

## COMMERCIAL BANK FINANCE TO AGRICULTURE IN INDIA-THE RECENT TRENDS AND ISSUES

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### ABSTRACT

*Timely and adequate credit at affordable rates is crucial to agricultural development, as in any form of productive activity. Agricultural credit was traditionally supplied in India by such indigenous sources of credit like the landlords, agricultural and professional moneylenders, traders, commission agents and relatives. While these sources had certain conveniences like easy accessibility and availability and absence of loan formalities, they had certain disadvantages such as high and usurious rate of interest, exploiting nature of the moneylenders, inadequacy, etc. In order to overcome these limitations and to make adequate credit available to the agriculturists, the modern credit institutions were developed in a multi-agency framework, the cooperative credit societies and banks, the regional rural banks and commercial banks forming the three components of this multi-agency approach. Data show that it is the commercial banks which are the most popular and pre-dominant among these three sources. The Kisan Credit Card system introduced in 1998-99 is a recent innovation in the field of agricultural credit. The card is also made an ATM card recently. A serious problem in the field of agricultural credit is the increasing overdues, giving rise to the Non-performing Assets (NPAs) of the banks, resulting in loss to the lending banks, at the micro level, and waste of lendable resources, at the macro level of the economy. It is, therefore, necessary that the volume of NPAs is reduced through such measures like an objective assessment of loan applications, avoidance of over-financing and proper end-use supervision of the loan.*

### Introduction

Credit plays an important role in any productive activity, whether in the agricultural field or in the manufacturing or commercial fields, enabling the producers to procure the inputs, in materials and labour,

required to be used in the process of production, and to distribute the products in the markets so as to sell them to the consumers. The modern scientific and technological advances in the field of agricultural production have made agricultural operations capital-intensive in

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nature, thereby increasing the agriculturists' need for credit. Besides, the seasonal nature of the incomes of the agriculturists, due to the seasonal nature of agricultural crops, makes credit all the more important in the agricultural field since, besides the need for credit to acquire productive resources or agricultural inputs, the agriculturists need credit to tide over the slack seasons of agriculture during which consumption expenditure may have to be met by credit. To be effective, credit should be timely, adequate and affordable to the agriculturists.

Commercial banks form an important source of agricultural credit in India. This paper is an attempt at analysing the recent trends in financing agriculture by the commercial banks in India and at discussing the issues related to the delivery and productive use of such credit. The discussion is undertaken against the traditional sources of agricultural credit in the country. Though the focus of the paper is on the financing of agriculture by the commercial banks, the study considers the role of the regional rural banks and the cooperative banks also in financing agriculture in the country partly because these three institutions constitute the three agents that form the modern multi-agency institutional system of agricultural credit in the country, and partly because it helps to contrast the predominant role of the commercial banks in financing agriculture when compared with the role played by the other two institutions which are parts of the multi-agency system of agricultural credit in the country. The analysis is limited to the direct financing of agriculture by the commercial banks and excludes the related special schemes so as to limit the size of the paper.

The study is based entirely on secondary data drawn from published reports of the Reserve Bank of India, the

Government of India, books and journals and no attempt is made to collect primary data through primary investigation. The analysis considers the trends in the financing of agriculture by the banks in the country since 1991, the year in which banking sector reforms were launched as part of wide ranging economic reforms launched in the country in that year. Certain issues related to the effective financing of agriculture are outlined at the end of the paper.

### **Traditional Sources of Agricultural Credit in India**

Agriculturists' need for credit was traditionally met by different indigenous agencies in India, such as the agricultural and professional moneylenders, village merchants, commission agents, landlords, indigenous bankers, relatives and friends and the role of the modern credit institutions, like the cooperative credit institutions and the commercial banks, was limited in the provision of agricultural credit in the country. The data presented in Table 1 show the limited role played by the modern credit institutions in providing agricultural credit in India in 1951-52 and in 1961-62. These data show that the combined share of the Government, the cooperative credit institutions and the commercial banks in the total credit of ₹ 750 crore extended to agriculture in the country in 1951-52 was only 7.3 per cent. While this share increased to 18.7 per cent in the total credit of ₹ 1,034 crore in 1961-62, the role of these institutions in the provision of agricultural credit in the country was still limited.

While these indigenous sources of agricultural credit in the country had certain advantages, such as their local nature, easy availability and approachability, procedural simplicity, absence of loan-formalities, etc., they suffered from serious disadvantages

such as high and usurious rates of interest, exploiting nature of the moneylenders, landlords, local merchants and the indigenous bankers. Besides, these sources were also found to be highly inadequate to meet fully the credit needs of the agriculturists in the country.

