

CHAPTER 16

EFFORTS TOWARDS OTHER IMPROVEMENTS IN LONG-TERM CO-OPERATIVE CREDIT STRUCTURE

AS a result of the efforts made in the last three decades for improving their organizational competence and operational capabilities, LDBs have come to play an important role, both quantitatively and qualitatively, in the provision of investment credit for agriculture and allied activities. All the same, there are several shortcomings and deficiencies in their working. The Madhava Das Committee on LDBs (1975) which we have referred to earlier, has made several recommendations for streamlining their working; but the response thereto has not been, by and large, quite encouraging with the result that LDBs continue to suffer from certain problems, affecting smooth flow of term finance for accelerated rural development. In this chapter, we consider these problems in the light of our discussions with the various state governments, representatives of LDBs etc., and make our recommendations thereon.

STRUCTURAL WEAKNESS AND REHABILITATION PROGRAMME

16.2 The present structure of LDBs which is federal in many states and unitary in some has evolved over the years in response to the requirements of the respective states. LDBs and their Federation, on our eliciting their views in this regard, have expressed themselves against any change in the present pattern. We agree that the existing structure need not be disturbed merely for bringing about uniformity.

16.3 A major problem to-day in the long-term co-operative credit structure is that, in a number of cases, investment credit dispensed by LDBs has not been productively deployed, as a result of which, the overdues are showing a rising trend, rendering several PLDBs in the federal set-up and branches of SLDBs in the unitary structure, either eligible for only restricted lending or ineligible to undertake any fresh lending programme. As indicated in Chapter 4, as many as 360 PLDBs/branches of SLDBs, whose overdues as on 30 June 1979 exceeded the cut-off point at 55 per cent of demand, were ineligible to lend for fresh investments. Another 452 units had only restricted lending eligibility according to the range of their overdues as on 30

June 1979. As per information available in the RBI, the position had further deteriorated by end June 1980 ; the number of units having overdues above the cut-off point had risen to 712 as on that date. During our field visits and state-level discussions, we observed that a sizeable proportion of the overdues stemmed from either non-utilisation or misapplication of the loans advanced. Needless to say, it will spell disaster to LDBs if investment finance provided by them is not applied to generate income at levels enough to secure its prompt return flow. If these institutions are to obtain their due share of the scarce long-term resources, it would be necessary for them to demonstrate in actual practice that the resources provided to them for this purpose are being utilised for effectively-supervised investment schemes capable of augmenting productivity and income of the beneficiaries. What causes concern to the Committee is the lack of evidence to show that this problem has received the serious and earnest attention that it deserves from the state governments and LDBs. Apart from plugging the lacunae in the existing arrangements for monitoring and supervision and tightening up of the post-credit follow-up machinery on the lines suggested by us later in this chapter, what is imperative is the undertaking, on a priority basis, of a case-by-case investigation of loans advanced by each of those PLDBs/branches of SLDBs which are below the cut-off point with a view to identifying (a) cases of wilful default in which, even after completion of investments, repayment of loan instalments have been deliberately withheld, (b) cases of non-utilisation and misapplication of loans advanced either by not drawing the second and subsequent instalments of loans or by not executing the project, despite drawal of the instalments and (c) cases where, inspite of the proper utilisation of the loans availed, the investment remains incomplete due to post-sanction cost escalations or other factors. The Committee emphasises that, if LDBs are to serve as useful and effective channels of investment credit, it is squarely the responsibility of the state governments, who are the guarantors of their debentures, to carry out an exercise of this kind within a specific time-frame of not more than one year and also to formulate, on the basis of the results thereof, a comprehensive rehabilitation programme to be implemented over a period of one or two years, on the following lines in consultation with/and active involvement of, the RBI/ARDC/NABARD :

- (i) In cases where the investments are incomplete due to inadequacy of loan amounts sanctioned already, additional finance may be provided to the borrowers to complete the project ;

- (ii) In respect of loans covered by items (a) and (b) above, stringent and punitive measures should be instituted forthwith for recovery of the dues. The loan accounts in such cases should be summarily foreclosed and, coercive proceedings launched against the defaulters for recovery of their outstanding dues. Also, departmental action should be taken against all the concerned officials who furnished false utilisation certificates on the strength of which the loan instalments were disbursed ; and
- (iii) The rehabilitation programme should *inter-alia* provide for increasing the coverage of small-farmer and other weaker section clientele and improving the loan operations in terms of progressive increases in lendings, diversification of advances portfolio, effective monitoring and supervision over the use of credit, timely recovery of loans out of incremental income generated by the investments financed, strengthening of the administrative, technical and supervisory staff of the banks with adequate grant-in-aid from the state government, etc. Wherever necessary, it should also provide for financial assistance from the state government in the form of share capital contribution out of its own budgetary resources to enable the concerned LDBs notionally to reduce their overdues and for enabling them to move to the lending eligibility slab immediately above the cut-off point. This, however, should be a purely temporary measure for the banks to finance fresh investments of new and non-defaulter members until such time they improve their recovery performance with action initiated on the lines indicated above.

