**REPORT OF THE ADVISORY COMMITTEE**
**ON FLOW OF CREDIT TO AGRICULTURE**
**AND RELATED ACTIVITIES FROM THE BANKING SYSTEM**

**PART 'A'**

**RECOMMENDAITIONS WHICH HAVE BEEN ACCEPTED**
**AND COMMUNICATED TO BANKS FOR COMPLIANCE**

| Recommendation | Action taken |
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| 1. The Committee feels that reckoning units only in the producing areas/rural areas for bank finance under priority sector restricts the flow of credit for building up such facilities. It recommends that the stipulation regarding location of the storage units be removed, subject to these units storing mainly agricultural products. **[Paragraph - 2.26]** | Announced in the Annual Policy Statement for 2004-05 and circular issued on 18 May, 2004. |
| 2. With increasing emphasis on securitisation of assets, banks have the option of purchasing securitised loans from other banks/companies. At present, such investments by banks are not reckoned for the purpose of computing their priority sector lending. The Committee feels that banks' investments in securitised assets comprising wholly of direct advances to agriculture may be treated as their direct lending to agriculture under the priority sector. Similarly, if the securitised assets represent indirect finance to agriculture, the investment in such assets may be treated as indirect finance to agriculture. **[Paragraph - 2.27]** | Announced in the Annual Policy Statement for 2004-05 and circular issued on 18 May, 2004. |
| 3. The Committee suggests that Reserve Bank may advise banks to waive margin/security requirements for agricultural loans up to Rs 50,000 and agri-business and agri-clinics up to Rs 5 lakh. **[Paragraph - 3.11]** | Announced in the Annual Policy Statement for 2004-05 and circular issued on 18 May, 2004. |
| 4. The Committee recommends that while the current norm of default for two crop seasons could be retained for classification of loans as NPA, the added stipulation of two half years could be removed. Crop season for this purpose would mean the period | Announced in the Annual Policy Statement for 2004-05 and circular issued on 24 June, 2004 by DBOD. |

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| required for the concerned crops to mature for harvesting. The technical committee appointed for fixation of scales of finance could also determine durations of seasons for different crops in a given area in consultation with agricultural scientists to avoid adoption of arbitrary norms by any individual bank. This would be ratified by DLCC/SLBC. Two crop seasons after the due date should refer to only those two consecutive crop seasons in which the farmer normally undertakes crop production. For long duration crops, a loan may be treated as non-performing if interest or principal remains unpaid for one crop season (as defined above) after becoming due.<br>**[Paragraph - 5.7]** | |
| 5. Both crop and term loans are repaid out of farm income. If crops fail due to natural calamities, recovery of *all* loans is adversely affected. Therefore, relaxations suggested in respect of crop loans may also be, *mutatis mutandis*, made applicable to agricultural term loans.<br>**[Paragraph – 5.8]** | Announced in the Annual Policy Statement for 2004-05 and circular issued on 24 June, 2004 by DBOD. |
| 6. The Committee recognises the importance of offering thrift products as a service to the MFI clientele. It feels, however, that NGO-MFIs could play an important role in facilitating their clients' access to savings services of the regulated banks. The Committee considers that NGO-MFIs may not be permitted to accept public deposits unless they comply with the extant Reserve Bank regulatory framework, to protect the interests of depositors. When they do not accept public deposits, MFIs need not be regulated by the Reserve Bank.<br>**[Paragraph 6.26]** | Announced in the Annual Policy Statement for 2004-05. |

**PART 'B'**

**RECOMMENDAITIONS WHICH CAN BE ACCEPTED/ IMPLEMENTED IMMEDIATELY**

| **Recommendation** | **Action proposed to be taken** |
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| 1. The Committee observes that fixing targets on the basis of disbursements would not establish a link between the total advances of a bank and its lending to agriculture. The Committee also feels that the entire issue of fixation of targets for lending to the priority sector including agriculture needs a comprehensive review. Pending such a review, the existing target of 18 per cent of net bank credit for lending to agriculture should continue. **[Paragraph - 2.16]** | We agree with the recommendation. |
| 2. Reserve Bank may continue to monitor performance of banks under SACP and indicate the expected growth rate in disbursements over the previous year. **[Paragraph - 2.18]** | We agree with the recommendation. |
| 3. The Committee is of the view that the existing system of relating interest rates on deposits placed in RIDF (now renamed Lok Nayak Jai Prakash Narayan Fund) inversely to the shortfall in agricultural lending is adequately punitive. Banks with higher shortfalls earn lower rates of interest, which could be less than their cost of funds. **[Paragraph - 2.20]** | We agree with the recommendation. |
| 4. Banks presently use the scale of finance suggested by the district level technical committees as the criterion, although it is meant only to be indicative. Scales of finance, therefore, need to be reviewed and revised to meet credit needs of more capital intensive agriculture, using newer technologies and superior inputs. **[Paragraph - 3.5 (ii)]**<br><br>5. At present, banks adopt scales of finance based on the use of | We agree with the recommendation. SLBC convenor banks are being advised to take necessary action. |

