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Restructuring the Co-operative Credit System through Integration of Short Term and Long Term Structures

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INTRODUCTION

Co-operatives form the major component of the institutional rural credit system in our country, the other components being commercial banks and Regional Rural Banks. Co-operatives offer short-term and long-term credit through two separate channels whereas the other two agencies offer all types of credit without separate channels. The evolution of long-term and short-term co-operative structures has distinct historic antecedents. The short term credit to agriculture is extended through the three tier co-operative structure consisting of State Co-operative Bank (SCB) at the apex level, District Central Co-operative Bank (DCCB) at the district level and Primary Agricultural Co-operative Credit Societies (PACS) at the grassroot (village) level. Term credit needs were met through the two-tier structure with State Co-operative Agricultural and Rural Development Banks (SCARDB) at the state level and Primary Co-operative Agricultural and Rural Development Banks (PARDBS) (earlier known as Land Development/Mortgage Banks-LDB/LMB) at taluka level.

Institutional rural credit is fraught with the fundamental challenge of fulfilling the social obligations without compromising on the quality of service and institutional strength. High transaction costs and mounting non-performing assets pose premier challenges to these institutions and hence the thinking on restructuring. With low asset base and lower degree of professionalism and business acumen, co-operatives have been weak partners in the credit system. As far as the two exclusive channels of co-operative credit are concerned, there had been a thinking whether the integration of the two channels would do any good to the credit system by way of imparting cost economy and competitive ness. The question of continuance or otherwise of the existing system rests on the present needs of the beneficiaries, stage of development of the institutions and the need to adapt to the changing dimensions of the economy. Moreover, some degree of integration has been taking place at the functional level as, over time, short-term structure is encouraged to purvey term loans and the long-term structure is allowed to mobilise deposits, thus thinning down the dividing line between the two wings. The issue of integration of the co-operative structures was earlier examined in depth by Hazari Committee (ARDC,1976) which recommended the integration of both the wings of co-operatives. Integration of co-operative structures can be expected to become an important landmark in restructuring the co-operative system. This assumes importance as it is a pre-requisite to the de-layering of the co-operative structure as recommended by Narasimham Committee on Banking Sector Reforms (Government of India, 1998). This step would benefit the ultimate borrowers by way of rationalising the functioning of co-operative structure. Andhra Pradesh is the only state which has implemented the integration during 1986 till date. In view of the above, we examine in this paper the issue of integrating the co-operative wings and examine the impact of integration in the light of the experience of the state of Andhra Pradesh.

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The views expressed are those of the authors' alone.

DATA BASE AND METHODOLOGY

The data on working of the co-operatives in the state, compiled from *Statistical Statements Relating to Co-operative Movement in India* published by National Bank for Agriculture and Rural Development(NABARD), are used. The data on short-term structure and long-term structure are available separately till 1985-86 (pre-integration) and then onwards (post-integration) the details are available for the joint structure. The criteria for the evaluation are: status of assets and liabilities, changes in the loan portfolio, changes in the management costs and changes in the health of the co-operatives. Earlier Ramireddy(1996) has evaluated the single window system by comparing the pre- and post-integration periods in Visakhapatnam district of Andhra Pradesh using data at discrete intervals. Since time-series data may reveal a better picture, in this paper, we cover a period from 1980-81 to 1994-95. For making the data for pre-integration period and post-integration period comparable we aggregated the data for District Central Co-operative Banks(DCCBs) and Primary Co- operative Agricultural and Rural Development Banks (PARDBs) before 1985-86. Wherever needed we estimated the expected values of certain parameters for post-integration period using the trend in the pre-integration period separately for the PARDBs and DCCBs. The estimated values for 1986-94 for PARDBs and DCCBs are aggregated to get a simulated value, i.e., the value a parameter would possibly take in the absence of integration. These simulated values are compared with the actuals.

RESULTS AND DISCUSSION

Need for Integration of Co-operative Wings

It was often argued against integration (see for the details ARDC, 1976). The reasons stated are: (i) Historically the LDB was created out of the felt need and recommendation of a number of expert bodies including Royal Commission on Agriculture (1928) and the Central Banking Enquiry Committee(1931). (ii) The dichotomy in the co-operative structure is a division of labour and ensures specialisation. (iii) The LDBs performed even better than commercial banks at times and showed considerable dynamism in their working in the past. They developed expertise and technical competence and stood the test of time. (iv) It may be advantageous to retain the identity of LDBs in view of the special pattern of resource mobilisation. (v) In case of failure of one line of credit the other line will be there if the dichotomy is maintained. (vi) As multi-agency approach was adopted as a national policy, the LDBs need not be merged. Justification for the establishment of Agricultural Refinance and Development Corporation (ARDC) would also justify leaving the LDB as separate units. (vii) There will be administrative problems on account of staff, etc.

