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loans are normally granted for the purchase of inputs like fertilizers, seeds, pesticides, hired manual labour, etc. Table IV, which presents data regarding price and quantity elasticities of credit requirements for these inputs, discloses that fertilizers and pesticides have higher price elasticities than seeds and manual labour. In other words, changes in the prices of these inputs have a greater bearing on the credit requirements than those in the prices of seeds and manual labour which has the lowest elasticity.

TABLE IV—PRICE AND QUANTITY ELASTICITIES OF CREDIT

| Year | Price elasticities | | | | Quantity elasticities | | | |
|---|---|---|---|---|---|---|---|---|
| | Fertilizers | Seeds | Pesticidies | Manual labour | Fertilizers | Seeds | Pesticides | Manual labour |
| 1973 .. .. | ·6731 | ·2122 | ·3456 | ·1876 | ·3216 | ·1213 | ·1875 | ·4112 |
| 1974 .. .. | ·6948 | ·2234 | ·3718 | ·1845 | ·3612 | ·1327 | ·2212 | ·4067 |
| 1975 .. .. | ·7487 | ·2718 | ·4077 | ·1749 | ·4028 | ·1005 | ·2461 | ·4412 |
| 1976 .. .. | ·7768 | ·2211 | ·4118 | ·1435 | ·4217 | ·1267 | ·2614 | ·4628 |
| 1977 .. .. | ·7784 | ·2348 | ·4165 | ·1672 | ·4284 | ·1134 | ·2510 | ·4618 |

The quantity of fertilizers and manual labour (*i.e.*, in terms of man-days) do seem to have significant impact on the size of loans. The quantity elasticity of the latter is somewhat greater than that of the former. Yet these two basic inputs bring about a significant change in the magnitude of credit needs.

In sum, it may be inferred that (*a*) funds have been flowing out of villages where competition amongst banks is non-existent. (*b*) Commercial banks are not much inclined in directing and channelising the non-deposit resources obtaining in the urban centres. (*c*) Competition among bank themselves has a positive impact on a village economy. (*d*) They are confining their lending activities mostly to short-term requirements. And (*e*) credit needs are enhancing steadily due to increasing doses of inputs and their prices.

# SOME BASIC CONFLICTS IN RURAL CREDIT (WITH REFERENCE TO FARMERS' SERVICE CO-OPERATIVE SOCIETIES)

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The Report of the Banking Commission (1972) had noted that there were very large credit gaps especially in institutional arrangements in respect of small, marginal and sub-marginal farmers and other rural producers which called for a different approach. The Report recommended the formation of Rural Banks for dispensing rural credit. Three years later, the National Commission on Agriculture had occasion to comment that both the co-ope-

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rative and the commercial banks lacked the ability and understanding to tackle the special needs of small farmers let alone those of marginal farmers and agricultural labourers. Both on grounds of equity and optimum use of manpower and land, it was necessary to subsume the small and marginal holdings into the national programme of modernization and development of agriculture. The crux of successful financing of small and marginal farmers lay in the gearing up of a comprehensive organization for their production, introducing subsidiary occupations, planning investment for improvement and diversification of productive capacity on a collective as well as individual basis and organizing inputs and services as well as processing and marketing on a joint basis. The responsibility was too great for the financial institutions alone to undertake. Towards this end, the National Commission on Agriculture mooted the concept of the Farmers' Service Society (FSS) with emphasis on integrated credit, input supply and marketing facilities in their Interim Report on Credit Services. However, the FSS remains primarily a co-operative institution. The paper makes an attempt to identify some of the basic conflicts in co-operative rural finance with the help of illustrative data from the case study of a farmers' service co-operative society in Karnataka.[1]

## FARMERS' SERVICE SOCIETY

The FSS is essentially a registered co-operative body. We discuss here some of the special features and points of departure.

