

Microfinance for Agriculture: Perspectives from India



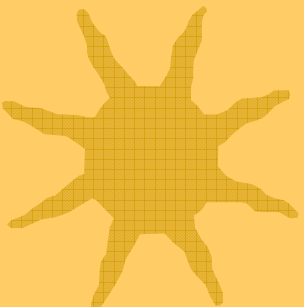
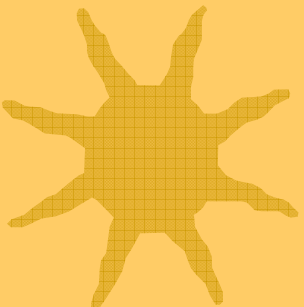
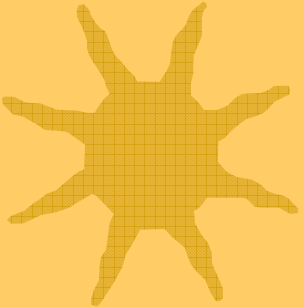
SATISH PILLARISSETTI

National Bank for Agriculture and
Rural Development (NABARD)

INDIA



PROLOGUE



- ★ State interventions in rural finance markets proved disastrous for institutions
- ★ But private sector did not step in when state owned banks failed
- ★ Microfinance-basically an urban phenomenon
- ★ Rural microfinance-mainly for microenterprise financing
- ★ Focus again on agricultural banks
- ★ Indian approach-two fold:revitalize RFIs and innovate microfinance technologies for agri-credit

Institutional Arrangements for Rural Credit



Reserve Bank Of India

Government Of India

NABARD

**Regional Rural Banks(96)
Branches – 14500**

**Rural
Cooperatives**

**Commercial Banks(84)
Semi Urban Branches – 15370
Rural Branches – 30776**

**SCBs – 31
DCCBs – 367
Branches-13230
PACS- 108779
ARDBs- 20
PARDBs – 727
Branches-1958**

Depositors & Borrowers

MFIs (800)

Self-Help Groups



Pre Reform Era

- ★ Till 1990s-Lack of Operational Freedom
- ★ Controls by Government and Central Bank
- ★ Concern was outreach- Viability aspects neglected
- ★ No freedom for business decisions
- ★ Micro-regulations on credit flow
- ★ By 1990s- Rural Finance Sector-Losses-Bad Debts
- ★ Stage: Close Down or Complete Overhaul

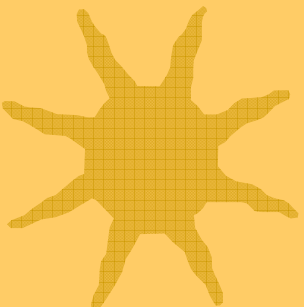
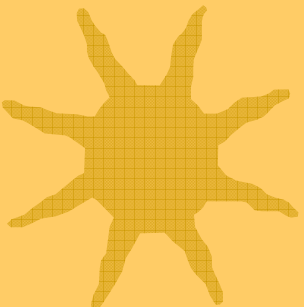
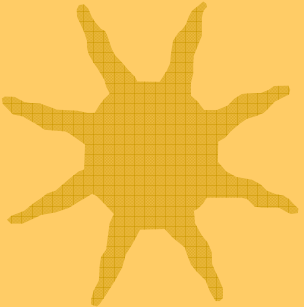


Banking Sector Reforms

- ★ Banking Sector Reforms since 1991-92
- ★ Deregulation of interest rates
- ★ Flexibility and Freedom of Operation
- ★ Reduction of Government ownership
- ★ International best practices in prudential norms
- ★ Reduction in pre-emptions
- ★ Entry of new Private Sector Banks



Reforms in Rural Banking



- ★ Development Action Plans (DAPs) for Cooperatives and RRBs to take advantage of banking sector reforms
- ★ Bottom-up plans based on strengths and weaknesses of institutions
- ★ Specific remedial measures for viability
- ★ Institutions in losses: current viability first; sustainable viability later
- ★ Recasting of lending and deposit portfolios to achieve viability
- ★ Performance obligations in form of MoUs