These disadvantages of the traditional sources of agricultural credit in the country led to an emphasis on the growth and expansion of the modern institutional sources of agricultural credit in the country, such as the cooperative credit societies and the cooperative banks, the commercial banks and the regional rural banks.

**A Multi-agency Approach:** A multi-agency approach is being adopted to cater to the growing needs for credit of the Indian agricultural sector. Such a multi-agency approach is justified on the grounds of suitability of the different sources for different purposes, preferences of the borrowers and the inadequacy of any single agency to meet fully the credit needs of the agricultural sector of the country. Cooperative banks and cooperative credit societies, commercial banks and the regional rural banks are the three types of credit institutions that form this multi-agency system of institutional credit to agriculture in India,

It is essential to note that this multi-agency approach to agricultural credit in India is not, however, a new approach. Agricultural credit in India was traditionally catered to by a host of institutions. What is new in the approach is that, unlike the traditional multi-agency approach, the present day multi-agency approach consists of formal credit institutions whose modus operandi are well regulated by legislative provisions and supervisory authorities.

Table 1 presents data pertaining to the amount of credit extended by these three categories of institutions to agriculture in India during the period from 1991-92 to 2010-11. The data show that the total amount of credit extended to agriculture in the country by these three institutions together increased from ₹ 11,202 crore in 1991-92 to ₹ 4,46,779 crore in 2010-11, marking an increase of 3,888.39 per cent during the period.

**Increasing Role of the Commercial Banks:**

The data in Table 1 show that while the role of the commercial banks in financing the agricultural sector in the country has been increasing relatively to that of the cooperative credit societies and cooperative banks during the period, the role of the regional rural banks had remained, more or less, the same. The regional rural banks supplied 9.84 per cent of the total agricultural credit in the country in 2010-11 against their share of 5.32 per cent in 1991-92. The share of the cooperative credit institutions in providing agricultural credit in the country declined considerably during the period from 61.82 per cent in 1992-93, it was 51.78 per cent in the previous year, to 15.69 per cent in 2010-11. The commercial banks supplied 74.47 per cent of the total credit extended to agriculture in the country in 2010-11 against their share of 32.70 per cent in 1992-93, this share being 42.90 per cent in 1991-92. These data, thus, show the predominant role of the commercial banks in financing agriculture in the country.

This is evidently due to the fact that the agriculturists prefer the commercial banks to the cooperative credit institutions as a source of credit because of their ubiquitous nature in financing the credit needs of their customers. This justifies the present day policy of inclusive banking in the

**Table 1: Institutional Financing of Agriculture in India, 1990-91 to 2010-11**

(Amount in ₹ crore)

Year	Cooperative Banks	Regional Rural Banks	Commercial Banks	Total
1991-92	5,800 (51.78)	596 (5.32)	4,806 (42.90)	11,202 (100.00)
1992-93	9,378 (61.82)	831 (5.48)	4,960 (32.70)	15,169 (100.00)
1993-94	10,117 (61.34)	977 (5.78)	5,400 (32.74)	16,494 (100.00)
1994-95	9,406 (50.18)	1,083 (5.78)	8,255 (44.04)	18,744 (100.00)
1995-96	10,479 (47.56)	1,381 (6.27)	10,172 (46.17)	22,032 (100.00)
1996-97	11,944 (45.22)	1,684 (6.38)	12,783 (48.40)	26,411 (100.00)
1997-98	14,085 (44.08)	2,040 (6.38)	15,831 (49.54)	31,956 (100.00)
1998-99	15,957 (43.29)	2,460 (6.67)	18,443 (50.04)	36,860 (100.00)
1999-2000	18,363 (39.69)	3,172 (6.85)	24,733 (53.46)	46,268 (100.00)
2000-01	20,801 (39.38)	4,219 (7.98)	27,807 (52.64)	52,827 (100.00)
2001-02	23,604 (38.04)	4,854 (7.83)	33,587 (54.13)	62,045 (100.00)
2002-03	24,296 (34.31)	5,467 (7.72)	41,047 (57.97)	70,810 (100.00)
2003-04	26,959 (30.99)	7,581 (8.72)	52,441 (60.29)	86,981 (100.00)

(Contd...)

