

## Research Paper



## THE ROLE OF COOPERATIVE FINANCE IN RURAL INDIA

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### ABSTRACT

**F**inancial or credit co-operatives are a link between institutional and informal credit agencies. The purpose of the creation of such co-operatives was to expand rural credit and to displace informal finance in rural India. Today, the need of these financial services is very important for rural areas, as they can reach the small farmers easily, entail group liability and so reduce the risks of loan defaulter.

This article examines, (i) the nature and extent of these financial co-operatives in rural areas and how they affect the lending process of rural India both institutional and non-institutional credit (ii) It tries to evaluate the factors like, how far these co-operatives were successful in mobilizing the savings of the villagers and lower the risks of borrowers' incentive to pay.

**KEYWORDS:** co-operatives, financial services, lending process, economic development

### INTRODUCTION

Credit cooperatives were started in India to provide cheap institutional credit to poor, especially in village areas, in order to liberate farmers from debt burden of money lenders. In India, the concept of credit cooperatives began in the year 1912 when MaClagen committee advocated that every village should be covered by credit cooperatives. After independence, cooperatives in general and rural cooperatives in particular were in Central stage for rapid and equitable economic development and became the central force of state policy.

Cooperatives in India nowadays are involved with economic activity like agriculture, forestry, marketing and insurance and cover 90 percent of rural households of Indian villages. As per NSSO reports (2013), formal source of finance in rural sector has increased but still informal sources provide largest credit to agriculture farmers. It is worth mentioning here that 64 percent of informal sources of credit is used by agricultural farmers. Access to credit among villages is not a big issue but no access to credit with low interest rate shows that the government is not successful in implementing the financial inclusion plan with rural economy.

Agriculture household's survey reports (2013) indicate that large farmers borrow 72 percent and marginal and small farmers use only 14 percent of formal sources of credit. Instead, institutional finance should be lent to poor farmers who have been left out on the processes of financial inclusion. In the past decades several institutions have appeared in the distribution of formal credit such as cooperatives, still there is a need for proper regulatory

framework which can include the involuntary exclusion of poor class. In this context this paper examines, (i) the nature and extent of these financial co-operatives in rural areas and how they affect the lending process of rural India both institutional and non-institutional (ii) It tries to evaluate the factors that, how far these co-operatives were successful in mobilizing the savings of the villagers and lower the risks of borrowers' incentive to pay.

### OBJECTIVE OF THE STUDY

The main objective of this paper is to analyze the role of cooperatives as an organization, to evaluate the factors and their role in rural credit i.e. how successful they are in terms of financial inclusion.

### RESEARCH METHODOLOGY

- Research Design: - Exploratory and empirical research design based on secondary data.
- Sources of Data: - NABARD reports, NAFSCOB, RBI report on currency and finance.
- Tool of Analysis: -The data collected for the study was analyzed logically and meaningfully to arrive at meaningful conclusions.

**Period of Study:** - Data for a period of 10 years, 2005-2015.

### SURVEY OF LITERATURE

- Huppi & Feder (1990): 'The role of groups and credit cooperatives in rural lending'. Mohan (2005): 'The Three Tier Credit Cooperatives in India-Governance and Management'. Sarma and Kumar.R (2008), 'Rural Short Term Cooperative Credit



Structure'. Abhinav (2012): 'Role of Cooperative in Agriculture Credit', Virendra, Gena and Wankhede (2015)- Role of Cooperatives in improving livelihood of farmers on sustainable basis, Wadavi madhav (2011), 'Rural Credit Cooperative Institutions: lesson for successes. Various report of the Task Force on Revival of Credit Cooperatives. Various issues of NABARD reports.

- ❖ Credit cooperatives have the potential to provide affordable credit to small scale and marginal farmers as they can reduce transaction costs and lower the risk of default.
- ❖ Issues and concerns of rural cooperatives-
  - ✓ Inadequacy of credit, Constraint on timely availability of credit,
  - ✓ Increase in non-performing assets,
  - ✓ High interest rates,
  - ✓ Neglect of small and marginal farmers,
  - ✓ Low credit deposit ratio,
  - ✓ Governances standard,
  - ✓ Legal issues,
  - ✓ Democratic process of selection of members,
  - ✓ Solvency and operational issues.
  - ✓ They stress the need for revival of the cooperative credit institutions and suggested various reforms.

- ✓ These committees emphasized to make cooperatives self-reliant, autonomous and fully democratic institutions.
- ✓ Through the efforts of cooperatives, the farmers are able to increase the efficiency of various farm inputs and overall crop productivity.

