supported by 'Institutional Strengthening Programme' for weak and non-solvent institutions. The term "viability" denotes solvency of a client bank. VC would be applied at the bank level as profitability of a branch is susceptible to several adjustments. The new discipline of VC will apply to all client banks of NABARD except the commercial banks. While in the case of RRBs, their merger with the sponsor banks has been recommended, pending such merger VC will apply equally to RRBs. VC implies that the solvent co-operative banks and RRBs will be eligible for full refinance from NABARD (subject to its satisfaction about the size and scope of lending programme); conversely the non-solvent banks will not get any refinance. As a pre-condition to the unrestricted refinance from NABARD, all client banks will have to achieve, by 30th June 1992, and maintain each year thereafter, 80 per cent recoveries in respect of their current demand. (Para 12.17)

156. To obviate sudden stoppage of refinance to non-solvent banks, the non-solvent co-operative banks and RRBs as also those in danger of losing

their solvency would be taken under ISP aimed at enhancing their viability and, as a part of ISP, provided with refinance on a suitable basis. As a pre-condition for refinance, banks under ISP should show improvement in recoveries and achieve in two to three years 80 per cent recovery under current demand. If a bank fails to implement ISP, or remains non-viable despite undergoing ISP, it would be deemed a non-bankable risk and, therefore, ineligible for further refinance from NABARD.(Para 12.18)

157. Application of viability criteria to commercial banks would virtually amount to making them eligible for unrestricted refinance on a permanent basis irrespective of the quality of their agricultural lending. A modified eligibility criterion has, therefore, been recommended in the case of commercial bank branches, in terms of which, from the year 1992-93 :

- a) branches achieving recovery of 80 per cent and above in relation to current demand and 25 per cent recovery under arrear demand would qualify for unrestricted refinance;
- b) those having recovery between 40 per cent and 80 per cent in relation to current demand and 25 per cent recovery under arrear demand would get restricted refinance;
- c) while those having recovery below 40 per cent under current demand and less than 25 per cent under arrear demand will not be eligible for any refinance facilities from NABARD.

Till the year 1992-93, commercial bank branches may continue to be governed by the existing eligibility criteria.(Para 12.25)

158. NABARD's efforts to improve, through Rehabilitation Programmes, the financial position and functioning of the co-operative banks have been both unsuccessful and too narrow-based. The Institutional Strengthening Programme is, therefore, intended to replace the existing Rehabilitation Programme. Non-solvent co-operative banks and RRBs and those in danger of losing their solvency will be the target group for ISP. After identifying the root causes of non-solvency/weaknesses of each identified bank, a ISP scheme

would be developed for each individual bank to attack the areas of its weaknesses. It is envisaged that while NABARD will develop credit strategies and components of ISP and issue operative guidelines it would be directly responsible for the strengthening of identified apex agencies i.e. SCBs and SLDBs only, whereas direct responsibility for monitoring and implementation of ISP schemes of district and primary level credit institutions would be that of the concerned SCB/SLDB. State governments will have a crucial role to play in implementing the programme as co-operatives function under state laws which vest in the state governments a very wide range of powers and authority. For effective co-ordination of various agencies at different levels-national, state and field planning and implementing ISP, constitution of Review Committee at two levels, state level and district level, in each state has been envisaged. While the chapter gives a comprehensive blueprint of ISP, outlining the programme components, roles and responsibilities of concerned agencies, etc. ISP cannot be an instant panacea which will revive the fortunes of all non-solvent banks. Majority of these banks have deep-rooted problems beyond their control. The strengthening of these institutions would, therefore, take time and hardwork by banks themselves, their apexes, government, other agencies and NABARD. (Paras 12.28, 32 to 45)

159. In the case of commercial banks, branches which fail to show, in respect of their agricultural loaning, recovery of atleast 40 per cent under current demand and 25 per cent under arrear demand should be taken under ISP, and provided refinance, on a suitable basis, as part of ISP. Unlike the comprehensive ISP for co-operative banks intended to retrieve them from non-solvency, the ISP for commercial banks would be simple, aimed at improving their recovery position and refinance from NABARD. (Paras 12.60 & 61)

Chapter XIII : Staff Training and Manpower Development

160. One lesson that emerges from experience in agricultural banking in India is that policies have often marched ahead of organisation and organisation, ahead of personnel. The relative lack of adequately trained personnel has been a major constraint in both the deepening and widening of credit in pursuit of rural development. In fact, the requirement for adequately motivated and trained man-power is growing substantially due to increase

in volume and variety of banking services and progressive changes that are on the anvil in the working methods of banks. (Paras 13.01, 02 and 05)

161. The key components of proper training system for the rural banker should be (a) meeting the needs of the financial institutions, (b) skill upgradation of the banker and (c) development of his overall personality as a banker. (Para 13.03)

162. The major problems of commercial banks in the development of staff for rural banking are their low motivation, low level of sympathy for the disadvantaged classes, bureaucratic approach as well as gaps both in knowledge and skills. In the co-operatives and the RRBs, in addition to these problems there are problems of recruitment based often on patronage, caste and community considerations. (Para 13.06)

163. We have observed several weaknesses - both quantitative and qualitative - in the present training arrangements particularly relating to rural banking. Physical and other infrastructural facilities in the commercial banking sector are, by and large, sufficient to meet the emerging training needs of their personnel. However, in the case of co-operatives, except LDBs the overall capacity for training is much less when compared with the total staff. As far as the quality of training is concerned the glaring weaknesses have been inadequate linkage between planning and training and near absence of strategic planning in many banks. As a result, training and man-power planning have not taken firm root in most of the banks. Training is not perceived as an essential need by the operating managers and the image of training in the line organisation is not very high. Hence there is a need to improve the quality of training in most training institutions. (Paras 13.17 to 21)

164. In particular, these weaknesses are evident in the training of secretaries of PACSs. The existing co-operative training institutes are not adapted to the special training needs of the secretaries and other personnel of PACSs. Moreover, there is very little influence of the state co-operative banks on the programmes intended for secretaries of PACSs. There is an immediate need for improvement in the training of secretaries of PACSs. This should be the responsibility of the state co-operative banks in each state for which

they should set up specialised training institutes. In addition to the secretaries, Management Committee members of PACSs, personnel of SCB/DCCBs are also to be trained.(Para 13.24)

165. The Principals and Training Managers who have the responsibility of managing training functions should also be trained in various aspects of training policies and strategies so that they can tackle the problem of training effectively and make training purpose oriented in their institutions. (Para 13.29)

166. There is a need for a comprehensive assessment of the training needs in different sectors. Such a survey should also take into account the staff required at different levels, types of training needed by them, the existing gaps in training etc. It would be difficult to frame common strategy or draw priorities for training without such an overall assessment of training needs in fields related to rural credit. Since substantial increase in the financial allocation for training is not possible, it is important that new cost saving and net work expanding methods of training are devised to meet the existing gaps in training. (Para 13.30)

167. A responsible apex agency must begin and continue to develop a comprehensive training strategy and a set of national priorities and standards. This agency should develop a plan to make optimum use of the facilities and other resources of the various training agencies and institutions. There is also a need for greater collaborative arrangements among various training institutions dealing in rural banking. This responsibility should be assigned to RBI. NABARD should be associated with RBI in discharging these functions. (Para 13.31)

168. Training of trainers is one of most crucial aspects of banking up-gradation. Upto now, the apex level institutions have devoted most of their attention to direct training of middle level officers. We feel that there is a need for shift in emphasis at the apex level from direct training to training of trainers and production of training materials. Direct training of their own staff should be the responsibility of the apex co-operative banks and commercial banks. (Para 13.34)

169. Another weak area we have observed in the training system is the post training follow-up. Firstly, it is necessary to evaluate the training programme itself after completion of such programme. It is necessary to ensure that after training, the placement of trainees is appropriate to the training received. It will also be necessary to evaluate the trainees on the job after completion of training. Such a feed back would be necessary to make training relevant to the demands of the job. Gradual induction of computers into staff training would increase the efficiency of various training techniques. (Paras 13.35 & 36)

Chapter XIV : Accounting Systems and Policies, Computerisation and Management Information Systems

170. Observations/recommendations made on the subject are subject to the general comments given in paras 14.01 to 14.06 of the chapter.

171. Although the banking institutions maintain full accounting records in the form of double entry accounts, it is observed that the banks do not generally follow the system of product costing or cost of profit centre accounting by type of lending. The general ledgers in vogue designed as they are do not provide the requisite financial information either for management purpose or for furnishing returns required by higher level or regulatory authorities. (Paras (14.09 and 10)

172. Generally, accounting in the SCBs and commercial bank branches at the field level is exclusively manual. (Para 14.13)

173. Although the staff employed in accounting in the apex and district level banks are generally educated, there are only very few Chartered Accountants employed. There is also a general lack of formal accounting training for staff. (Paras 14.14 to 16)

174. The computerisation of the accounting systems of the client institutions is not expected to take place within any meaningful time span. Hence, it is suggested that in the meanwhile, a manual based accounting system, which can be computerised, may be adopted immediately and computerised in due course. The system can generate the financial data required for the MIS. (Para 14.17)

175. While we agree with the basic approach of the consultants in recommending the adoption of a model general ledger which will have separate accounts for different types of lending, our view is that the general ledger need not necessarily throw up all the information/analysis required. The general ledger as suggested by the consultants will be difficult to be maintained as long as the accounting system is not computerised. It is necessary to have recourse to subsidiary ledgers for this purpose. (Paras 14.19 to 22)

176. To provide for automatic ageing of overdues, client banks should open new SAO loan accounts each year. The task of ageing of the overdues on MT and LT lending could be simplified and speeded up by designing the loan ledger records similar to the general ledger accounts. (Paras 14.24 & 25)

177. It is possible that some PACSs would not find it easy to implement the methodology discussed above. At the same time there is as much need for an accounting system to provide management information at PACS level as at higher levels, specially for updating data on recoveries. (Para 14.27)

178. NABARD should prepare a manual for the entire accounting and the financial MIS procedures and distribute the same to client institutions and also arrange for training seminars for the client banks. (Para 14.28)

179. In a multiple tier system, as in the co-operative structure, remittances to higher level institutions should be allocated as between interest and principal in the same manner as at the ultimate borrower level. NABARD should include both interest and principal in its definition of demand, collection and balance for SCBs and DCCBs. (Paras 14.30 to 35 and 6.101)

180. Provisions should be made to fully cover anticipated bad debts, whether there are profits or not and must be charged against profit. The provision should be deducted from the asset in the balance sheet to show the estimated net realisable value of the asset. To establish the true picture of the institution's solvency to receive refinance under VC approach, it will be necessary to deduct from the owned funds, the quantum of estimated bad debts and accumulated losses. This system may be stipulated in the co-operative law. (Paras 14.40 to 43)

181. NABARD should stipulate the use by co-operative banks of the RBI recommended accounting policy on interest receivable. (Para 14.46)

182. NABARD should stipulate that standard accounting policies be adopted by the client banks in the recommended periodic financial reports it will call for from them. (Para 14.47)

183. There is almost a total lack of computerisation in the agricultural credit system. While the commercial banks have made some progress with computerisation, no use of computer was noticed in rural branches. In co-operatives also computerisation is all but unknown except for a few cases in the higher tiers. (Para 14.49)

184. The commercial banks as a group have however, developed computerised applications to service their wide range of business needs including compilation of returns on agricultural credit (MIS). (Para 14.50)

185. There has been a co-ordinated development of computerisation in commercial banks following a plan laid down by a Steering Committee of the RBI. However, the specific applications and the extent to which computer technology could be introduced have been hampered by the "Memorandum of settlements between the IBA and the INBEC". (Para 14.51)

186. As the whole banking system gets increasingly computerised it will have a favourable impact on customer service and the reduction of transaction costs of the commercial banks' operations. (Para 14.04)

187. The spare capacity, if available, at the established computer facilities at district level by NIC the banks should use the same for compiling information on various banking operations of the branches in the district with the help of the Lead Bank of the district. (Paras 14.05 to 07)

188. Many of the SLDBs had done no evaluation of computer technology. However, there is an understanding at the LDB Federation level of the need for computers. (Para 14.53)

189. Although some of the state co-operative banks had introduced computers, agricultural credit information or accounting was not processed anywhere. (Para 14.54)

190. It appears that there is no overall co-ordination of computerised information flow throughout the banking industry as a whole although RBI is directing computerisation in CBs and NABARD is liaising with each of the two co-operative federations and with the IBA. (Para 14.55)

191. Due to several factors, it would be impractical to consider general computerisation at primary/lower levels and hence it is recommended that a computerised MIS at district level be established initially, until the current impediments at the lower levels are removed. The full computerisation of the banks' accounting system in India is recommended for implementation before the end of this century. (Para 14.58)

192. Because of the massive number of primary level institutions in the Indian agricultural credit system and infrastructural problems, the application of computer to the accounting functions could not be recommended at this stage. Instead, a simple interim manual accounting method may be implemented at all levels, until the recommended MIS is in operation. The introduction of computers in staff training would increase the efficiency of training techniques and also create computer awareness. (Paras 14.60 and 61)

193. Both the RBI Computer Committee and the NIC have conducted extensive evaluation of computer hardware and software requirements. The recommended hardware has already been installed in a number of banks, to assess its suitability and the performance of the software. (Paras 14.63 and 64)

194. In view of the unavailability of adequately trained computer personnel in India and to avail of the advantages of economies of scale in the purchase of hardware and software and for the reason of ongoing operational costs, it is felt that a single computer centre operation should be established at district level. (Para 14.68)

195. For those banks who have not introduced computerisation in their

organisation, the creation of subsidiary service company by the management systems and standard committee (MISSC) is one method that can be adopted. The operations of the company may be conducted on a "User pays principle." (Para 14.70)

196. There are a number of benefits in favour of using the existing computer facilities already established in a bank in the district, inasmuch as the computer centre is, already physically established, operational and/or software staff are available. Operational costs would be shared on time and materials basis. (Paras 14.73 to 75)

197. The NIC has commenced operations of its system DISNIC at a number of pilot sites through different states of India. The DISNIC will provide the capability to gather information on the monitoring schemes and socio-economic information required by State planning agencies and the Central Government, as also a workable solution for processing of agricultural credit management information. There is a commonality between the NIC data base and our recommended agricultural MIS data base at district level. (Paras 14.77 to 79 and 84)

198. Of the alternatives discussed above, the NIC option is recommended as it is a safe, speedy and reliable way to introduce computerisation into agricultural credit at an early date. NABARD should hold immediate discussions with NIC on its computerisation strategy on installing super mini computers at each of the 438 district centres. (Paras 14.81 and 82)

199. MIS is a necessary tool for the management and control of agricultural credit at the apex level. (Para 14.85)

200. To overcome the problem of multiple returns, to be submitted by primary level to higher level institutions, rationalisation of returns is recommended for introduction in commercial banks. (Para 14.86)

201. Due to absence of mechanisation and limited manpower resources, the impact of compilation of data on PACSs is very great and time consuming. (Para 14.87)

202. The national apex body should review the financial soundness of client banks. A commonly used methodology is through "CAMEL" which encompasses five broad areas of financial control information. The "CAMEL" concept is recommended selectively to highlight those areas where management has decision making prerogatives which can affect the financial performance of the bank and those areas which must be monitored by apex level, in pursuit of its objectives of reviewing financial integrity. The medium for channelling this information should be through periodic proforma financial reports. NABARD may require these forms to be submitted by client banks to ROs. NABARD should train client bank management and senior accountants in the advantages, use and preparation of the recommended reporting system. (Paras 14.92 and 93)

203. The initial priority for introduction of computers into agricultural credit, must be setting up of agreed standard for MIS. The RBI has introduced an institution and branch numbering system for commercial banks to be quoted on returns. The major activities of the MSS Committee to be formed for the purpose, will be directed to the generation of accurate and meaningful data on agricultural credit. NABARD must play the principal role in the control, direction and financing of the MSS Committee through its R & D funds. It is recommended that this Committee would be charged with the responsibility of formulating overall policy/strategy for MIS. (Paras 14.94 to 97)

204. The recommendation for the creation of a computerised district data base of account information provides a vehicle for consistent flexible reporting. The availability of such a constantly updated and consistent information base, will render many of the fixed period returns unnecessary. (Para 14.98)

205. The district data base can also become a credit information bureau. This will act as a safeguard, preventing the sanctioning of multiple loans for the same purpose by different institutions. (Para 14.99)

Chapter XV : The Overdues Syndrome

206. The high incidence of overdues in the agricultural credit system has become a major constraint to the expansion and smooth delivery of credit.

However, the bulk of the overdues get recovered in course of time leaving only a small proportion of it ultimately becoming irrecoverable. It is only these which turn bad. It would, therefore, be wrong to construe, as is sometimes done, all "overdues" as "bad debts". Our estimate of bad debts as on June 30, 1986, of the credit agencies under agricultural loaning works out to Rs.846 crores forming 5.1 per cent of the total agricultural loans outstanding on that date. But overdues in absolute terms have increased during the last one decade. Thus, the overdues at the level of the ultimate borrowers of all credit agencies increased from Rs.853 crores at the end of June 1976 to Rs.4,262 crores at the end of June 1986 and constituted 42 per cent of total demand. (Paras 15.004 and 009)

207. The overall position in respect of recovery of loans has continued to be unsatisfactory in all types of credit agencies although it varied as among the different agencies and different regions/states. Recoveries in aggregate were thus relatively better in land development banks than in PACSs, commercial banks, and RRBs, the position being the poorest in RRBs. Statewise, the recovery of agricultural credit was consistently better in certain states like Punjab, Kerala and Haryana irrespective of the type of agency dispensing credit, whereas it was far from satisfactory in some other states like Manipur, Tripura, Assam and Meghalaya. Similarly, recoveries were better in the irrigated areas and in cases where high value crops were grown. Since recycling is as important as mobilization of additional resources, effective measures are called for bringing down overdues to the minimum level within a definite time-frame. (Paras 15.007 and 009)

208. During the field survey involving interviews of defaulters to different credit agencies, it was found that 22.6 per cent of the respondents attributed their defaults to natural calamities and adverse weather conditions 17.1 per cent respondents to low income generation, 3.9 per cent respondents to unforeseen developments, 2.3 per cent respondents to diversion of loans and one per cent of respondents to defective loan policy/procedures. 54 per cent respondents did not indicate any specific reason for their defaults, some of which could be cases of 'wilful' defaults. (Para 15.018)

209. A wide range of external and internal factors influence the level of

and trend in overdues. Factors external to the credit agency comprise natural calamities like floods and droughts, absence of backward and forward linkages, defective legal framework and lack of government assistance in effecting recoveries through legal measures, socio-political environment in which the credit agencies are required to function, etc. In agricultural projects and production programmes the absence of linkages for ensuring input supplies, and extension services on the one hand and processing, storage, marketing and other services on the other, have been serious lacunae, impairing effective use of the assets and impeding the production activities. For combating these, the Directorate of Institutional Finance in each state should be strengthened. It is necessary that a multi-disciplinary team of experts undertakes long-term planning of the agricultural sector and develops projects which will provide the necessary linkages and supporting services. The main thrust of the plan would be to secure optimum exploitation of the growth potential of the area through formulation of location-specific bankable projects and planned deployment of state resources to build up the necessary infrastructure and linkages. (Paras 15.027 and 076)

210. The existing dual legal framework for recovery viz. legislation on the lines recommended by Talwar Committee in the case of commercial banks and RRBs, and Co-operative Societies Acts in various states for co-operative credit institutions, itself suffers from various shortcomings. Administrative arrangements for recovery through legal measures, such as recovery staff, are inadequate resulting in heavy arrears in disposal of recovery cases. Besides improvements necessary for making the existing legal framework more effective and augmentation of concerned government staff for effecting recoveries, what is called for in the long-term is the need for a single common legal framework covering both co-operatives and commercial banks for the country as a whole, constitution of Special Tribunals at the state level and a single Government Department in each state exclusively entrusted with the task of execution of awards obtained through such Tribunals. (Para 15.097)

211. Providing loans to groups of persons or associations of farmers for a common purpose needs to be facilitated and in fact encouraged. Unlike individual loans, the group loans besides being secured by the joint and several liability of those constituting the group/association, are also backed by their

responsibility including moral one to discharge the loan liability. Similarly, there is an imperative need to educate the borrowers on the right use of bank credit and the commercial disciplines that go with it. (Para 15.079)

212. There has been a growing tendency to use agricultural credit as an instrument for achieving short-term populist objectives. Government measures such as write off of agricultural dues, concessions/relief announced by political functionaries from public platforms, stay orders on legal processes of recovery, disbursement of loans/assets at the hands of political dignitaries in loan melas, etc. have vitiated the recovery climate. The need for a strong political will cannot be over-emphasised if politicisation of the agricultural credit institutions is to be checked. A general consensus is also needed among all political parties so as to ensure that agricultural credit is not used as an instrument for achieving political purposes. Government of India and State Governments should evolve a concrete long-term policy for recovery of agricultural dues and take a firm and objective view in respect of wilful defaulters. (Para 15.077)