A FSS has to be sponsored by a financing bank, either a central co-operative or a commercial bank. It is to have an eleven to thirteen-member board including five representatives of small farmers and two other members, four nominees of Government, one of the financing bank and the Managing Director, who, to begin with, would be from the cadre of the financing bank appointed by the FSS in consultation and concurrence of the bank. The bank is to prescribe the norms and procedures of financing to be administered by the FSS. Besides providing funds to meet the credit needs of the members, the bank is to extend various lines of credit to the FSS for its activities regarding services and inputs. Thus the FSS achieves two new functions with a management breakthrough with a fullfledged Managing Director from the financing bank itself and secondly with all the necessary credit, short, medium and long-term, and inputs, backward and forward linkages and services under a single roof.

An important aspect of effective credit service, as emphasized by the National Commission on Agriculture, in the context of the FSS, is that it should help the farmer to reach a self-sustaining stage to the extent of about 70 per cent of his normal working capital requirements, over a period of five years or so. For the first time it is recognized that "...the same area being tilled the same way and producing the same output cannot claim the same or more seasonal credit year by year, if access to credit is to be provided to more

1. The case study was carried out by the second author in June 1977.

and more people".[2] This is a welcome point of departure, though belatedly accepted.[3]

## THE CONFLICTS

A FAO study points out that "...the subsistence basis of agricultural production and the typical mentality of the rural population correlated with it, must still be considered strong impediments to agricultural development on modern lines. Progressive governments have to convince a conservative rural population to do what is not in their living tradition and does not fit into the social and economic pattern of rural life".[4] It should be obvious that the coming together of the three elements, the borrower, the co-operative and the Government—and in this case all the three being at variance in the matter of objectives and administration—would lead to a number of inevitable conflicts. Some of the major ones only are denoted below.

Certain specific objections to the co-operative form of organization in the matter of rural finance may also be noted in the above context. These are: (*i*) the condition that loyalty to a philosophy is insisted upon as a pre-condition for making credit available to prospective borrowers seems to go against the basic principle of credit, that is, that it should flow to those in need of it, who have repayment capacity and whose purpose is productive;[5] (*ii*) the borrower, if he needs credit, has to become a member of that society alone which has jurisdiction over his village, irrespective of the merits of the society relating to its efficiency and sound management.[6] While the FSS is apparently expected to satisfy the second condition, the first objection gets all the more strengthened because the dissolution or amalgamation of all the existing co-operatives in the area is a pre-condition to the formation of a FSS.

The new credit policy recommending the creation of the FSS tries to involve the financing bank by giving it a more active role. It would be interesting to observe that the FSS plays its triple role, namely, as a financier sanctioning and disbursing credit mainly to the weaker sections, as a buyer and seller of goods and services to and for them and as the extension agency and an educator of co-operative discipline. It must be owned that the three roles have certain positive, though peripheral areas of conflict.

We proceed to itemise some of the major unresolved conflicts in brief.

(*i*) Like the earlier co-operatives, the FSS also continues to rely heavily on Government assistance such as contribution to share capital, fully paid

2. Government of India: Report of the National Commission on Agriculture 1976, Part XII—Supporting Services and Incentives, Ministry of Agriculture and Irrigation, New Delhi, 1976, p. 25.

3. Obviously, a farmer who cannot afford the cost of exploiting his land rationally, by applying fertilizers and pesticides, cannot expect high returns. Credit has no place in subsistence farming. "Agricultural Credit for Development" in Working Group of FAO (Ed.): World Conference on Credit for Farmers in Developing Countries, October 14-21, 1975, Monograph 13, Lombarde, Milan 1975, p. 63.

4. Food and Agriculture Organization of the United Nations: Agricultural Credit through Co-operatives and Other Institutions, FAO Agricultural Studies, No. 68, Rome, Italy, 1965, pp. 38-39.