**Table 1: (Contd...)**

(Amount in ₹ crore)

Year	Cooperative Banks	Regional Rural Banks	Commercial Banks	Total
2004-05	30,638 (26.59)	11,718 (10.17)	72,886 (63.24)	1,15,243 (100.00)
2005-06	39,786 (22.04)	15,223 (8.44)	1,25,477 (69.52)	1,80,486 (100.00)
2006-07	42,480 (18.52)	20,435 (8.91)	1,66,485 (72.57)	2,29,400 (100.00)
2007-08	48,258 (18.95)	25,312 (9.94)	1,81,088 (71.11)	2,54,658 (100.00)
2008-09	46,192 (15.30)	26,765 (8.87)	2,28,951 (75.83)	3,01,908 (100.00)
2009-10	63,497 (16.51)	35,218 (9.16)	2,85,799 (74.33)	3,84,514 (100.00)
2010-11	70,105 (15.69)	43,968 (9.84)	3,32,706 (74.47)	4,46,779 (100.00)

Source: (1) Government of India - Economic Survey, Different Issues.

(2) Reserve Bank of India, Report on Trend and Progress of Banking in India, 2004-05, P.69, Box.

Note: Figures within brackets indicate percentage to total.

country under which the banks are advised to open branches in centres with a population of 2,000 and above so that the rural reach of the commercial banks is increased.<sup>2</sup>

**The Kisan Credit Card Scheme:** Innovative measures are being adopted in recent years to increase the flow of institutional credit to agriculture in India in recent years.

The Kisan Credit Card Scheme,<sup>3</sup> introduced in the country in 1998-99, in August 1988,<sup>4</sup> is one such recent step<sup>5</sup> adopted in order to increase the institutional flow of credit to agriculture for productive purposes. The scheme enables the agriculturists to have a standing credit arrangement with the banks so that they can draw the required amount of credit, within the stipulated limit, without any delay. The

scheme involves the issue of a credit card to an agriculturist which authorises him to withdraw from the bank an amount of money, subject to the limit fixed, whenever he needs for undertaking productive agricultural activities and repaying such borrowed amount within a year. It is a "revolving cash credit facility involving any number of drawals and repayments within the limit".<sup>6</sup> The credit limit is "to be fixed on

the basis of operational landholding, cropping pattern and scale of finance".<sup>7</sup> Each drawal has to be repaid within a period of twelve months and the rate of interest and other terms are prescribed by the Reserve Bank of India.<sup>8</sup> The scheme was modified from time to time and "from January 31, 2006, the scheme has been extended to all types of loan requirements of borrowers of State Cooperative Agriculture Rural Development

**Table 2: Number of Kisan Credit Cards Issued, Year-wise and Agency-wise  
(Number in Lakhs)**

Year	Cooperative Banks	RRBs	Commercial Banks	Total
1998-99	1.56 (19.90)	0.06 (0.76)	6.22 (79.34)	7.84 (100.00)
99-2000	35.95 (70.02)	1.73 (3.37)	13.66 (26.61)	51.34 (100.00)
2000-01	56.14 (64.89)	6.48 (7.49)	23.90 (27.62)	86.52 (100.00)
2001-02	54.36 (58.20)	8.34 (8.92)	30.71 (32.88)	93.41 (100.00)
2002-03	45.79 (55.55)	9.64 (11.69)	27.00 (32.76)	82.43 (100.00)
2003-04	48.78 (52.75)	12.75 (13.79)	30.94 (33.46)	92.47 (100.00)
2004-05	35.56 (36.74)	17.29 (17.86)	43.95 (45.40)	96.80 (100.00)
2005-06	25.98 (32.43)	12.49 (15.59)	41.65 (51.98)	80.12 (100.00)
2006-07	22.97 (26.99)	14.06 (16.52)	48.08 (56.49)	85.11 (100.00)

(Contd...)

**Table 2: (Contd...)**

Year	Cooperative Banks	RRBs	Commercial Banks	Total
2007-08	20.91 (24.69)	17.73 (20.93)	46.06 (54.38)	84.70 (100.00)
2008-09	13.44 (15.64)	14.15 (16.47)	58.34 (67.89)	85.93 (100.00)
2009-10	17.43 (19.35)	19.50 (21.65)	53.13 (59.00)	90.06 (100.00)
2010-11	28.12 (27.65)	17.44 (17.45)	55.83 (54.90)	101.69 (100.00)
Total	424.57 491.26	(39.37) (45.56)	162.53 1078.36	(15.07) (100.00)

Source: From 98-99 to 2007-08, Govt. of India, Economic Survey, 2008-09, P.102, Table- 5.6 From 2008-09 to 2010-11 Govt. of India – Economic Survey, 2011-12, P.111, Table- 5.9.

For 2011-12-Economic Survey, 2012-13, P.112, Table-5.8.

Note: Figures within brackets indicate percentage to total.