213. Mass programmes for disbursement of loans such as 'Loan Melas' should be stopped as they have deleterious effects on the functioning of credit agencies. (Para 15.052)

214. Factors internal to the credit system, directly affecting recoveries, include defective loan policies and procedures, inadequate supervision over credit and unsatisfactory management. These relate to the unrealistic scales of finance/unit costs, delay in sanction and disbursement of loans, fixation of defective repayment schedules, failure to provide working capital to borrowers under term credit, over-emphasis on target approach, etc. Several recommendations on streamlining the crop loan system have been made by earlier committees and policy decisions taken but these have regrettably remained unimplemented. There is also need for scrupulous adherence to prescribed policies/procedures as well as suitable changes in loan policies, such as shifting of due date for rabi crops loans from 30th June to 31st August so that repayment dates have meaningful relation to marketing season, need for periodical revision of unit costs, etc. Other corrective measures called for relate to switch over in appropriate areas or cases to cash credit

system and disbursement in cash instead of in kind. Thus, in areas where perennial irrigation facilities are available and multiple cropping is in vogue, banks could switch over from fixed duration (crop) loans to cash credit system in providing crop finance. This would obviate the delays necessarily involved in the sanction and disbursement of loans for each crop season. In other areas, banks and co-operative societies could switch over to the preparation of the normal credit limit statements for a three year period subject to the safeguards indicated. Similarly, in areas where farmers are fertiliser conscious and are already accustomed to the use of fertilisers, there need be no insistence on disbursement in 'kind' and the banks may be given discretion to determine the mode of disbursement of credit for inputs purchase. Besides, it is equally necessary that where defaults arise on account of defective policies, corrective measures are taken to rehabilitate the non-wilful defaulters so as to obviate denial of fresh credit to them. There is also a need for a long term recovery strategy envisaging annual recovery targets and efforts to achieve them and case-by-case analysis of overdues, etc. besides strengthening the supervision staff in the credit institutions. (Paras 6.66, 68, 69, 74 and 15.058, 068 to 069)

215. With a view to facilitating borrowers who want to hold on to their produce for a longer period after harvest for securing a better price they may be given extension of time for repayment of the loans by three months and be treated as eligible for fresh loans for the next crop, provided they deposit with PACS, produce of a value sufficient to cover their loans and interest. As and when the PACS is able to sell the produce in the market on the instructions of the borrower within this extended period, it would adjust the sale proceeds against his loan account. A pilot scheme may be introduced on a selective basis in PACSs, having proper godown facilities and personnel, for testing the operational efficacy and modalities of this facility. (Paras 15.070 and 071)

216. More attention and effort also need to be given to linking of credit with marketing and processing. (Para 15.074)

217. Overdues position has got unduly inflated on account of lack of a realistic policy in regard to assessing bad debts and the failure of credit

agencies, particularly co-operatives, to writes off their bad debts. It is necessary that each credit agency makes, as a charge on its Profit and Loss Account, full provision for estimated bad debts, irrespective of whether it earns profit or not, and writes off its irrecoverable debts periodically. (Para 15.106)

218. Where overdues under term loans are attributable to system failures or procedural lacunae and not because of lapses of the borrowers, the solution would be on appropriate corrective measures to rehabilitate the defaulters. In all such cases, therefore, a case-by-case analysis needs to be undertaken so as to ensure that there is no denial of institutional credit to them. (Para 15.060)

219. Overdues are at once a symptom and a cause of the weakness of the credit system, compounded further by the socio-economic environment in which the system operates. A number of recommendations have been made which seek to up-grade and strengthen the total framework, structure and management of the credit system. These would call for concerted action both in precept and practice by all concerned at all levels. It is, however, equally necessary that a programme of action be also simultaneously drawn up to contain and recover the overdues. The various recovery disciplines and stipulations laid down so far take the current demand and the arrear demand as one whole, with the result that the inevitably poor performance in recovery of old overdues pulls down the overall recovery percentage, leaving the institution disheartened and with, at best, only a marginal improvement in its eligibility for further finance. It is, therefore, necessary that in the programme of action for recovery, separate norms are set for the two categories of demand. The expected performance norm for current demand should be a recovery of at least 90 per cent in perennially irrigated areas and 80 per cent in other areas, to be achieved within a period of three years. Likewise, a programme of action should be drawn up for the arrear (overdues) demand also, but the norms of yearwise performance and the time span for its achievement will be determined for each institution individually having regard to the particular nature and age of the overdues. If the recovery of current demand itself reaches the desired level, further growth of overdues would have been substantially contained. The NABARD needs to consider the nature of specific incentives it could offer to institutions which have successfully implemented the action programme. (Paras 15.117 - 119)

Chapter XVI : Natural Calamities - Crop Insurance and other Relief Measures

220. A common cause of overdues in the credit system is the incidence of natural calamities like droughts, floods, hail-storms, etc. which result in heavy damages to the standing crops and result in heavy default in repayment of loans. The stabilisation arrangement, in vogue in the agricultural credit system, seeks to find solution to the problems of the farmers sustaining crop damages in the event of natural calamities through conversions/rescheduling of due dates of loans with a view to recovering the loans at a future date. In fact, such conversions/rescheduling only add to the debt burden of the borrowers and are not an adequate answer to the problems of such borrowers. An appropriate solution, it is felt, would be the crop insurance. A Comprehensive Crop Insurance Scheme conceived on right lines and implemented effectively should form a major plank of the agricultural development strategy. (Para 16.13 and 14)

221. The present Comprehensive Crop Insurance Scheme (CCIS) which has been in operation since Kharif 1985, suffers from several shortcomings. Firstly, the scheme is confined to a few crops viz. rice, wheat, millets, oilseeds and pulses in certain defined areas to be notified by each state government. Secondly, state governments have been selecting only such crops and areas where crop-yields are unstable, with the result that cross-subsidization has not been possible. The scheme should cover all cultivated areas and principal crops cultivated and it should be compulsory at least to all borrowing farmers raising the selected crops in the state. (Paras 16.16 and 28)

222. The insurance premia under the scheme, are uniformly fixed on an ad-hoc basis at 1 per cent of insured sum for oilseeds and pulses and 2 per cent for rice, wheat and millets, which are too low to make the scheme viable with the result that the scheme incurs heavy losses year after year. The scheme is operated on an 'area basis' i.e. a complete district/taluka is taken as a basic unit for determining the threshold yield and assessing the crop losses and where the actual yield is less than 80 per cent of the threshold yield, all farmers in the area become eligible for indemnities. The 'area basis' of the scheme entails payment of indemnities to those farmers also who may not have sustained crop losses. For obviating this, it has been suggested that the basic unit may be reduced from district/taluka to a small group

of villages with a specific programme to have 'gram panchayats' as basic units in the near future and that the insurance premia be fixed crop-wise and area-wise on an actuarial basis. The premium should be shared among the farmers, lending agencies and government, the share of the farmers and lending agency being kept to the minimum. (Para 16.23 and 28)

223. While the scheme (the present scheme) has proved to be non-viable it has also failed to indemnify the affected farmer-borrower even to the extent of his crop loan liability. Under the scheme the threshold yield is based on the average yield for the previous five years which also include calamity years so that the threshold yield is too low to entitle affected borrowers for a reasonable relief. It has been suggested that while fixing the threshold yield the calamity years be excluded and only normal years taken into account. Further, the indemnities available under the scheme to the borrowers suffering 50 per cent crop damages work out to around 37.5 per cent of crop loans and where crop losses are total, the indemnities cover only the amount of crop loan but not interest payable thereon. The indemnities under the crop insurance scheme should cover the cost of production including a reasonable amount to cover the imputed cost of family labour and interest on crop loan. (Para 16.32)

224. It is also desirable to have a separate Corporation established under Act of Parliament for implementing the comprehensive scheme of crop insurance as proposed in this report. (Para 16.35)

225. With a view to ensure that the scheme becomes viable, the possibilities of 'reinsurance' within and without the country i.e. abroad should be explored. (Para 16.29)

Chapter XVII : Risk in Agricultural Lending - Credit Guarantee Cover

226. Two guarantee schemes, viz., Small Loans Guarantee Scheme, 1971 and Small Loans (Co-operative Credit Societies) Guarantee Scheme, 1982 operated by the Deposit Insurance and Credit Guarantee Corporation (DICGC) provide guarantee cover to the credit institutions in respect of their credit facilities to farmers and agriculturists. Of these, the latter extending guarantee cover to the co-operative credit institutions, on a selective basis, has

failed to take off as credit co-operatives did not evince any interest in the scheme. The DICGC should formulate a revised scheme covering all PACSs and LDBs. (Paras 17.04 and 05)

227. The major problem of the other scheme viz. Small Loans Guarantee Scheme, 1971 applicable to commercial banks and regional rural banks is that it is non-viable; the amount of claims lodged by credit institutions has exceeded guarantee fees receipts from 1984 and since 1987, the claims actually paid have exceeded the fees. At the end of 1987, the Corporation had a deficit of Rs.202 crores in the Credit Guarantee Fund and a net deficit of Rs.135 crores when all three funds viz. Credit Guarantee Fund, Deposit Insurance Fund and the General Fund were taken together. The Corporation has stepped up, with effect from 1st April 1989, its guarantee fee from 0.75 per cent to 1.50 per cent of the guaranteed advances which does not seem to be adequate. With a view to mitigating the problem of viability of the corporation's guarantee schemes it has been recommended that :

- a) the rate of guarantee fee may be determined on an actuarial basis. (Para 17.17);
- b) Since lending agencies have no capacity to absorb any further increase in the guarantee fee, their liability may be limited to 1.5 per cent as at present and any increase in the guarantee fee that may be necessary may be subsidised by Government. (Para 17.18);
- c) As a pre-condition for invoking the guarantee cover, the credit agencies should be required to ensure that:
 - i) a period of three years has elapsed between the due date of loan and invocation of guarantee and (Para 17.15)
 - ii) all possible avenues (including legal measures) for recovery are exhausted. (Paras 17.15); and
- d) Government of India should allow exemption to the Corporation from payment of Income Tax, Super Tax or any other tax on Corporation's income, profits and gains. (Para 17.20)

- e) RBI should bear the entire cost of staff of the Corporation during the next five to six years i.e. till the end of the VIII Plan. (Para 17.21)

228. It is also considered necessary that in the case of advances under the Poverty Alleviation Programmes, to borrowers who are more risk prone, a higher level of guarantee fees is charged since these schemes are undertaken by the credit agencies under state directives and Government should subsidize the difference in the fees or provide to credit agencies risk fund contribution at two per cent of the loans disbursed under such programmes. (Para 17.19)

Chapter XVIII : Interest Rates, Costs and Margins

229. An administered interest rate structure came to be evolved in India in view of the distortions in the money and capital markets so as to ensure flow of adequate credit to preferred sectors and target groups at certain concessional rates of interest while working towards maximising the returns to the savers on their deposits. The Sukhamoy Chakravarty Committee which had examined the interest rate structure obtaining in the financial systems in the country, had, brought out the deficiencies of the administered interest rates. These are summarised below briefly :-

- i) It failed to promote the effective use of credit and the concessional rates of interest appeared to have allowed projects of doubtful viability to be undertaken, and
- ii) It has resulted in poor customer service and low profitability of the banking systems. (Para 18.01)

230. However, in the present stage of development of the Indian Money and Capital Market, determination of interests rates cannot be entirely left to market forces and a fair degree of regulation of interest rates is necessary so as to provide for an orderly mobilisation of financial savings for the purposes of planned economic development and in the interest of the viability of operations of banks of widely varying sizes in terms of deposits and advances and differing greatly in regard to the quality of their human resources. (Para 18.02)

231. The banks in India have presently little or no control over the interest rates to be allowed on deposits or the interest rates to be charged on loans and advances to various types of borrowers, leaving the only course open to them viz. to keep the operational costs to as low a level as possible. (Para 18.03)

232. Under the administered system the only way the banks can keep their head above water is to cross subsidize the losses suffered on a substantial portion of their resources by higher incomes earned on the deployment of remaining resources in commercial lendings. But the scope for such subsidization is not available to RRBs at all and available only marginally to co-operative banks. Even in the case of commercial banks cross subsidization is possible only within certain limits and not on unlimited scale. (Paras 18.04. to 06)

233. There is, however, scope for them to increase their margins by improving internal efficiency and increasing the volume of business. The banks would, therefore, have to diversify their activities and services so that with the resulting increases in the volume of business, the per unit cost could be reduced. Notwithstanding this, there is need to have a second look at the administered rates and more particularly the rates on concessional lending. The Sukhmoy Chakravarty Committee was of the view that there was scope for reducing the extent of concessionality apart from reducing the number of categories for which different concessional rates have been specified to not more than two. The rate in the case of the lowest category itself, it felt, should be 3 per cent above the maximum deposit rate. (Paras 18.07 to 09)

234. In the long run, concessional credit neither benefits the borrowers nor the lending institutions. Too low a rate of interest is generally equated with grants even as too high a rate comes to be equated with usury. (Paras 18.10 and 11)

235. All in all the position as it emerges is that in the present Indian situation while a degree of concessionality deserves to be retained in favour of the weak and the very weak sections of the community, there is hardly any justification for continuing the same in the case of other sections. Accord-

ingly, there should only be two categories as far as agricultural lendings are concerned, viz. (i) a narrow band exclusively for small and marginal farmers, where the concessional rate will be applicable but even this will be 1.5 per cent above the highest rate of interest on deposits allowed by scheduled commercial banks and (ii) the others i.e. the rest of the borrowers where the rate of interest will be free from directions/regulation subject, however, to a ceiling of 15.5 per cent which is the existing maximum. (Para 18.12)

236. Considering that 53 per cent of the deposits of commercial banks are presently utilised for maintaining cash on hand, CRR and SLR, the return on which is about 8 per cent, the surplus of income accrues from the remaining 47 per cent of the deposits invested mostly in loans and advances. Of these only 26 per cent of the deposits earn higher income at rates above 14 per cent to cross subsidize the losses incurred on mandatory credit granted at uneconomic rates of interest. The scope for cross-subsidization in commercial banks also is thus very limited. (Para 18.15)

237. The studies to assess the currently available margins were based on select institutions viz. PACSs, DCCBs, SCBs, PLDBs and SLDBs under co-operatives and the head offices and branches of public sector banks under commercial banks and the regional rural banks. Of the total number of institutions selected for the purpose, about 80 per cent were ground level units. The study covered three years viz. 1983-84, 1984-85 and 1985-86 for co-operatives and 1984, 1985 and 1986 for the commercial banks and regional rural banks. (Paras 18.18 to 24)

238. As the studies bring out, the agricultural credit delivery system at grass root level is, prima-facie, financially not sound inasmuch as the net margins are negative in the case of PLDBs and PACSs even when the costs of overdues and bad debts are excluded. However, the pattern of incomes and costs was seen to be quite uneven in respect of various such institutions. (Paras 18.25 to 30)

239. There were variations in all respects including financial parameters in the case of PACSs studied. The variations were, however, minimal in respect of incomes from agricultural credit. In these cases where non-credit business

was undertaken by the societies , they earned enough margins which in a large number of cases subsidized the losses of the societies in respect of agricultural credit business. (Paras 18.31 to 33)

240. The analysis has shown a strong relationship between the size of a society and transaction costs which was of a quadratic type. The larger societies could achieve break-even level by stepping up their business by 40 to 70 per cent. (Paras 18.34 and 35)

241. The risk cost, as an approximate estimate, is placed at one per cent of the outstanding advances of PACSs. (Para 18.36)

242. The reduction in the interest rates effective 1st March 1988 together with the changes in the interest rates on refinance has not affected the margins available to PACSs in view of the lower rates effective from that date, on borrowings from higher agencies. (Para 18.37)

243. If the agricultural lendings of a PACS have to be financially viable, the gross margin should be adequate to cover the transaction costs of 4.50 per cent, risk costs of 1 per cent and a surplus of 0.50 per cent. This means the gross margin of 6.00 per cent is required (minimum) at PACS level. While the concessional rate of interest for weaker sections may be retained at 1.5 percentage points above the highest rate of interest allowed on deposits by the scheduled commercial banks, the rate of interest for the rest of the borrowers could be free from directives subject, however, to a ceiling of 15.5 per cent. (Para 18.39)

244. The study has brought out that DCCBs which is the middle tier in the co-operative hierarchy, have an average gross margin of 4.09 per cent with average transaction cost at 3.18 per cent. After 1st March 1988 there has been a drop of about 1 per cent in the interest income of DCCBs on agricultural loans. To enable the agricultural lendings of a DCCB to be self-supporting, the gross margin requirement works out to 3.5 per cent. (Paras 18.42 and 43)

245. In the case of the SCB which is at the apex in the co-operative credit

structure in a state, the gross margin requirement is estimated to be 1.5 per cent. (Para 18.48)

246. A PLDB on an average has the gross margin of 2.39 per cent and transaction cost of 3.39 per cent in respect of its agricultural advances. Taking into account the investment income, the PLDBs have a net margin of 0.28 per cent. The size of a PLDB has significant impact on income, financial cost and margin. In order to enable a PLDB to be self-supporting, a gross margin of 5 per cent is required taking into account the transaction cost of 3.5 per cent, risk costs of one per cent and surplus requirements of 0.50 per cent. (Paras 18.50 to 55)

247. A SLDB under federal system will require gross margin of 2 per cent, taking into account the transaction cost of 1.50 per cent and surplus of 0.50 per cent while an SLDB under unitary system would need a gross margin of 5.5 per cent comprising transaction cost of 4 per cent, risk cost of one per cent and surplus of 0.5 per cent. (Paras 18.56 to 59)

248. The RRBs have a gross margin of 3.20 per cent with average transaction cost at 6.90 per cent. The risk cost and the minimum surplus requirement have been placed at 1.25 and 0.50 per cent. Accordingly, the gross margin requirement of an RRB works out to 8.65 per cent to meet which an RRB will need to have an average lending rate of 16.45 per cent under the existing interest rate structure. This is obviously not possible in view of the entire lendings going to small/marginal farmers. Consequently, the RRBs can hardly ever become viable. For this reason, among others, it has been recommended elsewhere in this report that the RRBs be merged with the concerned sponsoring banks which have the capacity of cross subsidisation to cover the losses on account of weaker section financing. (Paras 18.60 to 62)

249. For a commercial bank, the financial costs and income realisable are Rs.7.48 and Rs.11.62 respectively per Rs.100, resulting in the gross margin of Rs.4.14. The transaction costs are Rs.6.00. The net margin works out to (-) 1.86. The risk cost is estimated at one per cent. The rural, semi-urban and urban branches reveal variations in various financial parameters. (Paras 18.63 to 67)

250. The gross margin requirement of a commercial bank works out to 7 per cent to cover the transaction cost of 6 per cent and risk cost of 1 per cent. (Para 18.68)

251. NABARD's contribution in the total agricultural credit dispensed by all the formal lending institutions by the end of June 1986 has been 45 per cent. The share of co-operatives in NABARD's refinancing volume has been on the decline. In contrast to this, both commercial banks and RRBs are borrowing relatively more and more. (Para 18.69)

252. The requirements of gross margins indicated earlier have been worked out on the basis of the findings of the studies undertaken. These margins are considered necessary if the agricultural lending is to be viable in itself. (Paras 18.49, 76 and 77). It should, however, be clarified that :

- a) These margin requirements are necessary under the existing interest rates structure only and they may be different at different times depending upon the changes that may take place in the interest rates structure of banks on deposits, borrowings and advances.
- b) The indication of separate margin requirements for each tier of the co-operative credit structure is only to assess the viability of each link in the chain as a separate entity. An aggregation of the margins recommended for different levels would, therefore, bear no significance.
- c) The lending agencies could become viable even with lesser margins on their agricultural lending depending upon the scope for cross-subsidization available to them.
- d) Similarly, as the volume of business and the internal efficiency of the lending agency increases, the margin requirement will decline as a result of reduction of transaction cost per unit.
- e) If the interest rates fixed for agricultural lending to different categories of borrowers under Government directives to subserve the social objectives do not ensure availability of the indicated margins, the Government should make good the loss to the lending institutions.

