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ROLE OF COMMERCIAL BANKS ON FINANCING THE AGRICULTURE SECTOR IN INDIA

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Abstract

Commercial banks play a crucial role in facilitating the economic progress of a nation by mobilizing and channelling the savings of individuals towards productive investments. They also contribute to economic growth by creating new demand deposits through loan disbursements and investment activities. Moreover, commercial banks support domestic and international trade by accepting and discounting bills of exchange. By ensuring compliance with Basel II regulations, all commercial banks in India, with the exception of Regional Rural Banks and Local Area Banks, have established a sound foundation for their operations. Given India's status as an emerging economy, the presence of a well-structured banking system is essential. Commercial banks serve as the primary means to generate the flow of credit in the market. With a scarcity of capital in India, banks can play a pivotal role in promoting capital formation, controlling speculation, maintaining equilibrium between demand and availability, and directing resources to desired sectors. When the banking system of a country operates effectively, efficiently, and with discipline, it leads to rapid growth in various sectors of the economy. Agriculture, being the backbone of India's economy, relies heavily on commercial banks for credit flow, employment generation in rural areas, and overall economic development. This research aims to explore the impact and significance of commercial banks in fostering these aspects, utilizing secondary data to provide valuable insights into their contributions to India's economic progress.

Keywords: *Commercial Banks, Agriculture Sector, Micro Finance, Agro Indus Credit, KCCS*

1. INTRODUCTION

The banking sector has undergone significant transformations with the advent of liberalization, privatization, and globalization. Credit plays a vital role in the development of agriculture as it enables farmers to invest in new ventures and adopt advanced technologies. Agricultural credit holds great importance due to the unique role of Indian agriculture in the country's macroeconomic framework and its significant contribution to poverty alleviation. Recognizing the significance of agricultural credit for promoting agricultural growth and development, there has been a consistent emphasis on strengthening the institutional framework for agricultural credit since the beginning of planned development in India. India has a high poverty rate, with 22 percent of the world's poor residing in the country. This alarming poverty incidence is a global concern, as poverty eradication is integral to achieving sustainable development goals.

Therefore, reducing poverty in India is crucial for global progress. Commercial banks are financial institutions that offer various services such as accepting deposits, providing business loans, and offering basic investment products. They primarily cater to corporations and large businesses, distinguishing them from retail banks that serve individual customers. Commercial banks hold a substantial share, approximately 48 percent, of the total institutional credit extended to agriculture, followed by co-operative banks with 46 percent and Regional Rural Banks (RRBs) with 6 percent. However, studies have revealed that many ordinary people still lack access to institutional credit. Various formal institutional agencies, including co-operatives, RRBs, scheduled commercial banks, non-banking financial institutions, and self-help groups, are involved in meeting the short- and long-term financial needs of farmers. Efforts have been made to strengthen the institutional mechanisms in rural areas, aiming to enhance agricultural financing and support.

Functions of Commercial Banks

Commercial banks play a crucial role in meeting the financial needs of various sectors such as agriculture, industry, trade, and communication, making them significant contributors to economic and social requirements. In recent times, banks have adopted a customer-centric approach and expanded their range of services. The functions of commercial banks can be categorized into primary functions and secondary functions. The primary functions include accepting different types of deposits from the public, such as savings accounts, recurring accounts, and fixed deposits, which are payable after a specified period. Commercial banks also provide various forms of loans and advances, including overdraft facilities, cash credits, bill discounting, and term loans, to clients against appropriate security.

One of the most significant functions of commercial banks is credit creation. When granting a loan, banks do not provide cash to the borrower directly. Instead, they open a deposit account from which the borrower can withdraw funds. This process of granting a loan leads to the creation of deposits, known as credit creation by commercial banks. In addition to their primary functions, commercial banks perform several secondary functions, including agency functions and utility functions. Agency functions involve tasks such as collecting and clearing cheques, dividends, and interest warrants, making payments for rent and insurance premiums, handling foreign exchange transactions, buying and selling securities, and serving as trustees, attorneys, correspondents, and executors. Utility functions include providing safety locker facilities, offering money transfer services, issuing traveler's cheques, acting as referees, accepting various bills for payment (such as phone bills, gas bills, and water bills), providing merchant banking services, and issuing various cards like credit cards, debit cards, and smart cards.

Review of Literature

Akoijam (2013) emphasized the importance of a robust rural credit system to strengthen the economic position of agriculture and farmers in rural areas. To enhance the agriculture sector in India, focus should be placed on increasing production, improving marketing, processing farm produce, and ensuring responsive rural credit. Creating an environment that recognizes agriculture as vibrant and responsive can make rural areas more attractive.

Anwar and Khan (2015) highlighted that the sustainable economic development of any economy relies on the sustainable development of the agriculture sector. Policies focusing on the commercialization and modernization of agriculture are essential for its growth.

Bashirand Hassan (2010) concluded that there was a positive correlation between credit provision by commercial banks to the agriculture sector and agricultural produce, specifically focusing on wheat production. This credit support led to improved living standards in rural areas, poverty reduction, and overall economic growth.

Bharti (2018) highlighted that in many developing countries, including India, agriculture was a major economic activity, and access to finance was a critical constraint for developing a profitable agriculture sector. Promoting microfinance institutions and implementing appropriate policies could address the issue of limited access to finance. Developing a self-reliant model rather than relying on subsidies or grants was deemed important, and ensuring access to suitable credit could transform agriculture into a profitable endeavour.

