Financial Inclusion Among Small & Marginal Farmers to Achieve Inclusive Growth in India

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Introduction

This research paper aims to explore the status of financial inclusion among small and marginal farmers and to suggest policy measures to achieve inclusive growth in India. This paper is organized into a viii section. Despite the rapid development of financial services, most smallholders worldwide remain without access to financial services. Rural poverty is a multidimensional phenomenon, having wider implications for the economy. Rural poverty causes low demand for commodities produced not only in the agricultural sector but also in secondary and tertiary sectors. Among the poor, landless labor, small and marginal farmers constitute a majority in India. Financial inclusion is the backbone for removing rural poverty. The growing importance of the private sector reduced the speed of financial inclusion. Being trapped in a vicious circle of poverty, a lesser proportion of the rural population has capital to invest in agriculture and other self-employment avenues. Doubling farmer's income is a major objective, to be achieved for the sustainable development of the economy in general and agriculture in particular. Agricultural finance is a sub-set of rural finance dedicated to financing agriculture-related activities, such as input supply, production, distribution, wholesaling, and marketing. Financial transactions in rural areas involve higher transaction costs and risks because of the greater spatial dispersion of the population, further causing low quality of infrastructure. Rich farmers can access formal credit at lower interest since they have networks and collateral property. Asset-poor households have access to limited credit due to a lack of collateral security of assets. Poor farmers may also turn down loans, even if they qualify because they are unwilling to bear the risk of losing collateral (World Development Report, 2008).

Access to timely credit is a critical determinant of the profitability of agriculture. Credit market failure is considered one of the major factors for the persistence of the incidence of poverty among small and marginal farmers. The majority of the poor live in rural areas, yet most of them lack access to the range of financial services they need. Financial services available to them are relatively costly or rigid, whether from formal or informal sources. Financial institutions seeking to work in rural areas face numerous constraints, such as poor infrastructure and low education levels. Moreover, the main products of many microfinance institutions—short-term working capital loans with frequent expected repayments—are not well-suited to seasonal or longer-term agricultural activities.

Smallholdings play an important role in raising agricultural development and poverty reduction. The small and marginal holdings constitute the majority (more than 85 percent) of the total operational holdings in the eastern region, northeastern region, and central region. Timely credit will strengthen the input purchasing power of the farmers and ultimately lead to increased productivity of crops and other enterprises viz...Poultry, dairy fisheries, etc. The role of small farms in development and poverty reduction is well recognized. The global experience of growth and poverty reduction shows that Gross Domestic Product growth originating in agriculture is at least twice as effective in reducing poverty.

Section ii

Review of Literature

Sharma and Prasad (1971) stated that the introduction of the latest technology without credit facilities would not have a significant influence on the income of the farmers. Agriculture credit has a direct relationship with the income level of farm productivity and agriculture development.

Naryanan (1987) studied most of the villagers who took loans were small and marginal farmers and agricultural laborers. Further, he observed that due to inadequate credit given to them, there was no increment in the income of beneficiaries.

Ghate (1988) felt that one of the important reasons for continued dependence on moneylenders is that the formal credit delivery structure has not stretched to the villages despite its penetration. The formal credit delivery channels also lack the personal bonds that moneylenders enjoy with the borrowers. Borrowers obtain their loans more promptly from non-institutional sources.

Burgess and Pande (2005) found that a one percent increase in the number of rural banked locations reduced rural poverty by roughly 0.4 percent and increased total output by 0.30 percent.

Lipton, (2006), the role of small farms in development and poverty reduction is well recognized. The global experience of growth and poverty reduction shows that GDP growth originating in agriculture is at least twice as effective in reducing poverty as GDP growth originating outside agriculture (WDR, 2008). Smallholdings play an important role in raising agricultural development and poverty reduction

Golait (2007) examined the issues in agricultural credit in India. The analysis revealed that the credit delivery to the agriculture sector continues to be inadequate. It appeared that the banking system is still hesitant on various grounds to purvey credit to small and marginal farmers.

Thapa and Gaiha (2011), expressed that small holdings also face new challenges in the integration of value chains, liberalization, and globalization effects, market volatility and other risks and vulnerability, an adaptation to climate change, etc.

Section iii

Features of Small and Marginal Farmers

The small and marginal farmers largely undertake subsistence farming, small size of land holdings, and tenurial systems. Facing problems such as lack of access to inputs, lack of knowledge, poor technologies, inability to keep produce until good prices prevail in the market, and lack of ability to crop diversification etc. Due to these limiting factors, the small and marginal farmers suffer from low productivity, low employment, less income, and poor standard of living. Hence the small and marginal farmers either remained as labourers in the village or adopted distress migration practices to work in India and abroad.

