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Evolution of agriculture finance in India: a historical perspective

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Abstract

Purpose – Lack of access to finance is one of the major contributing to low profitability in agriculture. Various policy interventions were performed for promoting access to finance. However, access to finance always remained one of the biggest challenges to Indian policymakers. The purpose of this paper is to explore the policy interventions in the areas of agriculture finance.

Design/methodology/approach – This paper makes an attempt to explore the relation of earlier policy initiatives with the current microfinance industry as well. The data for the paper are collected from Reserve Bank of India Archive Museum at Pune. This Museum is having huge collection of archives of policy documents of the Indian financial sector and is one of its kinds in India.

Findings – The study concludes that many of the interventions of today were earlier experimented or proposed in the past but, due to some or the other reason those, interventions were not successful. The study concludes that if those interventions had been implemented that time, it would have taken India in one of the tops in the list of financial inclusion.

Originality/value – This paper is a unique in its feature as it has tried to link the evolution of agriculture finance and the microfinance industry of India as microfinance is an integral part of agricultural finance in India.

Keywords Microfinance, History, Agriculture finance

Paper type General review

Introduction

Agriculture is the backbone of the Indian economy. In total, 70 percent of Indians depend on agriculture for their livelihood. Indian agriculture is predominantly rain-fed and therefore unable to provide sustainable income generation around the year. Agriculture accounts for 14 percent of India's gross domestic product (GDP). Agriculture and allied sectors contributed USD244.74 billion to GDP in FY 16. According to the advanced estimates of the Ministry of Statistics and Programme Implementation, Government of India (GOI), agriculture and allied sectors recorded a CAGR of 6.64 percent in 2007-2016. Further, the share of agriculture and allied sectors (including livestock, forestry, and fishery) is expected to be 17 percent of the gross value added (GVA) in 2016-2017 at 2011-2012 prices (India Brand Equity Foundation (IBEF), 2017). As compared to overall GDP, the growth of agriculture GDP has been low. Data from the Ministry of Agriculture and Farmers Welfare, GOI shows that there has been a continuous decline in the share of agriculture and allied sectors in the GVA, from 18.2 percent in 2012-2013 to 17 percent in 2015-2016 at current prices (Annual Report, Ministry of Agriculture, 2016-2017). The income of farmers and others in agriculture and allied sectors can be raised only if the rate of growth of agriculture GDP is increased. In addition, there is wide variation in the performance of different states in terms of growth of agriculture. Hence, any economic analysis should also consider the equally important factor of regional variation.

Hence, the key question is: despite being a major livelihood source for more than 70 percent of Indians, why has the share of agriculture in total GDP been declining? The answer is fairly complex because agriculture in India faces many problems. Fragmented landholdings, dependency on monsoon, lack of irrigation, inadequate infrastructure, and

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poor market linkages are some of the factors that result in low agricultural productivity and hence low profitability. The only way to increase the contribution of agriculture in GDP is to increase profitability of agriculture. Among the various factors contributing to low profitability of agriculture, the foremost is lack of access to credit. Improving and extending agriculture financing remains an important challenge and top priority for Indian policymakers.

To raise productivity, farming in the post-green revolution period has become increasingly input oriented, with farmers adopting various forms of agricultural inputs. Farmers need credit for purchasing agricultural inputs, although the long-term impact of this practice is a debatable issue. The timely application of these inputs is an important factor in determining the profitability of crops. In this context, availability of timely, adequate, and affordable credit for farming practices is crucial. Various studies have shown that access to finance plays an important role in the profitability of agriculture. Profitable agriculture leads to sustainable agriculture.

In recognition of the importance of enhanced and convenient access to finance in agriculture, various policies and programs have been formulated to support agriculture financing. Microfinance has emerged as a response to the failure of the government as well as the market to provide access to financing to farmers. This is important because inclusive growth has been the prime developmental agenda for developing countries like India. Recent initiatives like the Pradhan Mantri Jan Dhan Yojana (PMJDY) (launched on August 28, 2014) and the Pradhan Mantri Mudra Yojana (PMMY) (launched on April 8, 2015) indicate the priorities of policymakers regarding inclusive growth. A recent report released in 2015 on the status of financial inclusion in India conducted by Intermedia, a global research consultancy, estimates that 43 percent of those who work primarily in the agricultural sector do not have access to a bank account. The survey also reveals wide disparity between farmers and farm workers: 36 percent of farmers *vis-à-vis* 55 percent of farm workers do not have a registered bank account (Reserve Bank of India (RBI), 2015). The preliminary findings on the impact of the PMJDY reveal that many farmers and farm workers opened accounts as zero balance accounts, and hence the survey questioned the use of bank accounts rather than the provision of improved access as a criterion for measuring financial inclusion. Institutional credit to the agricultural sector increased at a CAGR of 12.8 percent during 2007-2014 (IBEF, 2017). Even after 70 years of independence, the goal of financial inclusion remains a distant dream. The history of the evolution of agriculture finance offers many useful insights in understanding the current policies of agriculture finance in India.

Objectives of the study

This paper traces the history of agricultural finance, analyses the problems of agricultural finance, and explores the role of microfinance institutions (MFIs) in providing finance for agricultural practices in India. It also examines the impact of previous policies on the current financial inclusion policy of India. The objectives of the study are:

- to explore the policy interventions for promoting agriculture finance in India; and
- to analyze the impact of past policy interventions on the current policy interventions for financial inclusion in the country.