16.4 The Committee observes that in the matter of realising overdues, LDBs are considerably handicapped for want of bidders in auction of lands mortgaged to them by borrowers. The Committee is of the view that an effective way of assisting LDBs to get over this difficulty is for the state governments themselves to purchase the mortgaged lands in settlement of the LDBs' claim and arrange to dispose them either by outright sale or on long-term lease to identified target groups consisting of small and marginal farmers and agricultural labourers in the area. This method, the Committee feels, will not only help thwart the attempts of habitual and wilful defaulters to gang up but will also enable the vulnerable groups to improve the size of their holdings and their viability. The state governments may

set up a suitable organization under the Registrar of Co-operative Societies or some other appropriate authority to deal with this matter. In this connection, the Committee is happy to find that the Karnataka Government has already taken the lead in this regard by placing a sum of Rs. 1 crore at the disposal of the Registrar of Co-operative Societies for purchase of lands of defaulters in auction. The Committee hopes that the other state governments will also follow suit.

16.5 In the case of those PLDBs/SLDB branches which have restricted lending eligibility, the state governments may carry out a case-by-case and on-the-spot scrutiny of the loans for ensuring productive use of credit and early completion of the investments and also take action for recovery of overdues in the manner indicated in the preceding paragraphs.

16.6 Should the rehabilitation programme, as mentioned above, fail to produce the desired results within the time limit specified, the state governments should not hesitate to take action for winding up the units concerned and allowing other institutions under the multi-agency system to take care of the investment credit needs of the area.

16.7 In the case of unitary structure, it is desirable to associate local non-officials with the functioning of the branches of the SLDB and involve them actively in the development of the branch. Towards this end, a branch advisory committee having representatives from various blocks and of different categories of rural population engaged in agriculture and allied activities including those belonging to scheduled castes, scheduled tribes, small and marginal farmers, agricultural labourers and rural artisans should be constituted for each branch and their support enlisted in scheme formulation and implementation and recovery of loans. The bylaws of SLDBs concerned may be amended suitably providing for the constitution of such branch advisory committees with the approval of their Board of Directors and steps be taken to make them function as quickly as possible.

Problem of Viability

16.8 Related to the organizational structure is the problem of viability of LDBs. Various Committees and Working Groups have, in the past, gone into this question. The Madhava Das Committee suggested that a PLDB or a branch of SLDB should have a minimum loan business of Rs. 35 lakhs to function as a viable unit. More

recently, the Committee on Interest Rate Spreads in the Agricultural Lending Sector appointed by the RBI in 1978 reviewed this norm, taking into account the general escalation in wage structure, the growing need for the LDB structure to appoint technical supervisors and to pay more attention to scientific methods of loan appraisal, verification of utilisation of loans as also the recovery of loan instalments and came to the conclusion that, with the benefit of an interest margin of 1.75 per cent, it should be possible for a PLDB to attain viability at a level of outstanding loan business of Rs. 40 lakhs. It had further indicated that for obtaining the benefit of an interest margin of 1.75 per cent, the LDB should have an overall margin of about 2 to 2.25 per cent in relation to its current borrowings and lendings and hence, the SLDB in each state, in consultation with the affiliated PLDBs, might fix the appropriate margin to be allowed to the latter so that they could attain financial viability within a period of say, 3 years. In this context we observe that, with the increase in lending rates to ultimate borrowers suggested by the Reserve Bank in terms of its instructions issued in August 1980, the margin available to LDBs has gone up, ranging between 3.75 per cent and 3.85 per cent on ARDC loans and 3.40 per cent and 4.55 per cent on normal loans. The state governments should therefore take steps to ensure that a major portion of this margin percolates to the primary level institutions to make them strong and viable units. Being crucial to structural stability, the viability of the institutions has to be sustained and hence it is important that such of the PLDBs/SLDBs' branches as have no prospect of attaining viability due to dearth of lending potential and other geo-physical constraints are either amalgamated to command a wider coverage and business potential or merged with the adjacent viable PLDB/branch. We would suggest that the state governments and the SLDBs should review the cases of all such non-viable units and take necessary steps as indicated above, to rationalize the structure, keeping the viability objective in view.

LENDING DISCIPLINE

16.9 As discussed in Chapter 4, even though the lending operations of LDBs have, over the years, increased considerably in absolute terms, the progress in some states cannot be considered encouraging when compared with the local needs and the achievements in long-term lending of the commercial banking sector which is relatively new to the field. Further, in recent years, LDBs in developed states like Karnataka, Gujarat and Tamil Nadu have shown a declining trend in their annual lending. This is also reflected in the extent of avail-

ment of refinance by SLDBs from the ARDC. Whereas the magnitude of refinance disbursed to SLDBs upto 30 June 1980 was of the order of Rs. 983 crores, constituting 56.6 per cent of total refinance disbursements, the share of SLDBs in the total refinance has been progressively declining since 1975-76 as indicated below:

Agency	Refinance disbursed during				
	1975-76	1976-77	1977-78	1978-79	1979-80
(1)	(2)	(3)	(4)	(5)	(6)
SLDBs	99 (57.9)	127 (57.4)	112 (47.9)	131 (46.0)	164 (59.8)
Scheduled commercial banks ..	71 (41.5)	93 (42.1)	120 (51.3)	150 (52.6)	239 (58.0)

Source : ARDC's Annual Report for 1979-80.

Note : Figures in brackets indicate percentages to total. The total of the two percentages does not add to 100 as the figures of SCBs are not included in the table.

The most important factor that is said to limit the lending capacity of the banks is the recovery-linked lending norms prescribed by the ARDC and the RBI. This is examined in the ensuing paragraphs.