In practice, the majority of the small and marginal farmers are using their own and loan funds for productive as well as unproductive purposes, which will eventually lead to indebtedness. A productive debt creates its means of payment but an unproductive debt becomes a great burden for repayment of principal and interest amount. Agricultural credit is a problem when it cannot be obtained and it is also a problem when it can be borrowed but cannot be repaid. In India, agricultural credit has twofold problems of inadequacy and nonavailability...

The income of small and marginal farmers is inadequate to meet their routine family expenses. Hence their finance are inadequate or almost nil, hence they have to depend on outside finance only. Further, their income accrues during a limited period of the year while their various expenses are distributed throughout the year. Given this, the budget arrangement is imperative to adjust both. Hence, agriculture finance in general and agricultural credit in particular is vital among the various constraints faced by these small and marginal farmers.

Section iv

The Growing Need for Credit

The credit needs of the agricultural sector have been expanding during recent times due to increases in the cost of inputs, general price index, commercialization, and modernization of agriculture. Globalization caused price volatility in the domestic and international markets, as a consequence farmers' incomes and loan repayment capacity became uncertain. The proportion of small and marginal farmers is increasing and they form more than four-fifths of the operational holdings. With spiraling costs of input-intensive cultivation, there is an increasing need for credit, but in the absence of security against various uncertainties, and a commensurate rise in returns, the farmer's risk gets further accentuated (Taskforce on credit-related issues to farmers,2010).

Section v

The Problems of Small and Marginal Farmers

The uncertainties in growth in agriculture are explained by the fact that more than 50 percent of agriculture in India depends on monsoons which aggravates the production risks (Economic Survey 2017-18). The debt burden of small and marginal farmers is higher due to their over-dependency on noninstitutional credit sources in the absence of friendly formal credit institutions. Small and marginal farmers are excluded due to their inability to give collateral security and procedural bottlenecks. Farmers face uncertainties from weather, spurious inputs, pests and diseases, and market shocks among other risks. Inadequate and untimely credit along with procedural bottlenecks from formal institutions add to his/her burden.

Microfinance institutions (MFIs) have been criticized for seeking higher interest rates and are mostly confined to the states with fairly well-developed banking systems. About 36 percent of the debt of farmers from informal sources had interest ranging from 20 to 25 percent. Another 38 percent of loans had been borrowed at an even higher rate of 30 percent and above, indicating the excessive interest burden of such debt on small and marginal farmers. The continued dependence of small and marginal farmers on informal sources of credit such as private moneylenders was attributed to constraints in the rural banking network and services arising out of financial sector reforms. Rigid procedures and systems of formal sources prevent easy access by small and marginal farmers, with easy and more flexible methods of lending adopted by informal sources (Reserve Bank of India, 2013).

Section vi

The Problems of Financial Institutions

Dispersed demand for financial services due to low levels of economic activity and low density of population in rural areas. A smaller number of clientele is the reason for more transaction costs to the banks. High information and transaction costs are linked to poor infrastructure (roads, telecommunications) and lack of client information (no personal identification or functioning asset registries). The weak institutional capacity of rural finance providers is related to the limited availability of educated and well-trained people in smaller rural communities. Crowding-out effect of subsidized and/or directed credit from state-owned banks or donor projects. Seasonality of many agricultural activities and long maturation periods for others, resulting in variable demand for savings and credit, uneven cash flow, and, lags between loan disbursal and repayments. Risks linked specifically to farming, such as variable rainfall, pests and diseases, price fluctuations, and small farmers' poor access to inputs, advice, and markets.

Section vii

Failure of Formal Credit Initiatives

Institutional finance is the lifeblood of the modern economic system without which no system can survive. In agricultural development also its role is crucial. Adequate institutional credit is considered to be the most important factor, if suitably provided, will go a long way to put the economy of the farmers especially the small and marginal farmers on a sound footing (Several, 1998)

After independence, credit institutions serving the agricultural sector were developed in several phases, despite the credit needs of agriculture in general and small and marginal farmers in particular have not been met fully and an overwhelming number of farm households have not been able to borrow from institutional sources. An increasingly large share of agricultural credit is going to farm sizes of more than five acres. Also, the average amount of loans outstanding per account has grown much more rapidly in the case of farm sizes of more than five acres and above as compared to small and marginal farm sizes. Moneylenders and other non-institutional sources charged exorbitant rates of interest from farmers who often had to mortgage, and sometimes sell their lands to clear their debts (Govt of India, 2007).

All India Debt and Investment Survey (AIDIS) by the NSSO shows that non-institutional agencies still accounted for as much as 44 percent of outstanding dues in 2012-13, an increase from the 36 percent level in 1990-91. About half of 14 crore farm households were covered by formal institutions, while the remaining were dependent on informal sources such as moneylenders who charge exorbitantly high rates of interest (Annual Report NABARD, 2012-13).