253. NABARD's existing margin at 0.60 per cent is considered sufficient so long as it confines only to refinancing activities. A higher margin will be required for NABARD to enable it to take up developmental activities aimed at improving the financial health of the client credit institutions. (Para 18.73)

Chapter XIX : Autonomy of Credit Institutions

254. There has been a massive expansion in the loan business and branch network of the commercial banks in the last two decades since their nationalisation in 1969. The expansion has not, however, been without the concomittant systemic stresses and strains. Among these, the most disconcerting are (i) the mounting overdues under agricultural loans and sticky advances locked up in sick units in the industrial sector and (ii) the progressive erosion of profitability of the banks. (Para 19.01)

255. One of the important reasons for the declining profitability of banks has been their increasing involvement in providing 'mandatory credit' entailing very rigid 'target setting' pursuant to policy directives by Government. A second reason has been the concessionality they are required to extend in favour of weaker sections. (Paras 19.02 and 03)

256. It is not, however, suggested that the credit systems should or can distance themselves from development programmes. On the contrary, the banks must actively involve themselves in supporting development programmes of the Government evolved in the furtherance of its social objectives. But the irrational manner in which the coverage of 'mandatory credit' is being extended and the 'target setting' is overstretched, causes much concern. The resulting strain is going far beyond what the banking system could contend with and its overall profitability could tolerate. A second point of concern is that interference of the Government and its functionaries with the commercial judgement of the banker and marginalising his role in the appraisal and scrutiny of the projects he is called upon to finance. The short-circuiting of the appraisal procedures and flouting of the established credit norms to suit populist goals would be destructive of the credit delivery system itself and in the process, self-defeating in achieving the goals set for the development programmes themselves. (Paras 19.04 & 05)

257. There has been increasing politicisation of the credit institutions. In co-operatives, it takes the form of taking over managements through normal electoral process or through wholesale supersession of elected boards by the state governments. In commercial banks this is done through nomination of directors acceptable to the Government rather than for their professional credentials or not constituting the full boards. In the co-operatives, politicisation is compounded by increasing officialisation inasmuch as practically all key positions in the management cadre, in the higher tiers particularly are increasingly filled in by Government officials. (Paras 19.06 & 07)

258. There has been a tendency on the part of state governments to show total indifference to effecting or helping recovery of co-operative dues especially close to election to legislatures. Promises of writes off of co-operative dues are also made from the political platforms. Such writes off generate a psychology of non-repayment vitiating the recovery climate everywhere. (Para 19.07)

259. The officialisation of cadres in the co-operatives affects the professionalisation within the cadres. Further, not only some of the officials are not qualified to hold these posts, but they are transferred frequently. The net result is the poor professionalisation of managements in the co-operatives. (Para 19.08)

260. In the case of commercial banks the state control emanates from the Central Government. Commercial banks are as over controlled, over regulated and over managed by the Central Government as the co-operatives are by the state governments. In the implementation of the special programmes and in particular, the poverty alleviation programme, politicisation tends to manifest itself more brazenly. There is growing compulsion on commercial banks to provide financial assistance to projects which are not even potentially viable and borrowers whose commercial viability cannot be improved with bank credit. The beneficiaries of such programmes are often selected not on the very criteria laid down but are selected on extraneous considerations and are granted loans without proper scrutiny. This adversely affects the bank-client relationship and ends in large scale defaults. (Para 19.09)

261. The loans disbursed in Loan Melas were found in many cases, to have been granted without adequate scrutiny or even without applications being received in advance. In the case of such loans which are disbursed by political functionaries not only the bank-client relationship gets lost but even the bank's authority to demand repayments gets adversely affected. (Para 19.10)

262. In the case of NABARD, which functions at the apex of the agricultural credit system at the national level, its operational role is affected by the Central Government pressures on commercial banks in the case of priority sector lending and poverty alleviation programmes and by the state governments' pressures on the co-operatives. Though governmental and political interference are somewhat indirect in the case of NABARD, its task of containing the pressures becomes thereby more difficult. The governmental pressures adversely affect the working of NABARD and its effectiveness in enforcing the needed credit discipline on the credit delivery systems. (Paras 19.11 to 13)

263. What has been even a more disturbing trend has been the growing inroads into the areas of responsibility of RBI itself. As a central banking and monetary authority, the Reserve Bank has distinct responsibilities in the matter of regulatory frame-work relating to money and credit, as well as fixation of interest rates on various types of deposits and loans and advances by banks. The RBI Act provides for an environment in which the Reserve Bank can effectively exercise its responsibilities free from any governmental interference. Even at the time of nationalisation of Reserve Bank in 1949, the then Finance Minister had held out the assurance that the Reserve Bank of India would continue to function as a fully autonomous body. Despite these assurances the Bank's functional freedom is getting increasingly abridged. (Paras 19.14 to 17)

264. In conclusion, it is necessary to stress the urgent need to arrest the growing trend towards the progressive infringement of the authority of the credit system at all levels. The case for respecting the autonomy is not for its own sake but in the larger interest of its healthy survival and the fulfilment of State's social programmes which the system is called upon to support. (Para 19.18)

Chapter XX : The Role of the Apex Level Institutions, Reserve Bank of India and Government

265. Following the recommendations of the Rural Credit Survey Committee, both policy and effort of the Government and the RBI came to be directed towards making co-operatives the sole purveyors of rural credit. However, in view of the new break-through in agricultural technology, the demand for credit increased much beyond the capability of the co-operative credit system. Further, over the years many weaknesses have crept in the co-operative credit system. In the result the credit gap had widened which necessitated supplementing the efforts of the co-operatives by the other credit systems. There was thus towards the latter part of sixties, a shift in policy and commercial banks were inducted in a substantial measure in the field of agricultural credit. Organisation of RRBs in 1975 was yet another attempt to take commercial bank credit to the remote corners of the country and also to cater exclusively to the weaker sections of the society. All the three streams of the credit are ultimately linked either through the state apex organisations in the case of co-operatives or through the head office in the case of RRBs and commercial banks to NABARD for resources to supplement their own. In certain areas where provision of credit is for non-agricultural sector they are linked to IDBI. (Paras 20.01 - 02)

266. The apex level in the main comprises besides the NABARD, the NCDC, the REC, the IDBI, the NCUI and the RBI. The role of both state and Central Governments are equally important. Most of the apex level institutions are linked to Government of India in respect of broad policy objectives and RBI for policy, funding and operational control. (Para 20.04)

267. Apart from setting up Primary Co-operative Development Fund for providing financial assistance to PACSs, NABARD should contribute by way of grants to the PCDFs from out of its R & D Fund. (Para 20.06)

268. Both NABARD and NCDC should work in co-ordination and finance more and more agro-industrial projects. Regular meetings of both the institutions can make possible such a co-ordination. (Para 20.08)

269. The NCDC has launched an innovative programme whereunder the

local resource potential of the selected district is assessed by a specially constituted multi-disciplinary team of experts and suitable programmes of investment in agriculture, allied activities and non-farm sector and strengthening of the co-operative infrastructure are devised to secure full exploitation of the potential. NABARD should take note of this programme and work out with NCDC the modalities for joint support to it. (Para 20.09)

270. To avoid overlapping of functions, there should be proper co-ordination between NABARD and IDBI. Considering NABARD's better ties with rural institutions, it can consider refinancing traditional sectors such as KVIC and state K & VI Boards. (Para 20.15)

271. The programme of rural electrification should be complementary to the agricultural projects financed by NABARD. Hence the question of raising resources required for financing rural electrification is intimately related to the general problem of production-oriented rural credit with which the NABARD is concerned. There should be a NABARD-REC co-ordination committee to improve institutional communication and develop common areas of interest. (Paras 20.17 to 22)

272. The vast network of co-operative credit institutions and commercial banks provides effective boost to the growth and modernisation of rural sector credit. Defaults, inadequate appraisals, permissive lending etc. have to be tackled firmly. Hence, the RBI's innovative approach and active collaboration from Government's side is of crucial importance. Since the supervision and control over the commercial banks lies with the RBI, it has a special role in exercising vigilance on recovery of agricultural dues. As far as recovery of loans by co-operative banks is concerned, NABARD should monitor it carefully. (Paras 20.28 to 30)

Chapter XXI : Integrated Rural Development Programme

273. Considering the vast dimensions of rural poverty, there is, in our view, every justification for direct intervention on behalf of the specific identified poor families so as to give them access to productive assets, such as the Integrated Rural Development Programme, seeks to do, to enable them to increase their levels of income above the poverty line. Exposure of these

families to the discipline inherent in their involvement with institutional credit can be a factor of profound social and economic significance in modernising society. (Para 21.19)

274. However, several deficiencies and inefficiencies have been noticed in the implementation of the Integrated Rural Development Programme, such as wrong identification of beneficiaries, leakages through corruption and malpractices, absence of backward and forward linkages while identifying projects, over-concern with the achievement of targets, inadequacies in the banking structure, excessive concentration on the primary sector activities (Para 21.11) in the implementation of these programmes etc. These inefficiencies were found to exist at all stages of implementation of the programme, starting from the very identification of potential beneficiaries to the supervision and follow-up of the borrowers. In our view, it should be a matter of serious concern that the percentage of beneficiaries who have actually crossed the poverty line (Rs.6,400 per annum) through assistance under this programme is only 13 per cent for the country as a whole, with many states being below this average. Despite these deficiencies, we believe that IRDP could emerge as an effective poverty alleviation programme if certain major changes can be brought in its concept and practice as suggested by us. (Paras 21.20 and 21)

275. Firstly, there must be a meaningful village, block and district level planning to diagnose what activity can be profitably pursued by IRDP participants, at what scale and with what additional services. The concept of IRDP needs to be re-oriented from the present one in which provision of credit is seen as the complete instrument of uplift to a concept where all services and inputs needed are made available to make the new enterprises succeed. Targeting must be realistic in terms of resources and opportunities available. Fixation of uniform targets for all blocks irrespective of varying poverty levels and potentials for development, only make the programme mechanistic and far from productive. We suggest a target of not more than 20 million families during the Eighth Five Year Plan, of which 10 million could be a core target split up uniformly for all the blocks and the balance 10 million broken down blockwise based on the resource potential for each block. A Master List of all the families below the poverty line should be prepared

at one go for all the villages in a block, from which the bankers should identify the families and the projects suitable for financing under IRDP. (Paras 21.23, 24, 39, 41 and 42)

276. The rural banking personnel must enforce normal banking discipline in the choice (out of the listed poor) and supervision of borrowers to preserve the integrity of the banking system and to meaningfully realise the opportunity of bringing the poor within the pale of responsible entrepreneurship. Under constant pressure from government agencies there has been almost a complete erosion in the banking discipline in respect of loans under IRDP. A degree of casualness is beginning to creep into the work ethos of the rural branches of commercial banks, with most of them remaining content with 'walk-in' business besides sponsored programmes like IRDP. We would like to give a clear warning that if this decline in responsible banking attitudes is not checked, its adverse effects will fast spill over also to the normal run of business of the banks, in the process imperilling the whole banking system. (Para 21.25)

277. There is need for several procedural changes in lending under IRDP. Greater emphasis on provision of working capital, fixation of reasonable schedules for repayment, etc., can go a long way in improving the effectiveness of the programme. (Para 21.26)

278. The subsidy to help the poor to overcome their special disability arising from extreme poverty must be provided in a manner which encourages and facilitates the discipline of financial responsibility. There were widespread complaints that subsidy amount was not reaching the beneficiary in full; such leakages are estimated to be as high as 20 per cent and above. This factor itself is bringing the programme into disrepute and is causing resentment among genuine beneficiaries who feel cheated of their full share of assistance. We feel that there is a need to review and revise the mechanism of subsidy administration. Instead of adjusting the capital subsidy to unit cost at the beginning, the same should be retained as a fixed deposit with the bank in favour of the beneficiary and adjusted towards the last one or two loan repayment instalments. (Para 21.27)

279. We feel that an integrated view needs to be taken of a self-employment programme like the IRDP and wage-employment programmes like NREP and RLEGP, recently combined into an enlarged programme entitled "Jawahar Rozgar Yojana" with a considerably higher outlay. Priority for IRDP assistance may be given to those who have some asset base. The remaining ones, mostly belonging to 'destitute' and 'very very poor' categories will not be able to cross the poverty line, except in a few cases, with assistance under IRDP. Assistance would, therefore, need to be given for them both under wage-employment and self-employment programmes simultaneously. Of course, some of them will have to be looked after entirely under the wage-employment programme. Such selection of beneficiaries and allocation among different programmes will have to be done in a planned and calculated way by the DRDA and banks jointly. (Para 21.28)

Chapter XXII : Demand for Agricultural Credit - Projections

280. The demand for short-term and the medium and long-term credit for agriculture from institutional sources has been projected upto the year 1999-2000. While estimating the projected demand for credit, the balance of loans and advances outstanding (i.e. stock) has been estimated as at the end of the year, and not the amount of loans expected to be issued (i.e. flow) during the year. This procedure has been adopted to enable proper comparison of the demand for credit with the resources in the form of stock that will be available with the banks for financing agriculture and allied activities which have been worked out as a percentage of the estimated total outstanding advances (i.e. stock). Hence, for the purpose of comparison, the estimates of demand for credit and the supply of credit are made in terms of outstandings. (Para 22.39)

281. The basic assumption made in respect of the short-term credit requirements for crop production, is that there is a relationship between the value of output of a crop and the cost of cultivation for production of that crop. Such a relationship varies from crop to crop, and for the same crop, from season to season, from state to state and within the same state, from area to area depending on the agro-climatic conditions. The relationship also depends on the technology and practices adopted for cultivation. (Para 22.41)

282. The model adopted for estimation of the financial requirements for crop production is based on the above assumptions. The production cost has two major components, namely, the labour cost and the cost of materials. Under labour cost, the man and the woman days required are worked out separately as certain agricultural operations are done by men alone and certain others are done exclusively by women. Further, the daily wages paid to a man and a woman are different. The labour cost for each crop, for each season, on a per hectare basis for a particular area has been worked out on the basis of man/woman days required for each type of agricultural operation like preparatory tillage, preparation of land for sowing, sowing, application of fertilisers, mulching, weeding, irrigation, application of pesticides, harvesting, threshing, etc. These man/woman days are converted into cash equivalent (wherever there is opportunity cost of labour), based on the normal daily wages for man/woman agricultural labourer. This labour cost, together with the cost per hectare for materials such as seeds, fertilisers and pesticides, and the cost of electricity/diesel for irrigation, hire charges for bullocks/tractors for tillage, etc. will constitute the total cost for the agricultural production operations, per hectare. This expenditure for production, is deemed as the short-term financial requirement for raising the particular crop, per hectare, for a given season and area. (Paras 22.42 and 43)

283. For making projections, the compound growth rate in respect of each crop has been worked out separately for each of the major producing states. Further, projections on an all India basis have also been made in respect of each crop. The main crops for which separate projections are made are rice, wheat and other cereals, gram, other pulses, groundnut, other oilseeds, cotton, sugarcane and potato. The details are given in tables 17 to 26. The crop-wise and the statewise financial requirements estimated are given in tables 28 and 29 respectively. (Paras 22.47, 50 and 51)

284. After estimating the financial requirements for crop production, the demand for credit from all sources, i.e. institutional and non-institutional, has been worked out. For this purpose, it has been assumed that the small and marginal farmers will require credit to the full extent of the cash and kind expenditure for crop production and 50 per cent of the imputed value of family labour. The small and marginal farmers may not have their own

resources to meet even a part of the expenditure for raising crops. Further, a portion of the imputed value of family labour taken into account for estimation of credit requirements, would cover a part of the consumption credit needed by such farmers. In respect of the medium and the large farmers, it is assumed that 25 per cent and 50 per cent respectively of the cash and kind expenditure for raising crops would be met by them out of their own savings. Hence, the demand for credit requirements from the medium and the large farmers will amount to 75 per cent and 50 per cent respectively of the cash and kind expenditure. No credit will be required by such farmers to cover the imputed value of family labour. On the basis of these assumptions, the demand for credit from all sources has been worked out. The details are given in table 32. (Para 22.62)

285. After estimating the demand for short-term credit for crop production from all sources, the demand for short-term credit on institutional agencies has been estimated on the following assumptions. Several medium and large farmers may not approach institutional agencies as they are getting finance from non-institutional sources such as friends and relatives. Taking these aspects into account, it is assumed that the percentage of demand for credit that will be called upon to be met by institutional credit agencies would be as under :

Category of farmers	Percentage of short-term credit for crop production that will be required to be met by institutional credit agencies by the year.	
	1994-95	1995-2000
Small & marginal farmers	60	75
Medium farmers	40	50
Large farmers	40	50

On the basis of the above assumptions, the demand for credit from institutional agencies works out to Rs.15733 crores for 1994-95 and Rs.23888 crores for 1999-2000. The details are given in table 34. (Para 22.63)

286. Based on the growth rate of output of livestock during the period 1970-71 to 1984-85, the growth rates for the periods 1985-86 to 1989-90,

1990-91 to 1994-95 and 1995-96 to 1999-2000 have been projected. Thereafter, the value of output of livestock has been projected upto the year 1999-2000. Though no short-term credit is normally given at present, for meeting the recurring expenditure of milch cattle or poultry, which account for about 80 per cent of the value of production under livestock, it is desirable to provide some short-term credit, not exceeding the cost of feed for one month, so that the farmers' liquidity position is not affected adversely immediately on investment. The feed cost for one month will amount to 8.33 per cent of the cost of the feed per year. In respect of other animals under livestock viz. sheep, goats, pigs etc. it may be desirable to give a slightly larger proportion of the cost of purchased feed as short-term credit. Taking this aspect into account, the short-term credit for livestock is estimated at 10 per cent of the financial requirements (i.e. cost of purchased inputs) per year. The estimated short-term credit requirements for livestock estimated for the years 1994-95 and 1999-2000 are Rs.939 crores and Rs.1,185 crores respectively. (Para 22.71)

287. The short-term credit requirements for fisheries per annum are estimated at five per cent of the total fixed capital investments for fisheries work out to Rs.120 crores and Rs.200 crores for 1994-95 and 1999-2000 respectively. (Para 22.72)

288. The short-term credit requirements for input distribution estimated at two per cent of the total short-term credit requirements for crop production work out to Rs.315 crores and Rs.478 crores respectively for 1994-95 & 1999-2000. (Para 22.74)

289. The methodology for assessing the term credit requirements is based on the hypothesis that the credit requirement is dependent on the private gross capital formation (GCF) in agriculture. The data of GCF in agriculture have been obtained from the statistics published by the Central Statistical Organisation (CSO) for the years 1970-71 to 1984-85. These include capital formation in agriculture for both private and public sectors. The data of public sector GCF are deducted to obtain the private gross capital formation. The data on capital formation by the private sector include farm investments on items such as land development, irrigation works, orchards plantations,

agricultural implements and machinery and livestock. Hence, they cover crop production and livestock sector of the agricultural production sub-system. The growth rates of GCF have been estimated for the periods 1986-1990, 1991 to 1995 and 1996 to 2000 AD, for different purposes. Thereafter the value of GCF has been estimated for different items upto the year 1999-2000. The details are given in table 42 and 43.(Paras 22.76 to 78)

290. After working out the GCF of different items for the year 1984-85, they are compared with the purpose-wise supply of credit through all institutional sources such as commercial banks, regional rural banks and co-operatives. The details are given in table 44. Thereafter the percentage of GCF to be covered by institutional credit for various purposes during the years 1989-90, 1994-95 and 1999-2000 has been estimated. Based on these estimates, the term credit requirements projected for 1994-95 and 1999-2000 are Rs.4,903 crores and Rs.7,595 crores respectively.(Para 22.83)

291. The term credit requirements projected are the term loans to be issued during a particular year. To convert the term loans issued during a particular year, to stock as at the end of the year, the relationship between the term loans issued during a year and the balance outstanding as at the end of that year has been examined for a period of 10 years. It is observed that the ratio of term loans issued during a year to the balance outstanding as at the end of that year is 1:3.46. The details are given in table 50. Using this ratio, the outstandings in respect of term credit for the years 1989-90, 1994-95 and 1999-2000 have been worked out and furnished in table 51. (Paras 22.84 and 85)

292. Term credit requirements for forestry have been estimated on an approximate basis. The details are indicated in table 52. The term credit requirements estimated for the years 1989-90, 1994-95 and 1999-2000 are the cumulative requirements of term credit for five years ending those years. Hence, it will be necessary to estimate the cumulative credit requirements, in terms of outstandings, or in other words convert into stock. To convert the cumulative term credit requirements for five consecutive years to stock as at the end of the fifth year, the relationship between the cumulative total of term loans issued for five years and the balance outstanding

as at the end of the fifth year has been examined. The details are given in table 53. It is observed that this ratio of the cumulative total of term loans issued for five consecutive years ending a particular year to the balance outstanding at the end of the fifth year is 1:0.93. Using the ratio of 1:0.93 the outstandings in term credit for forestry for the years 1989-90, 1994-95 and 1999-2000 have been estimated and furnished in table 54. (Paras 22.92 and 93)

293. The term credit requirements for inland and marine fisheries have been estimated on an approximate basis. The details are given in paragraphs 22.96 and 22.97.