## NATURE AND EXTENT OF CREDIT COOPERATIVES

Credit cooperatives are financial services which include rural cooperative credit institutions and urban cooperative banks. Rural cooperative credit covers 70 percent of all rural credit outlets and provide 36 percent of total credit required in rural areas. It provides both short and long-term credit for various purpose which include agriculture, purchase of machinery, land, livestock consumers durables, etc. Short term credit is provided by the three institutions know as State cooperative Banks (SCB), District Central Cooperative Banks (DCCB) and Primary Agricultural Credit Societies (PACS). Long term credit includes Primary Cooperative Agriculture and Rural development Banks (PCARDB)

The credit cooperative took a concrete shape in 1904 when cooperative credit societies Act was passed. Today inspite of widespread expansion, rural credit market is not categorized as competitive market. Non-institutional credit still exists as one important source of financial services in India.

**Table-1 Institutional and Non-Institutional Rural Credit (in percent)**

Sources of Credit	1991-92	2001-02	2011-12	2015-16
Institutional	66.3	61.3	60.3	59
Regional Rural Banks	8	8.71	10.65	13.41
Cooperatives	18	30.54	17.21	26.99
Commercial Banks	29	60.29	72.13	59.61
Non-Institutional	30.6	38.90	39.70	41.0

Sources: - All India Debt and Investment Survey, Various Issues NSSO.

The presence of informal sources of credit is nearly 40 percent (Table-1) which evinces that in rural areas institutional credit is inadequate in terms of growing needs of the villagers. Among the institutional sources, commercial banks were the most followed by cooperatives during the period 1995- 2015. The share of cooperatives increased from 18 percent in the year 2001 to 30.54 percent in 2011. Later on, it declined to 26 percent during the year 2015. This shows that large number of buyers are not able to enter freely in intuitional credit market. The presence of too much legal processes, identification issues, debt issues of villagers, refinance status etc. make them to divert to other sources of credit for help.

Rural cooperatives structure is one of the largest networks and is considered to be an integral part of financial

inclusion, still the small and marginal farmers story tells us that they are in the situation of misery and distress with no access to credit to fund their requirement. Various committees had been set up in the past to inquire the problems faced by the villagers of small means but it seemed that there is no linkage between the demand and processes of credit availability. In order to understand the networks of credit cooperatives support system let us first look into the structure of cooperatives implemented in rural areas.

The short-term credit cooperative structure is federal in nature. It consists of 32 state cooperative banks (1038 branches), 370 district central cooperatives banks (1331 branches) and 92432 primary agricultural societies spread all over India.

**Table-2: Trends in State Cooperative Banks**

Year	Number	Reserves	Deposits	Borrowings	Loan Issued	Loans Outstanding
2006-07	31	-0.89	5.88	30.37	9.48	18.39
2007-08	31	4.20	18.21	1.15	8.56	5.64
2008-09	31	3.61	24.15	-6.85	9.41	-3.45
2009-10	31	2.91	16.36	12.20	-17.22	1.77
2010-11	31	13.80	-1.68	38.11	31.93	33.29
2011-12	31	-7.39	-1.59	30.43	18.80	17.15
2012-13	31	-3.72	9.34	17.59	-6.07	18.35
2013-14	32	-9.30	10.25	19.60	21.50	10.60

Source: - Various Report of Trend and Progress in Banking in India, RBI.

The total number of state credit cooperative banks remain constant (Table-2), during the period 2005 to 2015. The aggregate reserves increased marginally but its growth rate became negative eventually. Growth rate of deposits in aggregate increased from 5 percent to 10 percent which was negative in the year 2010 to 2011. It shows that total borrowings and total loans issued increased by 20 percent and 21 percent respectively. However, the gap between the loans issued and loan outstanding has increased during the period 2005-2015. According to NABARD annual reports, Trend and Progress in Banking the aggregate accumulated loss

of state cooperative banks have increased from 49 cr. to 602 cr. from 2005 to 2015.

The second most important short-term credit structure consists of 370 district credit cooperative banks (DCCBs). The total number of district credit cooperative banks (Table-3), has increased from 365 to 370 numbers during the period 2005-2015. The total reserves fall from 52,41 lakhs in 2005-06 to 31.8 lakhs in 2012-13. In the year 2013-14 it reduced to 4.14 lakhs. The total borrowings have declined to 12 lakhs from 22.83 lakhs in the period 2005-2015. Table-3 evinces that the total loans outstanding in view of loans issues increased mostly every year during the period 2005-2015.