Reforms in Rural Banking

- ★ Due to professional management and better governance RRBs performed better in turnaround
- ★ Banks innovated products to increase outreach and business volumes
- ★ But cooperatives carried huge accumulated losses as their Balance Sheets not cleaned up during reforms
- ★ A revival package of \$ 3,750 millions now designed for short term cooperatives
- ★ Amalgamation process of RRBs going on



Microfinance in India

- ★ Largest provider of credit to the small and marginal in India: Banking Sector
- ★ Microfinance Institutions:
 - NGO-MFIs
 - Non-Profit Companies
 - Mutual Benefit MFIs: Cooperatives
 - Non-Banking Financial Companies
- ★ > 90 % of Microfinance business: SHG-Bank Linkage Programme



Self Help Group-Bank Linkage Model

- ★ Initiated in 1992 as Pilot Project by NABARD – The Apex Bank for Rural Finance
- ★ Three fold Objective of the Project:
 1. To Evolve Supplementary Credit Strategies for Meeting the Credit Needs of the Poor by Combining the Flexibility, Sensitivity and Responsiveness of the Informal Credit System with the Strength of Technical & Administrative Capabilities and Financial Resources of Formal Financial Institutions



Self Help Group-Bank Linkage Model

2. To encourage banking activity, both on the thrift and credit sides, in a segment of the population that the formal financial institutions usually find it difficult to reach
 3. To improve credit flow to rural poor with reduced transaction costs, both for the financing bank and the borrower
- ★ Linkage with banks for credit

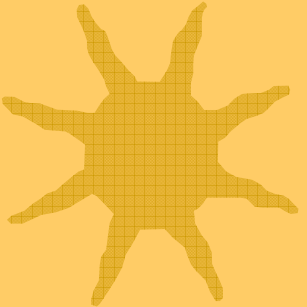


SHG-Bank Linkage: The Success

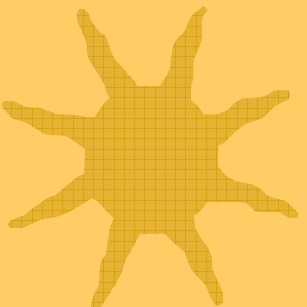
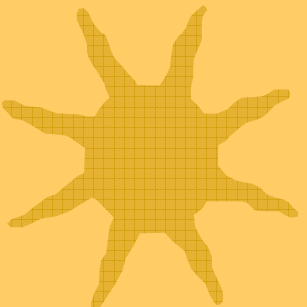
- ★ **Credit through > 45,000 Bank Branches of 500 Banks-Commercial Banks, Cooperative Banks, Regional Rural Banks**
- ★ **> 4,500 NGOs, Government agencies, departments and numerous grass root level rural volunteers**
- ★ **SHGs linked with Bank Credit : 2,924,973
(as on 31-03-07)**
- ★ **Cumulative Credit disbursed \$ 4.5 billion (as on 31-03-07)**
- ★ **Reached nearly 41million poor families**



Microfinance for Agriculture

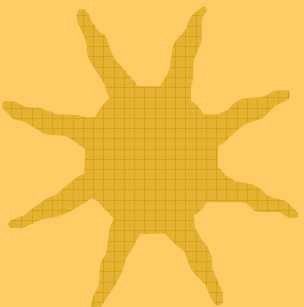
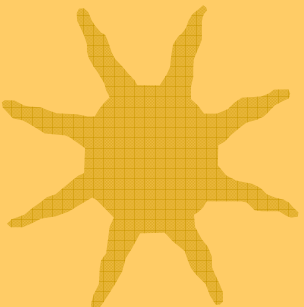
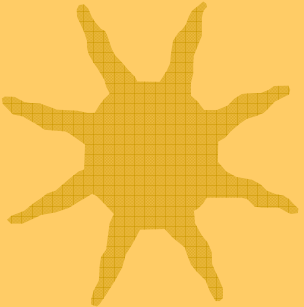