16.10 Upto the end of the financial year 1970-71, the debenture programme of SLDBs was being regulated on the basis of percentage of overdues at the SLDB level. But, in 1971-72, the RBI felt that, as a measure of financial discipline and also for stimulating recovery efforts, it would be advisable to link the lending eligibility of PLDBs/branches of SLDBs to their recovery performance and, accordingly, from September 1973, SLDBs were required to regulate their advances as a percentage of the annual lending programme of their affiliated units in relation to overdues in such units. In 1975, the RBI set up, a "Standing Committee on Debenture Norms" for evolving common norms for issue of ordinary and special development debentures. Since then, the regulatory norms are being reviewed from time to time by this Committee.

16.11 The salient features of the regulatory norms are: (i) a PLDB/branch of SLDB with overdues upto a tolerance limit of 25 per cent of demand will have unrestricted lending eligibility; (ii) banks with overdues exceeding a cut-off point (55 per cent at present) will not be eligible to be financed out of funds borrowed from the ARDC or by way of normal debentures; and (iii) banks with overdues between the tolerance level and the cut-off point will be eligible for lending subject to a slab system, the intention being that, the higher the recovery percentage, the greater will be its lending eligibility.

16.12 During the implementation of the Second ARDC Credit Project (1977-79), some modifications and relaxations in the norms of discipline were recommended by the Standing Committee on De-benture Norms and these were finalised by the RBI and the ARDC in consultation with the Government of India and IDA. According to the earlier arrangement, the classification of PLDBs/branches of SLDBs was based on their overdues in slabs of 10 percentage points for units having overdues above 25 per cent of demand. This was changed in January 1979 to slabs of 5 percentage points each and somewhat higher limits were fixed for each slab. Accordingly, the revised over-due slabs and lending eligibility which are now operative are as under:

Range of overdues (Percentage to demand)	Eligibility for lending (As percentage of average of loans issued during preceding 3 years or during the previous year whichever is higher)	Limits for fresh lending
(1)	(2)	(3)
26 - 30	100	30
31 - 35	90	30
36 - 40	80	25
41 - 45	75	25
46 - 50	70	20
51 - 55	65	20

In addition, banks falling in each slab are allowed limits for fresh lending which are fixed as a percentage of the previous year's loans or of the average of the previous three years whichever is higher. These figures are shown in column 3 of the above table.

16.13 Banks having overdues exceeding the cut-off point at 55 per cent of demand have ceased to be eligible for any lending programme except to meet the committed expenditure of second and subsequent instalments in respect of loans for which first instalment was already disbursed. However, with a view to encouraging larger credit flow to small farmers, PLDBs/branches of SLDBs with restricted lending eligibility, are allowed to draw funds from SLDBs for financing small farmers identified as such in SFDA, DPAP, CADP areas. This is in recognition of the fact that in these areas arrangements exist to identify and supervise borrowers. This relaxation in respect of financing small farmers has been extended in October 1979 to PLDBs/branches of SLDBs, having "nil" lending eligibility, provided a time-bound programme of rehabilitation, covering among others, measures to strengthen the organization, improving financial viability, augmenting technical support and reducing overdues over a reasonable period of

time is drawn up for the concerned unit and implemented and provided there are also arrangements to the satisfaction of the RBI/ARDC for monitoring and supervision of the credit schemes.

16.14 We have been informed that in accordance with the agreement executed with the IDA for the ARDC's Third Credit Project (1980-81) there are proposals to revise the cut-off point of overdues to 50 per cent and also to insist on a comprehensive rehabilitation programme of the entire structure in a state before refinancing is allowed, if half or more of the PLDBs or branches of the SLDB have become ineligible as a result of the new cut-off point. These proposals, if implemented, are likely to affect adversely LDBs' operations in several states and a large number of units will cease to be eligible for any lending programme.

16.15 During the course of our discussions with the representatives of LDBs, three points were made: first, the norms, particularly the method of fixing lending limits, have had a regressive effect on several LDBs; second, the policy of ARDC of fixing the period of the loan as 7-9 years as against the earlier practice of 15 years, has not been fully accepted by the borrowers; and third, the stipulation of the ARDC that the instalment payments for redemption of debentures by LDBs shall be the same as the instalment payments fixed for the ultimate borrowers, has taken away the flexibility available to LDBs under the previous practice of maintaining a sinking fund and redeeming through a single payment at the end of the period of the debenture.

16.16 We feel that these and other points that have been identified as responsible for the deterioration of the LDB system in recent years deserve to be examined with reference to the policy objective of building sound and strong institutions to serve the rural people. It is obvious that no bank can survive if it closes its doors, inch by inch to begin with and finally after a period, to its clientele and a regulation or discipline that brings this about inexorably, however well intentioned it might be, can only be described as self-defeating. We have no doubt that the present regulation which has been introduced in the wake of credits from the IDA has been devised with the most commendable purpose of ensuring prompt recycling of funds with strict reference to such unassailable concepts as the life of the assets created, the incremental income accrued and timely recovery. But the experience of the last 8 years or so, has shown that more time is necessary for the borrowers to adjust themselves to the shorter tenure of loans and the consequent increase in the amount of instalment of repayment. It

takes time for the rural borrowers to appreciate and follow the excellent purposes and concepts implicit in the lending discipline. In this context, we also take note of the improvements already made or under contemplation. In July 1978, the ARDC agreed to fix the maturity periods of debentures so as to make them longer by 2 years than the corresponding loans to ultimate borrowers except in the case of 15 year loans. The ARDC has also agreed to reschedule the loan repayments in the event of natural calamities. LDBs have been allowed to pay their annual redemption instalments at the end of the year instead of different dates during the year. More recently, the period of loans to ultimate borrowers, in the case of wells and pumpsets has been extended from 7 years to 9. We have also been informed that the Debenture Norms Committee is working on a revised regulation which will provide a minimum lending limit to all the LDBs having overdues in excess of the cut-off point and thus take away the regressive features of the present regulation. We, therefore, recommend that the existing norms and guidelines be reviewed immediately by the ARDC/RBI in consultation with the GOI in the light of past experience and realities in the field.