5. Technical Studies prepared for the Banking Commission, Vol. II, Reserve Bank of India, 1972, p. 61.

6. "...while he is thus required to become a member of a co-operative having jurisdiction over his area and no other, the society has no corresponding obligation to satisfy his entire credit needs". *ibid*, p. 62.

services of Government technical personnel, direct subsidies, etc. This kind of dependence tends to create a paternalistic type of relationship in which dependence, control and continued reliance on outside sources overshadows and frequently prevents local initiative, self-management and efficient organization. "This has posed a dilemma as to how to achieve a working compromise between the essential role of outside agencies as stimulators and assistants of co-operative movement, especially in the initial stages, and local initiative and democratic control which is so essential for the success of the movement".[7]

(*ii*) The control and selection of the Managing Director of a FSS often vests with the sponsoring bank which, in the case of a commercial one, is strictly a business institution that may have no sympathy for the 'unsuccessful', and/or uncreditworthy small production units like the farm firms of the small and marginal farmers. The professional managing director is likely to be guided by his loyalty to the parent bank in the matter of social responsibility, selective lending and accountability.

With the creation of the FSS, it has been stipulated that the weaker sections could be provided credit on the basis of the surety of solvent farmer. It can be easily foreseen that the condition would erode the actual amount of loan moneys that the small borrower would ultimately receive.

The National Commission on Agriculture had occasion to comment, on some evidence collected by it on the working of a number of FSSs, to the effect that the managing director, under the pressure of showing quick results is tempted to concentrate on lending and trading operations to the neglect of other duties. Another cause of the Commission's concern had been that the planning of the form and content of extension services and the minimum nucleus needed for it—the functions being the much needed points of departure from the erstwhile credit co-operatives—have tended to be postponable matters.

(*iii*) A serious objection to co-operativisation in India has been the voluntary nature of its membership. The FSS while undertaking membership drives initially, would invariably enrol the weakest as well as the largest of the local farmers thus disrupting the fabric of homogeneity. The Indian farmer finds it difficult, because of his poverty and the uncertainty of his agriculture, to identify himself with the larger social good, namely, the need for increasing agricultural production. The voluntary aspect of co-operative membership is likely to conflict with the implementation of schemes for the general social good such as minor irrigation for area development purposes.[8]

(*iv*) The FSS in question exhibited the oft-mentioned objection that co-operative credit tends to gravitate to larger farmers which, as may be rea-

7. P. Y. Chinchankar and M. V. Namjoshi (Eds.): Co-operation and Dynamics of Change, Somaiya Publications Pvt. Ltd., Bombay-14, 1977, p. 409.

8. "To look after the management of soil and water resources in a recognized block of land, however, a co-operative form of organization with voluntary membership will not do. An organization which must make such day-to-day decisions in a given block of land must enforce them. All cultivators of land within the given block must therefore of necessity be members of the proposed organization". See V. M. Dandekar, Presidential Address: "Planning in Indian Agriculture", *Indian Journal of Agricultural Economics*, Vol. XXII, No. 1, January-March 1967, p. 22.

lised, is one of the ills of open membership and lack of homogeneity. This is revealed in Table I which gives the per loan amount sanctioned for different purposes to different classes of borrowers.

TABLE I—AMOUNT PER LOAN SANCTIONED TO DIFFERENT BORROWERS

(*Rs.*)

| Purpose | Agricultural labourers | Small/marginal farmers | Others (medium and large farmers) |
|---|---|---|---|
| 1. Well loans .. .. .. | — | 6,130 | 9,806 |
| 2. Agricultural machinery loans .. | — | 2,818 | 3,583 |
| 3. Dairy loans .. .. .. | 1,346 | 2,000 | 2,143 |
| 4. Sheep loans .. .. .. | 1,225 | 1,612 | 1,904 |
| 5. Sericulture loans .. .. .. | — | 1,458 | 2,014 |

In this context, other particulars such as the proportion of borrowers to the total members in each category and the proportion of total credit may also be noted. The proportion of borrowing members to the total was 52.8 per cent for agricultural labourers, 57.5 per cent for small and marginal farmers and 100 per cent for 'others', *i.e.*, medium and large farmers. The proportion of total credit disbursed to these three categories was 4.5 per cent, 42.2 per cent and 53.3 per cent respectively.

(*v*) One of the constraints to the successful working of co-operatives has been the non-identification, on the part of departmental personnel, with the principle of co-operation. Departmental indifference would also plague the FSS more so because the control has shifted to the financing bank. Table II does not need any comment in this context.