- ★ In 2006-07 bank credit to agriculture: \$40.82 bln- 40 % to small & marginal farmers
- ★ In 2006-07 all microfinance credit flow: \$1.87 bln
- ★ Of which only 8 % for agriculture and 14 % for animal husbandry
- ★ Microfinance has not been able to take care of agri finance needs in India
- ★ NABARD initiated innovations in microfinance to make it suitable for agricultural finance





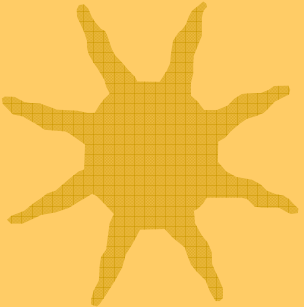
Joint Liability Groups



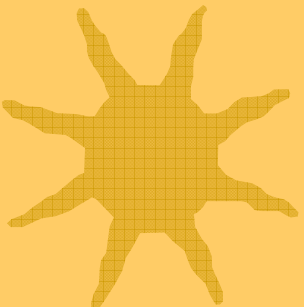
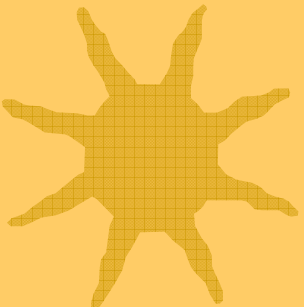
- ★ SHG features unattractive to farmers' needs
- ★ Formal banks unable to cater to marginal farmers and tenant farmers
- ★ Project of Joint Liability Groups on lines of BAAC of Thailand
- ★ Informal group of 4-10 farmers for availing bank credit individually or a group through mutual guarantee
- ★ Members offer joint undertaking to bank for repayment of loans
- ★ Credit not linked to savings and no collateral
- ★ Successfully working in 8 states; NABARD working for upscaling



Credit plus approaches

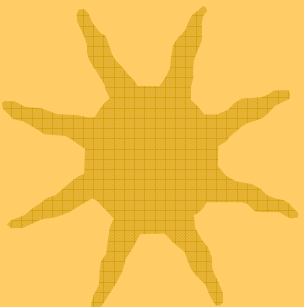
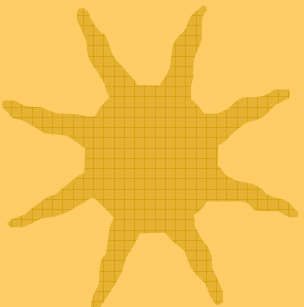
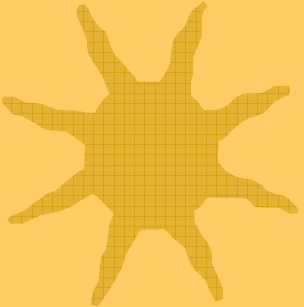


- ★ Agriculture requires credit plus new technology know-how
- ★ Agri productivity increases with improved technology
- ★ Green Revolutions doubled crop yields
- ★ Extension services required for technology dissemination
- ★ Synergy needed between providers of technology and credit
- ★ Four innovative models demonstrate credit plus approaches to microfinance





Farmers' Friend Groups



- ★ Rythu Mithra (Farmer's Friend) Groups (RMGs) promoted by state government in Andhra Pradesh
- ★ Groups of 15 small, marginal and tenant farmers
- ★ RMGs serve as conduit for technology transfer and market information
- ★ Agriculture Department is the nodal agency: facilitates formation and working
- ★ Linked to bank credit through NABARD's pilot project
- ★ Unbanked farmers brought into credit fold for first time