16.17 While pleading for a realistic set of norms for lending, we would reiterate that the health of an investment lending system depends largely on the care and attention devoted to appraisal of investment proposals, systematic follow-up after sanction of loans and prompt recovery of loan instalments. It is the duty of the state governments to ensure that LDBs are equipped for these purposes and that nothing is done to thwart these purposes on political or other considerations.

DIVERSIFICATION OF LENDING

16.18 In the multi-agency financing system for integrated rural development that entails provision of multi-term and multi-purpose credit to the rural community, LDBs cannot remain, for all time, to be institutions lending only for land-based activities. Unless they finance non-land based activities, LDBs cannot be said to serve the rural poor who have hardly any land and who need long-term finance for widening their production and income base. Moreover, with the narrowing of traditional lending avenues like minor irrigation programmes, land improvement and farm mechanisation which have already been covered to a large extent, LDBs will find it increasingly difficult in the years to come, to increase their business unless they diversify their operations on a large scale. During our visits to Karnataka, Punjab, Haryana, Andhra Pradesh and Tamil Nadu, we noticed

that the scope for LDBs to thrive mainly on minor irrigation lendings is getting narrower on account of near-saturation in ground water exploitation. But, not much thought and attention seem to have been bestowed by several LDBs in exploring new avenues. Illustratively, we observed that in one of the districts of Punjab, nearly two-thirds of LDBs' advances in 1978-79 had gone for installation of tube wells and tractor purchase. Also in the heavy black soils of Madhya Pradesh with 50 to 60 inches of rainfall, there was no effort at financing viable drainage schemes. Our visit to Koraput district in Orissa revealed that, despite the scope for term-credit extension to sericulture, horticulture, etc., no attempts worth mention had been made in this direction by the co-operative credit sector.

16.19 Marginal farmers with very small holdings cannot become viable without being supported by adequate capital finance for off-farm activities in addition to farm-based activities. Also, the vast majority of non-land holders have to be assisted with credit for acquisition of production assets. Thus, diversification has to be two-pronged—one in the direction of financing such land-based activities as plantations, sericulture, horticulture, pisciculture, farm forestry, etc. and the other, in respect of non-land based purposes like dairying, poultry farming, piggery, sheep rearing, installation of *gobar* gas plants, construction of rural warehouses/godowns, cold storage plants, agro-processing, rural housing/farm houses, agro-based rural industries, cottage industries, rural artisans, agro-service centres, development of market yards, etc. No longer can these banks remain merely land development banks or even agricultural development banks as in Andhra Pradesh. They have to become rural development banks so that they can play their due role in integrated rural development. We urge that necessary legal and organizational steps be taken expeditiously to achieve this objective.

16.20 It is likely that the proposal to extend the jurisdiction of LDBs to non-land based activities, particularly to the rural industrial sector, may be objected to on the ground that there are other agencies to serve these activities. State Financial Corporations refinanced by the IDBI, special agencies like Handloom Corporations and KVI Boards may claim that they have built up the necessary expertise and organization and that LDBs need not be allowed to encroach on their areas. In this context, we feel that while weightage should be given to the existing expertise and organizational capabilities, no monopoly need be given to any one type of institution. Some overlap is desirable in accordance with the spirit of the multi-agency system and

there is some merit in permitting a bank serving agriculture, to extend its services to agro-processing and other related activities. Accordingly, LDBs should be considered as suitable agencies for lending to (i) agro-processing units such as rice mills, oil *ghanis*, fruit canning or preservation, (ii) units providing subsidiary occupation to the rural population such as handloom, tannery, etc. (iii) servicing sector such as saw mills, units manufacturing small agricultural implements and units servicing agricultural equipments and machinery like tractors, pumpsets and custom hiring units. This list is not exhaustive.

Organizational Capabilities for Diversified Lending

16.21 Lending for non-traditional and newly emerging rural development activities needs skills and expertise of the right type for project formulation, appraisal, monitoring and evaluation of the schemes. The Reserve Bank of India had pointed out to LDBs in September 1976 that while they could avail themselves of the assistance of the technical departments of the state governments for technical appraisal of the schemes, they should have their own technical staff at the regional and branch/primary levels. It was envisaged that, in order to ensure a co-ordinated approach in financing investment programmes, SLDBs should set up requisite number of regional offices with adequate trained staff including supporting technical staff. They were also expected to establish at their head office, a project planning division, a technical division and a statistical division. According to information available, 13 SLDBs have set up technical divisions. But it is only in a few SLDBs that the technical division can be said to have the needed expertise and know-how. Others continue to depend heavily on the technical staff of the state governments. Where technical expertise is sought from the state government on deputation terms, the response is often belated owing to non-availability of sufficient and willing personnel for deputation. According to our information, even where the services of technical personnel are made available on deputation, the experience of most of the LDBs seems to be discouraging, either because of mid-term withdrawal of deputationists by the concerned departments of the government or because of lack of required experience of those deputed. During our discussions with the representatives of one of the SLDBs, we were told that the state government had withdrawn the staff deputed by it although the bank was still in need of them. Further, the transferability of government staff resulting in interruption of their services as also their non-accountability to the institutions concerned, adversely affect programme lending. In cases where project formulation was left to the govern-

ment staff entirely, there were instances where projects were prepared without ensuring local response and wholehearted participation of beneficiaries. There are, of course, instances in which the government staff on deputation have done commendable work and contributed to the growth of good business. Such instances are in fact a tribute to the qualities of the individuals concerned. But, they are rare and do not provide a justification for the system as such. If the staff are to be loyal and devoted, they have to be direct employees of the lending institution.