**Table-3 Trends in District Credit Cooperative Banks (DCCBs)**

Year	Number	Reserves	Deposits	Borrowings	Loan Issued	Loans Outstanding
2005-06	365	52.41	4.47	22.83	14.83	12.78
2006-07	366	-15.90	19.30	6.05	9.95	12.53
2007-08	369	0.63	16.56	-13.03	-3.49	-1.96
2008-09	370	0.38	19.58	2.17	31.53	27.03
2009-10	370	0.93	10.07	52.30	36.13	4.78
2010-11	370	7.66	11.06	25.60	5.21	18.71
2011-12	370	22.24	10.88	20.48	24.59	17.04
2012-13	370	31.80	10.80	20.50	34.00	16.80
2013-14	370	-4.14	13.30	12.00	6.60	10.10

Source: - Various Report of Trend and Progress in Banking in India, RBI

District credit cooperative banks deposits and reserve increased during the period (table- 3) but it shows it is declined till the year 2013 from 2006. The trend evinced that borrowing increased from 20 percent to 25 percent but the gap between loan issued and loan outstanding became narrow in the respective period. According to reports, out of 103 DCCBs accumulated losses, 13 losses were above Rs. 100 Cr.

This shows that overall performance of DCCBs is weak during the period 2005-2015 which is a matter of concern.

Primary agricultural credit societies, the credit institutions at the grass root level provide short term credit directly to individual members. The total membership in PACS was 93488 lakhs on 2013 which was increased marginally to 13012 lakhs in 2015. Though small and marginal farmers are the major borrower from the PACS, the borrower to member ratio declined during the 2005 to 2013. Its growth of deposits and borrowings increased by 5 percent and 17 percent respectively in the same period.

**Table-4: Trend in Primary Agriculture Credit Societies (PACS)**

Year	Number	Members	Borrowings Members	Growth of Own Funds	Growth of Deposits	Growth of Borrowings
2004-05	1.06	1354	513	9.52	4.59	17.9
2005-06	1.09	1274	451	1.03	3.08	1.91
2006-07	1.06	1252	461	18.8	20.05	6.57
2007-08	0.97	1258	479	-0.31	-2.00	11.40
2008-09	0.97	1298	787	7.28	14.0	0.47
2009-10	0.95	1323	765	5.70	34.4	5.77
2010-11	0.94	1264	598	0.85	5.64	-6.8
2011-12	0.90	1061	523	27.0	34.7	84.20
2012-13	0.92	1136	449	15.7	33.5	5.09
2013-14	0.93	1275	495	-	-	-
2014-15	0.93	1301	481	-	-	-

Source: - Various Report of Trend and Progress in Banking in India, RBI

According to banking Commission's various reports PACSs has limited coverage in most of the rural India. The three-important reason pointed out with PACS are low effective coverage, weak ratio of membership with rural households and low amount of loans in proportion to other sources of loans to rural households. The commission report suggested the reorganization plan by setting up new norms

and societies to cover large areas, but the progress is slow. There are many difficulties associated in the rehabilitation of weak PACS because of inadequate resources, overdues and mismanagement within the system. The reserve bank of India has also suggested various productive activities to fulfil the need for credit of villagers.

**Graph-1- Total demand and loan issued by PACS**



Sources: - 52<sup>nd</sup> NAFSCAB annual reports

Graph -1 evince that there is marginal gap between the total demand for loans and loans sanctioned by PACS. From the year 2010 onwards, there is no gap and total demand is met by PACS. However, a large number of PACS are dealing with severe financial problems due to lack of deposits and low recovery rates. According to the RBI report (2003-04), ‘Developments in cooperative banking’ Nabard, in particular, has been extending funds to develop the infrastructure and taking various initiatives to strengthen the effectiveness of rural cooperative banks.

**TREND IN LONG TERM CREDIT STRUCTURE**

The long term cooperative credit structure consists of State Cooperative Agriculture and Rural Development

Banks (SCARDBs-19) and Primary Cooperative Agriculture and Rural Development Banks (PCARDBs-745). Most of these cooperative banks have weak resource base and they raise their own funds from reserves and share capital.

SCARDBs provide capital for land development mainly for agriculture, farm mechanization and for non-farm sector. The total numbers of SCARDBs remain constant during the year 2006-2015 at 20 (Table-5) but the share capital shows a fluctuating trend. The SCARDBs share capital increased from negative 0.5 to 3.05 during the period 2006-2014 showing a growth rate of 8 to 10 percent. The deposits have also increased from negative 7.52 to 18.41. On the other hand, loans issued have increased from 16.2 percent to 25.27 percent in the period 2006-2015.