Some of these arguments are facile and mostly appeal on administrative grounds rather than on economic grounds. Other arguments related to expertise, resource mobilisation, etc., which must have been valid around mid-1970s, lost their relevance in today's context. The structural framework should, therefore, be reviewed in the light of the needs of the beneficiaries, general economic setting prevailing and the expectations from the co-operatives at present. Today, the co-operatives are expected to be more responsive, provide quick and quality service, run on business lines achieving self-reliance and viability. They are compared with other institutional agencies and are expected to follow prudential norms of accounting and provisioning as prescribed for commercial banks. They are also given freedom to decide their deposit and lending rates. The commercial banks are allegedly shying away from rural lending. This increases pressures on co-operative system which has to fill the gap. Further, agriculture itself is undergoing rapid changes and rural economy is diversifying towards secondary and tertiary sectors. This brings shifts in the quantum and pattern of demand for rural credit (Agrawal *et al.*, 1997; Planning Commission, 1996; Satyasai and Viswanathan, 1997 a, b). The composition of short-term and long-term loans also undergoes change. Hence, the co-operatives may have to build expertise to deal with these new demand patterns and the dichotomy of co-operative structure on the traditional lines may render the whole set-up redundant and irrelevant.

Thus there is a need for integration of co-operatives to enable them to cater to short- and long-term needs while saving on costs. Integration is beneficial as it offers single point of service to rural producers and hence, can take care of the complementarity between the short-term and investment needs. Cost economies may also be achieved on account of cost of supervision and senior management. Better supervision will be ensured as the integration would enable the co-operative societies to appoint qualified full time secretary and would also release some manpower involved in similar jobs but in different wings of co-operatives which can be redeployed profitably for supervision which is at present very weak. There will be saving in the cost and efforts in mobilising resources if a single structure replaces the two wings.

Impact of Integration

Business

Table 1 gives data on working capital (assets) and loans issued in co-operative system. Working capital rose from Rs. 552 crores in 1980-81 to Rs. 1,035 crores in 1985-86 and

TABLE 1. WORKING CAPITAL AND LOANS ISSUED

(Rs. crores)

Items (1)	Working capital (2)	Loans issued (Short-term + medium-term) (3)	Proportion of loans to working capital (per cent) (4)
Pre-integration			
1980-81	552	211	38.2
1981-82	651	233	35.8
1982-83	776	273	35.1
1983-84	824	329	39.9
1984-85	930	310	33.3
1985-86	1,035	279	26.9
Post-integration			
1986-87	1,197	553	46.2
1987-88	1,488	652	43.8
1988-89	1,605	641	39.9
1989-90	1,893	399	21.1
1990-91	2,066	579	28.0
1991-92	2,151	376	17.5
1992-93	2,521	870	34.5
1993-94	2,716	870	32.0
1994-95	3,030	922	30.4
Compound annual rate of growth (per cent)			
1980-85	12.21*	6.99*	-5.23*
1986-94	10.92	5.77	-5.15

* The difference in the growth rates between the two periods is not significant unless specified.

further to Rs.3,030 crores in 1994-95. The growth rates are 12.21 per cent and 10.92 per cent during pre- and post-integration periods respectively. Loans issued (both short-term and medium-term loans) by all DCCBs and PARDBs together in the state increased from Rs.211 crores in 1980-81 to Rs.279 crores in 1985-86 and rose to Rs.922 crores by 1994-95. The growth rate in the pre-integration period is 6.99 per cent which is higher than 5.77 per cent registered in post-integration period. That is, there was some deceleration, though not significant, in the flow of credit after the integration. The proportion of loans issued to working capital showed a consistent decline in both the periods notwithstanding the rise in absolute amounts.

Table 2 gives details of short-term and medium/long-term loans issued by the co-operatives in different years. The flow of short-term loans accelerated from 8.40 per cent per annum during the pre-integration period to 8.33 per cent per annum during the post-integration period. The term loans (medium and long-term), on the other hand, showed a decline in the growth rate from 6.33 per cent in the pre-integration period to 1.87 per cent in the post-integration period.