294. The projected demand for credit from institutional agencies for Agricultural Production Sub-system (APS) and the Agricultural Input Distribution Sub-System (AID) has been summarised in table 59. It will be observed therefrom that the credit outstanding as at the end of the years 1989-90, 1994-95 and 1999-2000 would be Rs.21,587 crores, Rs.35,187 crores and Rs.53,322 crores respectively. (Para 22.98)

295. The above projections are made at 1984-85 prices. It will be erroneous to presume that there will be no increase in input prices at all during the next decade or so. At the same time, no estimate of the inflation rate or its impact on agricultural input prices can be reasonably made for a period extending over ten years. For the purpose of this exercise it is assumed that the inflation impact on demand for credit would be 5.0 per cent per annum. The credit requirements have been worked out on this basis. In this connection, it may be stated that the rate used, should not be presumed to be the annual inflation rate during the next 10 to 15 years, but represents only the assumption of the impact of inflation during that period on the demand for credit. Accordingly, the demand for credit for the years 1989-90, 1994-95 and 1999-2000 will be Rs.27,856 crores Rs.57,316 crores and Rs.1,10,873 crores respectively. (Para 22.99)

Chapter XXIII : Supply of Agricultural Credit - Estimates of Resources

296. During the 10 year period ended June 1987, the deposits increased at a compound rate of 18.97 per cent per annum. However, the growth of

deposits during the year 1986-87 amounted to 16.9 per cent only. The decline in growth may be due to the diversion of savings of the households sector into the new issues in the capital market and the new financial instruments produced during the previous couple of years. In view of the above and due to the restrictive policy adopted in respect of branch licensing, the growth rate of deposits for the period of 1987-88 to 1989-90 is estimated at a compound rate of 17.0 per cent per annum. Further, in view of the competition from a wide range of alternative saving instruments including those in the capital market, the compound growth rate of deposits during the years 1990-91 to 1994-95 may be lower at 15 per cent per annum. The growth rate of deposits is likely to decline further during the period 1995-96 to 1999-2000 AD, in view of the high level of deposits that would have been reached by the year 1994-95. The compound rate of growth of deposits during the period is, therefore, estimated at 12 per cent per annum only. The details about the projections are given in paragraph 23.23.

297. During the 10 year period ended June 1987, the total deposits of State Co-operative Banks (SCBs), the District Central Co-operative Banks (DCCBs) and the Primary Agricultural Credit Societies (PACs) increased at a compound rate of 17.2 per cent per annum. However, the growth rate of deposits during the five years ended June 1987 amounted to only 16 per cent per annum. It is estimated that the compound growth rate of deposits of co-operatives during the period 1987-88 to 1994-95 would slightly decline to 15 per cent per annum. Further, in view of the high level of deposits that would have been reached by the year 1994-95 the compound growth rate of deposits of co-operatives during the period 1995-96 to 1999-2000 is likely to decline to 13 per cent per annum. The details about the projections are given in table 15. (Paras 23.24 and 27)

298. For assessing the availability of resources for financing agriculture and allied activities, the credit deposit ratios for 10 year period ended June 1986, were analysed. Thereafter projections in respect of future credit deposit ratios are estimated. As the deposits for future years have already been estimated, the credit deposit ratios will enable us to arrive at the total loanable resources for future years. Thereafter, the percentage of credit for agriculture and allied activities to total credit has been projected for future years. By

using this ratio, the amounts of credit for agriculture and allied activities that could be given by commercial banks upto the year 2000 AD have been assessed. (Para 23.32)

299. The credit deposit ratio declined from 71.4 per cent as at the end of June 1977 to 62.3 per cent as at the end of June 1986. In view of the declining trend of the credit deposit ratio, it is estimated that the credit deposit ratio would further decline to about 58 per cent, 55 per cent and 52 per cent as at the end of June 1990, 1995 and 2000 AD respectively. (Para 23.33)

300. The total advances, i.e including indirect advances of commercial banks, for agriculture and allied activities, outstanding as at the end of December 1986, constituted 18.56 per cent of the total advances outstanding as on that date. It is estimated that the advances for agriculture and allied activities (including indirect advances) would reach the level of 20 per cent of the total outstanding advances by the end of June 1990. The share of advances for agriculture and allied activities to the total outstanding, might decline marginally to 18 per cent by June 1995 and remain around that level upto June 2000, due to the high base level that would be reached by June 1990 and due to the competing claims on credit from agro-processing industries, marketing and storage of agricultural produce and agricultural exports which are the forward linkages of the agricultural production sub system. (Para 23.34)

301. Based on the credit deposit ratio of 58 per cent, 55 per cent and 52 per cent as at the end of June, 1990, 1995 and 2000 AD respectively, and the resources that would be available for financing agriculture and allied activities at 20 per cent of the total outstanding advances as at the end of June 1990, and 18 per cent each at the end of June 1995 and 2000, the resources available for financing agriculture and allied activities would amount to 11.60 per cent, 9.90 per cent and 9.36 per cent of the deposits as the end of June 1990, 1995 and 2000 AD respectively. On the basis of projections in respect. of deposits, the resources that will be available for financing agriculture and allied activities by commercial banks have been worked out. The details are indicated in table 19. (Para 23.35)

302. In respect of co-operatives, the SCBs and DCCBs will have to maintain cash reserve and liquid assets at 3 per cent and 25 per cent respectively of the deposits. The PACSs will also have to maintain liquid resources. These, together with cash in hand, may amount to about 35 per cent of the total deposits. Hence, about 65 per cent of the deposits will be available for loans and advances for agriculture and allied activities and for non-agricultural purposes. Presuming that 10 per cent of deposits will be required for non-agricultural purposes, and based on the projections of deposits of co-operatives, the resources available for financing agriculture and allied activities have been worked out at 55 per cent of the deposits. The details are given in table 20. (Para 23.36)

303. The share of commercial banks in the total short-term and the medium and long-term advances for agriculture and allied activities, outstanding as at the end of June 1975 amounted to only 21.39 per cent and 20.20 per cent respectively. However, there has been an increasing trend in the share of commercial banks, in the total advances for agriculture and allied activities. As at the end of June 1985, the share of commercial banks in the total short-term and the medium and long-term advances outstanding for agriculture and allied activities, amounted to 43.35 per cent and 59.26 per cent respectively. It is, therefore, estimated that the share of commercial banks in the short-term credit on the one side and the medium and long-term loans outstanding for agriculture and allied activities on the other, will increase to 50.0 per cent and 65.0 per cent respectively by the year 1989-90 and may stabilise at that level. This would mean that the declining trend in the share of co-operatives would be arrested as a result of the series of measures suggested towards institutional strengthening, democratisation of co-operatives and the greater involvement of the members in managing the societies. The summary position of shares of commercial banks and co-operatives in the loans outstanding for agriculture and allied activities during the years 1974-75 and 1984-85 and the estimated shares in future are indicated in table 21. (Para 23.37)

304. On the basis of share of the commercial banks and the co-operatives as estimated, the credit requirements to be met by the commercial banks as at the end of June 1990, 1995 and 2000, at 1984-85 prices, and assuming

increase in credit requirements at 5.0 per cent per annum on account of increase in input prices, have been worked out and indicated in table 22. (Para 23.38)

305. It will be observed from the foregoing analysis that there may not be any appreciable constraint of resources in the commercial banking system at 1984-85 prices to finance the projected credit requirements to be met, upto the year 1999-2000. However, at 5.0 per cent increase per annum in the credit requirements, on account of increase in prices, which seems likely, there will be constraint of resources for financing the agricultural credit of Rs.64,037 crores for the year 1999-2000 to be financed by commercial banks, the resources available for the purpose will be only Rs.57,035 crores. (Para 23.40)

306. The credit requirements to be met by the co-operatives as at the end of June 1990, 1995 and 2000, at 1984-85 prices and assuming increase in credit requirements at 5.0 per cent per annum on account of increase in input prices, have been worked out and indicated in table 24. The co-operatives at present depend on NABARD in an appreciable manner for long-term finance. The resources for long-term lending by the LDBs are raised mainly by flotation of special debentures subscribed by NABARD, Central and state governments and by issuing of ordinary debentures. However, in respect of short-term credit, a substantial portion of the resources will be available from the internal resources of the co-operatives. (Para 23.44)

307. The position of demand for credit for agriculture, estimated at constant prices (1984-85 prices) and the resources available, indicate that there may be no difficulty for the commercial banking system to meet its share of the demand for agricultural credit. However, with the increase in credit requirements at 5.0 per cent per annum, on account of increase in input prices, which seems likely, the commercial banks would face constraint of resources for financing their share of the agricultural credit demand in 2000 AD, though not earlier in 1989-90 or 1994-95. This position is, however, subject to our assumptions, based on which the demand for credit and the supply of resources are worked out, not getting vitiated by external factors operating in the economy of the country during the next 10 years or so.

If however, the demand for credit increases and/or the growth of deposits lags behind, because of such reasons as new measures by Government and other financial institutions to attract the savings of the community, there could be a resource crunch under both the scenarios. In the case of co-operatives they have resource deficit for all the years under the second scenario, i.e. credit requirements increasing at 5.0 per cent per annum. They would, as we see it, continue to depend on refinance from NABARD as hitherto, though on a declining scale in the case of short-term loans. This gap is expected to be filled in by NABARD providing necessary refinance. This aspect is discussed in the chapter titled 'National Bank for Agriculture and Rural Development : Role, Organisation and Management'. (Para 23.46)

Chapter XXIV : Credit for Agro-processing and Marketing-Projections

308. With the increase in production of agricultural produce, the forward linkages such as (a) agro-processing industries, (b) storage, transportation and marketing and (c) export of agricultural produce, will have to be strengthened to enable the farmers to realise remunerative prices for the increased produce. The demand for credit for these sub-sectors has been projected upto the year 1999-2000. (Para 24.01)

309. For the purpose of this study, the agro-processing industries would be those, which use not less than 50 per cent of the raw materials from agriculture and where the value added as a result of the processing undertaken is not more than 50 per cent of the final value of output. The agro-processing industries can be grouped under three broad heads, viz. the industries based on (i) crop production (ii) wood and (iii) livestock production. The agro-processing industries based on crop production can be sub-divided into six heads viz. the industries based on foodgrains, oilseeds, sugarcane, fruits and vegetables, fibre crops and plantation crops. The summary of credit requirements for the agro-processing industries is indicated at paragraph 24.59.

310. In this analysis, the credit requirements of the wholesale trade, in the private sector, in agricultural commodities, for marketing (including transportation) and storage for the years 1989-90, 1994-95, 1999-2000 have been projected. The summary of credit requirements is indicated in paragraph 24.74.

311. The short-term credit requirements for export of various agricultural commodities are indicated in paragraph 24.83.

312. The summary of projections in respect of credit requirements for agro-processing industries, marketing (including transportation) and storage and for export of agricultural produce, is given in table 36. These projections have been made at 1984-85 prices. The credit requirements are likely to increase on account of the increase in prices. Hence, an attempt has been made to estimate the credit requirements at current prices also. We have, for the purpose of this exercise assumed the inflation impact on demand for credit at 5.0 per cent per annum and worked out the credit requirements. The details of the projections are given in table 37. It may, however, be added that the rate used here should not be presumed to be the annual inflation during the next ten to fifteen years, but represents only the assumption of the impact of inflation during that period on the demand for credit. (Paras 24.84 and 85)

313. It will be observed that the total credit requirements by the end of June 2000, in respect of the above sectors related to agriculture, will increase from Rs.16,127 crores at 1984-85 prices to Rs.33,527 crores, assuming increase in credit requirements at 5.0 per cent per annum. The credit requirements of these sectors will be met, mainly by the commercial banks and partly by the co-operative banks, out of their resources for non-agricultural advances. (Para 24.85)

314. Presuming that the entire demand for credit for agro-processing industries, marketing (including transportation) and storage and the agricultural exports, is to be met by the commercial banks alone, we have estimated the shares of these sectors in the total outstanding advances of commercial banks as at the end of June 1990, 1995 and 2000. The details are given in table 39. It will be observed therefrom that the shares of agro-processing industries, marketing and storage of agricultural produce and the agricultural exports, in the total outstanding advances of commercial banks would not be unreasonably high compared to their present levels. Further, the actual share of these sectors in the total outstanding advances of commercial banks would be lower, as the demand for credit by these sectors would be met partly by the co-operative banks. (Paras 24.87 and 88)

ACTION POINTS ON THE
RECOMMENDATIONS

ACTION POINTS ON THE RECOMMENDATIONS

I - MAJOR AREAS OF CONCERN

The more important among the recommendations which require priority considerations and consequently call for expeditious action are listed below, subject-wise. The time-frame within which action is to be completed will have to be settled jointly by the Government of India, Reserve Bank and NABARD.

The Agricultural Economy

1. Supply and demand pattern in respect of inputs needs correction to eliminate mis-matches. A higher level of public investment is needed to correct imbalances between supply and demand.
2. Land reforms should receive top priority so as to boost productivity of investments in agriculture.
3. Declining size of farms, over-exploitation of ground water and energy constraints are limitations in expanding production.
4. Greater attention needs to be paid to the areas of resource conservation, soil and water management, conservation of flora and fauna, etc., so as to have sustained agricultural development.
5. A more pragmatic approach will have to be adopted in formulating and implementing price support policies.
6. High priority should be accorded to dryland farming with a view to raising the productivity of unirrigated lands and reducing unemployment in agricultural sector.
7. A conscious policy decision will have to be taken to strengthen agricultural research institutions so that new cost-effective technologies and inputs can be developed.

(Action by GOI/state governments)

Credit Planning

8. A District Credit Plan must emerge from the District Development Plan and similarly a Block Credit Plan from the Block Development Plan. A vertical linkage between the district, block and village development plans, a lateral linkage between development plans and credit plans at the district, block and village levels and a horizontal linkage among base level financial institutions needs to be developed.

9. The aim should be to make the Service Area Approach a Development Area Approach where every block will be allotted to the bank which has the largest presence there through its many branches. Other banks with relatively smaller presence in that block should be allotted other blocks where they have larger presence. Such a homogenisation of blocks is necessary to avoid wastages of resources and efforts.

(Action by GOI, RBI and state governments)

Interest Rates

10. In the present state of development of the Indian money market and capital market, interest rates cannot be entirely left to the market forces to determine and a fair degree of regulation is necessary with a view to providing for an orderly mobilisation of financial savings for the purpose of planned economic development and in the interest of the viability of the operations of banks.

11. It is, however, simultaneously recognised that there is a need to make the administered rate system less complex, more flexible and to this end to reduce both the extent of concessionality and categories of concessional loans.

12. So far as lendings for agriculture are concerned, the proposal is to have in all only two categories of which only one, a narrow band that would be eligible for concessional finance and the other which will be the rest of the borrowers for whom there will be no concessionality.

13. The concessional finance category will comprise small and marginal farmers and other weaker sections only. The NABARD definition for these sections will be uniformly adopted and the rate applicable will itself be 1.50

percentage point above the highest interest rate allowed for deposits in scheduled commercial banks. The other category comprising the rest will be free from any regulation except to the extent of ceiling on the rate of interest which will be the existing maximum of 15.50 per cent.

14. Taking into consideration all aspects for determining the costs and margins and interest earnings having regard to the concessional rate and the ceiling as recommended, the rates of interest have to be so determined by the lending institutions that the interest earnings in the aggregate by the ground level institutions viz. PACSs, PLDBs, RRBs and commercial bank branches, could yield gross margins as indicated below :

<u>Institutions</u>	<u>Gross margin</u>
PACSs	6 per cent
PLDBs	5 per cent
RRBs	8.65 per cent
Commercial banks	7 per cent

In the case of co-operatives, the gross margin requirements for the higher level organisations would be as follows :

<u>Institutions</u>	<u>Gross margin</u>
DCCBs	3.5
SCBs	1.5
SLDB (Federal)	2.0
SLDB (Unitary)	5.5

It needs, however, to be stated that the margin requirements at DCCB, SCB and SLDB (Federal) are meant only as margin requirements for these institutions viewed in the context of their functioning as separate entities and therefore, are not to be aggregated.

15. Since margins are not merely a function of interest rate on deposits and interest earned on loans, but equally validly, a function of transaction costs which in turn are a function of a institutional efficiency and volume of business handled, the endeavour both in co-operative and commercial banking systems has to be for improving the quality of service and thereby increase the volume

of business so that the per unit transaction costs of lending institutions are brought down to the minimum.

16. In the event, the lending institutions are unable to earn the gross margins as estimated as a result of a lower interest rate to any category of borrowers enforced on them in pursuance to government directives in this regard, the shortfall in the interest earnings should be made good to the institutions by the Government so that the gross margin levels upto the required extent.

(Action by GOI, RBI and NABARD)

Commercial Banks

17. The targets fixed for financing the weaker sections and the rural poor, have to be such that the banks can bear the losses on this score through the earnings from their commercial lendings. Mandatory lending has accordingly to be within limits which cross-subsidisation permits so that the viability of the institutions is not adversely affected.

18. The banking system should be made more cost effective than it has been by enhancing staff productivity through proper staff deployment and imaginative manpower development.

19. Mandatory credit by commercial banks which entails target setting, should not result in dilution of the accountability of the banks. To this end, it is necessary that once policies have been laid down and targets set, there should be no interference by any external authority in decision making so far as appraisal and sanction of projects and steps initiated for recovery of loans are concerned. It is also necessary to ensure that the targets set to subserve social objectives are within the bank's financial capacity to bear the losses.

20. There is need to strengthen the equity base of commercial banks in view of the increasing trend in their risk bearing advances. This increase has to be such as to take it to two per cent of the total assets by the year 1990, three per cent by 1995 and around four per cent by 2000 as against the existing level of 1.77 per cent.

(Action by GOI, RBI and the commercial banks)

Regional Rural Banks

21. Regional Rural Banks as a pilot experiment, was conceived when the commercial banks did not have adequate branch network in the rural areas and their staff had not yet oriented themselves to either the problems of rural areas or the special demands of rural lending and as a result, expansion of commercial banks bypassed the weaker sections in the remote areas of the country.

22. In the last 13 years or so, the situation has vastly changed in all these critical areas with the result that the logic and rationale which necessitated the setting up of RRBs in the mid-seventies do not any longer exist.

23. The performance of RRBs since 1975 till date has shown that non-viability is built into the system the way it is structured. The subsidies and concessions have not helped them to become vibrant rural lending institutions in the service of the poor. Instead they have become institutions extending poor service to the weaker sections.

24. It is only a strong and viable structure which can extend the much needed service to the poor. In the circumstances there is hardly any place for RRBs in any future set up for ensuring effective delivery of credit for the weaker sections.

25. Several alternatives such as extending their services to more resilient sections of the rural community, giving a subsidiary status to the RRBs, etc. and let them function as separate entities were considered but not found feasible. There is thus no alternative to a merger of the banks (RRBs) with the sponsor banks concerned.

26. With the merger as proposed, the branches of RRBs will become branches of the sponsor banks and the Head Offices of RRBs merged either with the regional or zonal offices of the sponsor banks. Where such offices do not exist, the RRBs would transform themselves into zonal or regional offices as

the case may be, of the sponsor banks. Suitable amendment to the existing RRBs Act should be made to enable the merger.

27. The losses of RRBs should be shared between Government of India, the sponsor bank and the state government concerned in the same proportion as their existing shareholdings in the RRBs viz. 50:35:15.

28. The branches of RRBs which on merger would become the branches of the sponsor banks, should maintain the past levels in lending to target groups and progressively step them up depending upon the extent of the coverage of the target groups in their respective service area.

29. On the merger of RRBs, the commercial banks should increase their lendings to weaker sections from the current 10 per cent to 15 per cent of the net bank credit.

(Action by GOI, RBI and the state governments)

Co-operative Banking System - Certain General Issues

30. Several state governments have in the recent past resorted to massive supersession of elected boards of management in the co-operative credit structure. This is violative of the basic rationale of organising a credit institution as a co-operative.

31. In a substantial measure the lack of performance by the co-operative banking system could be attributed to this unwhole-some practice. The state governments should, therefore, refrain from using the trust reposed in them under the law governing the co-operatives to supersede the elected boards of management.

32. There have been for quite some time also serious inroads into the autonomy of co-operative credit institutions by the state governments and/or the Registrars of Co-operative Societies. In the interest of the healthy development of the co-operative credit system, it is necessary that such arbitrary powers vested in the Government or the Registrar of Co-operative Societies are withdrawn and the law amended to this effect.

33. Co-operative institutions of all types including the co-operative credit institutions have come to be highly politicised bodies, the fortunes of these thus changing with changing governments.

34. One area in which politicisation has brought about considerable damage to the credit system has been the tendency on the part of the state governments to announce general writes off of co-operatives dues largely to subserve the political interests.