Banks (SCARDBs). It covers short-term/medium-term credit and long-term credit and a reasonable component of consumption credit within the overall limit sanctioned to the borrowers."<sup>9</sup>

The scheme became popular very soon and Table 2 presents the data pertaining to the progress of the scheme. The data presented in Table 2 show that the total number of Kisan Credit Cards issued to agriculturists by the three institutions, Cooperative Banks, Regional Rural Banks (RRBs) and the Commercial Banks, which are the three types of credit institutions that form the modern multi-agency approach to agricultural credit in the country, together increased from 7.84 lakhs at the end of 1998-99 to a total of 101.69 lakhs at the end of 2010-11.

The relative roles of the three institutions in issuing Kisan credit cards had been changing during the period as shown by the data contained in the Table. The commercial banks played the predominant role in issuing Kisan Credit Cards, though their role had been decreasing relatively to those of the other two institutions during the period. While the share of the commercial banks in the total number of Kisan Credit Cards issued in 1998-99 was 79.34 per cent, followed by the Cooperative banks with a share of 19.90 per cent and the Regional Rural Banks with a share of 0.76 per cent, the share of the commercial banks at the end of 2010-11 was 54.90 per cent, followed by the cooperative banks with a share of 27.65 per cent and the Regional Rural Banks issuing the remaining 17.45 per cent of the total number of Kisan Credit Cards as at the end of 2010-

11. The data show that though the relative role of the commercial banks in issuing Kisan Credit Cards had decreased during the period, they still play the predominant role in issuing Kisan Credit Cards with a share of 54.90 per cent in the total number of Kisan Credit Cards with the agriculturists at the end of 2010 – 11. This is again a pointer to the marked preference of the commercial banks by the agriculturists for availing of institutional credit.

**Trends in the Sanction of Credit Limit:** The data pertaining to the total amount of credit limit sanctioned to the agriculturists during the period from 2006-07 to 2011-12 under the Kisan Credit Card scheme are presented in Table 3. These data show that the total credit limit sanctioned to the agricultural sector in the country by the three groups of institutions together under the Kisan Credit Cards scheme stood at ₹ 91,676 crore at the end of 2011-12, the share of the commercial banks being 75.83 per cent in this total,

**Table 3: Credit Limits Sanctioned to Agriculture by Cooperative Banks, RRBs and Commercial Banks Under The Kisan Credit Card Scheme, 2008-09 to 2011-12 (Amount in ₹ crore)**

Year	Cooperative Banks	RRBs	Commercial Banks	Total
2006-07	13,141 (28.12)	7,373 (15.78)	26,215 (56.10)	46,729 (100.00)
2007-08	19,991 (22.64)	8,783 (9.95)	59,530 (67.41)	88,304 (100.00)
2008-09	8,428 (15.88)	5,648 (10.64)	39,009 (73.48)	53,085 (100.00)
2009-10	7,606 (13.19)	10,132 (17.56)	39,940 (69.25)	57,678 (100.00)
2010-11	10,719 (14.76)	11,468 (15.79)	50,438 (69.45)	72,625 (100.00)
2011-12	10,642 (11.61)	11,516 (12.56)	69,518 (75.83)	91,676 (100.00)
Total*	1,61,956 (27.35)	76,946 (13.00)	3,53,145 (59.65)	5,92,047 (100.00)

Source: Government of India- Economic Survey, 2009-10, P.99, Table-5.8; Economic Survey, 2011-12, P.111, Table-5.9, and Economic Survey, 2012-13, P.112, Table- 5.8.

Notes: i) \*:Since the inception of the scheme in 1998.

ii) Figures within brackets indicate percentage to total.

followed by the Regional Rural Banks with a share of 12.56 per cent and the Cooperative banks supplying the remaining 11.61 per cent of the total outstanding credit limit of ₹ 91,676 crore at the end of 2011-12 under the scheme.

The data, thus, show the predominant role played by the commercial banks in financing agriculture, both in terms of the number of Kisan Credit Cards issued as well as in terms of the amount of credit extended to the agricultural sector in the country.

The Kisan Credit Card scheme was modified in March 2012 according to which "the Kisan Credit Card passbook has been replaced by an ATM-cum-debit card to all eligible and willing farmers in a time-bound manner"<sup>10</sup> so as to speed up the agriculturists' access to institutional credit facility.

**The Interest Subvention Scheme:** The cost of credit is an important factor in any scheme of effective institutional credit to agriculture. The bane of the traditional sources of agricultural credit in India was that it was exorbitantly costly in terms of the rate of interest. Unless the cost of institutional credit is low and affordable to the agriculturists, much progress cannot be made in financing agricultural progress in the country.