TABLE 2. SHORT-TERM AND INVESTMENT LOANS ADVANCED

(Rs. crores)

Year	Amount of loans				Percentage of actual to expected loans		Ratio of short-term to medium-term (including long-term)	
	Actual		Expected					
	Short-term	Medium-term*	Short-term	Medium-term	Short-term	Medium-term	Actual	Expected
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Pre-integration								
1980-81	90	120	121	118	75	101	0.75	1.02
1981-82	149	84	132	118	113	71	1.78	1.12
1982-83	164	108	143	130	115	83	1.52	1.10
1983-84	215	114	156	144	138	79	1.89	1.08
1984-85	158	152	170	149	93	102	1.04	1.14
1985-86	149	130	185	165	81	79	1.15	1.12
Post-integration								
1986-87	268	286	201	171	133	167	0.94	1.18
1987-88	443	209	218	134	203	156	2.12	1.63
1988-89	447	194	237	142	188	136	2.31	1.67
1989-90	228	171	258	151	88	113	1.33	1.71
1990-91	299	280	281	161	106	174	1.07	1.74
1991-92	212	164	306	172	69	96	1.29	1.78
1992-93	576	295	332	183	173	161	1.95	1.82
1993-94	619	251	361	195	171	129	2.46	1.86
1994-95	653	270	393	207	166	130	2.42	1.90
Compound annual rate of growth (per cent)								
1980-85	8.40	6.33	-	-	-	-	2.07	1.34
1986-94	8.33	1.87	-	-	-	-	6.46	4.19

* Medium-term includes long-term credit.

But the amount during the post-integration period averaging at Rs. 235 crores is double the average amount of Rs. 118 crores during the pre-integration period. The actual short-term loans during the post-integration period was, on an average, 145 per cent of the expected loans estimated using the trend during the pre-integration period. The actual term loans on an average were 156 per cent of the expected amount. That is, the flow of short-term and term loans is higher during the post-integration period than what would have been possible had there been no integration. The ratio between short-term and term loans which averaged at 1.3 during the pre-integration period improved to 1.77 during the post-integration period.

In terms of outstandings, the short-term loans outstanding rose at 12.94 per cent during the pre-integration period to 14.08 per cent during the post- integration period (Table 3). The outstanding term loans increased at 9.79 per cent and 10.35 per cent in these two periods respectively. The actual short-term loan outstanding was higher than the expected outstanding amounts while the actual term loan outstanding was lower than the expected values. That is, the growth of term loans is below the expectations. The ratio of short-term to term loans outstanding has improved between pre-integration period and post-integration period from an average ratio of 0.40 to 0.60. Further, the ratio is consistently higher than expected.

TABLE 3. SHORT-TERM AND INVESTMENT LOANS OUTSTANDING

(Rs. crores)

	Amount of loans				Percentage of actual to expected loans		Ratio of short-term to medium-term (including long-term)	
	Actual		Expected				Actual	Expected
Year	Short-term	Medium-term	Short-term	Medium-term	Short-term	Medium-term		
(1)	(2)	(3)	(4)	(5)	(6)	(7)	(8)	(9)
Pre-integration								
1980-81	98	309	111	307	89	101	0.32	0.36
1981-82	133	326	126	337	106	97	0.41	0.37
1982-83	153	378	143	370	107	102	0.40	0.39
1983-84	184	397	163	407	113	97	0.46	0.40
1984-85	175	480	186	448	94	107	0.36	0.41
1985-86	199	482	211	494	94	98	0.41	0.43
Post-integration								
1986-87	224	458	241	544	93	84	0.49	0.44
1987-88	331	559	274	601	121	93	0.59	0.46
1988-89	403	615	312	663	129	93	0.66	0.47
1989-90	538	682	355	733	152	93	0.79	0.48
1990-91	443	752	404	811	110	93	0.59	0.50
1991-92	482	842	459	898	105	94	0.57	0.51
1992-93	659	904	523	995	126	91	0.73	0.53
1993-94	732	984	595	1,104	123	89	0.74	0.54
1994-95	820	1,106	677	1,225	121	90	0.74	0.55
Compound annual rate of growth (per cent)								
1980-85	12.94	9.79	-	-	-		3.14	3.42
1986-94	14.08	10.35	-	-	-	-	3.73	2.80#

Difference in growth rates between the two periods is significant at 5 per cent level.

Table 4 gives the flow of short-term and term credit per gross cropped hectare(ha). Both types of credit showed growth in absolute terms. Short-term credit grew from about Rs. 74 per ha in 1980-81 to Rs. 512 per ha in 1994-95. The growth rate, however, was faster in the pre-integration period at 9.04 per cent per annum compared to 7.62 per cent in the post-integration period. Term credit, on the other hand, rose from about Rs. 98 per ha in 1980-81 to Rs. 211 per ha in 1994-95. The growth rate was lower in the second period than the first period. On comparison, the actual flow of credit was consistently higher than the expected flow for short-term and term credit during the post-integration period. This is suggestive of the favourable impact of integration.