TABLE II—NUMBER OF BOARD MEETINGS UPTO MAY 1977

| Designation | Number of meetings held upto 3-5-77 | Number of meetings attended |
|---|---|---|
| 1. Asst. Registrar of Co-operative Societies .. .. | 36 | 9 |
| 2. Project Officer, SFDA .. .. .. .. | 36 | 13 |
| 3. Asst. Director of Agriculture .. .. .. | 36 | 6 |
| 4. Asst. Director of Animal Husbandry .. .. | 36 | 18 |

The FSS also reported the non-availability of the services of the Sales Officer from the co-operative department, who was expected to continuously assist the society in its recovery programme, particularly the recovery of dues from members of the defunct societies, six in number, merged with the FSS in question. The department's argument that the FSS could like sales officers on deputation by bearing 50 per cent of total cost (emoluments inclusive of travelling and other expenses) would not be acceptable to many FSSs in the State.

(*vi*) We come to the most important point, that of the possiblity of a break-even in the matter of the FSS. The National Commission on Agriculture has been at pains to insist that the FSS is to be a strictly business proposition. The FSS under study has, however, already recorded progressively decreasing loans during the three years of its existence.

A break-even can be hoped only if two conditions are satisfied. In the first instance, the FSS should operate to its fullest capacity in the enrolment of members, maintenance of linkages and maximum modernization of agriculture in the case of its members. The data of the FSS under study actually revealed that 57 per cent of its membership have not opted for any credit services at all. It should be remembered that agricultural production is subject to certain proven constraints such as pre-determined income goals,[9] capital rationing practices[10] especially in dry and uncertain agriculture, etc.

The second condition is that the members should not only patronise the many services offered by the FSS, such as storage and marketing, tractor services, etc., but should also make punctual repayments of the loans taken and conform to the extension services offered. This would almost amount to crying for the moon. In the capitalistic mode of production as we have in India, it is unlikely that the farmers would forgo their decision-making privileges even while owing allegiance to the co-operative philosophy.

In the context of the second condition, it is revealing to note that a little over two-thirds of the repayment dues could be collected, as may be seen from Table III.

TABLE III—PERFORMANCE OF FSS AS ON 30-6-1976 (SECOND YEAR)

(*Rs.*)

| Particulars | Short-term loans | Medium-term loans | Total |
|---|---|---|---|
| 1. Demand .. .. .. | 3,18,903 | 3,09,757 | 6,28,660 |
| 2. Collection (recovery) .. | 2,19,027 | 2,09,091 | 4,28,118 |
| 3. Balance .. .. .. | 99,876 | 1,00,666 | 2,00,542 |
| Percentage of recovery to demand .. .. .. | 68·7 | 76·5 | 68·1 |

In an eventuality of the above nature, with overdues around 32 per cent, the cost of the FSS would inevitably tend to outrun the expected total social benefits, which in the given set up of the organization of the FSS are proposed to be made good by direct subsidies, free services of pre-paid departmental technical personnel, share capital assistance by the Government and the con-

9. "Farmers do not farm for maximum profit but are inclined to meet certain income goals and do not abandon practices unless forced to do so". E. L. Baun, H. G. Diesslin and Earl O. Heady (Eds.): Capital and Credit Needs in a Changing Agriculture, Iowa State University Press, Ames, Iowa, 1961, p. 378.

10. "If a firm is to maintain itself as a going concern in the face of unfavourable contingencies capital rationing makes it necessary that the firm protects itself by maintaining increased assets in a liquid form". Earl O. Heady: Economics of Agricultural Production and Resource Use, Prentice-Hall, Inc., Englewood Cliffs, New Jersey, U.S.A. 1952, p. 39.

tributed services of an external managing director. The break-even would be nothing short of a well-calculated self-deception.

The case study of the FSS under discussion lists a number of other impediments in the working of the society such as improper demarcation of area, bureaucratic inertia, untimely and inadequate supply of inputs, under-capacity utilization of tractor services, godowns, etc. One could also discuss other constraints like the peculiar structure of the FSS, principles of selective lending, allocation of resoures, co-ordination with other related institutions, etc.