Methodology

This paper is based on a review of the secondary literature. Data for this paper were collected from the RBI Archives Museum in Pune, Maharashtra. The Reserve Bank of India Archives, located in Pune, and earlier known as the Central Records and

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Documentation Centre, was established on August 24, 1981 with the twin objectives of serving as a repository of non-current permanent records and as a central archives of the Reserve Bank of India for research purposes. The museum has 24,842 files, covering various policy documents of the RBI. Additionally, this paper relies on various secondary sources like research papers, articles, news reports, etc. for information on agricultural finance policies in India.

History of agricultural finance in India

The history of agricultural finance can be broken into two phases, that is, pre-independence and post-independence.

Pre-independence

The development of agricultural finance in the pre-independence period can be further grouped into three categories.

Background of the Cooperative Credit Societies Act, 1904. The origin of agricultural finance can be traced to the seventeenth century when the need for banking systems to provide credit facilities was recognized, and various attempts were made to establish a banking system in India.

Evolution of banks. According to a report on the history of the Reserve Bank of India (RBI) (1970), the earliest reference to an attempt to set up a bank in India dates to January 1773 when Warren Hastings, Governor (later Governor-General) of Bengal, proposed establishing a general bank in Bengal and Bahar (now known as Bihar). The plan for the proposed bank was approved and the bank was set up in April 1773. However, this experiment did not last long, and a resolution was passed on February 15, 1775 for the closure of the bank. Nevertheless, even during the short period of its existence, it is reported that the bank made a considerable profit (RBI, 1970). The report by the RBI (1970) further states that the next attempt to establish a central bank was made in 1807-2008, by Mr Robert Rickards, a member of the Bombay Government, to form a general bank, jointly owned by the public and the government. In 1806, the first Presidency Bank was established as the Bank of Calcutta, with an initial capital of Sicca Rs 50 lakh, of which one-fifth was taken up by the government. In 1836, another proposal for a "Great Banking Establishment for British India" was submitted to the Court of Directors of the East India Company by a body of merchants in England having trade relations with India. The proposal was not accepted because of the unfavorable opinion of the Bank of Bengal, to whom it was referred to for comments. Two banks were set up, namely the Bank of Bombay in 1840 with a capital of Rs 52 lakh, and the Bank of Madras in 1840, with a capital of Rs 30 lakh. In 1884, a suggestion was made for the setting up of a "central bank of issue" on the model of the Netherlands Bank, but it was not pursued on the ground that "India possessed a sound banking and currency system."

Foreign banks. Meanwhile, some foreign banks were also established in India. Karunagaran (2006) noted that simultaneously some foreign banks were also being set up in India, including the Bank of India in 1836 and the Bank of Asia in 1840. The first Anglo Indian commercial bank with the name Bank of Western India was established in 1842. After three year, this was followed by the opening of the Chartered Bank of India, Australia and China and the Chartered Bank of Asia in 1853 (Khandelwal, 1965). Nevertheless, despite the existence of several foreign banks, agricultural finance was always a neglected sector. According to a report by the RBI, there was no evidence of these foreign banks financing agriculture and rural activities. Even the Indian joint stock banks played a negligible role in providing agricultural finance (RBI, 1970). As a result, various reports concluded that toward the end of the nineteenth century, Indian peasants were under the pathetic grip of

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debt (Bowen, 1953). India's predominantly agriculture-based economy was vulnerable because of the pathetic conditions of Indian farmers.

Evolution of cooperatives. Before 1900, agriculture was the predominant source of livelihood in India. Factory industry did not exist in India before 1850 (Saini, 1969). Two major crops, that is, cotton and jute, are cultivated extensively in India, and as a result, between 1850 and 1860, two factory industries, cotton and jute, were established. During this period, two major (cotton and jute) and two minor industries (paper and wool) existed in India. For the entire half-century that followed, these two industries remained the major components of the industrial sector of the Indian economy.

Simultaneously, recurrent famines affected Indian agriculture. In the 1860s, various parts of India faced devastating famines, forcing farmers to pay exorbitant interest rates and leading to disastrous consequences like agrarian riots and rural distress (Table I). In 1875, the GOI appointed a committee on riots on whose recommendation the Dekkhan Agriculturists' Relief Act of 1879 was passed. This is considered one of the earliest legislative measures dealing with agriculture credit and indebtedness.

Various committees were formed to look into this matter (Dantwala, 1952). The first in the series was the Col. Baird Committee in the year 1860-1861. Unfortunately, this committee did not put forward any significant recommendation. Later, the George Campbell Commission was formed in the year 1866 to investigate the causes of famine and to recommend measures to prevent recurrences in the future. The committee held the government system responsible for agrarian distress and recommended that the government should organize relief measures during famines.

The Deccan Riots Commission of 1875 reported that one-third of occupants of government lands was under debt. The Famine Commission of 1880 reported that one-third of the landholders in the country was in deep debt and another one-third was also in debt, but was in a position to redeem their debts. On the recommendations of the Famine Commission of 1880, two important laws were enacted. These were the Land Improvement Loans Act of 1883 (long-term loans) and the Agriculturists' Loans Act of 1884 (short-term needs). The objective of these laws was to issue loans to agriculturists. However, one of the lacunae was that under the provisions of these Acts, loans were granted for some specified purposes only (RBI Archives, File No. F7680, pp. 14-15). Nevertheless, these steps were significant because this was the first time that any legislation was passed under which the government assumed responsibility for providing a part of the credit needs of farmers (Dantwala, 1952). Despite the formulation and implementation of the famine policy, India repeatedly faced famines. A severe famine occurred in 1896-1897, and another famine occurred in 1899-1900.