Section viii

The Way Forward

The sustainability of small and marginal farmers is crucial for livelihoods in rural areas and for the entire country. It is true that small holdings have higher productivity than medium and large farms. Indian agriculture is the home of small and marginal farmers (80%); therefore, the future of sustainable agriculture growth and food security in India depends on the performance of small and marginal farmers.

As a measure to check distress sales, post-harvest loans for storage in accredited warehouses against Negotiable Warehouse Receipts (NWRs) are available for up to 6 months for KCC holding small & marginal farmers; this provision should be increased to one year. The Interest Subvention Scheme (ISS) has been operational since 2006-07. Under this scheme, the farmers can avail concessional crop loans of up to Rs.3 lakh at a 7 percent rate of interest. It also provides for an additional subvention of 3 percent for prompt repayment within a period of one year from the date of advance; it should be increased to two years. To give relief to small and marginal farmers who would have to borrow at 9 percent for the post-harvest storage of their produce, the central government has approved an interest subvention of 2 percent i.e. an effective interest rate of 7 percent for loans up to 6 months; this provision should be increased to one year.

Provide opportunities for farmers to diversify their income-generating opportunities to reduce various risks by facilitating the development of agricultural sub-sectors like livestock and fisheries and other nonfarm activities. Unless state-owned agricultural banks undergo a radical transformation in governance arrangements that can insulate them from political capture, they are unlikely to function in a commercially sustainable manner and serve the needs of smallholders. With legal frameworks in place, m-banking usage should be promoted to ensure transparency and timely delivery of credit. Insurance can make potential borrowers more willing to bear the risk. The premium at present charged should be reduced to minimize the burden of debt.

The credit from institutional sources will complement all such government initiatives like Soil Health Card, Input Management, Per Drop More Crop in Pradhan Mantri Krishi Sinchai Yojana (PMKSY), PMFBY, e-NAM, etc. There should be better coordination between banking staff and rural development staff by enhancing the skills of the staff. Build rural infrastructure i.e. warehouses, roads, and transport mechanisms.

Reduce political interference in day to day functioning of financial institutions. Rank banks based on meeting the credit needs of small and marginal farmers. Impose agricultural cess/surcharge on direct taxpayers, to create funds for helping small and marginal farmers. There is a need to extend the spread of rural branch networks by scheduled commercial banks, RRBs, and cooperatives. Security of tenure should be guaranteed to the tenants because many of the small and marginal farmers are the tenants.

Strengthen the absorptive capacity along with an increased credit flow. There is also a need to expand the share of small farmers in total credit disbursement. Providing credit counseling to small and marginal farmers, simplifying procedures, and transparency in providing credit, need special attention. Transaction costs in the form of procedural delays, more paperwork, repeated trips to the banks, and corruption in banks should be reduced.

Facilitate farm households to diversify their livelihood activities through the development of non-farm activities. This requires adequate infrastructure and the setting up of appropriate institutions for skill formation, training, and education. Motivate and facilitate farmers to establish their own financial services organizations through which they can access farm credit, regardless of whether they have land title deeds or not.

Expansion of the private sector is the order of the day; hence incentives should be given to the private sector to complement the financial services being extended by the public sector banks. There should be a cap on the maximum rate of interest being charged by the money lenders. Instead of farmers running around banks, banking staff should go to villages by operating mobile banking services, thereby wastage of man days can be averted. Priority should be given to disbursing loans to female-headed small and marginal farmers.

Conclusion

Financial literacy and counseling campaigns be undertaken to increase awareness among farmers. Support for strengthening and creation of non-farm activities: Bridge the gap between farm and non-farm activities of small farmers, since small farm activities are hardly sufficient to meet the basic needs of the small farmers. The reach of formal financial markets is not deep enough in rural areas, so the moneylender was dispensable, what is needed is that exploitative actions of moneylenders be curbed. All the state governments should computerize and update land records and make them accessible to farmers/lenders in a transparent manner for easy access to loans. Strictly implement the legislation by providing definite upper limits on the rate of interest and curbing coercive recovery practices. Small farmers face several challenges in access to inputs and marketing. They need a level playing field with large farms in terms of accessing land, water, inputs, credit, technology, and markets. Strengthen micro-financial institutions by reducing the present loopholes. Debt-waiving schemes may give temporary relief to the farmers, but they will endanger the sustainability of the banking system and debtors will become dependent on the government and also become wilful defaulters. Keeping the essentiality under consideration there is an urgent need to declare credit as a fundamental right for the protection of the right to life (Article 21).

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