## REMEDIES

While academic prescriptions are not difficult, it is generally agreed that the problem of rural credit cannot afford a single solution for a vast country like India. Some possible remedies suggest themselves. They will have to be examined in fuller details and their implications spelled out. What is needed is that the motivation of the borrower to change should be stimulated by pragmatic approaches instead of mechanical application to a formal organization whose aims are poorly understood by new members and which they hardly consider as theirs.

(*i*) A large segment of the population in India is stratified along caste lines, is culturally backward and lives below subsistence level. Such a stratification appears to warrant separate institutions.[11] They require much more service including closer supervision than the more commercialised large farmers and more flexible policies relating to credit collateral, down payment requirements and repayment schedules. These institutions could be made responsible to a special apex institution at the State level, which would qualify for the absorption of all types of subsidies, concession and direct help.

(*ii*) As a matter of experiment at least, it would be interesting to try out a reformulated approach to the problem. Instead of taking the inputs and services to the door-step of the rural producer, the market might be taken to his door-step, of course with adequate provision of credit to those who are stimulated by the availability of an assured offtake at really remunerative prices, subsidised at the national or State level. This approach has been the single important reason for the continued existence of the trader-cum-money-lender on the Indian rural scene. The effect of such assured offtake has been amply demonstrated by the operations of a large number of sugar co-operatives in the State of Maharashtra. The growers are left to concentrate on opitmum production of cane, the linkages effectively achieved with minimum overdues and all the farmers, including the small ones and agricultural labourers, gainfully employed and adequately benefited.

(*iii*) An alternative could be to make the borrowers feel more responsible towards the lending institutions. The present system, especially the co-ope-

11. "It is clear, though, that any system intended to reach large numbers of low income producers will have to be based on different principles from those systems assigned to reach relatively few large farmers. Because of special problems of dealing with small farmer, a case could be made for separate credit institutions to look after them". The International Bank for Reconstruction and Development: Agricultural Credit, Sector Policy Paper, Rural Development Series, Washington, D.C., U.S.A., 1974, p. 32.

rative one, is primarily composed of borrowers disbursing borrowed funds among themselves. With the State policy so firmly supporting and standing by it, the system has exhibited signs of forgetting the social purpose behind the State assistance that the credit is essentially a repayable loan and not an outright grant made to the members of the credit co-operative. In this context, a policy of guided (as opposed to voluntary and open) creation of co-operatives or of selective admittance of members may not necessarily be considered as incompatible with the essentials of co-operation.[12]

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# ADEQUACY AND PRODUCTIVITY OF CREDIT ON THE SMALL FARMS IN THE PUNJAB

K. C. Dhawan and A. S. Kahlon*

With the technological changes, the need for credit in the case of majority of cultivators arises from the fact that their own savings are normally not adequate to finance various activities on their farms. Moreover, while their income accrues during limited period of the year, their expenses are spread throughout the year.

Credit plays a crucial role in oiling the wheels of agricultural production. It is said to be the life blood of agriculture and, therefore, the need for timely and adequate farm finance is obvious. To obtain a substantial increase in agricultural production, the provision of credit must be accompanied by and co-ordinated with a sufficient amount of technical advice and availability of physical inputs.

The marginal value productivity (MVP) of capital in agriculture having increased with the inception of new technology, the farmers are likely to depend more and more on borrowed capital to be able to adopt the new farm technology. Again, the problem of agricultural finance in India is not merely one of inadequate supply of funds, rather it is aggravated by its ineffective utilization. Credit serves a useful purpose only when it is used for productive purpose to generate a surplus after paying the interest and capital. Otherwise, its diversion for consumption purposes would affect the repaying capacity of borrowers and create overdues and defaults.

More specifically, the objectives of the study are (*i*) to examine the adequacy of credit supplied by different institutions to the small farms and (*ii*) to evaluate the economic rationale of credit obtained for different inputs on the small farms.

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12. Yair Levi, "Cooperation: In Search of New Dimensions", in Chinchankar and Namjoshi (Eds.): *op. cit.*, p. 410.

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