With a view to reducing the burden of interest on the agriculturists and also to encourage them to service the credit raised by them from the public sector banks, regional rural banks and rural cooperatives, a scheme of interest subvention was introduced in the country in 2011. The Government of India proposed, in the Union Budget for 2011-12, "to provide interest subvention of 1.5 per cent per annum for short term agriculture loans up to ₹ 3 lakh disbursed by public sector banks, cooperatives and RRBs. The additional

subvention for prompt paying farmers is proposed to be enhanced to 3 per cent per annum so that the effective interest rate charged to these farmers is 4 per cent per annum up to ₹ 3 lakh"<sup>11</sup>

### **The Problem of Overdues and Non-Performing Assets**

A disturbing aspect of the increasing flow of institutional credit to the agricultural sector in the country, which is true of financing the other sectors of the economy as well, is the inability of the agricultural borrowers to service the loans raised by them in time giving rise to the problem of Non-performing Assets (NPAs) of the financing institutions, with ramifications to the agricultural borrowers, the lending institutions and to the economy as a whole at the macro level.

Table 4 presents data pertaining to the non-performing assets of commercial banks in recent years in connection with their lending to the agricultural sector in the country. These data show that the NPAs of scheduled commercial banks in respect of their advances to agriculture was as high as 14.83 per cent of their total advances to the sector in 2001 and declined steadily thereafter to 2.11 per cent in 2009 and then increased to 2.49 per cent in 2010 and to 3.62 per cent in 2011 in conformity with the general trend in the NPAs of scheduled commercial banks in respect of their total advances in the country.<sup>12</sup>

Overdues in agricultural credit may be due to many reasons such as, i) crop failures due to various reasons, resulting in loss of incomes to the borrowers, resulting in their inability to service their borrowings in time; ii) high rates of interest and other associated costs of borrowing from the banks; iii) multiple financing by the banks, iv) over-financing by the lending institutions, which

**Table 4: NPAs of Scheduled Commercial Banks in Respect of Their Advances to Agriculture in India (Amount in ₹ crore)**

Year	Amount of Advances to Agriculture	Amount of NPAs	NPAs as Percentage of Advances
2001	51,922	7,699.12	14.83
2002	60,761	8,260.70	13.60
2003	71,609	8,244.13	11.51
2004	90,541	7,699	8.50
2005	1,24,269	7,719	6.21
2006	1,73,972	6,718	3.86
2007	2,30,398	7,367	3.20
2008	2,75,343	9,735	3.54
2009	3,38,656	7,149	2.11
2010	4,16,133	10,353	2.49
2011	4,60,333	16,660	3.62

Source: Reserve Bank of India- Report on Trend and Progress of Banking, Different Issues.

induce the borrowers to misuse the borrowed funds, resulting in overdues of credit; v) wrong selection of projects and crops by the agriculturists, such as, for instance, digging a bore well at a place where the possibility of striking adequate water is very dim, resulting in dead-weight loss to the agriculturists, wrong selection of crops resulting in insufficient income or loss of income; vi) wilful defaults on the part of the borrowers, etc. Irrespective of the factors that cause overdues in agricultural credit, they cause the non-performing assets of the banks that result in loss to the lending institutions and, through them, to the depositors at the micro level, and in slowing down the process of recycling of the lendable funds of the lending institutions, affecting adversely, thereby, the optimum productive use of bank resources, at the macro level, in the country.

#### **Certain Issues and Suggestions**

Having discussed the trends in the financing of agriculture by the commercial banks in India in the preceding pages, it is appropriate to make certain suggestions for the effective financing of agriculture by the commercial banks.

1. **Cost of Credit:** Effective financing of agriculture requires that the cost of credit, both interest cost and non-interest cost, raised from the financial institutions is low.<sup>13</sup> If institutional credit is costly, inadequate and is not available to the farmers easily and in time, due to the formalities and delays often involved in borrowing from the banks, they will be tempted to go to the moneylenders<sup>14</sup> to borrow, even though they charge a much higher rate of interest than the banks, and this

