

A PILOT STUDY ON THE SOURCES OF AGRICULTURAL FINANCE AND THE CHALLENGES ENCOUNTERED BY FARMERS

Dr. Umesh Gupta

Professor & Head, Mats School of Business Studies, MATS University, Pandri, Raipur,
(C.G.)

Abstract: *This paper examines the role of agricultural finance in India's rural economy, emphasizing its importance in supporting farmers with production, processing, and marketing activities [1]. It identifies the challenges farmers face in accessing finance, particularly smallholders, such as high risks, lack of collateral, and limited cooperation among stakeholders. The complex and unpredictable nature of agriculture makes it difficult for farmers to secure loans from formal financial institutions. Despite efforts to improve accessibility, issues like complicated loan procedures, inadequate infrastructure, and misuse of loans persist. Institutional sources such as cooperative societies, regional rural banks, and commercial banks play a significant role in supporting farmers, yet non-institutional sources like moneylenders and traders still dominate, often imposing high-interest rates that exacerbate farmers' financial struggles. The paper proposes several recommendations to address these challenges, including enhancing institutional lending, reducing regional imbalances, and offering consumption loans. Additionally, fostering better coordination among credit agencies, improving loan monitoring, and involving small farmers in decision-making processes are essential steps. By modernizing the agricultural finance system, India can ensure sustainable financial support for farmers, promoting agricultural growth and overall economic development [2]. Ultimately, a more inclusive and efficient agricultural finance system can enhance the economic well-being of farmers and contribute to the country's rural economy.*

Keywords: *moneylenders, loan procedures, collateral, financial support, cooperative societies.*

1. Introduction

Agricultural finance plays a crucial role in supporting India's rural economy, providing farmers with the necessary funds for various agricultural activities such as production, processing, and marketing. However, farmers, particularly smallholders, face significant challenges in accessing financial support [3]. These challenges include high risks associated with agriculture, lack of collateral, and limited cooperation among stakeholders in the financial system. The unpredictable and complex nature of agricultural activities makes it difficult for farmers to secure loans from formal financial institutions. While government and financial institutions have made efforts to improve accessibility to credit, issues such as complicated loan procedures, inadequate infrastructure, and misuse of loans continue to hinder progress. Institutional sources of agricultural finance, including cooperative societies, regional rural banks, and commercial banks, play an important role in providing financial support. However, non-institutional sources, such as moneylenders and traders, remain dominant in many areas, often charging exorbitant interest rates that further strain farmers' financial well-being. This paper explores these challenges and proposes recommendations to improve the agricultural finance landscape, including enhancing institutional lending, reducing regional imbalances, and introducing consumption loans [4]. By modernizing the agricultural finance system and ensuring more inclusive financial support, India can foster agricultural growth and contribute to the overall development of its rural economy.

2. Literature Review

Agricultural finance is essential for the economic stability and growth of rural areas, particularly in developing countries like India. Farmers rely on various sources of finance to support agricultural activities, including institutional and non-institutional credit [7, 3, 9]. However, accessing adequate financial resources remains a challenge, especially for smallholders. This literature review examines existing studies on the sources of agricultural finance and the obstacles farmers face, including high risks, collateral requirements, complicated loan procedures, and limited access to formal financial institutions [11]. It also explores potential solutions to improve accessibility and efficiency in agricultural financing.