The Government of Lord Curzon appointed the Anthony McDonald Committee in 1900 to suggest measures to counter the famine effectively. The Famine Commission of 1901 estimated that more than 80 percent of the cultivators were under debt (Jain and Singh, 2014). Nicholson, a British Officer in India, suggested introducing the Raiffeisen model of German agricultural credit cooperatives in India (Das *et al.*, 2006). Raiffeisen was the pioneer in developing the

Year	Name of Famine	Area
1769-1770	Great Bengal Famine	Bihar, Northern and Central Bengal
1783- 1784	Chalisa Famine	Delhi, Western Oudh, Eastern Punjab region, Rajputana and Kashmir
1791-1792	Doji Bara Famine	Hyderabad, Southern Maratha Colony, Deccan, Gujarat and Marwar
1876-1878	Great Famine	Madras and Bombay
1943-1944	Bengal Famine	Bengal

Source: https://atulkulkarni123.wordpress.com/2015/07/26/famine-policies-and-factory-acts/

Table I. Famous famines of India

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concept of cooperative, self-help and rural credit unions. Based on the recommendation of this committee, the first major initiative in the agricultural finance sector was taken, and the Cooperative Credit Societies Act was passed in 1904. The objective of this Act was to deal with the issue of farmer indebtedness by providing access to credit. Initially, cooperative societies were formed only for credit.

Timeline of milestones in agriculture finance:

(1) 1890-1901:
- Famine Commission; and
- Rural Agricultural Banks through the establishment of Mutual Credit Associations.

(2) 1904:
- Cooperative Credit Societies Act, 1904 – the first incorporation; and
- provision for rules and regulation.

(3) 1912:
- Cooperative Societies Act, 1912 (recognition to credit societies); and
- inclusion on non-credit societies.

(4) 1914:
- Maclagan Committee on Cooperation: building up a strong three-tier structure in every province with primaries at the base, the Central Cooperative Banks at the middle tier and the Provincial Cooperative Bank at the apex, basically to provide short-term and medium-term finance.

(5) 1919:
- Reforms Act: cooperation as a subject was transferred to the provinces. The Bombay Cooperative Societies Act of 1925, the first provincial Act to be passed, among others, introduced the principle of one-man-one-vote.

(6) 1928:
- Royal Commission on Agriculture in 1928 also reviewed the cooperative sector and among others recommended the setting up of land mortgage banks.

(7) 1929:
- all India Association of Cooperative Institutes.

(8) 1934:
- Reserve Bank of India (RBI).

(9) 1935:
- Sir Malcolm Darling submitted a report on cooperative credit to GOI. Sec. 54 – RBI to set up an ACD – expert staff advise central and state governments, state coop banks, coordinate RBI functions for agricultural credit; and
- April 1, 1935: ACD was set up.

(10) 1937:
- Mehta Committee: reorganization of cooperative credit societies as multi-purpose cooperatives.

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(11) 1942:

- Multi-Unit Cooperative Societies Act: delegated the power of the Central Registrar of Cooperatives to the State Registrars for all practical purposes.

(12) 1945:

- Cooperative Planning Committee: cooperative societies are a most suitable medium for the democratization of economic planning and examined each area of economic development.

(13) 1946:

- milk producers of Khera District of Gujarat went on a fifteen-day strike. Their refusal to supply milk forced the Bombay Government to withdraw its order granting monopoly procurement rights to Polson, a private dairy. History was made when two Primary Village Milk Producer Societies were registered in 1946.

(14) 1949:

- nationalization of RBI.

(15) 1950:

- postal saving bank, rural savings deposit talked about post office.

(16) 1951:

- all India Rural Credit Survey Committee (1951);
- cooperatives did not cover large parts of the country, and in such areas where it had been covered, a large segment of the agricultural population remained outside its membership. Even where membership did exist, the bulk of the credit requirement (75.2 percent) was met from other sources; and
- creation of SBI.

(17) 1952:

- land mortgage banks as agency for long-term finance.

(18) 1955:

- for financing of small-scale industries in 1955. Rules were formed. There was a grant provision of Rs 1,500. In total, 25 percent of this grant was a subsidy, and 75 percent was considered as loans at 4.5 percent interest rate. There was a provision of Rs 2,000 as a grant for artisans out of which Rs 1,000 was considered for working capital.

(19) 1962:

- ARC; and
- provision of medium-term loan.

(20) 1965:

- The Mirdha Committee: laid down standards to determine the genuineness of cooperative societies and suggest measures weed out non-genuine societies; to review the existing cooperative laws and practices to eliminate vested interest. The recommendations of the Committee resulted in amendments to the cooperative legislation in most states, which destroyed the autonomous and democratic character of cooperatives.

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(21) 1966:
- cooperative banks came under RBI regulation; and
- overdraft facility.

(22) 1969:
- Nationalization of Banks; and
- Lead Bank Schemes.

(23) 1974:
- introduction of priority sector lending.

(24) 1975:
- establishment of RRBs.

(25) 1980:
- six more banks were nationalized.

(26) 1981:
- NABARD Act: to provide refinance support to Cooperative Banks and to supplement the resources of Commercial Banks and RRBs to enhance credit flow to the agriculture and rural sector.

(27) 1982:
- Multi-State Cooperative Societies Act; and
- comprehensive central legislation to facilitate the organization and functioning of genuine multi-state societies and to bring uniformity in their administration and management.

(28) 1984:
- Multi-State Cooperative Societies Act, 2002.