- will ultimately put them in a debt trap.
2. **Proper Appraisal of Loan Applications:** An objective and proper appraisal of loan applications should form an essential part of financing agriculture in order to avoid the risk of the scarce resources at the disposal of the banks being wasted. The purpose of the loan, its need, the amount of credit required, the suitability and productive ability and economic sustainability of the project for which credit is asked, the credit absorptive capacity<sup>15</sup> of the applicants for loans, etc., have to be assessed and the borrowers properly advised on the suitability and the credit worthiness of the purpose of the loan. Such financial advisory service rendered by the bank to its prospective agricultural borrowers is essential in order to avoid the risk of the agriculturists borrowing for purposes which are not productively sustainable and, ultimately, impose a debt burden on them, besides resulting in waste of resources at the macro level.
  3. **Avoidance of Over-financing:** An aspect of agricultural finance, as in the case of any other finance, is the tendency of the borrowers to borrow, when credit schemes are many and credit is easily available, in amounts in excess of the genuine need of the project or purpose, and divert the excess amount for consumption or other unproductive purposes that result in bad debts. This risk has to be avoided while financing agriculture.
  4. **Credit is Only a Facilitator:** Credit by itself cannot promote agricultural development and raise farm incomes. Credit is only a facilitator, the timely availability of which enables the farmers to procure seeds, fertilisers, labour, pesticides and other direct inputs in agriculture. These direct inputs should be made available at cheap rates, in time and in adequate quantities so that the agriculturists can use the funds borrowed by them productively so as to raise agricultural production and earn higher levels of income that will enable them to service the loans raised. Adequate storing and marketing facilities should also be made available so that the agriculturists do not resort to distress sales of their products resulting in loss of income.
  5. **Appropriation of Agricultural Subsidies by the Suppliers:** It is often found that whenever the government grants a subsidy to the agriculturists on the purchase of farm equipments and inputs, with a view to reducing the cost of such items, the suppliers of these items promptly raise the prices of such items and thereby appropriate the benefit of the subsidy, without any benefit to the agriculturists.<sup>16</sup> This tendency of the suppliers of farm inputs has to be effectively checked by the government so that the benefit of such agricultural subsidisation schemes reach the farmers, for whom they are really intended, so that the cost of agriculture is held in check, with micro benefits to the farmers and macro gains to the economy and the society.
  6. **The Debt-waiver Scheme:** In order to reduce the burden of debt on the farmers, the Government of India announced, in the Union Budget 2008-09: "Direct agricultural loans disbursed by scheduled commercial banks, regional rural banks and

cooperative credit institutions up to March 31, 2007 overdue as on December 31, 2009 and which remained unpaid until February 29, 2008 are eligible for debt waiver or debt relief as the case may be. About 3.68 crore farmers have benefited from the scheme involving debt waiver and debt relief of ₹65,318.33 crore."<sup>17</sup>

While the debt-waiver or debt relief scheme is good in philosophy as a measure of freeing the farmers from the burden of heavy debt which they find it difficult to repay, it has a demoralising effect, when used indiscriminately, on agricultural borrowers. It tempts the borrowers to indulge in further borrowing, use the money for purposes other than the purpose for which the loan is raised, with the expectation of debt-waiving in future. It has a demoralising effect on the agriculturists, even on the genuine and honest agricultural borrowers, and, hence, should be used with caution.

7. **Proper End-use Supervision of Credit:** Any scheme of agricultural financing by the banks, as in any scheme of financing productive undertakings, has to be effectively watched and supervised so as to ensure proper end-use of the proceeds of the loan so that the proceeds of the loan are not diverted and wasted by the borrowers on unproductive uses that impose a debt burden on them that ultimately result in bad debts.
8. **Penal Action:** A punitive measure that needs to be adopted in order to reduce agricultural credit overdues, and the resulting non-performing assets to the financing banks, is to make the borrowers, who are found to

indulge in wilful defaults, ineligible for future bank credit so that the borrowers do not indulge in wilful defaults in future. Such a measure, will, however, become effective only when the banks take such a measure collectively so that a person who is denied credit by one bank does not get assistance from another bank, so that the penal action adopted by the former is not thwarted by the latter, as would often happen when the different banks function in a competitive banking environment.

### Conclusion

Timely and adequate credit, at reasonable rates of interest, is very important for agricultural development, and of any other form of economic activity. Agricultural credit was supplied in India, traditionally, by such indigenous institutions like the village moneylenders, village merchants, landlords, indigenous bankers and relatives. These sources of agricultural credit, being inadequate, were found to be costly in terms of the rate of interest, which very often tended to be usurious, though they had such positive aspects as their local availability, easy approachability and simplicity in loan procedures and formalities. The disadvantages of these forms of credit and their inadequacy were tried to be overcome in the country by developing formal institutional sources of credit in a multi-agency framework, the three components of which are the cooperative credit societies and banks, the commercial banks and the regional rural banks. Commercial banks are found to be the most popular among these three sources. The volume of credit made available to the agriculturists by these institutions had been growing in recent years. There are, however, certain problems. The problem of overdues, generating NPAs

of the financing institutions, is one such problem with ramifications to the financing institutions at the micro level and to the economy as a whole at the macro level. Credit is only a facilitator and it will help in promoting agricultural development only if non-credit inputs and facilities are available at economical rates and are adequate and timely. Adequate care should be taken, while financing agriculture, to assess the loan applications properly and objectively with regard to need, volume, economic viability

and sustainability of the project for which loan is sought. An effective end-use supervision of the proceeds of the loan granted should form an essential part of any scheme of bank finance to agriculture, so as to avoid possible diversion and misuse of the proceeds of the loans with adverse consequences to the borrower as well as to the financing institutions, at the micro level, and to the economy as a whole, at the macro level.