Summary of Literature Review

Author(s)	Work Done	Findings
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Ang & van Passel (2017)	Decomposed the Luenberger–Hicks–Moorsteen productivity indicator for U.S. agriculture.	Showed productivity changes in U.S. agriculture and identified efficiency and technological advancements as key drivers.
Aparicio et al. (2018)	Analyzed productivity changes in public education during economic crises using Hicks-Moorsteen indices.	Economic crises negatively impacted public education productivity, highlighting the need for targeted policy interventions.
Bachewe et al. (2018)	Assessed agricultural transformation in Ethiopia.	Identified progress in agricultural productivity but highlighted challenges in input access and market connectivity.
Beck et al. (2007)	Studied the relationship between finance, inequality, and poverty.	Found that financial development reduces inequality and benefits the poor by improving access to credit and economic opportunities.
Blundell et al. (2016)	Investigated female labor supply, human capital, and welfare reform.	Welfare reforms significantly influenced female labor supply and human capital investment, improving socioeconomic conditions.
Gong & Ruan (2018)	Explored the effects of agricultural reforms in China from 1978 to 2015.	Demonstrated increased productivity due to reforms, particularly in provincial agricultural production functions.
Huang et al. (2017)	Examined the impact of modernization and globalization on Chinese smallholder farmers.	Modernization and globalization have positively affected smallholder farmers, but challenges like market access and technology adoption remain.
Kumar & Choudhary (2018)	Investigated institutional versus non-institutional sources of agricultural finance.	Institutional sources provide structured and lower-interest loans, while non-institutional sources dominate due to easy accessibility.
Sinha & Mehra (2018)	Studied the impact of non-institutional finance on rural development.	Non-institutional finance supports immediate financial needs but often leads to debt traps due to high-interest rates.

Verma & Sharma (2017)	Reviewed challenges in agricultural financing in rural India.	Identified issues like inadequate formal credit access, high dependency on informal lenders, and lack of financial literacy among farmers.
Jain & Kumar (2017)	Analyzed the role of cooperative banks in agricultural financing in India.	Cooperative banks play a crucial role in supporting small farmers but face operational inefficiencies and lack of sufficient funds.
Kumari & Sahoo (2016)	Evaluated the impact of agricultural finance on farmers' productivity in rural India.	Agricultural finance significantly enhances productivity, but small farmers often face barriers in accessing institutional credit.
Rai & Prasad (2016)	Assessed rural credit sources and farmers' access to finance.	Formal credit sources are limited for small farmers, leading to reliance on non-institutional lenders who charge exorbitant interest rates.
Patel & Soni (2016)	Discussed challenges in financing small farmers in rural India.	Small farmers struggle due to high collateral requirements, lack of financial literacy, and limited formal financial infrastructure in rural areas.
Das & Singh (2016)	Analyzed the effects of non-institutional lending on smallholder farmers.	Non-institutional lending leads to debt cycles and hinders long-term financial stability among smallholder farmers.

Research Gap

Despite the critical role of agricultural finance in India's rural economy, significant gaps remain in understanding the accessibility and effectiveness of financial support for farmers. Existing literature focuses on institutional sources of finance, but there is limited exploration of the effectiveness of non-institutional sources, such as moneylenders, and their impact on farmers' financial well-being. Additionally, studies often overlook the role of financial literacy, regional disparities, and the participation of smallholders in decision-making processes. Further research is needed to address these issues comprehensively.

3. Problem Statement

Farmers, particularly smallholders, face significant challenges in accessing agricultural finance in India due to high risks, lack of collateral, and inadequate institutional support. Despite efforts to improve accessibility, issues like complicated loan procedures and reliance on exploitative non-institutional sources persist.

4. Methodology

This paper utilizes secondary data sources along with primary data gathered through questionnaires.

Scope of Agricultural Finance: Agricultural finance involves the funding of activities related to agriculture, spanning from production to market. While not all agricultural finance is rural, and not all rural finance is agricultural, financial service providers often offer rural, micro, or agricultural finance with overlapping objectives and opportunities [5]. Agricultural finance refers to the financial resources farmers require for their day-to-day farming activities, including purchasing fertilizers, seeds, pesticides, farm implements, tractors, pipelines, and other essential equipment.

Features of Agricultural Finance: The unique features of agricultural financing are outlined below:

Risks in Agriculture: Predicting risks and uncertainties in agriculture is particularly challenging. Farmers face numerous risks, such as droughts, floods, and other natural disasters, all of which can lead to significant losses [6]. Additionally, agricultural produce often deteriorates due to the lack of suitable storage facilities when supply exceeds demand, further complicating the situation. The unpredictability and numerous unknowns make agriculture a difficult industry for commercial banks and insurance firms to manage.

Challenges in Cooperation: Cooperation within the agricultural sector is limited. Farmers tend to be individualistic and often distrust collaboration, making it harder for them to access affordable borrowing options.