TABLE 4. FLOW OF CREDIT PER CROPPED HECTARE

(Rs.)

Year (1)	Actual Short-term loans (2)	Actual Term loans (3)	Expected Short-term loans (4)	Expected Term loans (5)
Pre-integration				
1980-81	73.67	97.80	98.75	96.46
1981-82	114.19	64.28	101.10	90.16
1982-83	128.66	84.81	112.35	101.70
1983-84	160.65	84.86	116.50	107.70
1984-85	129.43	124.34	138.96	122.20
1985-86	123.09	107.21	152.54	136.28
Post-integration				
1986-87	228.83	244.49	171.68	145.98
1987-88	364.48	171.71	179.63	109.97
1988-89	339.93	147.36	180.57	108.18
1989-90	172.16	129.11	194.81	114.23
1990-91	226.51	212.02	212.90	122.19
1991-92	160.45	124.67	231.60	130.10
1992-93	451.45	230.97	260.54	143.28
1993-94	484.96	196.96	283.37	152.56
1994-95	511.75	211.44	308.20	162.46
Compound annual rate of growth (per cent)				
1980-85	9.04	6.97	-	-
1986-94	7.62	1.16	-	-

Costs and efficiency

Table 5 presents the data on management costs. Total management costs (including salaries, rent, depreciation and others) which amounted to Rs. 13.28 crores in 1980-81 rose to Rs. 41.57 crores in 1985-86 and further to Rs. 104.08 crores in 1994-95. The growth rate during the post-integration period declined to 6.95 per cent compared to a very high growth rate of 20.26 per cent during the pre-integration period.

The management costs per thousand rupees of working capital averaged at Rs. 31.40 during the pre-integration period and at Rs. 35.60 during the post-integration period. However, after the initial high management costs of Rs. 49, Rs. 39 and Rs. 47 per Rs. 1,000 of working capital in the first three years after integration, the unit management costs showed a declining trend. The growth rate in the post-integration period was (-)3.96 compared to 8.05 in the pre-integration period. However, the average cost is higher in the 1990s compared to the early 1980s.

Management cost per unit of loans issued also showed considerable deceleration in the post-integration period as the growth rate declined from 13.82 per cent during 1980-85 to 1.18 per cent during 1986-94. The absolute level of management costs per Rs.1,000 loan issued, however, increased from Rs.63 in 1980-81 to Rs.113 in 1994-95. As the management costs (total and unit) showed deceleration during the post-integration period, it can be construed as a favourable cost economy onsetting after integration.

TABLE 5. COST OF MANAGEMENT IN THE CO-OPERATIVE STRUCTURE

Year (1)	Total management costs (Rs.crores) (2)	Management costs (Rs.)	
		Working capital (per Rs. 1000) (3)	Loans issued (per Rs.1000) (4)
Pre-integration			
1980-81	13.28	24.07	63.06
1981-82	17.59	27.01	75.54
1982-83	24.14	31.11	88.57
1983-84	26.20	31.78	79.69
1984-85	27.19	29.23	87.72
1985-86	41.57	40.17	149.19
Post-integration			
1986-87	58.70	49.04	106.06
1987-88	57.62	38.73	88.41
1988-89	75.26	46.90	117.44
1989-90	62.23	32.87	155.81
1990-91	60.41	29.24	104.41
1991-92	51.24	23.82	136.22
1992-93	98.49	39.07	113.16
1993-94	96.20	35.42	110.61
1994-95	104.08	34.35	112.84
Compound annual rate of growth (per cent)			
1980-85	20.26#	8.05#	13.28#
1986-94	6.95	-3.96	1.18

Difference in growth rates between two periods is significant at 5 per cent level.

Health of co-operatives

The co-operatives incurred losses in both the periods, and the magnitude of loss increased over time (Table 6). Bad debts rose from Rs. 11.65 crores in 1980-81 to Rs. 23.88 crores in 1985-86 and further to Rs. 42.20 crores in 1994-95. They showed a growth rate of 15.04 per cent in the pre-integration period compared to a very low growth rate of 0.94 per cent during the post-integration period. As a proportion to working capital the bad debts ranged from 1.75 to 2.31 per cent during the pre-integration period and peaked to 3.71 per cent in 1988-89 and gradually declined thereafter to 1.39 per cent in 1994-95. The growth rate decelerated from 2.82 per cent in the first period to (-) 9.98 per cent after integration. Bad debts as a percentage of loans outstanding, which grew at a rate of 4.41 per cent before integration, similarly declined at the rate of (-)10.84 per cent. Althrough the 15-year period the co-operative system in the state incurred losses in the aggregate and the losses mounted over time.