35. The tendency on the part of state governments to grant rebates on the interest rates needs to be curbed if the profitability of the co-operative credit institutions is not to be adversely affected. Secondly, such rebates bring down the interest burden far below the market rates which in turn leads to misuse of co-operative loans.

(Action to be pursued by RBI and NABARD with state governments)

Short-Term Co-operative Credit Structure

36. The three tier hierarchical system in the short-term co-operative credit structure is not only an accepted and appropriate pattern but it has also certain positive advantages. This hierarchical structure should not be tampered with.

37. The yardstick by which the viability of a PACS can be measured comprises its ability to appoint full time paid secretary, to have a regular office premises, to contribute adequately to statutory and other reserves, and pay a reasonable dividend.

38. The RBI guidelines which have been drawn up on this basis for reorganisation of societies should be strictly followed and reorganisation programme completed expeditiously in states where it has not yet been done.

39. An action programme should be drawn up for each PACS for making it viable. Viability includes capability for future development also. Accordingly, the action programme should include a comprehensive plan for the mobilisation of deposits, increase in the volume of business and enlarging the societies' non-credit activities on the one hand and keeping the overdues to the minimum.

Implementation of such a programme of action should be closely monitored by the concerned DCCB and SCB.

40. The cadre system for appointment of secretaries of PACSs where this is prevalent should be scrapped. PACSs should have freedom to recruit their own secretaries without which the boards of management cannot be made accountable for the performance of the societies.

41. The higher tier co-operative credit institutions should help their PACSs with infrastructure facilities like banking counters, safe, etc. To this end, the SCBs and DCCBs should create Co-operative Development Funds to provide assistance to PACSs.

42. DICGC should extend deposit insurance cover to PACSs. Pending this, the state co-operative banks conjointly with the state governments, may formulate a suitable scheme for providing insurance cover for deposits of PACSs in their respective states.

43. Wherever there is multiple cropping, the co-operatives could switchover to the cash credit system.

44. There is a need to have a relook at the accounting system so that the principal and interest collected by PACSs from their members are adjusted respectively against principal and interest due by the PACSs to DCCBs. A group of experts could go into this before the system is implemented.

45. It is necessary to have a two-way system of obligations among the different tiers in the hierarchy. Thus, the DCCB in relation to its member PACSs and the SCB in relation to its member DCCBs should have mutual obligations and rights so that the system could function, as a cohesive whole.

46. Under the above arrangement, the higher tier co-operative will have right to issue directives to the lower ones in order to secure better management and the lower tier will have the responsibility in this regard towards the higher tier.

(Action by NABARD conjointly with SCBs and state governments)

Long-Term Co-operative Credit Structure

47. The Co-operative Societies Acts and Rules in various states should be amended suitably so as to remove the legal restrictions which presently hamper the growth of Land Development Banks and provision of investment finance by them for non-farm activities and in new areas.

48. In view of the un-economical cost of interim finance required by the SLDBs, NABARD should provide this at a concessional rate of interest.

49. The ordinary debenture programmes of SLDBs may not exceed 10 per cent of the total. These debentures may carry a concessional rate of interest of 8 to 8.5 per cent to be subscribed by public sector institutions like LIC, GIC, SBI and nationalised banks apart from GOI, NABARD and state governments.

50. The integration of the two structures viz., the short-term and the long-term, is presently not called for since both structures are weak. There should, in fact, be concerted efforts to strengthen both the short-term and the long-term structures.

(Action by RBI, NABARD and state governments)

The National Bank for Agriculture and Rural Development (NABARD)

51. Though visualised as the apex body for the whole of the agricultural credit system in the country, NABARD's attention until now has been largely on its refinance function.

52. The NABARD needs to emerge in the coming years as the central driving force behind the credit delivery system in rural areas. With a view to ensuring this, NABARD should pay considerably greater attention to its developmental role.

53. In the above context NABARD should be able to give added thrust to its institution-building role particularly to the promotion of viable co-operatives and pay more attention to the non-farm business and agro-processing activities.

54. It is also necessary that its lever of refinance is more effectively used

by NABARD as an instrument to enforce financial disciplines and institutional development. To this end, NABARD should integrate its inspection function with the other two main functions, i.e. refinance and institutional development.

55. There is need to use NABARD's Research and Development Fund more imaginatively and aggressively to identify, evaluate, develop and promote new and practical initiatives in rural development.

56. NABARD will also have to, in the next decade, provide refinance to the client banks on an increasing scale to support investment credit in agriculture. Government of India and RBI should adequately strengthen the resources of NABARD for this purpose. NABARD will also have to gear itself to raise more resources from the market.

57. NABARD should use its refinance and statutory inspections to acquire greater clout over client institutions to enforce the required disciplines. Initially this could be achieved with the help of and in co-ordination with the Reserve Bank of India and in course of time, through enhancing its own image.

(Action by NABARD, GOI and RBI).

The National Co-operative Bank of India

58. In the absence of a national bank, the co-operative banking system has been a two way loser: first, it loses out to the commercial banks the deposits of co-operative surpluses and second, the better and more profitable clientele. The national co-operative bank is proposed to be established to fill this systemic gap.

59. The NCBI will function at the national level as a balancing centre for the co-operative credit system. It will also fill the long felt need of a bank at the national level to function as an effective spokesman of co-operative banking system at the bankers' and other similar national forums.

60. The NCBI will be a bank at the national level owned and operated by the co-operative credit system. It will not in any way overlap the functions of NABARD nor is it intended to be an agency for routing of refinance from

the Reserve Bank or Government of India which function is being performed by the NABARD and for which it has been established.

61. The establishment of NCBI should facilitate the co-operative credit system from the PACSs to the state co-operative banks at the state level in each state and laterally among the SCBs in all states to integrate themselves into a national co-operative banking system and thus foster mutualism and federalism amongst all the constituent units of the system which are the essence of any co-operative system. This should add to the cohesiveness of the co-operative credit movement.

(The two national level federations of state co-operative banks and state land development banks as well as the National Co-operative Union of India will pursue further action in this regard with the Government of India and Reserve Bank of India).

Integrated Rural Development Programme (IRDP)

62. Identification of families below the poverty line should be done in one go for all the villages in the block. This will become a Master List for the block and should be updated every three years. Beneficiary families should be selected from this list.

63. The targets under IRDP during the VIII Plan should be pegged at the existing level of 20 million families.

64. Targets for individual blocks should be fixed under two parts - a core target to be fulfilled by all the blocks and the other, the variable target depending on the potential of each block. Consequently each of the two parts will consist in the aggregate of 10 million families to be covered during the five year period of the plan.

65. The bankers must be fully involved both at the stage of selection of beneficiaries to be assisted and in the identification of purpose for which assistance is proposed to be extended. Without this, they cannot be made accountable for recoveries of loans granted.

66. Subsidy under IRDP would continue to be a capital subsidy as hitherto. This should be kept as a fixed deposit with the bank in favour of the beneficiary

earning normal rate of interest. The proceeds of this will be adjusted towards the last one or two instalments of the loan. This would help check leakages considerably.

67. It is also necessary that there is an integrated approach to all anti-poverty programmes more particularly wage employment programmes on the one hand and self-employment programmes like IRDP on the other. The Master List of the potential beneficiaries will facilitate such an integrated approach.
(Action by GOI, RBI and state governments)

Mandatory Credit and Autonomy

68. The banks in the context of the socio-economic milieu in the country, cannot distance themselves from the development programmes.

69. However, the irrational manner of the extension of the coverage of such 'mandatory credit' and over-stretching of the 'targets' in a way that goes beyond what the banking system could contend with have caused considerable strain on the financial soundness of lending institutions.

70. Another factor which has caused allround concern in recent times is the growing interference of the Government and its functionaries with the commercial judgement of the banker resulting in the latter being marginalised in discharging his basic operational functions. In the long run these trends might not only be destructive of the institutions but of the programmes themselves.

71. There has been growing politicisation of the credit institutions. The tendency on the part of the Government to appoint as directors on the boards of the banks, those acceptable to the Government rather than those who possess professional credentials or not constituting the boards at all, has accentuated the politicisation process. This needs to be kept in check.

72. In the co-operatives, politicisation has manifested itself by management take-overs either through the normal electoral process or when this fails, through wholesale supersession of the elected boards by the state governments.

The politicisation process is further compounded by the ever-increasing officialisation of the movement.

73. "Loan Melas" with a view to accelerating mass lending in the commercial banking system and the state government functionaries announcing intermittently writes off of co-operative dues, have generated a psychology of non-repayment vitiating the recovery climate in both the systems.

74. The excessive control by the Central Government in the case of commercial banks and of the co-operatives by the state governments have had a somewhat deleterious effect on the operational efficiency of the credit systems.

75. The sum total of politicisation in the two systems has been that projects of doubtful viability have come to be financed with the concomitant overdues syndrome, which is the bane of credit systems today.

76. The excessive control by government on the credit systems has, in turn, rendered even a national apex body like the NABARD often ineffective, in enforcing its disciplines.

77. As a matter of fact there have been subtle inroads into the autonomy of the Central Monetary Authority itself, although its statute has provided for an environment congenial to the Reserve Bank discharging its responsibilities free from any governmental interference.

78. Respect for the autonomy of credit systems at all levels is of paramount importance to ensure not only the healthy survival of the systems but even of the state's social programmes which the systems are called upon to support and involve themselves in.

(Action by GOI, RBI and state governments)

Overdues

79. The high incidence of overdues has become a major constraint to expansion and smooth delivery of credit. Since recycling is as important as mobilisation of additional resources, effective measures are called for to

bring down overdues to the minimum within a definite time-frame. It is therefore necessary that a time-bound action programme is drawn up.

80. In drawing up the action plan, the demand should be split into two - one, the current demand and the other, demand under arrears. The target should be to effect recoveries upto 80 per cent of current demand by June 1992, and in areas where there is perennial irrigation or multiple cropping this should be upto 90 per cent.

81. There is need for a common legal framework for commercial banks (including RRBs) and co-operatives in each state. It is necessary in this connection to establish special tribunals at the state level and within each state government there should be a special department for execution of decrees.

82. Since the defaults under many of the poverty alleviation programmes are higher than those under normal loaning, it is of paramount importance that once the policy in regard to and limits of mandatory lending are decided, the bankers are left free to exercise their professional judgement using the bank's normal banking norms for the grant of individual loans without any interference whatsoever.

83. There is above all, the need for a strong political will so as to stem politicisation of credit institutions and misuse of agricultural loans for achieving populist goals.

84. There should be a long term policy formulated at the state government level in each state for effective recovery of agricultural loans.

(Action by GOI and state governments. To be pursued by NABARD)

Crop Insurance

85. Measures adopted so far to combat the recurring problem of defaults due to natural calamities, such as the stabilisation arrangements entailing conversion and rescheduling of loans have only helped increase the debt burden of the borrowers rather than provide an effective solution to the problem.

86. From all considerations, crop insurance is an effective answer but the

present scheme of crop insurance which was introduced about 4 years ago has failed to produce the desired results.

87. The failure of the present Crop Insurance Scheme has been largely on account of its limited application in respect of the crops covered and the method of computation of both the premia and liability on account of claims.

88. Many alternatives were considered, but it was felt that a comprehensive crop insurance which would cover all major crops and all areas in the country with an obligation for all loanees of credit institutions to be participants in the scheme on the one hand and computation on an actuarial basis together with a government subsidy to meet the deficit in the rates of premia which are presently paid could alone effectively combat the problem of mounting defaults on account of recurrent natural calamities.

89. It is also considered desirable that the scheme should be administered by a separate Crop Insurance Corporation which may be established under an Act of Parliament. The mechanics of premia computation and the operation of the scheme could be worked out by an Expert Group.

(Action by GOI, RBI and NABARD)

Manpower Development

90. A comprehensive assessment of the training needs in different sectors has to be made so that a common strategy as well as a set of priorities for training in rural lending could be drawn up.

91. An apex agency should be responsible to co-ordinate, monitor and guide training arrangements in rural banking. This agency should be the Reserve Bank of India.

(Action by RBI / NABARD)

Eligibility for Refinance from NABARD

92. The existing 'eligibility criteria' governing NABARD's refinance under schematic loaning has, in practice done more harm than good to the client banks of NABARD. This, therefore, needs to be scrapped.

93. The background for laying down the eligibility criteria was to ensure that client banks did not indiscriminately resort to refinance facility from NABARD and that NABARD's refinance was available only to such of those institutions who were strong enough to absorb it. Since this in practice has not happened with the eligibility criteria as basis, the proposal is that this may be replaced by "viability criterion" on the lines recommended. The new discipline would apply with immediate effect to co-operative banks and in the case of RRBs, till their merger with sponsored banks as separately recommended.

94. In regard to the commercial bank branches, the viability criterion as proposed cannot, however, apply in view of the fact that the solvency concept which is the basis for viability criterion, does not have relevance to individual branches. In view of this, so far as commercial bank branches are concerned, they would be governed by the modified eligibility criteria as recommended. This can, however, take effect only from 1992-93 and therefore, until then, the existing eligibility criteria will continue to operate in the case of commercial bank branches.

(Action by NABARD)

Regional imbalances

95. It is necessary to have a bolder strategy for increasing the tempo of agricultural lendings in regions which have not received their due share of benefits from institutional credit. With a view to correcting the imbalance, a separate Agricultural and Rural Development Corporation should be established, in each of the three eastern region states, viz., Bihar, Orissa and West Bengal and another for all the states together in the North-Eastern region. All these corporations will be sponsored jointly by the Central and state governments.

(Action by GOI, RBI and state governments concerned)

Apex Level Institutions

96. There should be greater co-ordination between NABARD and NCDC since the two national level organisations undertake activities which have considerable commonalities.

97. Refinance support for the programmes under KVIC and State Khadi & Village Industries Board and handloom industries should continue to be the responsibility of NABARD.

98. RPCD of RBI should take up indepth studies of the problems of agricultural credit whether they relate to commercial banks or co-operative banks, to get a regular flow of feedback of field problems for policy adjustments.

99. Reserve Bank should take up a limited programme of inspections of co-operative banks and until their merger RRBs in the nature of quality control reviews of NABARD inspections.

100. Government of India and state governments should set up early the National Agricultural Credit Relief Fund for giving relief in a systematic manner to farmers affected by consecutive crop failures.

(Action by GOI, RBI, IDBI, NABARD and state governments)

II - OTHER ISSUES

The various other recommendations which call for follow-up action in pursuance to the action taken on the main recommendations are given below. In this case also the listing has been done subject-wise.

Commercial Banks

1. There is no need for the continuance of the DRI Scheme and the same may be discontinued forthwith. (Para 3.15 - Action by GOI and RBI)

2. The need for specialised staff for agriculture sector arises more at the controlling offices of the commercial banks than at the branch level while at the branch level it is necessary to have at all professional levels, staff who have the necessary proficiency in handling the different areas of bank's activities. They should also have a high degree of motivation. (Para 3.35 - Action by RBI and GOI)

3. The commercial banks should have the right staff who are properly trained and motivated to man their rural branches. Certain incentives both monetary and non-monetary are necessary for the staff posted in these rural branches to compensate the hardships of rural posting. (Para 3.37 - Action by RBI/GOI)

4. The banks should gear up their organisational structure, promote schematic lending, improve pre-lending appraisal of schemes and launch recovery drives in co-ordination with state government machinery so as to improve their recovery performance. (Para 3.38 - Action by RBI)

5. It is necessary to have better collaborative arrangements between bankers and the state government functionaries at the field level for effective implementation of the 'service area approach'. Since the co-operative credit system is still a more appropriate rural credit system which is close to the people, it is necessary to associate the co-operatives more closely under the 'service area approach'. (Para 3.50 - Action by RBI)

6. Since the commercial banks have already achieved the various targets and sub-targets relating to priority sector lending, agricultural advances, advances to weaker sections, etc. there is a need to review these norms. (Para 3.67 - Action by RBI)

7. Perfunctory assessment of infrastructural facilities, unrealistic assumptions relating to economic viability of the schemes, lack of proper assessment of scope of lending etc. are some of the deficiencies in the preparation of schemes by banks particularly under the poverty alleviation programmes. The banks should improve their quality of lending by remedying these deficiencies. (Para 3.68 - Action by RBI)

8. The commercial banks should strengthen their post-investment monitoring of the schemes. The evaluation should cover the economic impact of such schemes also. If necessary, professional firms or personnel may be commissioned for this purpose. (Para 3.70 - Action by RBI)

9. While working out repayment schedules for medium and long term loans, banks should take into account the life of the asset, incremental income generated and the consequent repayment capacity of the borrower. The period of repayment fixed should not normally be shorter than what is warranted by these considerations. (Para 3.74 - Action by RBI)

10. There is scope for further simplification of systems and procedures in rural lending. Pass-books should be issued to each cultivator to serve as a record of land holdings as well as borrowings from banks. (Para 3.75 - Action by RBI)

11. Banks cannot be expected to operate effectively without the essential infrastructural facilities like all-weather roads, proper communication facilities, police presence etc. It is, therefore, imperative that states provide such facilities before the commercial banks are asked to open branches in far flung rural places. (Para 3.77 - Action by RBI and GOI)

12. There is need to re-examine and streamline the instructions issued from time to time to the branch managers. They should be induced to take

credit decisions within the overall framework of guidelines and are accountable for their decisions. (Para 3.78 - Action by RBI)

13. There is a need for reduction in the number of returns, simplification of procedures and increasing mechanisation. Mechanisation can also help improved collection, recording and usage of data which could be used more effectively for policy decisions. (Para 3.79 - Action by RBI)

14. Banks should aim at improving the level of efficiency of staff serving in the rural areas measured in terms of the volume of business per employee. This indicator should be watched carefully and monitored branchwise by the management. (Para 3.80 - Action by RBI)

Certain General issues relating to the Co-operative Banking System

15. The higher tiers in the co-operative credit structure should guide their member co-operatives in improving their business and evolving an efficient supervision mechanism and professional/skilled management for the system as a whole. (Para 5.17 - Action by NABARD)

16. Progressively the responsibilities which lie with the Registrar of Co-operative Societies should be vested in the higher tier organisations so far as the lower tier is concerned. (Para 5.17 - Action by state governments and NABARD to pursue action)

17. The higher tier should take the responsibility for evolving appropriate training systems for the non-official office bearers and professional managers of the lower tier institutions. (Para 5.17 - Action by NABARD)

18. A separate fund should be established within the co-operative banking system funded by contributions out of the profits of PACSs, DCCBs and SCBs managed at the district level by the SCB to share the losses of the lower tier. (Para 5.18 - Action by NABARD)

19. The higher tier should have the right to convene the general body meeting of an institution in the lower tier if found necessary. The higher tier should also extend legal and other help to the lower tiers besides exercising

supervisory functions. (Para 5.18 - Action by NABARD)

20. SCBs should extend assistance for the development activities of DCCBs and in particular, provide management assistance to DCCBs which are weak. The SCBs should take the responsibility for approval of appointment of Chief Executives of DCCBs, training of secretaries of PACSs and staff of DCCBs and provide assistance in publicity, public relations, approval of annual budget etc. of DCCBs. (Para 5.20 - Action by NABARD)

21. There should be a shift of emphasis from borrowings to mobilisation of rural savings especially through savings deposits. (Para 5.32 - Action by NABARD)

22. Where supersession of the managing committee or Board of a society becomes absolutely necessary and effected and an interim administration takes over, the law should restrict the period of such interim administration not to exceed six months. In the case of PACSs, the administrator should be appointed by the DCCB and in the case of DCCBs similar powers, if needed to be exercised, should vest in the SCB. (Para 5.38 - Action by state governments. To be pursued by NABARD)

Short-term Co-operative Credit Structure

23. Each PACS should have atleast one full time paid secretary who can handle the business activities on a regular basis. (Para 6.049 - Action by NABARD)

24. The additional share capital requirement of each of the PACSs should be worked out in the light of the programme of action for development and the share capital contribution should be provided by the state government. NABARD should provide the minimum essential requirement of share capital loan to the state government for this purpose irrespective of the level of overdues and other considerations. (Para 6.051 - Action by NABARD)

25. The ratio of linking of share capital to borrowing at DCCB level for PACSs may be fixed at five per cent in respect of both small farmers and others. (Para 6.052 - Action by NABARD)

26. The ratio of share linking to borrowings in respect of cash credits to PACSs for marketing, consumer activities etc. may be reduced from 2.5 per cent to 1 per cent. (Para 6.053 - Action by NABARD)

27. A programme of deposit mobilisation should be drawn up for PACSs in a phased manner starting with those PACSs having necessary infrastructure, staff etc. and in subsequent phases covering the other societies. (Para 6.054 - Action by NABARD)

28. PACSs should endeavour to mobilise more of low cost (i.e. savings) deposits. (Para 6.057 - Action by NABARD)

29. Though there is no requirement under law for providing liquidity cover for deposits of PACSs, it is considered appropriate that they provide 15 per cent of their deposits as liquidity which should be kept in a special savings deposit account with the concerned DCCB. Amounts kept in excess of 15 per cent can be withdrawn by the PACS. The DCCB should pay on this special deposit account a rate of interest of 1.5 per cent higher than the applicable rate of interest on savings deposits. (Para 6.058 - Action by NABARD)

30. The normal credit statements need be prepared by PACSs only once in three years unless the scale of finance is changed in any intervening year. (Para 6.068 - Action by NABARD)

31. There should be no insistence on disbursement of the input component in kind in areas where farmers are already accustomed to the use of these inputs. (Para 6.069 - Action by NABARD)

32. The present stipulation that the cash component of the rabi loan will be disbursed only after repayment of the cash component of the kharif loan should be removed. (Para 6.073 - Action by NABARD)

33. The due date of repayment of rabi loans should be shifted from 30th June to 31st August. (Para 6.074 - Action by NABARD)

34. For providing promotion opportunities to secretaries of PACSs, the secretaries of PACSs may be allowed to compete for the posts of secretaries falling vacant in PACSs of higher business classification and also by the DCCBs earmarking a specific quota of appropriate posts to which recruitment may be made on merit only from secretaries of PACSs. (Para 6.081 - Action by NABARD)

35. Since it may be beyond the capacity of many of the PACSs to pay the salary of the secretary at an appropriate scale, a Fund at the level of the DCCB may be maintained to provide assistance to the extent of deficit in their capability to pay the full salary of the secretary. The SCB, DCCB concerned, PACSs and the state government should contribute to this fund. (Para 6.082 - Action by NABARD)

36. An incentive scheme wherein a part of the remuneration of the secretary will be related directly to the performance in generating additional business and profitability in different areas of activity of the PACS may be introduced. (Para 6.083 - Action by NABARD).