16.22 In this context, the Committee is gratified to note that the ARDC has recently evolved a scheme to provide financial assistance to LDBs for building up their capabilities through creation of technical cells for project preparation, appraisal, monitoring and evaluation. Assistance from the Corporation out of its Research and Development Fund for this purpose is in the form of a grant which is on a tapering scale for four years towards the expenditure on identifiable items like salary of key technical staff. At the expiry of the given period, the concerned institution is required to continue the organization at its own expense. We hope that, with this catalytic assistance, SLDBs will soon strengthen their technical skills and the state governments will help in the process by making available experienced personnel for appointment by SLDBs.

16.23 We have observed during our field and state-level discussions that the manpower position in LDBs in most of the states continues to be weak, particularly at the operating unit level, though there has been considerable expansion in investment lending techniques. The Madhava Das Committee has already made a series of recommendations in this regard. While the managerial competence at the apex level has shown signs of improvement in recent years, the system needs to be strengthened not only in regard to technical skills and expertise in varied disciplines for servicing multi-type lending programmes but also in respect of field level functionaries. In the changed context of LDBs having to play a vital role in programme lending to the weaker sections, the need for improving the manpower skills of LDBs at their operating units level can hardly be over-stressed.

16.24 As emphasised earlier, lending for rural development especially to the weaker sections, has to be based on properly-conceived and well-co-ordinated programmes. In Chapter 6, while discussing the problems of commercial banks, we have highlighted the importance of strengthening and developing the staff concerned with rural

lending in such a manner as to meet the requirements of the changing concepts and perspectives of rural credit programmes. Efforts in this direction have to be systematic and continuous. They should include recruitment in adequate number of the right type of personnel, with the right aptitude, requisite calibre and rural bias, training them for performance for the desired goals, motivating them through incentives and penalising wherever necessary for non-performance. We have not been able to study this in any great detail within the time available to us. We therefore suggest that the ARDC/NABARD should quickly study this problem in depth and take suitable measures to provide necessary support to develop the skills of the field-level functionaries of LDBs.

Other Aspects of Diversified Lending

16.25 Generally, LDBs disburse investment credit for periods beyond 5 years. Loans for periods exceeding one year but not more than 5 years are classified as medium-term and provided by SCBs and CCBs. Also in some of the states, LDBs are statutorily franchised to advance loans only for periods exceeding five years. In the multi-agency set-up of rural finance, this rigid classification is no longer expedient. Hence, the statute should be suitably amended to enable LDBs to provide all kinds of term loans including composite loans.

16.26 The present land mortgage lending system, statutorily to be followed by LDBs, has proved to be a major stumbling block to diversified lendings, and, in particular, to the extension of investment credit to the non-land owning households. According to information available, the recommendations of the Madhava Das Committee to the effect that the insistence upon mortgage of lands for loans given by LDBs should be given up and instead they should be enabled to grant loans on the basis of a charge on the lands or other assets created by the borrower, have not been given effect to, in a number of states. The statutory provisions now obtaining in most of the states, require that the debentures floated by LDBs should be backed by mortgage of unencumbered immovable properties wholly belonging to the borrower with full alienable rights. So much so, only the landed gentry has access to LDBs' credit and the entire non-land owning class of the rural households, constituting largely the group of rural poor, is outside the LDBs' fold. The Committee, during the course of its visits, came across several instances where potential and needy borrowers could not raise adequate credit from the LDBs on account of their insistence on the mortgage of lands to cover the loans. The reluctance of some

of the state governments to liberalise security standards for facilitating lending to the rural poor, despite the RBI's /ARDC's prompting them to do so, appears to stem from their apprehension that, giving up the security of land altogether, would result in accumulation of bad debts. But, the present predicament in some states with large overdues in LDBs shows, that mortgage of land has not by itself prevented the accumulation of bad debts. In the production-oriented lending system, it is proper techno-economic appraisal of the investment that is more important than security for the loan. With the increasing accent on financing non-land based activities under diversification programme, the concept of security has necessarily to shift from 'land' to assets created/acquired out of the loan. We therefore make the following recommendations :

- (a) Land, as security, either in the form of mortgage or as charge, is relevant only in respect of loans issued for land-based purposes. Where the borrowers for such purposes are in a position to furnish land security for the amount of loan to be advanced to them, it should be obtained, the asset acquired or purchased with the aid of the loan forming collateral for the loan.
- (b) Loans for non land-based activities either to land owners or to landless beneficiaries should be secured by hypothecation of the assets created or acquired out of the loan.