(29) 1995:
- RIDF was launched.

(30) 1998:
- Kisan Credit Card introduced.

(31) 1999:
- SGSY scheme launched.

(32) 2011:
- recapitalization of RRBs.

(33) 2014:
- Prime Minister Jan Dhan Yojana.

(34) 2015:
- MUDRA bank.

Similar land alienation acts were passed in Punjab, the United Provinces, and Central Provinces and Berar (Chandavarkar, 1983). Some states found it necessary to promote

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legislation for advancing loans for other purposes too. For example, the Bihar and Orissa Natural Calamities Loans Act, 1934, the Madras Land Improvement and Agriculturist Loans Rules, 1933, and the Bombay Land Improvement Act included various agricultural purposes as eligible purposes for getting loans (RBI Archives, File No. F7680, pp. 14-15).

This phase was also important in preparing the ground for the Cooperative Societies Act, 1904. Historically, credit cooperatives societies have played an important role in providing access to credit to farmers not only in India but also in many other countries. Cooperative societies are based on the principles of cooperation, that is, voluntary membership, mutual help, democratic decision-making, sharing of profit and loss, etc. Turvey (2017) noted that impelled by a famine in 1846-1847, the first cooperative loan bank was opened in 1849 in Germany. India also faced similar socio-economic conditions and grappled with several famines in the late eighteenth century. The origins of the urban cooperative banking movement in India can be traced to the close of the nineteenth century, when inspired by the success of experiments in the cooperative movement in Britain and the cooperative credit movement in Germany, such societies were set up in India.

The first known mutual aid society in India was probably the Anyonya Sahakari Mandali, organized in Baroda in 1889 under the guidance of Vithal Laxman, also known as Bhausaheb Kavthekar. Urban cooperative credit societies, in their formative phase, came to be organized on a community basis to meet the consumption-oriented credit needs of their members. Another type of cooperative society, the salary earners' society, became popular. The objective of this society was to inculcate habits of saving and self-help. This also played a significant role in popularizing the cooperative movement, especially among the middle class as well as organized labor. From its origins until today, the thrust of UCBs historically has been to mobilize savings from the middle- and low-income urban groups and to purvey credit to their members, many of whom belonged to the weaker sections (https://rbi.org.in/history/Brief_Fun_UrbanCoopBanks.html). Saving was recognized as one of the important components of the banking system, and government savings banks were established between 1833 and 1870 in selected districts. Later, in 1882-1883, saving banks were opened at post offices throughout the country.

1904-1934: establishment of the Reserve Bank of India. The adoption of the Cooperative Credit Societies Act, 1904 gave a real push to the movement. The first urban cooperative credit society was registered in Canjeevaram (Kanjivaram) in the erstwhile Madras province in October 1904. In Bombay Presidency, amongst the prominent credit societies were the Pioneer Urban in Bombay (November 11, 1905); the Number 1 Military Accounts Mutual Help Co-operative Credit Society in Poona (January 9, 1906); Cosmos in Poona (January 18, 1906); Gokak Urban (February 15, 1906) and Belgaum Pioneer (February 23, 1906) in Belgaum district; and the Kanakavli-Math Co-operative Credit Society and the Varavade Weavers' Urban Credit Society (March 13, 1906) in South Ratnagiri (now Sindhudurg) district. The most prominent amongst the early credit societies was the Bombay Urban Co-operative Credit Society, sponsored by Vithaldas Thackersey and Lallubhai Samaldas, and established on January 23, 1906 (https://rbi.org.in/history/Brief_Fun_UrbanCoopBanks.html). In Punjab, the first agricultural credit society in Firozpur district was registered on October 4, 1911, in Khalchi Kadim village.

The Cooperative Credit Societies Act, 1904 was revised in 1912, and other services were also included under its ambit. In 1914, the Maclagan Committee on Cooperation suggested the building up of a three-tier structure for strengthening cooperatives. The Usurious Loans Act, 1918 upheld the *damdupat* principle, which states that interest should never exceed the principal of the debt. The Act prohibited the compounding of the interest rate. The maximum interest rate allowed for a secured loan was 12.5 percent, and that for an unsecured loan was 18.75 percent. It also stated that 24 percent was the maximum interest

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rate allowed under any act (RBI Archives, File No. 7786, pp. 7-8). Further, the Bombay Co-operative Societies Act, 1925 introduced the principle of "one man, one vote."

Various efforts were made to improve the status of Indian farmers and to provide them with access to credit, but all the committees and reports were of the same opinion – that the situation of Indian farmers had not improved to any great extent. While documenting the condition of Indian farmers, Sir Malcolm Darling (1925) in his book *The Punjab Peasant in Prosperity and Debt* stated that "the Indian peasant is born in debt, lives in debt and dies in debt."

In 1921, the Imperial Bank of India was created through the amalgamation of the three Presidency Banks, which performed a few central banking functions, although it primarily remained a commercial bank. This phase was also characterized by the domination of moneylenders in agricultural finance. Several committees were formed during this period to analyze the condition of agricultural finance and to suggest ways of remedying the situation. In this regard, the most important were the Central Banking Enquiry Committee (1929) report and the associated provincial reports, of which the Madras Provincial Banking Enquiry Committee (1929-1930) report is regarded as a classic in this area (Shah *et al.*, 2007).