Das et al. (2009) conducted a study that indicated an increase in institutional credit to the agriculture sector in recent years, while the contribution of the agriculture sector to GDP had decreased. Unequal regional distribution was identified as a challenge in the distribution of institutional credit.

Dongand Featherstone (2012) found that credit constraints were one of the reasons for low productivity among small farmers. Insufficient access to credit limited their ability to invest in labor, education, and resources, leading to lower productivity. This situation often forced farmers to migrate to urban areas in search of employment, which resulted in social problems and hindered the education of their children. By addressing credit constraints, farmers would have better access to credit and higher productivity, allowing them to stay in rural areas.

Maia, Eusébio, and da Silveira (2020) concluded that farmers engaged in large-scale agriculture, utilized modern farming techniques, and had access to farm credit demonstrated higher productivity compared to those lacking these characteristics.

Paramasivan C, & Pasupathi R (2017) Agriculture is the primary occupation and the major economic factor of India. It provides more number of employment opportunities and business strategies to the society. Mostly, peoples from India are concerning with agriculture sector directly and indirectly. Not only agricultural industries, agro based industries are also generating agro products and also it creates more employment opportunities to the peoples like farmers, agricultural workers, industrial workers, wholesalers, retailers exporters and others.

Paramasivan and Rajaram (2016) reviewed that micro insurance, an emerging concept in recent times, plays a significant role in socio-economic development by involving substantial investments. Initially introduced as a financial service within the microfinance sector, micro insurance has evolved into a distinct sector. This paper provides an overview of the general concepts of micro insurance.

Ponnarasu and Mohanraj (2017) stressed the need for new policies in Indian agriculture that address technology, infrastructure, power supply at subsidized rates, and the availability of fertilizers, seeds, tractors, and credit through formal sources. These inputs are crucial for the development of a profitable agriculture sector.

Rajaram (2016) has found that risk is an inherent aspect of human life, and mitigating risk through financial alternatives is crucial. The insurance sector, as a component of the financial services industry, plays a vital role in mobilizing capital for both the economic progress of the nation and providing social protection for individuals.

Research Queries

How agriculture sector will create the Employment opportunities in rural areas?

Construction of various means of irrigation like dams, canals etc., generates employment in the agricultural sector.

How commercial banks increase the credit flow in agriculture sector?

Banks can open a network of branches in rural areas by providing agricultural credit.

How commercial banks help in alleviation of poverty?

Integrated Rural Development Programme (IRDP) contributes to poverty alleviation, focusing on the various administrative systems and methods used for identifying borrowers.

How commercial banks are helpful in economic development of India?

Commercial banks help for economy development by boosting capital formation in the country.

Findings and Policy Implications

The Reserve Bank of India (RBI) and the Indian Government are actively working to improve the current conditions of the agriculture sector in the country. This is bringing a sense of relief to rural communities, liberating them from the exploitative practices of money lenders. NABARD, as the apex institution for indirect financing in agriculture, plays a vital role as a supporter, advisor, and companion to farmers. The commendable progress made by NABARD in refinancing is noteworthy. However, research indicates that 66% of the population still lacks access to banking services and affordable credit, making it difficult for poor farmers to sustain themselves. Disturbingly, studies reveal that 40% of Indian farmers resort to suicide due to their inability to repay bank loans. While commercial banks contribute 43.1% of total agriculture credit, they also pose additional challenges. The Indian farming community continues to face persistent challenges in accessing agricultural credit, highlighting the prevailing issues that hinder their access to financial support.

- High rate of interest on loan
- Lack of financial knowledge
- Cumbersome process of getting loan
- Bank staff is not cooperative
- Lack of security of collateral
- Fear factor about recovery process

The number of bank branches in rural areas has seen a significant increase, rising from 1,833 to 35,850. This policy implemented by the RBI has proven to be highly effective as it enables farmers in rural areas to easily access loans and gain a better understanding of the loan application process. However, a significant challenge remains for banks, as they need to extend their reach to cover the remaining 70,000 villages in rural areas. This expansion of banking services will have a positive impact on the flow of agricultural credit in India. According to the *Reddy* Report, the current agriculture credit flow in rural areas stands at only 18%. To address this issue, the government must take proactive measures to boost credit flow in the agriculture sector. Since a majority of India's population, approximately 78%, depends on the agriculture sector, its growth is crucial for generating employment opportunities and overall national development. The last recorded contribution of the agriculture sector to India's GDP was 3.4%.

Conclusion

The Confederation of Indian Industry has identified several key challenges faced by Indian agriculture, including high-cost credit, a distorted market, unproductive intermediaries, controlled prices, and inadequate infrastructure. Additionally, poor irrigation facilities, reliance on traditional technology and practices, low economic status of farmers, fragmented landholdings, lack of post-harvest infrastructure, and insufficient farm extension services have also contributed to the sector's struggles. To address these issues, banks should prioritize investments in crucial infrastructure such as irrigation facilities, processing units, storage facilities, and marketing activities. There are ample opportunities for banks to contribute to the improvement of agricultural infrastructure. This study highlights the significant role of commercial banks in the country's development. Comparatively, rural areas lag behind urban areas in terms of development, primarily due to lower credit flow and the relatively smaller contribution of the agriculture sector to India's GDP. It is only through the growth of the agriculture sector that overall economic development can be achieved in India.

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