### Notes and References

1. It is the lack of these positive aspects of the traditional, indigenous sources of agricultural credit in India in the functioning of modern credit institutions, like the cooperatives, regional rural banks and commercial banks, that makes them not readily acceptable to the agriculturists who hesitate to approach these institutions. It is by incorporating these positive aspects into the functioning of the modern credit institutions that they can be made effective purveyors of rural credit in the country.
2. It may be remembered that the emphasis laid on the provision of banking facilities in the rural areas of the country during nationalised banking, from 1969 to 1991, tended to be de-emphasised later during banking sector reforms launched in 1991, emphasising the profitability of the banks, rather than providing banking service to the society. Consequently, as per the data available in the Reserve Bank of India reports, Report on Trend and Progress of Banking in India, of the relevant years, the number of rural branches of the commercial banks in the country decreased from 58.4 per cent of the total number at the end of June 1991 to 39.6 per cent at the end of June 2009. What is more glaring is that the total number of branches of commercial banks functioning in the rural areas of the country actually decreased from 35,187 to 31,798 between the two points of time, though the total number of branches of commercial banks functioning in the country as a whole increased from 60,190 to 80,369 during the period. The obvious reason for this change in the locational pattern of the branches of the commercial banks in the country during the period is that the rural branches are less profitable when compared with the profitability of the semi-urban and urban branches. The present policy of financial inclusion initiated by the Reserve Bank of India through its Annual Policy Statement for 2005-06, ( See: Reserve Bank of India- Report on Trend and Progress of Banking in India, 2007-08, P.36 ), and vigorously followed since 2009, asking the commercial banks "to cover all villages with more than 2,000 population with at least one banking outlet by March 2012." (See: Reserve Bank of India- Report on Trend and Progress of Banking in India, 2010-11, P.97). This policy of financial inclusion is, in reality, a measure, that re-emphasises the policy pursued during the period of nationalised banking in the country.

3. For details see: Govt. of India – Economic Survey, 1999-2000, P.142, Box 8.2.
4. Though the credit card scheme was introduced in the country only in 1998-99, academic discussions on such lines had been going on in the country for some time prior to its introduction. Bhat, for instance, suggested a scheme of agricultural credit involving a common passbook and a standing credit arrangement for the agriculturists so that they are guaranteed an assured amount of credit without delay. "The common agricultural passbook should also act as a ready credit card to the agriculturists and they should be made eligible for some amount of immediate credit or a certain amount of additional financing on its presentation at a bank or cooperative credit society so that the agricultural credit system is made timely and sufficiently elastic which are two of the basic requirements of a sound agricultural credit system," – See: Bhat, N S (1994)- Factors Causing Overdues in Agricultural Credit: A Case Study, in *Journal of Rural Development*, Hyderabad, Vol.13(1), January-March, 1994, PP.89-100.
5. For a discussion of the recent measures adopted by the Government for increasing the flow of institutional credit to agriculture in the country and also to help them in the form of interest and debt relief measures see Satish P.- Innovations in Agricultural Credit Market- Rationalisation of Policy Response; in *Indian Journal of Agricultural Economics*, Vol.67, No.1, Jan.-March, 2012, PP. 79-96.
6. Government of India- Economic Survey, 1999-2000; P.142, Box 8.2.
7. *ibid.* P.142, Box. 8.2.
8. *ibid.* P.142, Box 8.2.
9. Govt. of India- Economic Survey, 2007-08, P.164.
10. Govt. of India – Economic Survey, 2012-13, P.184.
11. Source: See Government of India- Economic Survey, 2011-12, P.111.

State governments have also been adopting measures to reduce the rate of interest on farm credit. The revised budget of the Government of Karnataka for 2013-14, for instance, proposes short-term loans to the agriculturists through the cooperative societies at a rate of interest of zero per cent up to an amount of ₹ 2 lakh, and at a rate of interest of 1 per cent between ₹ 2 lakh and ₹ 3 lakh and at 3 per cent for loans up to ₹10 lakh (See:The Hindu, July 13, 2013, P.1). These are, however, extremes, in terms of both the rate of interest and the amount of loan, that are better avoided since they send out the message that institutional credit is free and can be squandered away. They have a demoralising effect on the agricultural borrowers and a counter-exploiting element in them; the agriculturists exploiting the society through political lobbying for low rates of interest or zero rate of interest on farm loans, in counter to the moneylenders exploiting the agriculturists by charging high rates of interest on farm loans.