37. The mechanics of the two part salary system may be worked out by the SCB in consultation with the Registrar and others concerned. (Para 6.085 - Action by NABARD)

38. The secretary of PACSs should be trained by the DCCBs early in his career and should be given further training through refresher courses. (Para 6.080 - Action by NABARD)

39. The DCCBs should arrange to conduct appropriate orientation training programmes for the members of the managing committees of all the PACSs to enable the members of the committee to fulfil their role effectively. (Para 6.086 - Action by NABARD)

40. The DCCBs should have a regular system of meetings with the PACSs to interact with them on problems of mutual interest as also the developmental activities. (Para 6.086 - Action by NABARD)

41. The Government of India should extend the scheme for construction

of godown-cum-office premises, prepared and financed by NCDC, so that all viable PACSs should have proper office premises and godown space. (Para 6.093 - Action by GOI, NABARD, NCDC)

42. PACSs should be allowed to give consumption loans out of their own resources against tangible securities. In places where jewel loans are prevalent, PACSs should be allowed to grant consumption loans out of their own resources against security of gold. Consumption loans will be subject to a maximum of 20 per cent of the deposits raised by them. If the Jawahar Rozgar Yojana authorities guarantee repayment from wages earned by such a borrower, it should be accepted as security for consumption loans. (Para 6.095 & 6.096 - Action by GOI, state governments and NABARD)

43. The state governments should not charge the audit cost to the PACSs. (Para 6.102 - Action by state governments. To be pursued by NABARD)

44. Each DCCB should chalk out a vigorous programme of deposit mobilisation with the guidance and assistance of SCB. Various publicity and public relations techniques focussing more particularly on small savings will have to be devised by SCB/DCCBs. (Para 6.107 - Action by NABARD)

45. DCCB should be permitted to lend to non-members to the extent of not more than 20 per cent of the deposits raised by them. The non-members so financed should be made nominal/associate members without any voting rights. (Paras 6.110 & 6.112 - Action by NABARD)

46. NABARD should examine the scope of its present assistance pattern from its R & D Fund and make suitable modifications to enable SCBs and DCCBs to build their technical capability for scheme formulation and implementation. (Para 6.114 - Action by NABARD)

47. SCBs must develop expertise on investment portfolio management for its own benefit and that of DCCBs. (Para 6.115 - Action by NABARD)

48. A time bound Institutional Strengthening Programme should be drawn up for all non-viable institutions as recommended in Chapter XII of the Report. (Para 6.112 - Action by NABARD)

Long Term Co-operative Credit Structure

49. Urgent measures should be taken for bringing about effective functional co-ordination between two wings of the co-operative credit structure. (Para 7.20 - Action by NABARD)

50. State governments should contribute to the share capital of PLDBs under the programme of Institutional Strengthening, which have inadequate owned funds vis-a-vis heavy overdues. NABARD should relax its policy for granting loans to state governments for share capital contribution to PLDBs based on the level of overdues. (Para 7.24 - Action by state governments. NABARD to pursue)

51. State governments should grant additional share capital contribution to SLDBs brought under a programme of ISP to the extent required. NABARD should suitably relax the existing norms stipulated for becoming eligible for government share capital contribution by SLDBs. (Para 7.25 - Action by state governments and NABARD to pursue)

52. SLDBs which have adequate owned funds, should not collect any additional share capital from PLDBs in excess of the prescribed ratio of 3:2. (Para 7.26 - Action by NABARD)

53. SLDBs should be given the same tax concessions as are available for public sector bonds, National Savings Certificates, etc. on the term resources raised by them from individuals. (Para 7.27 - Action by GOI, NABARD and RBI)

54. NABARD should agree to refinance SLDBs by way of loans repayable in suitable instalments instead of special development debentures, wherever a legal provision for raising resources by way of loans exist and pursue with other states/LDBs to fall in line quickly. (Para 7.29 - Action by NABARD)

55. LDBs should take steps to diversify their activities and take up financing dry land development programmes, horticulture etc. (Para 7.33 - Action by NABARD)

56. LDBs may take up housing finance, on an agency basis only, on behalf

of National Housing Bank. LDBs should be paid reasonable agency charges for undertaking this activity. (Para 7.40 - Action by National Housing Bank and NABARD)

57. The state governments should amend the Co-operative Societies Act/ Bye-laws of LDBs suitably to enable the LDBs to take up housing finance on an agency basis. (Para 7.40 - Action by NABARD)

58. The state governments should take early steps to remove the difficulties encountered by borrowers in certain states in execution of mortgage of land. (Para 7.44 - Action by NABARD)

59. LDBs should evolve appropriate policies for recruitment, training etc. of staff and for man-power development for meeting future needs for introducing professional management. (Para 7.45 - Action by NABARD)

60. Well managed viable PACSs should be allowed to grant long-term loans where necessary. (Para 7.62 - Action by NABARD)

The National Co-operative Bank of India

61. The NCBI should function as a national data clearing centre for the co-operative credit system and should take up the publication of the "Review of the Co-operative Movement in India" and "Statistical statements relating to Co-operative Movement in India". (Para 8.15 - Action by NCBI)

62. The investments in the shares of the NCBI of eligible co-operative banks should be treated on par with those in the shares of the higher tier institutions for the purposes of the provisions of Banking Regulations Act. Similarly, in the case of other co-operative institutions, their investments in the NCBI equity, should be treated as permitted investments and it should not be necessary to seek separate permissions for the purpose. (Para 8.28 - Action by NABARD, RBI, RCS)

63. The Banking Regulations Act as applicable to co-operative societies may be suitably amended to provide that the deposits kept by the SCBs and urban co-operative banks with the NCBI will be treated as eligible assets

for liquid assets purposes under Section 24 of the B.R. Act. (Para 8.28 - Action by RBI)

64. The SCBs should be enabled to deposit to the extent of 50 per cent of their SLR with the NCBI. (Para 8.30 - Action by SCBs)

65. The reserve funds and other funds of SCBs and national level co-operative institutions which are to be invested statutorily outside their business should be kept in term deposits with the NCBI. (Para 8.32 - Action by Co-operatives, SCBs)

66. The NCBI should establish a development fund by appropriation from profits and contributions from co-operative federations, larger co-operative enterprises, state apexes both in the short and long-term structures to be utilised for assisting the SCBs and SLDBs to train secretaries/managers of primaries and for taking up research projects. (Para 8.46 - Action by NABARD, NCBI)

NABARD - Role, Organisation & Management

67. NABARD should closely monitor the implementation of the scheme of 'cyclical credit' introduced for the rain-fed areas and provide needed guidance to the banks. (Para 9.014 - Action by NABARD)

68. The NABARD has to continue its support, by way of refinance or otherwise, to the various poverty alleviation programmes and other special programmes launched by GOI. Selective relaxations of credit disciplines to help banks avail refinance under these schemes may be considered. (Para 9.017, 9.020 - Action by NABARD)

69. Since the existing arrangements for compensating the SCBs and DCCBs to maintain the levels of margins following the reduction in interest rates to the ultimate borrowers effective 1-3-1988, cannot be a substitute for a rational interest rate structure, there is need to review the position in this regard and evolve an appropriate interest rate structure for its refinance. The ratios should ensure that the co-operatives get adequate margins as suggested in the Chapter on "Interest Rates, Costs and Margins". (Para 9.023 - Action by GOI, RBI, NABARD)

70. The NABARD should re-emphasise area based schematic lending, modify its investment guidelines and encourage comprehensive integrated lending for rural development. It should take steps in conjunction with RBI to strengthen credit planning and help banks achieve better co-ordination with the district and other local authorities. (Para 9.024 - Action by RBI/NABARD)

71. The NABARD should ensure that its refinance operating cycle is working more effectively. Regional offices should be more actively involved in planning schemes to be refinanced so as to reflect the local needs. (Para 9.025 - Action by NABARD)

72. The potential linked district credit plans now being attempted by NABARD should eventually mitigate the macro and micro credit planning for the credit delivery system, and help upgrading the 'service area approach' to a 'development area approach'. (Para 9.027 - Action by RBI/NABARD)

73. The NABARD should closely monitor the working of the regional offices to ensure that they do exercise the various powers delegated to them. (Para 9.028 - Action by NABARD)

74. The NABARD should build up the capacity of the client banks so that the latter can satisfy themselves about the financial and technical viability on the basis of guidelines furnished by NABARD. This will help NABARD improve its own scheme scrutiny and sanctioning process. (Para 9.029 - Action by NABARD)

75. Unlike the commercial banks, the SLDBs and SCBs are not well equipped for the task of scheme preparation and effective monitoring. NABARD should strengthen their Technical Monitoring and Evaluation (TME) cells. Similarly the experiment of Technical Appraisal Group (TAG) for pooling the technical expertise of banks should be extended. (Para 9.029 - Action by NABARD)

76. The NABARD should arrange to disburse refinance at places convenient to the client banks. (Para 9.030 - Action by NABARD)

77. In selective cases, NABARD should take up direct lending particularly

in the case of Infrastructural Development Corporations for the Eastern and North-Eastern states, recommended in Chapter XI. (Para 9.031 to 9.032 - Action by NABARD)

78. The NABARD should closely watch the various pilot projects it has introduced for strengthening the weak PACSs, DCCBs and PLDBs and draw lessons from these for making suitable adjustments in the programmes. (Para 9.033, 34 and 35 - Action by NABARD)

79. Unlike RBI vis-a-vis commercial banks, NABARD has little say in the management of co-operative banks. A greater degree of professional management has to be brought about in the co-operatives by NABARD. This could be achieved by NABARD's representation in their management and having a say in the appointment of their Chief Executives. (Para 9.041 - Action by GOI/RBI/NABARD/state governments)

80. The scope and content of NABARD inspection reports should be improved. The analysis and recommendations therein should help the banks improve their performance and also provide NABARD useful information for monitoring and evaluation of its refinance. (Para 9.046 - Action by NABARD)

81. Consultants V have specifically reviewed the effectiveness of the NABARD's organisational structure and have recommended certain models. NABARD may adopt these models with such modification as it may consider appropriate. (Para 9.050 to 057 - Action by NABARD)

82. The Advisory Council of NABARD should be a compact body of experts not exceeding 12 in all drawn from universities, research institutes, client banks, Government departments and apex institutions. (Para 9.058 - Action by NABARD)

83. The current practice of NABARD Board discussing sectorwise state status papers on problems of individual states and giving policy directions may be continued. Such meetings with state level representatives will help solve the local problems. (Para 9.059 - Action by NABARD)

84. The NABARD should have a high profile corporate identity with effective regionalisation and decentralisation. There is also a need for increased employee motivation with acceptance of responsibility, authority and accountability. The regulatory role which is predominant now has to give way to that of development and service. (Para 9.060 to 065 - Action by NABARD)

85. Consultants V have made several recommendations relating to organisation and collection of information, monitoring and evaluation, management information systems and computerisation strategy, details of which are contained in Chapters XXIII, XXIV, XXV, XXVI & XXVII of their report. NABARD may consider these recommendations as modified by the Committee and initiate suitable action. (Para 9.066 to 082 - Action by NABARD)

86. The management of training of NABARD's own staff should be separated from that of client banks. Regarding its own staff NABARD should undertake a detailed analysis of training needs, develop a co-ordinated approach to management of training and improve the design and delivery of training programmes. (Para 9.087 to 088 - Action by NABARD)

87. The NABARD should identify the training needs of the client banks and provide the needed professional training advisory service to assist and guide them in making their training more effective. (Para 9.090, 091 - Action by NABARD)

88. There should be a closer co-ordination between BIRD and CAB with their respective areas of functioning broadly demarcated so as to avoid an overlap in their activities. (Para 9.094 - Action by NABARD).

89. NABARD may have to refinance short-term loans to co-operatives to an estimated extent of Rs.2,677 crores by the turn of the century. RBI should continue to provide this amount through the general line of credit to NABARD as hitherto. (Para 9.107 - Action by RBI)

90. With a view to enabling NABARD to play the enlarged role assigned to NABARD in agricultural sector as well as in the non-farm sector and provide the refinance support therefor it is necessary that its share capital is raised

by Rs.200 crores on a 50:50 basis by GOI & RBI. NABARD's resources have to be strengthened by other means also so that it can retain a reasonable profit margin. On its part, NABARD should gear itself to mobilise resources from the open market atleast to the extent of 10 percent of its annual requirements. (Para 9.108 to 124 - Action by GOI, RBI and NABARD)

Development Plans and Credit Planning

91. Credit Planning to be effective needs to be backward-linked with a development plan in physical terms and forward-linked, via. credit disbursing agencies, with the borrowers. (Para 10.05 - Action by RBI)

92. In the current state of data and information at the village and the block levels, it is appropriate to begin development planning at the district level. The district plans can then be split into block plans and village plans. (Para 10.07 - Action by RBI)

93. Unlike the National Plans or the state plans, the district plan would have to concern itself with the targeting of output and investment - both public and private. (Para 10.10 - Action by RBI)

94. Since the objective of a District Credit Plan is to convert the physical targets of output and investment in each activity into their credit equivalents and pursue their achievement and implementation, it is necessary to frame a set of physical targets of output and investment for different activities for the district for the reference period. (Para 10.15 - Action by GOI)

95. Once the District Credit Plan is available separately in terms of investment targets for the government and the credit targets for private investment as well as production activity in different sub-sectors, the credit plan will have to be split by the district Credit Planning Committee into separate sub-totals for each block. (Para 10.18 - Action by RBI)

96. The block planning committee should take over that part of the district development plan and the district credit plan which pertains to the block along with the activity targets for production and investment credit in different sub-sectors of the block economy. (Para 10.24 - Action by RBI)

Regional Imbalances

97. Each Agricultural and Rural Development Corporation should take up area-wise, potential-studies formulate projects and arrange for necessary linkages and supporting services for the projects. (Paras 11.30 to 32 - Action by GOI, NABARD and state governments)

98. State governments in the Eastern and North-Eastern region states should assume greater degree of responsibility to develop appropriate policies, mechanism and machinery for developing the needed infrastructure. (Para 11.33 - Action by the state governments concerned. Issue to be pursued by NABARD)

Eligibility Criterion for Refinance

99. Switchover to viability criterion would involve NABARD extending full refinance to solvent co-operative banks and RRBs. As a pre-condition for unrestricted refinance from NABARD, solvent client banks should improve recoveries and achieve recovery upto 80 percent of current demand by 30.6.92 (Para 12.17 - Action by NABARD)

100. Other banks should be taken under ISP and as a part of ISP the NABARD should provide suitable refinance to them. (Para 12.19 - Action by NABARD)

101. Branches of commercial banks failing to achieve recovery of 40 percent under current demand and 25 percent under arrear demand, should be taken under ISP, and as a part of ISP the NABARD should provide suitable refinance to them. (Para 12.25 - Action by NABARD)

102. For applying ISP, NABARD should classify co-operative banks/RRBs into (a) solvent (b) solvent but in danger of losing solvency and (c) Others. (Para 12.26 - Action by NABARD)

103. If a bank under ISP, fails to implement the programme or it remains non-viable despite implementation, the bank would be deemed a non-bankable risk and, therefore, would be ineligible for any further refinance from NABARD. (Para 12.18 - Action by NABARD)

Staff - Training & Man-power Development

104. There is a need to improve the quality of training in the training institutions. (Para 13.25 - Action by RBI & NABARD)

105. Specialised institutes should be set up in the co-operatives sector to train secretaries of PACSs so as to upgrade their functional capabilities. These institutes should be a part of SCB, which should be responsible for the quality of training for secretaries (Para 13.26 - Action by NABARD)

106. The members of the management committees of PACSs should also be trained so as to avoid any gap in the perceptions of the management committees and the secretary. This training should be a two level training, one a basic training programme in the principles of co-operation and the other, a short duration training on co-operative credit so as to up-date their knowledge. (Para 13.27 - Action by NABARD)

107. The training of personnel of SCB/DCCBs should also be strengthened (Para 13.28 - Action by NABARD)

108. The Principals and Training Managers would also need suitable training, so that they can tackle the problems of training effectively and make the training programmes purpose oriented. (Para 13.29 - Action by NABARD)

109. The personnel department of each bank should operate closely with the training department and training institute(s) to formulate effective training strategy. (Para 13.29 - Action by RBI/NABARD)

110. Greater collaborative arrangements among various training institutions dealing with rural banking are needed and should be arranged. (Para 13.32 - Action by RBI/banks)

111. It is necessary that BIRD should evolve itself into a central training organization on the lines of the NIBM, with a core-faculty engaged in training senior-executives and carry out high level research in rural credit. It should be a semi-autonomous agency with close relationship and firm financial support from NABARD. (Para 13.33 - Action by RBI/NABARD)

112. There is need for a shift in emphasis at the apex level from direct training to training of trainers and production of training materials. (Para 13.34 - Action by RBI/and NABARD)

113. As a sequel to each training programme it is necessary to (a) evaluate training programme itself, (b) ensure that the placement of trainees is appropriate and relevant to the training received; and (c) evaluate the trainees on the job performance. (Para 13.35 - Action by RBI and NABARD)

114. It is necessary to introduce computers into staff training gradually not only to increase the efficiency of training techniques but also to create computer awareness. (Para 13.36 - Action by RBI and NABARD)

Accounting System, Computerisation and Management Information Systems

115. The banks should adopt manual accounting system as proposed so that with its adoption, computerisation in due course is facilitated. (Para 14.17 - Action by RBI/NABARD)

116. In order to provide for automatic determination of ageing of overdues under short-term, banks should open new SAO Loan accounts each year. (Para 14.24 - Action by RBI/NABARD)

117. NABARD should prepare an accounting and MIS manual for the recommended systems and distribute this to client financial institutions. (Para 14.28 - Action by NABARD)

118. NABARD should run training seminars on the accounting and MIS manual for the banks. (Para 14.28 - Action by NABARD)

119. Accounting system may be changed in the co-operative sector to provide for remittance from lower level institutions to be allocated between interest and principal in the books of receiving institutions in the same manner as they have been allocated and accounted for in the books of the lower level institution, when it received payment. (Para 14.34 - Action by NABARD, state governments, SCBs, DCCBs, SLDBs)

120. NABARD should include interest in its definition of demand collection and balance for SCBs and DCCBs. (Para 14.35 - Action by NABARD)
121. Provisions for anticipated losses on bad and doubtful debts should be made by banks regardless of whether they are earning profits. (Para 14.40 - Action by NABARD and banks)
122. NABARD should deduct the quantum of bad debts when assessing an institution's solvency for viability criteria purposes. This could also be adopted for LDBs whose inadequate profits prevent them building up resources to sufficiently cover their genuine bad debts. (Para 14.41 - Action by NABARD)
123. NABARD should stipulate the use of the RBI accounting policy on interest by co-operative banks. (Para 14.42 - Action by NABARD)
124. For assessing the bad debts of LDBs, NABARD should consider and adopt the formula developed by the LDB federation. (Para 14.46 - Action by NABARD)
125. NABARD should stipulate that standard accounting policies be adopted by banks in the periodic financial reports. If this is not practicable, NABARD may require that supplementary information be provided with the financial reports explaining the accounting system followed. (Para 14.47 - Action by NABARD)
126. A computerised Management Information System (MIS) should be set up at the district level. (Para 14.57 - Action by RBI/NABARD)
127. A Management Systems and Standards (MSS) Committee should be formed. (Para 14.95 - Action by NABARD/RBI)
128. NABARD must play the principal role in control, direction and financing of the MSS Committee through its R&D Fund. (Para 14.96 - Action by NABARD)
129. The project of making the district level data base a credit information bureau should be included in the list of top priority studies to be financed by