LENDING PROCEDURES

16.27 The stepping-up of investment lending to the weaker sections envisaged under the rural development approach will, to a large extent, depend upon the simplification and rationalisation of the relevant systems and procedures. Apart from ensuring the availability of credit against such types of securities as the beneficiaries can readily offer, procedures which will hasten the flow of credit in adequate measure will have to be evolved. The Committee, during the course of its visits, had come across complaints of inordinate delay on the part of LDBs in the sanction of loans besides insufficiency of the quantum of credit. The system of scrutiny of loan applications and pre-sanction field inspection varied from bank to bank. Whereas in some states *e.g.*, Maharashtra, a public enquiry system* is in vogue for establishing legal title to the land offered in mortgage as security,

* Under this system, a public notice of each loan application to the bank is given and all persons having or claiming interest in the land offered as security are called upon to present their objections at a specified time and place — (*vide* section 118 of the Maharashtra Co-operative Societies Act).

in a few other states, the borrowers are required to obtain non-encumbrance certificates for a period of 12/13 years and also to produce all other documents necessary to prove their title to the lands. While in some states (*e.g.*, Tamil Nadu) the technical and financial appraisal of individual investments is required to be done by a team consisting of a technical supervisor, field supervisor of the LDB and the land valuation officer, the same is not followed in most other states. Again, the loan sanctioning powers have not been decentralised up to the primary level units *i.e.*, PLDB/branch of SLDB in some states. For eliminating undue delays arising from time-consuming procedures, one state, Orissa, has recently amended its co-operative statute with a view to enabling LDBs to grant loans against land mortgage without insisting on production of non-encumbrance certificates. Under the procedure adopted for this purpose, the intending borrower has only to make a declaration before an officer authorised by the Registrar of Co-operative Societies, solemnly affirming that the land to be mortgaged is free from encumbrances, that the mortgagor is in possession of the land and has the right to create the mortgage. In Rajasthan, the preliminaries pertaining to individual loan applications are sorted out in a camp participated by the functionaries of the lending bank and the applicants concerned. These and other procedural improvements need to be studied and suitably adopted by other states. The ARDC/NABARD should also examine such improvements for evolving appropriate guidelines in this regard.

16.28 In regard to the adequacy or otherwise of the quantum of credit dispensed by LDBs, case studies conducted by the ARDC during 1979, at our instance, in the area of Nuzvid PLDB in Krishna district of Andhra Pradesh and Devanahalli PLDB in Karnataka have revealed that the amount of loan provided by the respective LDBs to small farmers for minor irrigation programmes fell short of the actual cost of investment, necessitating their borrowing from money lenders for completion of the investment. In the case of Nuzvid PLDB, the small farmer-borrowers had to find about 20 per cent of the investment outlay on dug wells as their contribution; for other farmers, this was around 35 per cent. On composite investments like construction of wells and energisation, the small farmers' own contribution came to about 40 per cent of the investment cost. These illustrations point to the need for devising a procedural system that will allow for variations and adjustments in loan quantum depending upon investment specifications and actual outlay involved, including cost escalations on account of price rise during the period of execution of the investment programmes.

16.29 In all cases where subsidy is available to the borrowers of weaker sections, inclusive of the subsidy amount, the quantum of loan should be sufficient to cover the ultimate cost of the investment. As regards the disbursement of subsidy, we find that there is considerable delay in releasing it to the lending agency towards adjustment to the borrower's loan account. Under the practice now adopted by most of the LDBs, the subsidy element is included in the quantum of loan as a result of which the borrower has to bear the burden of interest on the subsidy portion also, until the subsidy is received by the bank and credited to his loan account. This is not in the interests of the borrower. The appropriate procedure would be that the amount of the loan should be exclusive of the quantum of subsidy and that the subsidy available to the borrowers should be released by the development agencies concerned to the lending institution sufficiently in advance of the disbursement of the loan, so that the latter could disburse it to the borrower along with the final instalment of the loan for the purpose of completing the investment. We urge upon the state governments to ensure compliance with this procedure. Further, the quantum of subsidy provided has tended to be unrealistic because of the ceiling fixed, though costs of investment have increased. We suggest that the subsidy available to the borrowers be increased suitably to take care of the increase in investment cost. A review of all these aspects of subsidies is necessary.

16.30 At present, loan repayments are scheduled by the LDBs on the basis of the repaying capacity assumed under the incremental income concept and the useful life of the asset created or acquired out of the loan. Also, for fixing loan instalments, most of the LDBs follow the equated annual instalment system, after giving the borrowers the benefit of a grace period of one or two years to take care of the gestation period of the investment. It has been pointed out that as the incremental income may not be fully realised in the first few years in all cases, it may be more convenient to fix the initial instalments somewhat lower and the later ones somewhat higher, instead of equated instalments. Varying instalments do, of course, involve a lot of accounting work and may not be favoured by LDB staff. But, the convenience of the borrower must prevail. As the gestation period of investments is a variable factor, being contingent upon the availability of the requisite infrastructural facilities and physical inputs, we suggest that the duration of the grace period should be sufficiently long to facilitate repayment out of incremental income generated. All this calls for study, on a continuous basis, by the ARDC/NABARD of the existing terms and procedures to improve them further.