Economic Delays in Agriculture: There is a considerable lag between effort and reward in agriculture, particularly when costs are incurred before any returns are realized. The demand for agricultural products can fluctuate during this period, disrupting farmers' financial arrangements. This uncertainty further complicates the financial landscape for farmers, providing justification for credit institutions to withhold financing for farm activities.

Credit for Consumption: Indian farmers often require credit not just for production, but also for consumption. Small farmers, in particular, need financing in the event of crop failure to meet their personal consumption needs. Furthermore, farmers frequently overspend on social and religious events, adding to their financial strain. Legal disputes also constitute a significant non-productive financial demand.

Small Farm Sizes: Indian farms are typically small in relation to the labor and capital invested. Moreover, the yield and quality of crops are highly unpredictable, leaving little security to offer as collateral for loans. This lack of collateral makes it difficult for small farmers to access credit from financial institutions [7].

Lack of Proper Security: While large farmers have sufficient resources to borrow from financial institutions, small farmers often struggle to secure credit to meet their financial needs. Small farmers often lack adequate collateral to secure loans, and they may not have the financial means to repay them. Consequently, they are often compelled to seek financial assistance from moneylenders.

The Complexity of the Agricultural Industry: Agriculture is a multifaceted industry, encompassing various types of production and marketing activities. The number of landholdings and the types of land tenure vary across regions, creating diverse and complex relationships among farmers [8]. These disparities make financing the agricultural sector a challenging task.

Sources of Agricultural Finance in India: Agriculture remains one of the largest sectors in India, employing a significant portion of the labor force and growing at 3.9% in 2021-22. Given the substantial number of people involved in agriculture or related sectors, agricultural finance plays a crucial role in supporting farming activities, as well as production, processing, and marketing of agricultural products. Agricultural finance in India can be broadly classified

into institutional and non-institutional sources. **Institutional sources** include organizations such as cooperatives, regional rural banks (RRBs), and scheduled commercial banks (SCBs). **Non-institutional sources** refer to financing provided by traders, moneylenders, agents, landlords, or even family members.

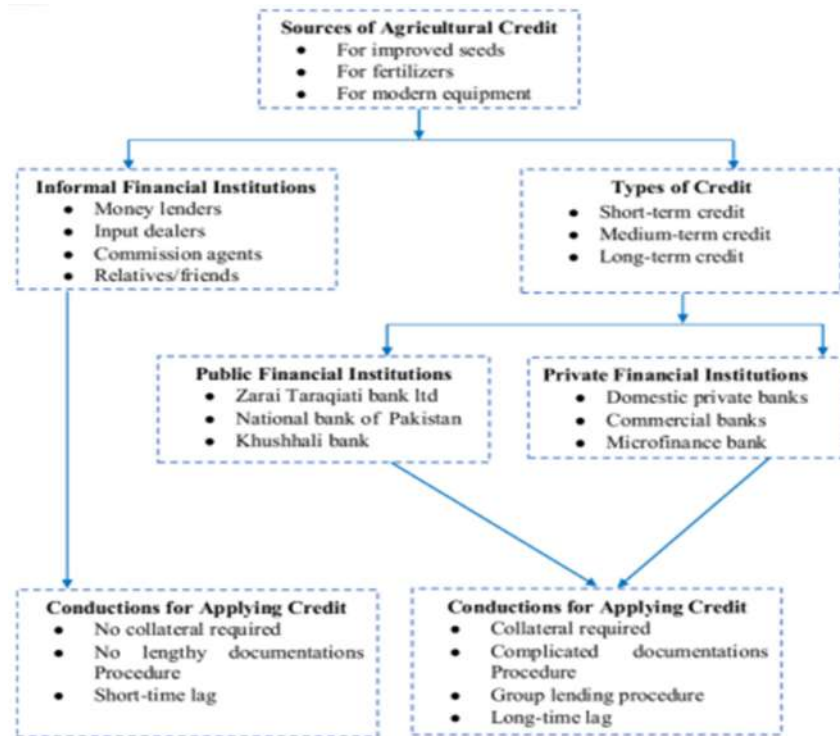


Figure 1 Rural financial services provided by format and informal source

5. Result & Discussion

Institutional Sources of Agricultural Finance in India

1. **Co-operative Societies:** Co-operative societies offer some of the most affordable loans for agriculture and related activities. Primary Agricultural Co-operative Societies (PACS) are among the oldest institutions for agricultural finance in India, providing short- and medium-term loans for farming activities [9]. Long-term loans are offered by Primary Co-operative Agriculture and Rural Development Banks (PCARDBs), while State Co-operative Agriculture and Rural Development Banks (SCARDBs) also provide long-term financing.