TABLE 6. HEALTH AND VIABILITY INDICATORS FOR CO-OPERATIVES

(Rs. crores)

Year	Profit (+) Loss (-)	Bad debts	Bad debts: As per cent of working capital	Bad debts: As per cent of outstanding loans
(1)	(2)	(3)	(4)	(5)
Pre-integration				
1980-81	0.00	11.65	2.11	2.86
1981-82	-2.99	12.49	1.92	2.72
1982-83	-9.76	13.58	1.75	2.56
1983-84	-9.01	14.81	1.80	2.55
1984-85	-15.69	21.22	2.28	3.24
1985-86	-8.42	23.88	2.31	3.51
Post-integration				
1986-87	-19.37	31.77	2.65	4.66
1987-88	-27.66	40.23	2.70	4.52
1988-89	-57.39	59.56	3.71	5.86
1989-90	-72.53	65.16	3.44	5.34
1990-91	33.65	52.06	2.52	4.36
1991-92	-48.29	34.05	1.58	2.57
1992-93	-50.32	48.00	1.90	3.07
1993-94	-97.93	47.65	1.75	2.78
1994-95	-89.84	42.20	1.39	2.19
Compound annual rate of growth (per cent)				
1980-85	-	15.04†	2.82†	4.41†
1986-94	-	0.94	-9.98	-10.84

† Difference in growth rates between two periods is significant at 5 per cent level.

The proportion of overdues is another indicator of the health of any credit system. Table 7 shows the overdues of co-operatives over time. The data show that the recovery levels did not grow at the same pace as the demand. As a result, the overdues as a proportion of demand increased from an average level of 43 per cent in the pre-integration period to about 50 per cent in the post-integration period. This trend may have to be ascribed largely to the Agricultural and Rural Debt Relief (ARDR) scheme, which showed its impact on recovery during 1989-90 to 1991-92 rather than due to the integration.

TABLE 7. DEMAND, COLLECTION AND BALANCE OF THE CO-OPERATIVES

(Rs. crores)

Year (1)	Demand (2)	Collection (3)	Balance (4)	Overdues (per cent) (5)
Pre-integration				43.00
1980-81	289.40	184.00	105.41	36.42
1981-82	346.55	216.19	130.35	37.61
1982-83	410.69	228.97	181.73	44.25
1983-84	492.61	316.76	175.86	35.70
1984-85	514.16	268.80	245.22	47.69
1985-86	564.78	290.48	274.29	48.57
Post-integration				49.77
1986-87	653.41	422.27	231.14	35.37
1987-88	738.94	436.59	302.35	40.92
1988-89	783.98	478.56	305.42	38.96
1989-90	924.05	184.00	740.05	80.09
1990-91	1,140.53	699.56	440.97	38.66
1991-92	817.99	257.29	560.70	68.55
1992-93	1,242.14	633.02	609.12	49.04
1993-94	1,329.70	743.83	585.87	44.06
1994-95	1,607.23	785.02	822.21	51.16
Compound annual rate of growth (per cent)				
1980-85	13.45	9.32	18.98	5.53
1986-94	5.53	8.29	13.61	3.34

CONCLUSIONS

The co-operative system in the country needs restructuring in view of the changing demand pattern for rural credit, higher expectations from the co-operatives which are expected to provide quick and quality service and to enable them to be viable and vibrant. De-layering of the co-operative system, integration of short-term and long-term co-operative structures are some of the alternative restructuring options often suggested. A review of the experience of Andhra Pradesh, where the integration option was followed since 1986-87, revealed some interesting trends. The flow of short-term and term loans is higher during the post-integration period than what would have been possible had there been no integration. The ratio between short-term and term loans which averaged at 1.3 during the pre-integration period improved to 1.77 during the post-integration period. This is a positive feature as the short-term and term credit should flow as complements. This is suggestive of the favourable impact of integration. The management costs (total as well as per thousand rupees of working capital and loans issued) showed deceleration during the post-integration period which can be construed as favourable cost economies onsetting after integration. Bad debts of the co-operatives, in absolute terms as well as relative to working capital and loans outstanding, showed declining trend. The proportion of overdues increased between the two periods which appear less likely due to integration than the ARDR scheme.

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