MONITORING OF LONG-TERM CREDIT

16.31 In regard to monitoring of long-term credit by higher financing agencies, the Committee observes that the Reserve Bank of India and the ARDC have made arrangements in this regard. Apart from regular inspection of SLDBs and a few of their branches/affiliate PLDBs conducted by the RBI on an annual basis, the officers of the LDB Cell set up in the regional offices of Agricultural Credit Department periodically visit PLDBs/branches of SLDBs for assessing the quality of lending, effectiveness or otherwise of the post-credit monitoring, if any, done by the lending agency, etc. During these visits, they also carry out a random test check of utilisation of loans by individual borrowers. The observations made by them are followed up with the banks and the state government concerned for necessary remedial action. In addition, the Special Investigation Cell in the Central Agricultural Credit Department of the RBI also conducts, from time to time, studies on production-oriented system of lending in LDBs. In the course of these studies, on-the-spot verification of end-use of loans is also done and the findings conveyed to the concerned state government/SLDB for taking corrective steps. The ARDC too is intimately involved in the follow up of its schemes through a series of monitoring and evaluation studies. The main findings of these studies also are followed up with the implementing banks. With the growing number of schemes being sanctioned year after year, the ARDC has since proposed to switch over from scheme-oriented monitoring to District-Oriented Monitoring (DOM) of its schemes. Under this new arrangement, the geographical area will be the unit and the schemes in the various disciplines and relating to all banks would be monitored. The Committee expects that the NABARD will not only continue these monitoring arrangements but will also strengthen them further.

16.32 As regards monitoring by the lending agency itself, the supervisory staff of LDBs are presently attending to verification and certification of the utilisation of loans, contacting the borrowers for recovery etc. The field staff of SLDBs also conduct test check of the supervision work carried out by the staff of primary units. Nevertheless, these arrangements have not been quite effective as testified by the findings, summarised below, of a few case studies conducted at our instance by the ARDC.

- (i) The study of the reasons for non-drawal of the second and subsequent instalments of several ARDC-assisted loans for

construction of new wells sanctioned by the Raisen District Land Development Bank in Madhya Pradesh, (conducted in August 1979) revealed that, out of 147 borrowers in Silwani, Gairatganj and Begumganj branches of the bank, who had drawn the first instalment of the loans between April 1976 and May 1977, 26 borrowers had not availed the second and third instalments while 55 borrowers had not lifted the third instalment till the end of June 1979. The reasons were stated to be scarcity of construction inputs including labour, collapse of wells already dug due to technical flaws in construction, and lack of urgency for irrigation as the moisture retained in the rainy season was sufficient for raising subsequent seasonal crops.

- (ii) In a similar case study conducted in Devanahalli PLDB in Karnataka, (August 1979) of 90 borrowers drawn on a sampling basis from among 349 loanees spread over 30 villages, it was noticed that all the sample borrowers were yet to draw all the instalments of well loans sanctioned to them. Only 14 out of these 90 loanees had completed the wells in all respects. The reasons adduced for non-drawal of the instalments were (i) failure of well (ii) utilisation of own resources and (iii) diversion of instalments drawn for purposes other than those stated in the loan applications.

In the light of the foregoing findings, it is necessary that LDBs strengthen their own machinery for post-disbursement follow-up with adequate staff, technically trained for the job. The follow-up machinery should be in action right from the stage of disbursement of the first instalment of the loan and the supervision mechanism should *inter-alia* provide for (i) ensuring utilisation of each loan instalment within a time limit to be stipulated therefor (for each type of investment), (ii) verification of utilisation of each instalment by the grass root staff of the PLDB/branch, within a period to be specified for the purpose, and its test check by the manager of the PLDB/branch of SLDB, (iii) proper documentation of the results of verification and (iv) a percentage test check of the verification done by the PLDB/branch by Regional/Divisional/Head Office of the SLDB.

16.33 For bringing about the necessary cohesion and co-ordination in monitoring arrangements, each SLDB should have an "Evaluation and Monitoring Cell" with adequate staff so as to ensure that resources routed to the primary level units are utilised productively and mid-course corrections in the terms of loans are effected, if required. This cell should be responsible for (a) keeping regular track of the execution of the projects and their completion within the stipulated time-schedule, (b) verification of utilisation of loan instalments at specified intervals, (c) review of availability of the requisite inputs and technical services to enable the beneficiaries to complete the project according to specifications accepted for loaning, (d) ensuring that the assumed level of incremental income is derived by the beneficiaries through appropriate cropping pattern adopted by them and (e) applying corrective measures if assumptions/norms on the basis of which loans are given, have undergone a change and in cases where misuse or non-utilisation of loans are noticed.

16.34 Programme lending, to be productive, requires co-ordinated arrangements for assured supply, to the borrowers, of necessary physical inputs, as for instance, cement, electric power, transmission lines, diesel oil, etc., in the case of minor irrigation programmes, quality breed for dairy/poultry projects etc. As emphasised by us in Chapter 9, it is the responsibility of the state governments to ensure this. LDBs, on their part, should be in constant touch with the concerned departments of the state governments so that timely action is initiated to eliminate the constraints or delay, if any, in input supplies for the borrowers to execute their investment projects well on time. The DCC should be used by LDBs to co-ordinate their work with the concerned departments of the state government in this regard, as indicated in Chapter 8.