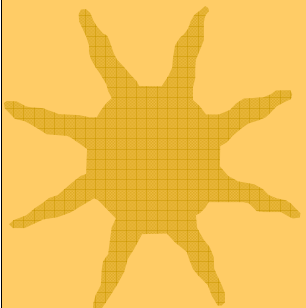
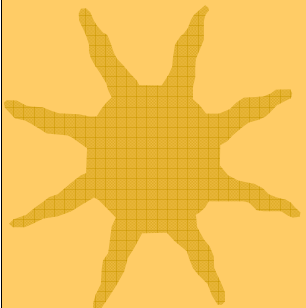
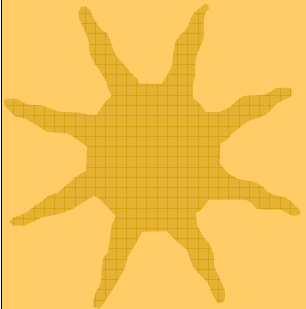


Farmers' Club model

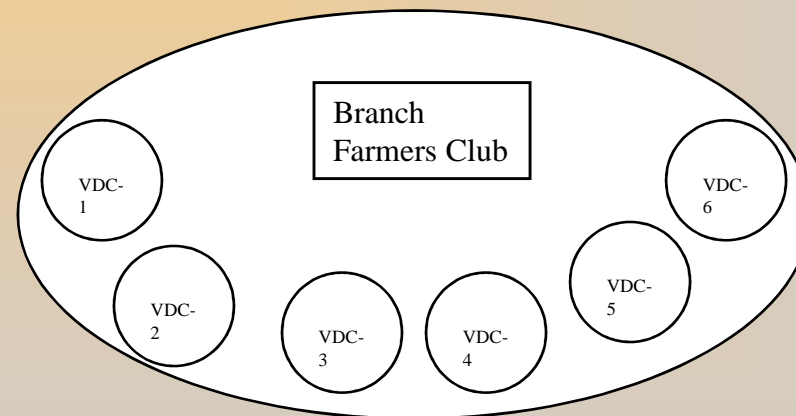
- ★ Pioneered by Aligarh RRB in Uttar Pradesh
- ★ SHGs in a village set up Village Development Committees (VDCs)
- ★ VDC acts as Farmers' Club for the village
- ★ All VDCs are linked to Branch Farmers' club and in turn to Bank branch
- ★ VDCs coordinate to ensure credit support to village
- ★ Coordinates with extension agencies and Government to ensure non-credit support
- ★ Liaises with input suppliers and marketing agencies
- ★ Works as local advocacy group



Farmers' Club model

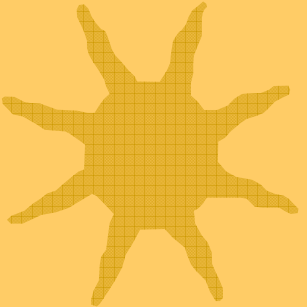


Service Area

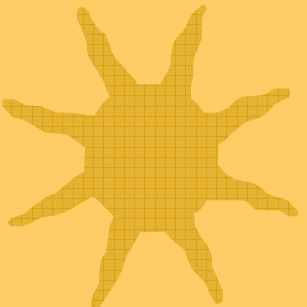




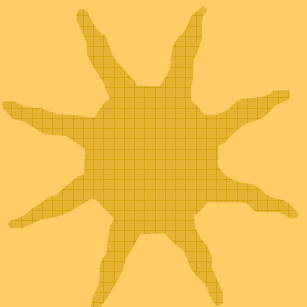
Village Council model



- ★ Aga Khan Rural Support Programme (AKRSP) in Gujarat organised farmers under Gram Vikas Mandals (Village Development Council) and Maaldari Vikas Mandals (Cattlerearers Development Council)



- ★ Councils have SHGs as sub-groups and work in watershed development, input distribution, technology dissemination



- ★ Councils undertake savings and credit services in a linkage with the regional banks

- ★ Example of bundling of credit and non-credit services to agri microfinance clientele