**Table-5 Trend in long term credit structure-SCARDBs.**

Year	Numbers	Share Capital	Borrowing	Deposits	Loans issued	Loans outstanding
2006-07	20	-0.5	-2.02	-7.52	-16.2	-5.35
2007-08	20	-0.6	-0.9	15.4	-8.8	-1.61
2008-09	20	3.1	-10.5	1.72	16.4	-11.1
2009-10	20	0.85	5.9	7.35	24.1	4.44
2010-11	20	120	2.4	21.4	21.8	8.9
2012-12	20	1.1	0.42	11.6	7.5	4.8
2012-13	20	-51	-1.9	26.3	-13.1	-3.4
2013-14	20	3.05	-0.24	18.41	25.27	8.83

Various Report of Trend and Progress in Banking in India, RBI.

The loan portfolios with high interest rates are the two-major constraint of SCARDBs and in the past played a significant role for limited expansion of credit to farm sector. Most of the reviews by Task force committee have stressed against legal framework and the targeted group for its non-performance instead of qualitative improvement. The qualitative approach should be defining in terms of resources support in geographical areas, purpose and options availability to business operations and viability related to loan issued rather than methodology of identification.

The criteria for primary cooperative agriculture and rural development banks (PCARDBs) is also the same which provide long term credit at district level. In Table-6, the total numbers of PCARDBS increased from 696 to 714 with 10 percent variation from 2006-2015. The total share capital increased marginally from negative 0.3 to 0.31 during the same period. The total borrowing showed a negative trend and total loans issued increased by 15 percent.

**Table-6: Trend in long term credit structure-PCARDBs.**

Year	Numbers	Share Capital	Borrowing	Deposits	Loans issued	Loans outstanding
2006-07	696	-0.3	-3.15	-9.7	-14.1	-5.36
2007-08	696	-0.6	-2.66	2.6	-7.51	-3.47
2008-09	697	65.8	-0.06	33.4	12.7	-4.4
2009-10	697	0.99	2.37	-3.85	20.0	3.87
2010-11	697	-10.0	5.12	7.7	34.8	3.18
2012-12	697	0.65	4.33	16.9	11.5	4.66
2012-13	714	4.6	4.15	25.7	0.29	2.98
2013-14	714	0.31	-0.46	4.32	3.28	-0.64

Various Report of Trend and Progress in Banking in India, RBI.

The main objective of PCARDBs is to implement development programmes by giving credit to farmers, artisans and retailers. They played an important role in nineties in technology transfer in rural areas such as wasteland development and purchase of high yielding seeds and fertilisers finance. The Table-6 points out that PCARDBs' performance is poor in terms of loans issued for various purposes. Task Force also recommended to improve their financial strength or merged with short term credit structure. Overdues scenario associated with recovery target and a proper assessment of cost and revenues are some of the major issues that should be addressed urgently to survive in the financial market. RBI and NABARD should frame suitable designs which can enhance their potential for developing rural economy in terms of financial inclusion.

### CONCLUSION

Rural credit cooperatives societies are working positively though the number of societies are marginally increased. In terms of their coverage, members doubled which indicates that the farmers are getting aware of its benefits and are interested to get membership in these societies.

These societies play an important role in meeting the growing needs of rural poor. The volume of credit flowing through these institutions has increased. However, performance of these institutions has been less satisfactory and getting worse due to increase in accumulated loss, low recovery and high non-performing assets. Around 50 percent of PACS, 25 percent of DCCBs and 12 percent of SCCBs in short term credit are loss making. Non-performing assets as percentage of loans outstanding at the level of SCCBs and DCCBs has increased by 21 percent and 24 percent respectively during the period 2005-2015.

In case of long term credit, the gap between loan issues and outstanding accounts are decreasing. The biggest challenge these societies are facing, is to meet financial needs adequately and effectively which can provide gainful employment in rural areas.

Various committees had been set up in the past to inquire about the problems faced by these cooperatives and to make recommendations for their revival. However, no concrete action has been taken on these recommendations.

There is a need to assess the credit needs of the rural people. Linkage between demand for credit and purpose of credit is needed.

Efforts are also needed to strengthen the data base of rural cooperative credit structure

Lastly, there is a need to understand the informal markets, their network of relationship that support them and the nature and the extent of informal linkages with the formal system of cooperatives.

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