In 1928, the Royal Commission on Agriculture in India examined the situation of agricultural credit in India. The commission in its report observed that "if cooperation fails, there will fail the best hope of rural India" (cf. Roy, 2002, p. 154). A study published in 1952 by a leading economist reported that the Central Banking Enquiry Committee had estimated rural indebtedness in 1929 at Rs 9,000 million. A decade later, in 1939, the RBI reported that the figure had doubled. This was a clear indication that cooperatives had not been able to achieve the goals set out for them. Catanach (1970) argued that cooperatives only served as an addition to the dealings of the rural moneylender, and not as an alternative source of credit for Indian farmers as originally envisaged by policymakers.

Based on the findings of these commissions, the Punjab Regulation of Accounts Act, 1930 and the Punjab Debtors' Protection Act, 1936 mandated the licensing and registration of moneylenders and the proper recording of transactions and accounts, respectively. However, these acts could not help debtors much as they were hesitant to bring moneylenders to court because of the fear of losing their sole source of credit in times of need (Chandavarkar, 1983).

The conditions of cooperatives in India also prompted the proposal for the establishment of a central bank. The Report of the Indian Finance and Currency Royal (Chamberlain) Commission in 1913-1914 also raised the issue of the founding of a central bank in the country. Taking this idea further, Professor J.M. Keynes prepared the first comprehensive plan for an Indian central bank. Keynes' plan, however, did not come into effect, owing to the outbreak of the First World War. The Imperial Bank continued to function primarily as a commercial bank and served as a banker to the government and as a banker's bank until the establishment of the Reserve Bank of India (1935) and Chand (2016). A bill to this effect was introduced in the Indian Legislative Assembly on September 8, 1933. The bill was passed and received the assent of the Governor-General on March 6, 1934, and became the Reserve Bank of India Act, 1934. The Reserve Bank of India was constituted under the act, and it commenced operations on April 1, 1935.

The RBI report on the history and evolution of the RBI states that the Reserve Bank of India was set up on the recommendation of the Royal Commission on Indian Currency and Finance, also known as the Hilton Young Commission; it was appointed on August 25, 1925, and published its report on August 4, 1926. Originally, the Reserve Bank was constituted as a shareholders' bank, based on the model of the leading foreign central banks of those days. The bank's fully paid-up share capital was Rs 5 crore divided into shares of Rs 100 each.

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Of this, Rs 49,780,000 were subscribed by private shareholders and Rs 220,000 were subscribed by the Central Government for disposal of 2,200 shares at par to the Directors of the Bank (including members of the Local Boards) seeking the minimum share qualification (RBI, 1970). The share certificates of the RBI are preserved at the RBI Archives Museum at the College of Agricultural Banking in Pune.

1935-1947: consolidation and expansion of the RBI. Just after the setting up of the RBI, one of the key focus areas was on financing agriculture. In 1935, Sir Malcolm Darling, was a member of the Indian Civil Service who was appointed Assistant Commissioner of the Punjab of British India, in 1904, submitted a report on cooperative credit to the GOI. The report recommended the setting up of an Agricultural Credit Department (ACD) to advise central and state governments as well as state cooperative banks and to coordinate RBI functions for the extension of agricultural credit. The ACD was set up in the RBI on April 1, 1935.

The activities of ACD were classified as (RBI Archives, File No. 7903, pp. 4-5):

(1) Planning and reorganization: preparing proposals, land reforms, small-scale industries (SSI) finance.

(2) Finance and inspection: provision of finance to provincial cooperative banks, remittance transfer facilities.

(3) Training and publication: conducting studies on problems of rural indebtedness.

A 1937-1938 report on the position of moneylenders by the All India Income Tax report and returns stated: "The business of money lending is not now as profitable as it is popularly assumed to be as special legislation is removing its unhealthy features. Reviewing the India position as a whole, it is not possible to say that the cooperative movement has yet succeeded in serving the reasonable demands of small credit adequately" (RBI Archives, File No. AC 85, p. 6). Nevertheless, realizing the need for a close integration of the monetary and credit policies of the bank and the macroeconomic policies of the government, the notion of state ownership of the bank was raised and was justified from time to time.

Post-independence

The post-independence phase of the development of agricultural finance in India can be classified into two broad periods, that is, pre-liberalization and post-liberalization.

Pre-liberalization. After independence, the GOI decided to nationalize the RBI. Under the Reserve Bank (Transfer to Public Ownership) Act, 1948, the GOI took over the RBI from private shareholders by paying adequate compensation to them. On January 1, 1949, the RBI began functioning as a state-owned central banking institution. The Banking Companies Act, 1949 was aimed at regulating banking companies in India. It gave the RBI the power to license banks; to regulate the shareholding and voting rights of shareholders; to supervise the appointment of board members and the management; to regulate the operations of banks; to lay down instructions for audits; to control moratorium, mergers, and liquidation; to issue directives in the interests of the public good and on banking policy; and to impose penalties. In 1965, the act was amended and cooperative banks were also brought into its ambit.