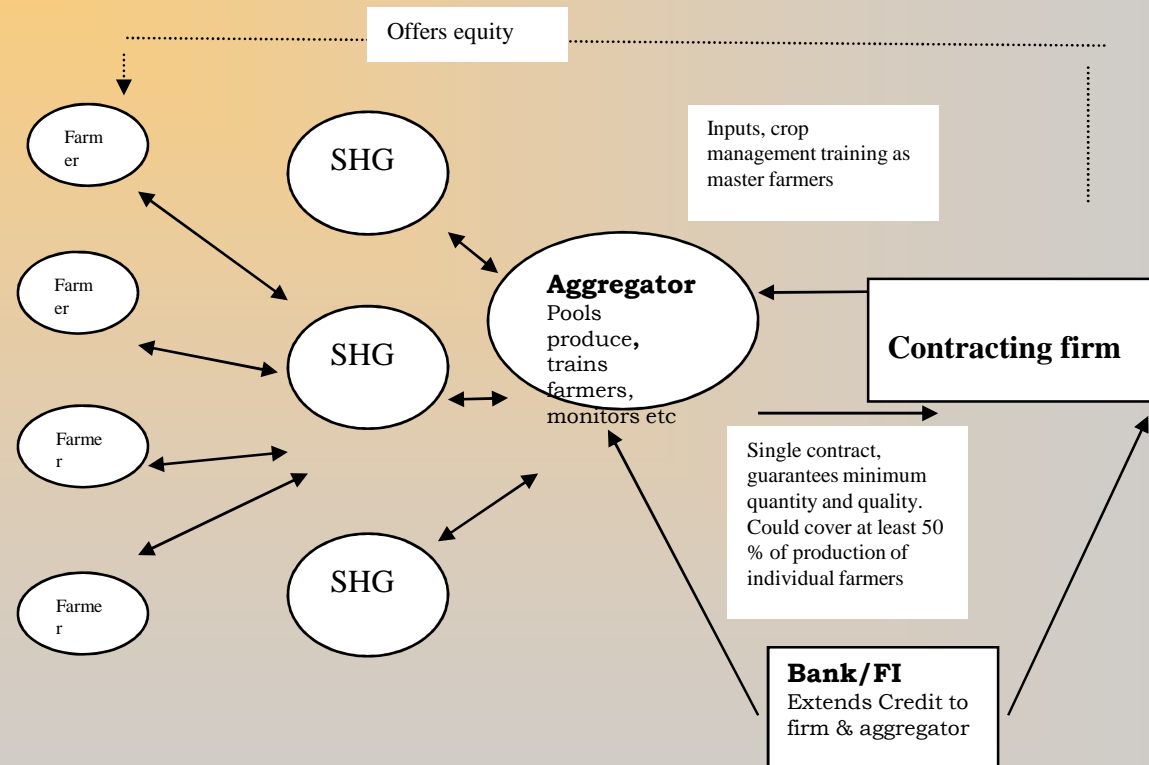


SHG-Contract farming linkage model

- ★ Kerala Horticulture Development Programme links farmers' SHGs in contract farming arrangements
- ★ Production activity organised through farmers' SHGs
- ★ Master Farmers selected by members act as link for technology, market and information
- ★ They also act a link with the bank for credit
- ★ Similar arrangements can be worked out in other contract farming arrangements
- ★ Such models can link small farmers with agri-business firms and ensure both credit and non-credit support

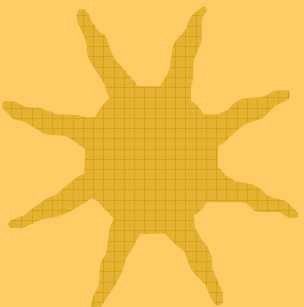
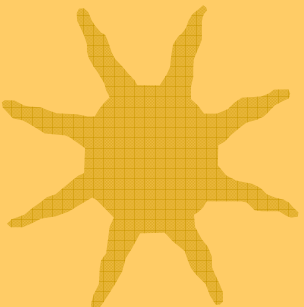
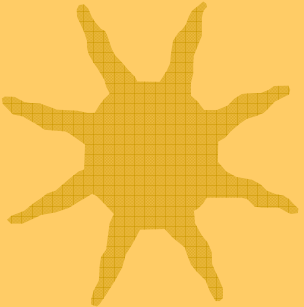