NABARD's R&D Fund. (Para 14.99 - Action by NABARD)

130. NABARD should hold immediate discussions with NIC on its computerised strategy of installing super mini computers at each of the 438 district centres to ascertain if there would be spare capacity for banks' use. (Para 14.81 - Action by NABARD)

131. The lead bank of the district should be responsible for obtaining the required information from all the branches in the district, in prescribed returns for feeding to the computer at the district level. (Para 14.05 - Action by RBI/NABARD)

Overdues

132. Measures should be initiated to improve recoveries upto 80 percent of current demand by 30 June 1992. However, in areas having perennial irrigation/multiple cropping, the recovery should be fixed even at a higher level. (Para 15.117 - Action by NABARD)

133. Active support and co-operation from the State Government machinery is necessary for the success of the above recovery programme. (Para 15.119 - Action by state governments)

134. Where defaults are attributable to institutional failures, corrective measures should be taken, on a case-by-case basis in order to rehabilitate "non-wilful" defaulters. (Para 15.118 - Action by NABARD)

135. In cases where a borrower desires to hold on to his produce in the expectation of higher prices, and he deposits the produce with the PACS, the Society should extend the due date of crop loan by three months. In such cases the higher financing agencies should in turn grant corresponding extensions in due dates to the PACSs. (Para 15.070 - Action by NABARD)

136. A pilot scheme may be launched so as to facilitate the above arrangements and to encourage the PACSs to take up marketing of agricultural produce. (Para 15.071 - Action by NABARD)

137. There should be a periodical review of the Units costs of all investments. In order to avoid delays, the lending banks should have the discretion to admit unit costs even when they exceed those fixed by NABARD, but upto 10 percent. If as a result, the lending bank becomes, eligible for higher refinance, NABARD should sanction it. (Para 15.061 - Action by NABARD)

138. The lending agency should invariably ascertain the requirements of working capital and ensure its availability at the time of scheme appraisal itself. (Para 15.062 - Action by NABARD)

139. The lending agencies should adequately strengthen supervision staff for improving the quality of their loaning. (Para 15.065 - Action by NABARD)

140. A package programme should be evolved which envisages fixation of recovery targets, acknowledgement of debt by all borrowers annually, improving contacts with borrowers and periodical write-off of bad debts. All credit agencies should implement such a programme. (Para 15.069 - Action by NABARD)

141. Efforts are necessary on a massive scale to educate the borrowers on the right use of bank credit for increasing agricultural production and inculcate in them the commercial discipline. (Para 15.068 - Action by NABARD)

142. Development of infrastructure, research and extension services for promoting agricultural production are a pre-requisite for better recoveries. (Para 15.110 - Action by NABARD and state governments)

143. Effective steps need to be taken for linking of credit with processing and marketing. This would help improving recoveries. (Para 15.074 - Action by NABARD)

144. The Directorate of Institutional Finance in each state should prepare location-specific bankable projects and get them sanctioned by the banks for ensuring the optimum exploitation of available potential in line with the overall perspective of agricultural development in the state. The Department should also develop necessary infrastructure and linkages for the projects. (Para 15.076 - Action by NABARD)

145. The comprehensive legislation as recommended by the Tiwari Committee for overcoming the lacunae in the Model Bill suggested by Talwar Committee, should be expedited. (Para 15.083 - Action by NABARD and GOI)

146. Amendments to the State Co-operative Societies Acts are called for to facilitate recovery through legal measures more effectively. (Para 15.086 to 096 - Action by NABARD and state governments)

147. Improvement in the recovery of agricultural dues is possible only if state governments extend more active government support and co-operation. (Para 15.095 - Action by state governments. To be pursued by NABARD)

148. Irrespective of whether they earn profits or not credit institutions should make provisions every year to cover bad debts by charge to its profit and loss. (Para 15.106 - Action by NABARD)

149. There is no useful purpose served in carrying in the books of the co-operative credit institutions, loans which have proved irrecoverable. It is, therefore, necessary to issue specific guidelines in this regard to the institutions concerned. (Para 15.104 - Action by NABARD)

150. The practice of group loaning is recommended for wider adoption. (Para 15.079 - Action by NABARD)

Natural Calamities

151. Govt. of India/State Government should plan development of non-farm activities as a principal source of livelihood for the cultivators in chronically flood/drought prone areas and where crop insurance may not be viable. (Paras 16.14 - Action by GOI and state governments)

152. The existing Comprehensive Crop Insurance Scheme needs to be amended on the following lines :

- (i) It should cover all cultivated areas and the principal crops cultivated.

- (ii) For ensuring cross-subsidisation, an essential element in any insurance scheme, there should be automatic coverage of all borrowing farmers raising selected crops in a state.
- (iii) The basic unit for determining the threshold yield and assessing the crop losses should be a small number of agro-climatically homogenous group of villages with the aim of having gram-panchayat as a basic unit.
- (iv) The threshold yield per hectare of crops may be fixed with reference to 'normal' yield (excluding calamity years) instead of 'average' yield.
- (v) For making insurance scheme viable, premia rates may be fixed on an actuarial basis, crop-wise, for different agro-climatic areas.
- (vi) The burden of premia rates may be shared among the insured farmers, the lending agency and Government, the share of farmers and lending agency being kept to the minimum.
- (vii) The possibilities of the insurance within the country or abroad should be explored.
- (viii) The sum insured, should cover the cost of production including interest on crop loans and a reasonable amount to cover the imputed cost of family labour of the farmer.
(Paras 16.23, 28, 29 and 32 - Action by GOI and DICGC)

153. An Expert Committee of Actuaries, Accountants, Agronomists, Meteorologists, Agricultural Economists may be set up to work out modalities of the proposed crop insurance scheme. (Para 16.36 - Action by GOI)

Credit Guarantee Cover

154. A separate credit guarantee scheme may be formulated covering all co-operative credit institutions at the primary level. (Para 17.05 - Action by DICGC)

155. There should be a periodical review of the ceiling regarding Corporation's maximum liability in respect of claims. (Para 17.05 - Action by DICGC)

156. There is a need to amend Section 25A of the DICGC Act to preclude transfer beyond prescribed limits, of amounts from Deposit Insurance Fund to the Credit Guarantee Fund and vice-versa. (Para 17.12 - Action by DICGC)

157. There is also the need to fix deposit insurance premia and credit guarantee fees on an actuarial basis so that the accruals to the respective funds match the withdrawals therefrom. (Para 17.13 - Action by DICGC)

158. The share of the lending agencies in the guarantee fee may be limited to 1.5 per cent, as at present, and any increase in the fees be subsidised by Government. (Para 17.18 - Action by GOI)

159. Government should subsidise the guarantee fees in respect of loans under poverty alleviation programmes or alternatively provide to the commercial banks (including RRBs) a risk fund contribution at 2 per cent of loans disbursed under poverty alleviation programme. (Para 17.19 - Action by GOI)

160. With a view to mitigating the problem of DICGC's non-viability;

- (i) the Corporation should be granted exemption from payment of income tax, sur-tax; and
- (ii) the RBI should bear the cost of Corporation's staff during the next 5-6 years.

(Para 17.20 and 21 - Action by RBI and GOI)

161. The genuineness of the guarantee claims needs to be test-checked. Suitable administrative machinery should be set up for this purpose. (Para 17.16 - Action by DICGC)

Apex Level Institutions

162. NABARD should contribute by way of grants to the Primary Co-operative Development Fund maintained in each of the SCBs from out of its R & D Fund, on a scale warranted by the programme content and the number of societies

to be covered for upgradation in the respective states. (Para 20.06 - Action by NABARD)

163. NABARD should take note of the innovative programme initiated by NCDC viz. Integrated Co-operative Development Programme and work out with NCDC the modalities of joint support. (Para 20.09 - Action by NABARD)

164. NABARD and NCDC should agree on an appropriate division of responsibilities at operational level and co-ordinate their activities by regular meetings of its co-ordination committee with representatives of all concerned departments. (Para 20.10 - Action by NABARD, NCDC, GOI, RBI)

165. NABARD should not normally refinance any rural electrification scheme unless they have the technical clearance from REC. If there is any constraint of resources, the Special Projects Agriculture Schemes should have the first claim for NABARD assistance among rural electrification projects. (Para 20.20 - Action by NABARD, REC)

166. Where there is delay in release of NABARD and nominated bank's share of SPA schemes, NABARD should provide interim finance to the full extent of its share to be adjusted against releases to be made in due course. Necessary modifications in the relative SPA agreements between REC, NABARD and commercial banks should be made in this regard. (Para 20.20 - Action by NABARD, REC)

167. For the above purpose, REC may be recognised as an institution eligible for direct finance from NABARD. (Para 20.20 - Action by NABARD, REC)

168. NABARD-REC Co-ordination Committee should be set up to improve institutional co-ordination and develop common areas of interest. (Para 20.22 - Action by NABARD, REC)

169. NABARD should establish effective co-ordination with NCUI to make optimum use of the experience and skills that NCUI/NCCT network possesses for training of personnel of co-operative credit institutions. NABARD should directly involve financially and otherwise, in training arrangements needed

for the agricultural credit system. (Para 20.24 - Action by NABARD, NCUI, NCCT)

170. The Regional offices of RPCD of RBI should be suitably strengthened so as to enable them to emerge as focal points of co-ordination between government agencies, co-operative banks, regional office of NABARD and commercial banks in the respective states. (Para 20.29 - Action by RBI)

171. RBI should assume a special role in exercising vigilance on recovery of agricultural loans by commercial banks and should monitor the definite action plans to be drawn by commercial banks at branch level to bring down the overdues within a specified time frame. (Para 20.30 - Action by RBI)

172. In the case of co-operatives, the NABARD should monitor the recovery of loans and the implementation of various suggestions made in the Report by making suitable arrangements for such monitoring. (Para 20.30 - Action by NABARD)

173. State governments with the assistance of Central Government should take up the responsibility of administrative and educative aspects of extension work. (Para 20.37 - Action by GOI and state governments)

174. State governments should remove some of the impediments which hamper the smooth working of the credit system e.g. co-ordination of various agencies involved in timely and adequate provision of input supplies and services, ensuring stability and adequacy of prices of agricultural commodities, legal provisions and staff for execution of decrees for recovery of agricultural loans. (Para 20.37 and 38 - Action by state governments)

175. State governments should provide financial and organisational support to the Institutional Strengthening Programme to ensure its success. (Para 20.39 - Action by state governments)

Integrated Rural Development Programme

176. Activities having sufficient potential in the area, based on its resource endowments, market potential and available infrastructure should only be selected under IRDP. (Para 21.32 - Action by GOI and RBI)

177. Technically feasible and economically viable projects and schemes should be formulated for a given area and then the families from the target group, selected on considerations of their pre-assistance asset base and skills (including traditional skills), their entrepreneurial traits and their own choice, should be fitted in such projects. (Para 21.32 - Action by GOI/RBI)

178. The preparation of viable projects should be a pre-condition for release of Central assistance for IRDP to the DRDAs. Likewise, NABARD should also make such project planning as a pre-condition to extending its refinance facility. (Paras 21.33 and 34 - Action by GOI, RBI and NABARD)

179. Fuller involvement of the popularly elected local bodies at village, block and district levels, is called for both in operational planning and implementation of the programme. (Para 21.35 - Action by GOI)

180. While sanctioning loan for any unit, the working capital needs should be very specifically assessed and financed. (Para 21.45 - Action by RBI)

181. The unit costs for different projects have come to acquire a certain rigidity. There is a need for a certain degree of flexibility to be allowed to the banks in deviating from the standard unit cost for purposes of financing and subsequent refinancing by NABARD. (Para 21.45 - Action by GOI, RBI and NABARD)

182. Government should contribute every year to the Bad Debt Reserve Fund of the commercial banks (including RRBs) at the rate of two per cent of the loans disbursed by them under IRDP during the preceding accounting year. (Para 21.46 - Action by GOI)

Appendix I

TERMS OF REFERENCE OF SEG

Senior Expert Group (SEG)

Objectives : The objective of the SEG is to evaluate the major problems and issues currently affecting the agricultural credit system, as outlined in the five Review studies, and to make recommendations for a program to strengthen the sector.

Detailed Terms of Reference : The main task of the SEG will be to prepare an integrated report for the strengthening of the Indian agricultural credit system, which will contain recommendations and an implementation timetable for the carrying out of the proposals. The SEG's other duties will include, but not be restricted to :

- (i) Guiding and monitoring the implementation of the Review studies including the general format of the consulting groups' working plans and agreed timetables; assist them whenever possible in obtaining the requisite information and the co-operation of all those concerned with the Review.
- (ii) Reviewing and commenting upon consultant's interim and draft reports and ensuring that prior to finalization, such reports are made available to GOI, RBI and the Bank for their comments. Following review of interim reports, SEG should recommend appropriate changes in work programs, where necessary, to RBI and discuss these changes in review meetings.
- (iii) Organizing review meetings with consulting groups.
- (iv) Familiarizing itself with the issues that have dominated agricultural credit over the past 20 years.
- (v) Addressing the broad questions affecting the agricultural credit system, including but not limited to those concerning :
 - (a) the future role of the credit system in view of Government plans for development of the agriculture sector ;
 - (b) future resource requirements of agricultural credit; and how they can be satisfied;
 - (c) the structure of the agricultural credit system, and the roles of its major components;
 - (d) control and supervision of the agricultural credit system;
 - (e) the role of lending margins and their impact on agricultural credit.
 - (f) improved recovery of agricultural loans ;
 - (g) the financial position of financial institutions, including desirable levels of reserves ; and
 - (h) recruitment and training of staff of financial institutions.
- (vi) Undertaking such activities as it deems necessary to reach a thorough understanding of the agricultural credit system.

Appendix II

TERMS OF REFERENCE FOR STUDIES

STUDY I : AGRICULTURAL CREDIT IN GENERAL

Objective : The objective of this study is to examine the role and operations of the entire agricultural credit system within the broader context of India's development and to make recommendations to enable the system to enhance credit quality, strengthen efficiency and effectiveness, and improve loan recovery.

Detailed Terms of Reference : The study should assess how, within the framework of India's current poverty alleviation and development policies, the role of the agricultural credit system should evolve; and which factors will have impact on its efficiency, effectiveness, and institutional integrity. Specifically, the study will assess the volume of future flows of funds into and out of agriculture sector, the effectiveness of schematic and special program lending within agriculture, the effect of lending targets, the role of subsidies, and the impact of loan recovery on the financial position of credit institutions. The consultants will examine the following issues pertaining to the role and operations of the entire agricultural credit system:

- (i) assess the effect of agricultural interest rates on demand, recoveries, and mobilization of deposits.
- (ii) review the present and future likely requirements for resources for investment in different subsectors and the agricultural credit system's overall role in mobilizing and allocating resources among subsectors.
- (iii) requirements for short and long-term agricultural credit. The impact of financial variables and the changing pattern of agricultural investments would be included.
- (iv) the role of agricultural credit in India; the linkages and inter-relationships between credit and subsidies; and how the special needs of certain subsectors of the community or certain regions can be met by subsidies or grants without detriment to the credit system; and what safeguards are needed when the credit system must be used as the conduit or agent of such special schemes.

Within the context of these general issues, the following should be investigated :

- (a) What is the role of direct subsidies in agriculture, and what is their effect on agricultural production and credit? How do subsidies affect credit operations, repayment discipline, and the selection of investments to be financed?
- (b) What is the magnitude and impact of special poverty alleviation programs and disaster relief programs on agricultural credit operations? How can the effectiveness, efficiency and control of these

programs be improved, and what role should the banking system play in these programs?

- (v) Assess the effect of the imposition of lending targets and/or quotas on credit operations. Review the reasons for targetting by various agencies and investigate whether alternative arrangements would be feasible and desirable. In this respect, review the role and effectiveness of district credit plans, their formulation and objectives and recommend how their effectiveness could be enhanced.
- (vi) Review how the granting of credit and control over subsequent repayments can be shielded from outside pressures (e.g., non-credit related interference at various levels). Assess the feasibility and impact of the proposed measures.
- (vii) Assess the effect of current levels of overdues of cooperative banks, regional rural banks and commercial banks on their financial position and review how these overdue levels affect credit discipline and institutional and financial integrity. Review policies and other measures which would enhance recovery.
- (viii) Examine the role of extension services, marketing organization and block development services that support credit operations, and propose how their roles could be enhanced.

STUDY II : THE ROLE AND EFFECTIVENESS OF LENDING INSTITUTIONS

Objective : The objective of this study will be to review the role and effectiveness of lending institutions engaged in the provision of agricultural credit and to make proposals and recommendations for such changes as appropriate, to establish a sound and viable credit system and institutions, which will be able to adequately provide service to the rural population.

Within the context of the Review, this study will be particularly complex, because it would deal with a multitude of agricultural credit institutions. To keep the study within manageable proportions, it will focus on a sample, including the number of branches of Land Development Banks (LDBs), Regional Rural Banks (RRBs), Commercial Banks (CBs), State Co-operative Banks (SCBs) and District Central Co-operative Banks (DCCBs). The number of banks in the sample would be as follows: LDBs - 8, RRBs - 10, CBs - 6 ^{1/}, SCBs - 6, and DCCBs - 10. In addition, the study would analyze the operations of a sample of 30 Primary Agricultural Credit Societies (PACs). The final selection of the sample will be made prior to the start of the study by the consultants in consultation with RBI, and take into account that: (i) the sample represents all major regions and agricultural systems; and (ii) the sizes of banks selected largely reflect the current size distribution of all banks.

Detailed Terms of Reference : The main focus of this study would be on the operations of agricultural credit institutions, and how the quality of lending operations and financial services to the farmers could be improved. Specifically the study would :

1/ The review would only deal with the agricultural operations of the CBs.

- (i) Analyze the present role played by the short-term co-operative credit institutions (PACs, DCCBs, SCBs), other co-operative banks (LDBs), and departments or divisions in charge of agricultural operations in CBs and RRB; examine their inter-relationships and methods of operation, particularly at the "grass roots" level.
- (ii) Examine the effectiveness and efficiency of each group of institutions including; (a) their financial structure and viability; (b) administration, personnel, training and managerial systems; and (c) branch expansion policies, taking into account the experience gained by the pilot scheme. 1 /.
- (iii) Following such analysis, make recommendations concerning the future role, structure, and functions of the co-operative credit institutions, RRBs, and agricultural credit operations of CBs.
- (iv) Examine the staffing and training requirements of credit institutions at all levels; assess the training capacity and capabilities presently available; paying particular attention to the appropriateness of the training being given in relation to the needs, particularly at the grass roots level, and make proposals on how the various groups of banks' training activities should be strengthened to satisfy future requirements over a five-year period, and who should be responsible for ensuring training quality; examine the availability of specialist staff for recruitment, and recruitment procedures; examine the implications of current employment practices on credit institutions.
- (v) Analyze loan recovery profiles for each group of banks, including overdues by age and bad debts with proposals as to how they should be dealt with. Review current methods to estimate bad debts and how bad debt is dealt with, and examine current NABARD guidelines dealing with bad debts.
- (vi) Analyze the root causes of overdues, ascertaining whether they are attributable to lending policies, staff shortages, faulty technology, outside interference etc., and make proposals for overcoming the problems.
- (vii) Examine the existing methods for debt rescheduling, including those under calamity conditions, and make recommendations for any changes required.
- (viii) Investigate the methods and legal aspects of loan recovery, particularly the effectiveness of present collateral arrangements; review whether the insistence of some banks upon legal mortgage

The pilot scheme, executed by NABARD attempts to improve credit delivery at the grass roots level by instituting regular visits by Bank staff to farmers, training activities, and improved management practices.

over land is necessary or effective; and determine what are the legal impediments, if any, to using direct methods of loan recovery such as stoppages from salaries or wages and compulsory stop orders on crop proceeds from such sources as ginneries, coffee factories and other marketing organizations; is the concept of joint liability by lending through associations and farmers' clubs pursued, are legal delays through the courts an impediment to loan recoveries and are they too costly; what is the role and impact of the credit insurance scheme of the Deposit Insurance and Credit Guarantee Corporation (DICGC), particularly on CBs and RRBs; what will be the impact of bad debt claims on the future financial position of DICGC; and, having considered all aspects of this subject, make proposals for such changes in the system as are deemed appropriate.