In 1950, the Rural Banking Enquiry Committee reported that India had only 16 banking offices per million of population as compared to 450 in Australia, 256 in the UK, and 129 in the USA. It added that these branches were mostly located in urban areas (RBI Archives, File No. 7804, p. 1). These data indicated the status of credit delivery in rural areas. This was a matter of concern for policymakers. Hence, a committee on the reorganization of cooperative credit was formed in 1951. The Land Mortgage Bank was established as an agency for providing long-term finance in 1952 (RBI Archives, File No. 8066, p. 87). In 1954,

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an all India survey on rural credit was carried out, which confirmed that formal credit institutions provided less than 9 percent of rural credit needs in India. This finding again highlighted the need for an increased focus on rural credit, and this led to the formation of the State Bank of India (SBI). The Imperial Bank of India was converted into a state-owned institution, that is, the SBI, on July 1, 1955. One of the immediate objectives was to establish additional branches, particularly at district headquarters. SBI was also expected to provide remittances and other facilities to cooperative and other banks and to mobilize rural savings. In 1955, for the first time in the history of rural and agricultural finance in India, financing of small-scale industries was discussed and rules were drawn up in this regard. There was a grant provision of Rs 1,500; 25 percent of this grant was a subsidy, and 75 percent was considered loans at an interest rate of 4.5 percent. There was a provision of Rs 2,000 as a grant for artisans out of which Rs 1,000 was considered as working capital.

A 1959 report on the role of the central bank in extending rural credit and cooperation noted that in a memorandum submitted to the Planning Commission in 1954 by Mr Chester Davis, it was stated that "The reserve bank has been giving new life and important leadership to the cooperative credit movement in recent years. Probably no other central bank in the world is doing as much to help, develop and finance cooperative rural credit institutions." The Cooperative Planning Committee (1946) popularly known as Saraiya Committee. The Committee on Cooperative processing headed by R.G. Saraiya in 1959 stated, "A vicious circle has been created. Banks cannot provide adequate finance because of dangers involved in agricultural finance, and the farmer cannot put forth his best effort because of lack of adequate finance. The vicious circle has to be broken at some points" (RBI Archives, File No. AC 85, p. 6). It was realized that it was becoming difficult to procure resources for financing cooperatives. In May 1960, a committee on cooperative credit recommended a systematic program for the revitalization of primary agricultural societies. Provision of the medium-term loan was added in 1962. The Credit Guarantee scheme for SSI was also launched in 1960.

In 1963, the Agricultural Refinance Corporation (ARC) was set up to provide refinance to central land mortgage banks, state cooperative banks, and scheduled commercial banks that were their shareholders. In 1964, the concept of financial literacy in the context of financial inclusion was discussed. In an article published in *The Hindu* on March 29, 1962 it was mentioned notes that there is an urgent need to promote agricultural financial literacy through pamphlets and visual aids. On February 1, 1964, the RBI was empowered to regulate the deposit acceptance activities of non-banking institutions. In 1966, a separate Department of Non-Banking Companies was established at the RBI, Calcutta. This law has been a restricting law for the current MFIs in India as it restricts NBFCs to mobilize savings. One year later, in 1967, another important decision was taken, that is, to bring the operations of the cooperative banking system under the regulatory ambit of the RBI under the country's banking laws.

In 1965, the Mirdha Committee on Cooperatives laid down the standards for determining the genuineness of cooperative societies and suggested measures to weed out non-genuine societies. In 1966, the operations of cooperative societies were brought under the RBI guidelines. Various committees were formed to examine the credit situation in India, but the findings suggested that despite various efforts to support agriculture financing, Indian farmers continued to be dependent on moneylenders for credit. The GOI undertook several efforts to support, extend, and improve agricultural finance, including the establishment of the SBI, the creation of the ARC, the nationalization of banks, the introduction of the Lead Bank Scheme, and the adoption of the service area approach. In December 1969, the Lead Bank Scheme was introduced, which envisioned a service area approach to banking to meet the credit gaps in the economy. In February 1970, the Agricultural Credit Board was set up

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to formulate and review policies in the area of rural credit. On January 14, 1971, the Export Credit Guarantee Corporation of India Ltd was established. The objective of this corporation was to facilitate credit to the priority sectors. On March 25, 1972, the Differential Rate of Interest (DRI) Scheme was introduced, which envisaged concessional interest rates on advances made by public sector banks to selected low-income groups. The proposed interest rate under this scheme was 4 percent.

It was noted that all these efforts were the result of a hit-and-miss, or trial and error, approach. None of the initiatives was able to deal effectively with the issue of access to agricultural finance for farmers. The inadequacy of rural credit remained a concern for policymakers even in the 1950s and 1960s. In the post-green revolution period, the need for rural credit increased further. Realizing the importance of providing enhanced access to credit and the failure of other initiatives in this regard, specialized institutions like Regional Rural Banks (RRBs) were set up in 1975. Unfortunately, they did not have the desired impact. On November 16, 1975, the ARC was renamed the Agricultural Refinance and Development Corporation, and the scope of its activities was widened. In 1976, the Village Adoption Scheme for banks was introduced. In 1978, the Integrated Rural Development Programme (IRDP) was launched. Until the introduction of IRDP, the major approach of the government had been subsidy driven. IRDP received lot of criticism by scholars and experts. Kurian (1987) described the program as a mixed bag. Rath (1985) argued that the effort to give cattle and other assets to farmer had yielded very limited results.

A huge amount was spent under IRDP, but it also could not achieve the desired objective of providing access to credit to farmers. Criticizing IRDP, Hirway (1988) noted that "IRDP is 'target oriented,' 'family oriented,' 'expenditure oriented,' but not 'result oriented' " (p. A90). Finally, in 1982, the National Bank for Agriculture and Rural Development (NABARD) was established as the apex institution to facilitate credit for agriculture. Until this time, the issue of credit access was mostly discussed in terms of its requirement in rural areas. Urban areas were largely neglected in this regard. It was only in 1984 that the focus shifted to urban areas and the Urban Banks Department was formed to supervise the affairs of urban cooperative banks. In 1989, the service area approach for rural lending became operational.