SHG-Contract farming linkage model





Interest rates and loan tenures



- ★ For microenterprise financing interest rates do not matter due to volume and velocity
- ★ In agriculture funds inflow seasonal, linked to harvest
- ★ Investment credit on project approach : higher interest rates could render projects unviable
- ★ Agriculture cannot sustain above market interest rates like microenterprises
- ★ Gestation periods long: production credit: 6-8 months; investment credit 3 –9 years
- ★ Microfinance technologies cannot sustain such loan tenures



CONCLUSION

FOUR PROPOSITIONS

- ★ Agricultural development banks, cooperative banks and regional banks have to be restructured and revitalized to provide credit to agriculture
- ★ Microfinance technologies in existing forms cannot cater to agriculture ; innovations needed;JLG, RMG and other experiments in India show a path forward

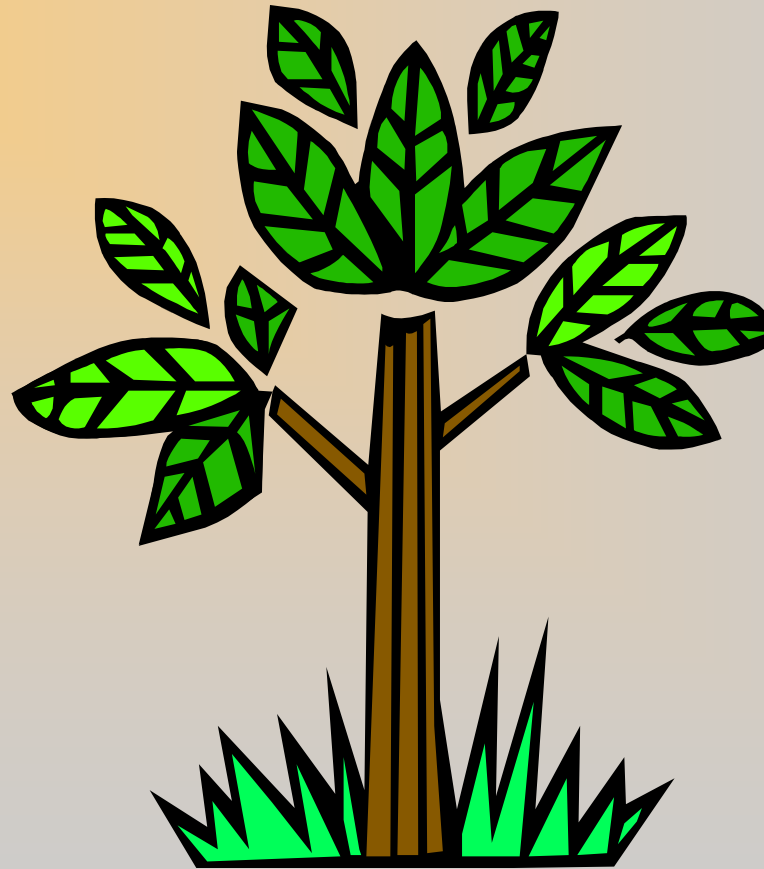


CONCLUSION

- ★ Nature of agricultural production and financial returns are such that interest rates and loan tenures cannot be similar to those of microenterprises. To take care of this feature agriculture requires second-tier refinance facilities
- ★ To ensure implementation of reform processes, to innovate policies and technologies and provide wholesale refinance, developing countries require financially strong and professionally managed apex development finance institutions like NABARD



THANK YOU



11 December 2007

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