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| traditional inputs. They need to be raised to facilitate adoption of new technologies and improved varieties of inputs. State Level Bankers' Committees may, therefore, review the scales, taking into account current costs of inputs, nature of soils, types of crops raised etc in the respective states and suggest modifications as may be needed.<br>**(Paragraph – 3.12)** | |
| 6. Machinery is becoming increasingly important as an instrument of transformation of agriculture into a diversified and commercial enterprise. A few banks have entered into tie-ups with major tractor and farm machinery manufacturers for financing them in a cost-effective manner. Other banks could explore such possibilities as well.<br>**[Paragraph - 3.5 (viii)]** | We agree. Banks are being advised to implement this. |
| 7. Procedural modifications in regard to agricultural advances, including simplification of procedures/forms for applications, agreements etc; rationalisation of internal returns of banks; delegation of more powers to branch managers; introduction of composite cash credit limits to agriculturists; introduction of new loan products with savings components; cash disbursement of loans; dispensing with the ‘No Dues Certificate’; discretion to banks on matters relating to margin/security requirements for agricultural loans above Rs 10,000 etc were introduced following the R V Gupta Committee recommendations. The Committee observed in its field visits, however, that few banks have complied with these directives and cumbersome procedures persist. Further, several branches of commercial banks insist on unreasonably high margin money or fixed deposits for sanction of loans, sometimes not commensurate with the quantum of loans. Such insistence results in denial of loans even to worthy borrowers who may not have adequate cash/collateral on hand. Controlling authorities of banks may review these lapses and take steps to rectify the situation.<br><br>**[Paragraph – 3.10]** | We agree. Banks are being advised to implement this. |

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| 8. The Committee feels that the interest rate is an important aspect of credit. It takes cognisance of the growing borrower expectations of uniformly lower interest rates on loans by different agencies extending credit to agriculture. A single mandatory rate for all banks is, however, not feasible at present, as capacity of the various agencies to deliver agricultural loans at lower rate of interest varies due to their differential cost structure. What ultimately matters to the borrower in addition to the rate of interest is the timeliness and adequacy of credit as well as the concomitant costs he may have to incur to avail credit. Therefore, banks need to pay attention to their systems and procedures to make their lending cost-effective. They have to consider also measures to save the borrower avoidable expenses for getting a loan sanctioned. **[Paragraph - 4.9]** | We agree. Banks are being advised to implement this. |
| 9. Banks should provide a separate flexible revolving credit limit to small borrowers of production or investment loans for meeting temporary shortfalls in family cash flows. Banks may evolve suitable credit products/packages in this regard. **Paragraph 6.5(ii)]** | Banks are being advised to implement this. |
| 10. The poor often shy away from formal institutions for want of information about procedures. Banks may adopt measures to reduce this information gap. Application forms for loan products should contain a comprehensive checklist of documents/information to be furnished as also procedural requirements to be complied with for availing of loans. **[Paragraph 6.5 (iii)]** | We agree. Banks are being advised to implement this. |
| 11. The Committee has examined various issues relating to financing of oral lessees and is of the opinion that Joint Liability Group (JLG) and SHG approaches have the potential of addressing the issues relating to these sections. Banks may have to explore these financing models through pilot projects until such times as states address issues of legalising tenancy. **[Paragraph 6.16]** | We agree. Banks are being advised to implement this. |

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| 12. The Committee came across complaints such as delays/refusal to open savings bank accounts of SHGs, large number of branch visits required to access credit, inadequate credit support extended by banks, delays in renewal of credit limits, and impounding of SHG savings as collateral for loans. This shows that even in states with sizeable numbers of SHGs financed, quality of linkage reflected in client satisfaction continues to be low. Banks need to address these issues urgently, to make access to financial services smooth and client-friendly.**(Paragraph – 6.13)** | We agree. Banks are being advised to implement this. |
| 13. The Committee endorses the need and rationale for an organisation such as NABARD as a development finance institution. All three functions of NABARD, i e credit, development and supervision continue to be of high relevance to the rural economy. Building a stronger rural credit system and converting credit needs into effective demand are the two most important expectations from NABARD.<br>**(Paragraph – 8.13)** | We agree. |
| 14. The Committee feels that the existing system of linking the interest rate on RIDF deposits inversely to the shortfall in agricultural lending seems adequate as a punitive measure, as banks with higher shortfalls receive lower interests, which would be less than their cost of funds. The interest rate structure as applicable to RIDF IX may be continued in case of deposits/advances under LNJPNF.<br><br>**(Paragraph – 9.22)** | We agree. As regards interest rate on RIDF-X being established in NABARD in terms of the FM's Budget Speech for the year 2004-05, GOI have already advised that the rates will be the same as in the case of RIDF-IX. |

## PART 'C'

The recommendations contained in the following paragraphs need further examination in consultation with NABARD, IBA, Government of India and other concerned agencies :

Paragraph Nos. 2.17, 2.18, 2.21 to 2.23, 2.25, 3.5(iii), 3.5(v), 3.6, to 3.9, 3.11, 3.17 to 3.20, 4.18 to 4.20, 4.22, 4,24, 4.26, 4.31, 4.32, 5.9 to 5.13, 6.5(i), 6.5(iv), 6.5(v), 6.7 to 6.9, 6.12, 6.14 to 6.17, 6.19, 6.25, 6.27, 7.12, 7.15, 7.21 to 7.24, 8.14, 8.16 to 8.32, 8.34 to 8.40, 9.21, 9.24, 9.25.