India has systematically pursued a supply led approach to increase agricultural credit, with the objectives of replacing moneylenders, relieving farmers of indebtedness, and achieving higher levels of agricultural credit, investment, and agricultural output. The report by Bell (1990) described India's success in replacing moneylenders as outstanding. The share of moneylenders dropped from 80 percent in 1951 to 36 percent in 1971 and to 16 percent in 1981 (Bell, 1990) A study by Binswanger and Khandker (1995) noted that expanded rural finance has led to less output and employment in agriculture than in the non-farm sector.

Post-liberalization. The year 1991 marked a major shift in the economic policy when the GOI opted for liberalization. Consequently, guidelines for the establishment of private sector banks were issued in 1993. In 1994, the lending rates of commercial banks were deregulated and the banks were mandated to declare their prime lending rates. This new policy approach was aimed at fostering greater competition in the banking sector to provide increased access to financial services. Kisan Credit Cards were introduced in 1998. In the year 2001, the RBI issued guidelines for internet banking. The Multi-state Cooperative Societies Act was passed in 2002. More recently, two major interventions, that is, Mudra Bank the PMMY and the PMJDY, were launched in 2015 and 2014, respectively. It is reported that in the 20 years following bank nationalization, the share of "exploitative" sources (professional moneylenders, landlords, and agriculturist moneylenders) in rural credit fell from an average of over 75 percent in 1951-1961 to less than 25 percent in 1991. On a positive note, the share of formal-sector lending more than doubled between 1971 and 1991 (Shah *et al.*, 2007).

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Infrastructural development was another important focus area of the government to facilitate and extend the benefits of liberalization. In 1995-1996, the Rural Infrastructure Development Fund (RIDF) was launched with an initial corpus of Rs 2,000 crore (data collected at the RBI Archives Museum, Pune). It is reported that the GOI allocated Rs 25,000 crore in 2017-2018 under RIDF (XXIII). In this post-liberalization phase, the interest rates for RRBs and cooperatives were also deregulated.

Meanwhile, questions were raised about the performance of RRBs because they had low Capital to Risk (Weighted) Assets Ratio (CRAR). A committee examined the financials of RRBs in 2009 and suggested recapitalization of these banks. As a result, the GOI has approved the recapitalization of RRBs to improve their CRAR in 2011 and was valid upto 2014. Later, it was extended for three more years. Currently, RRBs are going through a process of amalgamation and consolidation.

In 2007, the interest subvention scheme for farmers aimed at providing short-term credit to farmers at subsidized interest rates was launched. The policy came into force with effect from the Kharif season in 2006-2007. Farmers receive short-term credit at 7 percent, with an upper limit of Rs 3 lakh on the principal amount (Ministry of Finance, Government of India, 2011).

Microfinance and agricultural financing

Despite several efforts by policymakers to promote institutional agricultural finance, access to finance has remained a major constraint for Indian farmers. The growth of microfinance in India has been in response to the failure of institutional initiatives pertaining to rural credit and the attendant exploitation of farmers that is characteristic of an informal system of credit. Microfinance is the supply of financial services, that is, loans, savings, and other financial services that are tailored to the demands and needs of microenterprises. Problems associated with both formal and informal sources of finance persisted. Microfinance evolved as a semi-formal institution. The model was developed keeping the problems of formal and informal sources of credit in mind. As against the subsidy-driven model of agricultural finance in the pre-liberalization period, microfinance is a self-sustainable model. The drying up of sources of foreign funding in the post-liberalization period forced these development organizations to become self-sustainable in terms of financial resources. There was a shift in approach in the area of agriculture financing, that is, from the poverty-lending approach to the financial system approach.

Microfinance by non-government organizations (NGOs) in India was pioneered in 1972 when the Self Employed Women's Association (SEWA) was established by Ela Bhatt in Ahmedabad (https://web.archive.org/web/20140903204710/http://rightlivelihood.org/sewa.html). Indeed, SEWA started microfinance operations before Grameen Bank of Bangladesh did. In this sense, SEWA was the pioneer in implementing the concept of microcredit. However, SEWA adopted the individual banking model. In India, the concept of group lending emerged with the Mysore Resettlement and Development Agency (MYRADA), which started forming self-help groups (SHGs) in 1985. SHG is a unique homegrown model of microfinance, operational only in India. Many organizations like PRADAN and Mahila Arthik Vikas Mahamandal adopted the MYRADA model. In 1991-1992, NABARD started promoting SHGs on a large scale. In 1992, the SHG bank linkage program was launched as a pilot project. Realizing the success of the SHG model in promoting the agenda of financial inclusion and in increasing access to finance, NABARD replicated the SHG model and the SHG bank linkage program on a large scale. The SHG bank linkage program proved an important tool for the empowerment of women. Swain and Wallentin (2007) argued that SHG members are empowered through their participation in this microfinance program in the sense that they are able to resist existing gender norms and cultural values that restrict their ability to develop and to make choices.

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The microfinance industry witnessed a turnaround in 1996. BASIX, an institution aimed at the promotion of livelihood, founded in that year, popularized the concept of commercial microfinance. Various microfinance giants like SKS Microfinance and Spandana were set up in the wake of BASIX. The trend intensified in the post-2000 period when several microfinance organizations were established. As in the case of government initiatives, the focus of most MFIs remained communities in rural areas. In 2004, Ujjivan was started in Bengaluru with the objective of providing financial services to the urban poor. The microfinance industry began to grow rapidly. However, in 2005, the Andhra Pradesh crisis came as a major setback to the industry. In 2010, the Andhra Pradesh crisis hit the microfinance industry. However, the data suggest that microfinance has been making a comeback since 2013. Concerned about the severity of the problems caused by the lack of regulation in the microfinance industry, the GOI floated a microfinance regulation bill for discussion in 2007.