CO-ORDINATION BETWEEN PRODUCTION AND INVESTMENT CREDIT

16.35 A pre-requisite for full utilisation of investment credit is the availability, in adequate measure, of production credit to support it. The available data and information suggest that, as of now, the co-operative financing system in most of the states suffers from lack of effective co-ordination between its short-term and long-term wings; in the result, several long-term borrowers of LDBs are not in a position to obtain working capital finance for deriving optimum benefit from their investment. Some case studies conducted by the RBI in West Bengal and Andhra Pradesh for our use, have highlighted the following points:

- (i) Out of 23 cases of borrowers of investment credit from Hoogly PLDB (West Bengal) spread over Tarakeswar, Dhaniakali and Chinsurah-Magra Blocks for construction of wells, only 6 received production credit from PACS, 8 borrowed from non-institutional sources, 2 from commercial banks, 1 managed his production programme out of his son's remittance while the remaining 6, with no tangible security to offer, had no access to PACS credit and resorted to distress sale of produce to finance current production programme.
- (ii) 14 parties who borrowed for shallow tube wells did not receive production credit support for their investment credit to fructify.
- (iii) Though the LDB was required to furnish a list of borrowers to the central co-operative bank, no such list was sent after September 1978; even where the list was received from the LDB, the central co-operative bank, on its part, did not pursue the matter with the societies nor did the LDB enquire from the central co-operative bank as to the action taken to provide production credit.
- (iv) The study of cases of 20 borrowers of Jaggayyapet and Tiruvur PLDBs in Krishna district showed that, though most of the borrowers were members of PACS, only 7 of them had resorted to borrowing from the PACS; 2 borrowers were ineligible to draw short-term credit (being in default to the PACS); 8 had resources of their own; the remaining 3 preferred to borrow interest-free loans from their relatives.

16.36 A field study on the availability of short-term production credit to borrowers from LDBs, conducted in Punjab and Karnataka states during 1977-78 by the Economic Department of the RBI showed that 60 per cent of the loanees from LDBs received production credit from PACS and that the remaining 40 per cent did not get such loans mainly for want of co-ordination between these two structures.

16.37 It is, thus, obvious that there exists now a gap between the working capital needs of investment credit borrowers and their timely availability to them from the credit institutions. We consider that

even at the time of appraisal of the investments to be financed, the source of working capital needed for the investment to yield the assumed level of incremental income should be ascertained by the LDBs and, that in all cases, where the long-term borrowers require such credit, arrangements should be made to ensure its availability to them. The ARDC, we note, is providing refinance to cover production credit, wherever such credit forms an integral part of a composite development programme, as in the case of plantations, sericulture etc. We also understand that the ARDC is studying the question of refinancing ST credit needs of borrowers availing term loans for minor irrigation schemes. Several important issues arise such as raising the necessary resources, the mode of meeting the ST needs of the term loan beneficiaries in respect of lands outside the schemes and above all, the organizational capacity of LDBs. We would suggest that LDBs should invariably provide production finance along with term loans for activities such as plantations, sericulture and poultry. In cases where such composite loans are not to be given, LDBs should ensure that the concerned borrowers become members of PACS and are provided with production credit. If, as recommended earlier, PACS begin to act as agents of LDBs, this process will be greatly facilitated.

16.38 The Committee understands that a sub-committee constituted by the LDBs' Federation to go into the question of determining the extent and nature of co-ordination that should be secured between LDBs and PACS has since submitted its report (January 1980) suggesting functional co-ordination between the two agencies, on a selective basis to begin with. The LDBs' Federation may start a dialogue with the representatives of the ST co-operative credit structure and the state governments to decide upon the details of co-ordination arrangements as indicated by us in Chapter 14. Till such specific arrangements are made, co-ordination between ST and LT credit structures should be ensured by making it incumbent on all LDBs to furnish to the respective PACS in their jurisdiction, a list of borrowers who have completed their investment and also follow it up with a view to ascertaining whether the loanees have been supported by adequate production credit or not.

RECOVERY OF LOANS

16.39 Mounting overdues is a major problem confronting the LDBs in many states. In Chapter 4, we have indicated the magnitude of

overdues in LDBs in different states. The overdues, it is observed, are primarily caused by bad programming of investments, faulty loan appraisals, slackness in post-disbursement follow-up and supervision, lack of sufficient internal control over accounts, inadequacy of staff for recovery work and above all, wilful default on the part of the borrowers. Added to these are factors like natural calamities, lack of co-operation and assistance from the state governments in creating a proper recovery climate, political tendencies to render the recovery machinery ineffective at the time of elections to state legislatures, local bodies, etc. Poor recoveries have resulted not only in the inability of some of the SLDBs in meeting their sinking fund commitments, but also in curtailing the eligibility of many primary level units to undertake lending to the extent programmed. The high level of overdues, if unchecked, may eventually destabilise the entire long-term credit structure. This calls for sustained, earnest and serious efforts in planning and executing the recovery drive in a concerted manner. Apart from strengthening the machinery for effective post-credit follow-up, the SLDBs should set up a "Recovery Cell", manned by adequate staff to programme and monitor the recovery operations. For hastening the recovery process, we visualise other steps such as :

- (i) Purchase by the state government of mortgaged lands brought to sale in recovery proceedings launched against defaulters, as suggested earlier.
- (ii) Adoption by the state governments of a policy of positive assistance to the banks in recovery work, by taking such steps as are necessary to ensure that the recovery staff of LDBs and departmental staff attending to execution of decrees against defaulters are able to draw wherever and whenever required, the assistance of revenue/police officials of the government.
- (iii) Active involvement of non-official office bearers of LDBs in recovery work.

16.40 The various steps in the preceding paragraphs for improving the long-term co-operative credit structure will be of no avail, if the managements of LDBs themselves are not alive to their responsibilities and indulge in irregular sanction of loans, neglect recoveries and show slackness in control over staff. Wherever such delinquent

management is noticed, it should be sternly dealt with by the state governments in accordance with the co-operative statute and necessary steps taken to tone up the management of the banks concerned.

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Bombay, January 30, 1981.