12. The gross NPAs of scheduled commercial banks as a percentage of their gross advances in the country declined from a high of 12.7 per cent in 2000 to a low of 2.3 per cent in 2008 and then rose to 2.39 per cent in 2009-10 and declined to 2.25 per cent in 2010-11. Their net NPAs as a percentage of their net advances declined from a high of 6.8 per cent in 2000 to a low of 1.0 per cent in 2007 and then rose to 1.11 per cent in 2009-10 and then declined to 0.97 per cent in 2010-11. Source: Reserve Bank of India-Report on Trend and Progress of Banking in India, different issues.
13. Measures are being adopted by the Central as well as State governments to reduce the rate of interest on farm loans extended by the commercial banks. See footnote 11 above. It is, however, observed that even after the introduction of the scheme of interest subvention on farm loans extended by the commercial banks in 2006-07, "the cost of agricultural credit has generally been high"- See; D. Subba Rao- Agricultural Credit-Accomplishments and Challenges; NABARD 30th Anniversary Lecture delivered in Mumbai on July 12, 2012, accessed from website. Subba Rao lists such factors as "(i) insistence on collateral, (ii) complicated loan administration procedures, (iii) distance from the villages to the branches, (iv) higher monitoring and follow-up costs, (v) culture gap between bank officials and farmers, (vi) political interference, (vii) inflexible lending policies and procedures including cumbersome documentation, (viii) difficulties in recoveries of overdue loans, (ix) lack of provision for consumption credit, (x) absence of effective systems for screening credit risks and, finally (xi) a misplaced belief that the borrowers in the agricultural sector, particularly, small and marginal farmers with low per capita incomes are risky and hence non-bankable" that add to transaction costs of farm credit from the banks. See: *ibid*. These transaction costs when added to interest-costs increase the cost of institutional credit to the agriculturists.
14. A study by Usha Thorat shows that the share of the moneylenders in the outstanding debt of the households in the country increased from 17.5 per cent in 1991 to 29.6 per cent in 2002 in the case of the rural households and from 10.2 to 14.1 per cent in the case of the urban households in the country during the same period. See: Usha Thorat Smt. (2007) – Banking in the Hinterland; Reserve Bank of India Monthly Bulletin, March 2007, P.327, Table-6. These data show the increasing tendency among the households in the country to resort to borrowing from the moneylenders in preference to the banks.

D. Subba Rao, former Governor of The Reserve Bank of India pointed out that the decline in the share of the commercial banks in the total debt of cultivator households in the country from 35.2 per cent in 1991 to 26.3 per cent in 2002 and the increase in the share of the moneylenders from 17.5 per cent in 1991 to 26.8 per cent in 2002, based on NSSO data, was "mainly because of a pull back by commercial banks. This disquieting trend is, in part, due to a contraction in rural branch network in the 1990s, and in part, due to the general rigidities in procedures and systems of institutional sources of credit"- See: Dr. D. Subba Rao-Agricultural Credit – Accomplishments and Challenges; NABARD 30th Anniversary Lecture delivered in Mumbai on July 12, 2012, accessed from website.

15. Gyanendra Mani and Vivek K. Sinha in their study of the credit absorptive capacity of farmers in Uttar Pradesh mention such factors as quality of land, entrepreneurial skill of the farmers, area of land held, irrigation of land, educational level of the farmers, availability of family labour, nature of crops raised etc. as the main factors that determine the credit absorptive capacity of the farmers at the micro level. – See: Gyanendra Mani and Vivek K. Sinha- Credit Absorptive Capacity of Farmers in Uttar Pradesh; *Indian Journal of Agricultural Economics*; Vol.65, No. 4, October-December, 2010, PP.677-92.
16. It may be noted that this tendency can also be observed in the case of the financing schemes of banks and other financing institutions. As bank or other forms of institutional credit is easily available at low rates of interest for the purchase of durable consumer goods, houses, flats, motor cars and other durable consumer goods, and even in the case of educational and health services, the suppliers of these goods or services raise their prices and appropriate the benefits of such schemes and, thereby, exploit the consumers for whom such schemes are really meant.
17. Source: Government of India- Economic Survey, 2009-10, P. 196.