In 1999, the GOI included the SHG model in its major program, Swarna Jayanti Gram Swarozgar Yojana (SGSY). Much later than the concept of SHG, the JLG started in India, the JLG model had been formulated as a pilot scheme by NABARD in 2004-2005. SKS Microfinance, which was established in 1997, followed the Grameen Bank pattern and adopted the JLG structure as its model for microfinance. Later, many MFIs were established which followed the JLG structure. At present, three basic models of microfinance are operational in India, that is, SHG, JLG, and individual banking.

The majority of MFIs operate in rural areas. Agriculture and allied activities being major livelihood sources in rural areas, these MFIs are contributing significantly in financing agricultural operations. The JLG scheme was initiated by NABARD to enhance credit flow in agriculture. By end March 2015, over 1.1 million farmers were provided with a cumulative credit disbursement of Rs 112 billion (RBI, 2015). However, MFIs have been criticized for their high interest rates. Because MFIs are not allowed to mobilize savings, they have to take loans from banks for their operations. To become financially sustainable, MFIs need to lend at high interest rates. To make an impact through the expansion of financial services for agriculture at affordable rates, MFIs need policy support. A recent initiative by the RBI to provide small bank licenses to MFIs is a welcome step in the direction of enhancing agricultural finance. This will help MFIs to provide financial services at lower interest rates.

Discussions and conclusions

Various government and NGOs made several efforts to promote access to financial services. A key problem identified in dealing with the lack of access to credit has been lack of road and transportation infrastructure that allows connectivity and reach to banks, particularly in rural areas. To address the issue of poor infrastructure, the concept of microfinance relies on the provision of doorstep services. One of the most important factors in the success of a microfinance program is the nature and scope of its doorstep service delivery. It is interesting to note that a proposal for setting up "mobile banks" was sent to the RBI as far back as 1949. It was mentioned at the time that mobile banks had been successful as a tool of advertisement for banking facilities in areas where branch networks were well developed, as in England and Wales, whereas in places like Scotland where the banking system was less developed, mobile banks were not successful. It was reported that these mobile vans had fixed timings and that their schedules were known in advance to the local communities that they served. It was assumed that an initiative of this kind would also help Indian farmers and hence its adoption was proposed. However, the RBI rejected the proposal because the necessary infrastructure for supporting such an initiative did not exist at the time. Additionally, it was rejected because mobile vans were also prone to theft (RBI Archives, File No. 7788, p. 109).

Saving was a key element of financial services from the beginning. Initiatives like Bachat Kumbh Yojana, salary earner societies, and rotating savings and credit associations (ROSCAs)

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were meant to promote thrifty habits in communities. It is interesting to note that a similar program called Bachat Kumbh Yojana was operational in Rajasthan in late 1950s. This scheme involved the circulation of a clay pot to each member of a savings society and the decision by all members to save some money as per their convenience. At the end of the year, all members would bring their respective clay pots to the society and the pots would then be broken and the money saved would be extracted. The saved money would then be deposited in the account of the member at an interest rate of 4 to 5.5 percent. In the end of the year, the member having the highest savings would be rewarded, and those who were not able to save anything would have to save an average amount saved by each member of the same society. Later, the SHG was developed on a similar concept, but in this case, one box in each group was rotated among all the members of one group rather than allotting one pot to each member (RBI Archives, File No. F8159, pp. 77-78). Later, the SHG evolved as a unique model of microfinance in India. This model had a unique approach because it was based on promoting the habit of thrift first and later on moving to lending to the group, and that too only in proportion to the savings achieved by the groups. It was based on the assumption that "regular saving will lead to regular repayment." The model worked well in the Indian context and became the driver for one of the fastest growing microfinance movements in the world.

Financial inclusion has been an important focus of policymakers in recent years. The success of financial inclusion depends on spreading financial literacy among people. The importance of financial literacy was discussed in 1964. The article published in the leading newspaper, i.e. *The Hindu* in 1964 mentioned that notes the urgent need for promoting agriculture financial literacy through pamphlets and visual aids. The Y.H. Malegam Committee, set up to study issues and concerns in the MFI sector, suggested in its report to the RBI in January 2011 that interest rates for MFIs should be capped. This recommendation was widely criticized by many experts. However, it is interesting to note that the capping of interest rates was discussed by policymakers as early as 1918. Many initiatives for financial inclusion were proposed long back, but failed to be implemented for one reason or the other. Had these initiatives been implemented successfully at the time, India would have been a front-runner in terms of financial inclusion.

Agriculture is the key economic activity in many developing countries, including India. A major constraint in the achievement of profitable agriculture is the lack of access to finance by farmers. Various approaches have been tried to address this problem. In recent years, with the evolution of microfinance, the paradigm for agricultural finance has shifted from the poverty-lending approach to the financial system approach. Microfinance has the potential to meet the demand for agriculture credit. The need of the day is to create the right policy environment for the growth of microfinance so farmers can be helped through the provision of adequate and affordable credit. Recent initiatives like PMJDY and PMMY are important steps toward achieving this objective. It is important to promote a self-sustainable model like microfinance rather than subsidy- and grant-oriented models. Availability of adequate and affordable credit will help agriculture become a profitable venture, and this, in turn, will help agriculture GDP grow and contribute to the overall growth of GDP of India.

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