- (ix) Review the effectiveness of the concept of "lead bank" particularly with respect to the IRDP program and formulation of district credit plans.
- (x) Review current policies and practices with respect to branch expansion and assess their effect on lending efficiency and the effectiveness of credit delivery.

STUDY III : THE ROLE AND FUNCTIONS OF THE APEX LEVEL IN AGRICULTURAL CREDIT

Objective : The objective of this study will be to define and clarify the role and functions of the apex-level institutions within the agricultural credit framework, their relationship to each other, and their relationship to their client financial institutions.

Detailed Terms of Reference : This study aims at assessing the most desirable role for the apex-level, and what steps are required for the apex-level to assume and execute such role. Specifically, the study should focus on the following subjects :

- (i) Analyze the role and functions of the apex-level in agricultural credit, including, but not limited to : (a) financing and refinancing; (b) the supervision and control of loans made by all lending institutions engaged in agricultural credit; (c) institutional performance; (d) monitoring and guiding training activities; and (e) the planning and implementation of national and State policies.
- (ii) Assess the current role and influence of the apex-level in the policy making process at the Central and State Government level and analyze what role each should play in the development and implementation of agricultural credit policies.
- (iii) Assess the methods by which the apex-level reviews and controls the financial integrity of its client banks, particularly co-operative credit institutions. Review how current eligibility criteria affect the financial position of banks.

- (iv) Review the effectiveness of the present system of schematic and non-schematic lending and refinancing of term loans and assess whether and how improvements could be made.
- (v) Propose monitoring and control mechanisms which will ensure that the credit system is properly managed, lending is effective, and recoveries maintained at acceptable levels. In this respect, the question of eligibility criteria for institutions to participate in agricultural lending must be fully investigated, whether such criteria are effective and how they can be enforced, and make proposals for changes in the existing criteria system if deemed necessary. Recommend methods for maintaining up-to-date data on overdues, including statistics by lending categories and age of overdues.
- (vi) Examine institutional accounting systems, including those at the field level, and make recommendations for improvements. Determine what steps are needed to quicken the introduction of computer technology. Analyze the need for generating accurate and meaningful data on lending at the lower institutional level; assess what type of data are required at higher levels to maintain overall control over agricultural credit.
- (vii) Determine the role of the apex-level in enhancing the quality, effectiveness, and volume of staff training activities of its client banks.
- (viii) Having considered the above questions, formulate broad recommendations concerning the future role, objectives, and functions of NABARD, paying particular attention to :
 - (a) its capital structure and sources of funds;
 - (b) the adequacy and effectiveness of its legal mandate and its effectiveness in enforcing directives and guidelines;
 - (c) its role, functions and relationships with other national and State-level institutions involved in agricultural credits, including an analysis about the delineation of responsibilities;
 - (d) its relationship with other lending institutions (particulary CBs) and State Governments including an analysis of its responsibilities concerning: (i) bank inspections; and (ii) monitoring and evaluation of agricultural lending operations, institutional performance of financial institutions, and their financial position;
 - (e) how effectively and efficiently to ensure improvements in the quality of lending operations of institutions, including improvements in technical standards, management, and operational practices; and
 - (f) how to ensure and enforce appropriate staffing and staff training in individual credit institutions.

STUDY IV : LENDING COSTS AND MARGINS

Objective : The objective of this study is to assess whether currently available lending margins are sufficient, in comparison to the costs of lending operations in agricultural credit and, if not, to give recommendations to improve the situation.

Some of the main points which must be considered are listed below, but others may well arise during the review and should not be excluded. The aim of the review is to develop proposals for lending costs, and margins to ensure the proper functioning of an efficient credit system. The proposals should allow for adjustments which may be required from time to time in light of changes in the costs of resources, reserve requirements, etc.

Of relevance are the staffing needs and staff training facilities required for lending institutions, the critical overdues situation, and an assessment of bad debts. Allowance must be made for increases in staff and training facilities and bad debt reserves that may be recommended under Study II. (The Role and Effectiveness of Lending Institutions).

Another important aspect to be borne in mind is increasing CB participation in agricultural credit operations and the rapidly growing percentage of small loans provided under poverty alleviation schemes by CBs and RRBs.

A considerable amount of work has already been done on these subjects in the past by RBI and NABARD and considerable data are available which will need to be updated. The consultants would use the same sample of financial institutions as detailed in para 10 above to provide data for this study.

Detailed Terms of Reference : The study should:

- (i) estimate the costs of lending for the various groups of lending institutions which will take account of :
 - (a) the type of lending e.g. short-, medium- and long-term, whether secured or unsecured, the purposes for which the funds are lent, whether many small loans are involved and what degree of technical and other supervision will be required;
 - (b) the risks involved in various types of lending, in particular, the effectiveness or otherwise of collateral and the reserve requirements to protect the financial viability of institutions;
 - (c) the costs of raising funds internally and from other sources;
 - (d) the costs of overdues and bad debts in terms of reduced liquidity and costs of collection, taking into account the role of the credit insurance scheme of the Deposit Insurance and Credit Guarantee Corporation; and
 - (e) administration costs at all levels, taking into account the paramount importance of adequate supervision, particularly technical supervision, at the field level.

- (ii) review how institutions are currently meeting those costs; are they being subsidized directly or indirectly and whether these arrangements are satisfactory or should be modified. In addition, the study should review the level of DICGC fees and who should pay them;
- (iii) examine the present margins being obtained from various institutions; review whether such margins do provide adequate incentives for banks to lend effectively;
- (iv) review whether current NABARD margins are appropriate in the light of NABARD's estimates of future lending and operating costs, taking into account NABARD's likely costs of funds;
- (v) in light of conclusions reached from (i), (ii), (iii) and (iv) above, make recommendations for appropriate margins.

STUDY V : ORGANIZATION AND MANAGEMENT STUDY OF NABARD

Objective : The objective of the study is to prepare a set of recommendations and a timetable to strengthen NABARD's operations to make it a more effective apex institution for agricultural credit.

Study Implementation : The study will start about eight months after the other four studies have commenced. Its recommendations should be divided into two parts: (i) the long-term reforms required, and (ii) those which can be introduced immediately. The study should also take into account the results of improvements made during the proposed NABARD I project in NABARD'S organization and operations.

Detailed Terms of Reference : The study should address :

- (i) the staffing of NABARD, including managerial positions; are staff and training adequate at all levels and if not, what is required to remedy the situation as rapidly as possible; is delegation of authority and the use of discretionary powers effectively used and are personnel policies adequate;
- (ii) arising out of (i) above, what is the adequacy of staff training facilities both external and in-service; is training appropriate to functions performed; if training is inadequate, how can it be improved, not only in the long-term, but in the short-term;
- (iii) in view of the recommendations of the four other studies concerning the role and functions of NABARD, are NABARD's organization, operational and administrative guidelines and manuals, working methods, and management structure and management practices appropriate, and if not, how should they be adjusted. Specifically, the study should review;
 - (a) NABARD's accounting and data processing systems, and make recommendations for the introduction of a computer system;

- (b) NABARD's management information requirements and how they would be satisfied;
 - (c) NABARD's operational procedures for appraisal of individual investments and schemes; how can the quality of NABARD appraisals, including technical and financial evaluation be improved and made more effective; and how can control systems be set up to assure adherence to NABARD guidelines, conditions of disbursement, and eligibility criteria;
 - (d) NABARD's procedures for updating guidelines for investment costs, repayment schedules, and working capital requirements. How could they be made more up-to-date, flexible, and area specific; and
 - (e) the functions and operations of NABARD's regional offices; and
 - (f) the effectiveness of NABARD's organization structure and suggest changes where necessary.
- (iv) the effectiveness of NABARD's monitoring and evaluation systems, both for its own activities and for those investments it refinances. How can the effectiveness of monitoring and evaluation operations and follow-up be improved;
 - (v) the quality and effectiveness of NABARD's inspection operations. How should inspections be enforced, and how should their findings be used in the general operations of NABARD;
 - (vi) the quality and effectiveness of NABARD's participation and supervision of lending operations and credit planning at State, district and block levels. How should directives be enforced and how should effective NABARD participation in credit planning be ensured. Specifically, NABARD's functions with respect of IRDP should be strengthened and improvements recommended;
 - (vii) the capacity of NABARD to guide, monitor and evaluate efforts to strengthen the institutional framework and lending operations of financial institutions it refinance, or those requiring rehabilitation;
 - (viii) NABARD's role and capacity to monitor training activities of its client banks, and advise financial institutions on their training needs, training organization and effectiveness and efficiency of training activities; and
 - (ix) how the recommendations developed above to strengthen NABARD's operations, should be implemented, and what assistance, if any, NABARD should receive.

Appendix III

AGRICULTURAL CREDIT REVIEW SECRETARIAT

Shri R. Sundaravaradan *

Chief Officer

Shri V. P. Nargolkar

Joint Chief Officers

Shri S. John

Shri K. P. Padmanabhan

Shri A. B. Unde

Shri G. B. Bhooshanan

Deputy Chief Officers

Shri M. P. Sukumaran

Shri H. N. Bhohe

Assistant Chief Officers

Shri A. K. Har

Shri S. C. Kakar

Shri D. Ray

Shri T. J. D'mello

Shri P. R. Wanī

Development Officers

Shri A. B. Bhusari

Shri V. Hariharan

Staff Officers

Shri K. A. Shaikh

Shri D. J. Sabhnani

Private Secretary Gr.B

Shri J.A. Pinto

Shri K.A. Kanade

Private Secretary Gr. A

Shri S.V. Kelkar

Shri R. Venkataraman

Other Staff

Shri R. K. Bandekar

Smt. K. G. Kamat

Shri V. Ramachandran

Shri S. B. Panhale

Shri S. R. Pillai

Smt. K. V. Chauta

Smt. G. S. Parab

Smt. J. H. Lobo

Smt. H. G. Quadros

Smt. V. V. Kamath

Smt. V. L. Deorukhkar

Shri J. C. Gawai

Shri A. M. Bhalerao

Smt. P.Ranganathan

Smt. C.P. Haryani

Smt.M.K. Makhija

Shri V.K. Avhad

Shri A.G. Polekar

Shri S.M. Patankar

Shri Y.D. Pawar

Shri C.H. Salunkhe

Shri U.P. Nagvekar

Shri D.K. Gamre

Shri C.S. Bhangre

* He assisted the Committee in the preparation of Draft (Final) Report from January to March 1989.

Appendix IV

RESTRUCTURING THE CO-OPERATIVE CREDIT SYSTEM FOR STRENGTH

(A Brief Concept Paper)

A

THE PREMISES

1. The premises of this paper are :
 - a. that the present credit co-operatives are in a weak condition - and the urgent need is to strengthen them.
 - b. That one way of strengthening them - in addition to the many standard ways being recommended in the report such as : improvement of recoveries, lending procedures and supervision, training, management, full-time secretaries, deposit mobilization, etc. - is structural or systemic in nature in recognition of the postulate that tiny weak units (such as the co-operative credit institutions) if grouped or integrated into a unified and cohesive system can acquire the inherent capabilities and dynamics of generating strength for the system and for themselves provided the system is appropriately structured and equipped for a strengthening process.
 - c. That an appropriate structure - and this is true in any organized grouping of disparate units - is one which has a unifying, strong and concerned leader as an integral part of the system.
 - d. That to create a head or leader whose strength and capabilities have yet to be developed over time and have yet to be promoted by and derived from a weak membership is an approach whose chances of success are highly speculative - and one which should be avoided if there is at all an alternative. And there are in fact alternative (as explained in Part F).

B

THE STRUCTURAL CONCEPT

1. The Present

The existing co-operative credit structure is briefly described as follows:

- a. There are 2 types of state co-operative systems or structures - one for ST and one for LT. So in each state, we have 2 co-operative systems each with its own respective apexes. At present there are 31 ST state co-operative structures and 19 LT state co-operative structures each with its own respective apexes and members :

For ST :	Apex	=	SCB
	Members	=	DCCBs PACs

bound together by share captial relationship which binds the apex and the members into a state system.

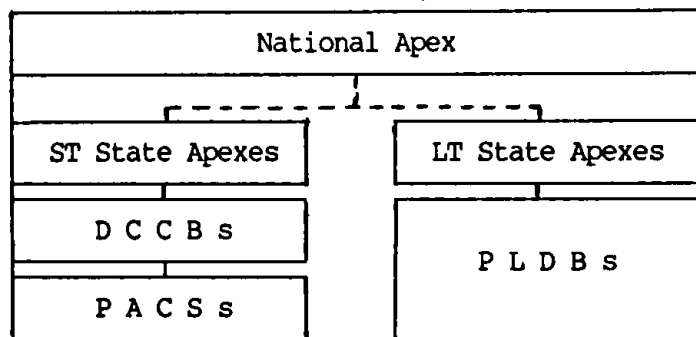
For LT : Apex = SLDB
 Members = PLDBs

(Likewise linked together into a state system by share capital as the link)

b. But these 50 independent and disparate systems are not linked or bound together into one national structure or system.

2. The Proposed

3. The proposed structure may be briefly described as follows :



- a. The big box is the "system" and the smaller boxes are the "components".
- b. All components are integral parts of the system and bound together by links such as share capital and/or indebtedness and/or such intangible bonds as mutuality of interest or sharing of fate, success or failure.

C

THE FUNCTIONAL CONCEPT

4. The Role of the National Apex

- a. To be the source of strength for, and to strengthen the system and its members which at present are badly in need of strengthening in terms of restoration of solvency, and viability and other strengthening measures to those in need of such measures.
- b. Because it is an integral part and leader of the system, the National Apex will feel the tremendous moral pressure of responsibility and concern for the sound condition and efficient functioning of the system of which it is a part (which feeling of responsibility and concern will be absent in case of a "detached apex").
- c. Because of said responsibility and concern, it should necessarily be clothed with concomitant authorities, such as :

- o. to give such financial assistance to component units as equity infusions, deposits, refinance, direct loans (as distinguished from refinance),
 - o. to give technical and advisory assistance and to exercise inspection authority over the system,
 - o. to exercise appropriate administrative and financial control and disciplinary powers over the system,
 - o. to exercise such other powers as may be deemed appropriate and consistent with the desired government power structure over the credit system.
- d. It will have such banking and related powers as may be deemed appropriate for effective service to the component units of the system and for its own viability and profitability (which powers may include export/import financing especially for, but need not be limited to, the agricultural sector).
- e. It will make possible to a certain extent welfare banking since Apex funds or Government funds, can be made to flow to the unbankable rural poor through the component units acting as agents, trustees or fund managers of said funds, or under some other arrangements as will insulate the lending units from the losses of welfare banking (this suggestion will actualize the postulate that the losses from unremunerative and negative-yielding welfare banking are the burden of the government).
- f. It should function as the mechanism for the nationwide transfer of funds from "surplus" areas to "deficit" areas.
- g. It will "pool" (for unified and co-ordinated dispersion) all government resources and funds especially intended for rural and agricultural financing.
- h. It will be the depository of the co-operative system (credit and non-credit).
- i. It will be the spokesman of the co-operative credit system.
5. The Role of the State Apexes :

As sub-apexes, the state apexes are to function along similar lines as the National Apex in so far as the state system is concerned.

D

THE NECESSARY ATTRIBUTES OF THE NATIONAL APEX

6. In the context of the objective of the restructuring (which is strengthening of the system and component members; making them viable; making them effective instruments for rural and agricultural credit; facilitating the flow of credit to the co-operative members and the rural poor), the

National Apex:

- a. Should be strong if it is to be the initial strengthening force of the system - or "primer" of strength, which in due time should result from efficient operations and profitability to be brought about by the standard strengthening processes.
- b. Should be profitable for viability, growth and continuing strength and for capability for cross-subsidization purposes.
- c. Should enjoy government support at the initial life of the system; government equity to be gradually "phased out" as co-operative ownership is "phased in" and as the system and members gather strength over time. The succeeding paragraphs are further elaboration of this paragraph.

E

WHY GOVERNMENT FINANCIAL SUPPORT TO THE NATIONAL APEX

7. Government support and involvement is essential but temporary and should only be present at the front-end of the process of strengthening of the credit structure. The main reasons for this postulate are the following:

- a. Welfare banking has been recognized and postulated to be a government responsibility and that responsibility can be given meaning by strong government support to the apex for "downstreaming" funds to the unbankable rural poor through the lending units as agents. It is the expectation and hope that the unbankable rural poor will in the process graduate to bankability and viability which will then obviate the need for the needed government support; but the "priming" funds logically should be government's.
 - b. The weak units of the envisioned co-operative credit system need financial strengthening and/or rehabilitation which can mean infusion of funds (such as equity, deposits, refinance, loans) which can involve considerable amounts and can be costly in terms of no immediate returns and yields, and even losses. It is again postulated that this is not the responsibility of private funds. Again, the expectation and hope is that the lending units will eventually achieve strength and viability which will then obviate the further use of government resources for propping them up ; but the "priming" funds should be government's.
 - c. The Apex needs a "seed" fund (meaning capital and other resources from Government) large enough to start up and see through the Apex to viable operations. Again, the expectation is that the Apex which should be a strong apex at the beginning will develop further viability, profitability and strength and obviate the continuance of government support, but the "priming" funds should be government's.
8. That government participation will, in due course and under a programmed basis, be gradually "phased out" as the private co-operative members

are "phased in" for eventual complete private ownership and control of the system.

9. To assume that government support is not needed especially at the start of a strengthening process for a weakened structure, might be highly unrealistic.

F

THE CREATION OF THE NATIONAL APEX : THE ALTERNATIVES

10. The obvious and traditional way of organizing a national apex is to organize it by the supporting base and intermediate level co-operative units. It should be from the start, owned and capitalized by the co-operative credit structure and that strength should flow from the base to the apex.

11. This procedure is traditional and normal for the creation of an apex if the purpose is primarily for having an organization at the national level, in which case there should be no objection to that approach.

12. But, the concept in this paper is that the restructuring is for evolving an integrated system for the purpose of strengthening the system and its members, and if those premises are accepted then the need is for a strong apex even at the beginning which has the capability to lead and spur the strengthening process.

13. Again, if strengthening is the objective, then the creation of a new apex whose strength is yet to be built may not be the appropriate approach and should be avoided if there are at all alternatives that will make possible initial strength. And it is felt that such alternatives exist.

14. Such alternatives are :

- a. First alternative: Organize the new national co-operative bank to meet nominal corporate requirements or what the co-operatives can meet and that the corporate shell shall be "fleshed" out with the transfer to it of all the financial, material and human resources, as well as physical facilities, systems, procedures, functions etc. of NABARD as may be deemed appropriate. OR
- b. Second alternative : Convert NABARD itself (under appropriate legal revisions of objectives, philosophy, organizational set up, corporate structure, concept) into the national co-operative credit apex.

15. With either of these alternatives, it is possible :

- a. To have likely success, not speculative success for the functioning of the apex. (In the initial functioning of the system, the weakening processes are great and if the newly created apex does not develop strength fast enough, the weakening forces will exhaust the initial reservoir of limited strength).

- b. To avoid the costly start-up activities : capitalization (how to raise it in the required amount); personnel (how to recruit and train); building and office equipment; systems and procedures; etc.
- c. To create an apex that can immediately function as the fountain-head of strength and leadership in the strengthening process.

G

CONCEPT NEEDS STUDY FOR FEASIBILITY AND ADVISABILITY

15. What has been presented is only a concept of one way to strengthen the co-operative credit system in terms of structure.
16. An in-depth study is necessary to ascertain the feasibility of the concept, and the advisability of adopting it. Some of the points that need to be addressed in the study are :
 - a. What are the legal impediments for state systems to organize themselves into a (national) system. If there are, can these be remedied by legislation?
 - b. How will the national apex be organized? As a bank? As a co-operative? Under what laws? Is there need for legislation?
 - c. If NABARD is to be the Apex, how should it be restructured: in concept, in organization, etc? If legislation is necessary, what legislation?
 - d. If NABARD's resources, facilities, etc are to be coalesced into the new Apex what are the legal requirements?
 - e. Should there be only one state apex (or sub apex)? Meaning: merge ST & LT Apex and members into one structure ?
 - f. What would be the role of the apex? What will be its authorities? its field operations? How do you ensure viability? How do you ensure "authority" over the "members".
 - g. How can strength be generated into the system so that the strength of the members becomes a part of the systemic strength?
 - h. How will the proposal conflict with the constitutional mandate that Co-operation is a state concern? And how can the conflict, if any, be cured?
 - i. What are the legal procedures and required amendments and laws to make possible the creation of a national apex along the lines suggested in the alternatives?
 - j. What should be the procedures for "phasing out" government ownership in the Apex and "phasing in " of co-operative ownership"?