2. **Land Development Banks:** Land Development Banks, also known as land mortgage banks, are another key source of agricultural finance in India. These banks are registered under the Co-operative Societies Act, and in certain states, they are referred to as Agricultural and Rural Development Banks (ARDBs). They provide long-term loans secured by land as collateral.
3. **Commercial Banks:** In addition to co-operative societies, commercial banks play an important role in financing agriculture. Scheduled commercial banks offer loans to farmers for purchasing agricultural equipment, covering post-harvest costs, and supporting dairy and fisheries activities. These banks also provide Kisan Credit Cards, which allow farmers to withdraw cash at ATMs. Introduced in 1998, the Kisan Credit Card scheme facilitates easy access to credit for farmers.
4. **Regional Rural Banks:** Regional Rural Banks (RRBs) are another critical source of agricultural finance. These government-owned banks were established following the recommendations of the Narasimhan Working Group in 1975 and the enactment of the Regional Rural Banks Act, 1976. RRBs are designed to cater to the financial needs of farmers in rural areas.
5. **Microfinance:** Microfinance offers an alternative to traditional banking for farmers who lack access to credit from banks or do not have sufficient collateral. Microfinance involves the provision of small, collateral-free loans through Microfinance Institutions (MFIs), which help farmers in need of financial support [10].
6. **Non-Banking Financial Companies (NBFCs):** Non-Banking Financial Companies (NBFCs) are another significant source of agricultural finance in India. NBFCs, often supported by online and app-based platforms, extend banking and credit services to farmers who are excluded from mainstream banking. These institutions provide financial services tailored to the needs of underserved farmers.

Non-institutional Sources of Agricultural Finance in India: Non-institutional sources of agricultural finance in India include moneylenders, family and friends, traders, landlords, and commission agents.

1. **Moneylenders, Agents, Traders, and Landlords:** For decades, moneylenders have played a significant role in providing credit to agricultural families in India's rural

areas. However, the interest rates charged by moneylenders are often exorbitant, pushing many families into a cycle of debt. Similarly, landlords also impose high interest rates, which are often unsustainable. Commission agents or traders also offer financial assistance to farmers, but their interest rates tend to be higher compared to institutional sources of finance. An alternative to these high-interest loans is to explore small business loans with more favorable rates, available through platforms like Bajaj MARKETS, offering hassle-free online access.

2. **Relatives and Friends:** While relatives and friends can provide support in times of financial emergencies, they are not a reliable, long-term solution. Given the critical role of agriculture in India's economy, securing farm credit is vital for adopting best practices and boosting production [11]. Non-institutional sources of finance have been available for years, but their high-interest rates and lack of proper documentation pose challenges. However, new loan products offered by NBFCs, backed by technology, have increased farmers' access to institutional credit. With flexible repayment options and no collateral required, platforms like Bajaj MARKETS offer affordable loans that help bridge this gap.

Challenges in Agricultural Finance: Despite efforts by the government to enhance loan availability in agriculture, several challenges persist:

1. **Complicated Loan Procedures:** Obtaining credit can be cumbersome due to complex requirements. Many farmers, especially those who are uneducated, struggle to provide the necessary documentation. As a result, they often turn to moneylenders for quicker loans, even though the interest rates are higher. Additionally, the time taken between submitting a loan application and receiving approval further discourages farmers from seeking institutional finance.
2. **Wastage of Time and Manpower:** Financial institutions, including commercial banks and state co-operative banks, are mostly located in urban areas, requiring farmers to travel multiple times to complete the loan process [12]. This results in unnecessary time and manpower expenditure.
3. **Lack of Coordination:** A lack of coordination between cooperatives and commercial banks in credit planning leads to unequal distribution of funds. Areas with robust credit structures receive ample funding, while regions with limited credit availability

continue to suffer. This disparity contributes to low agricultural yields and cultivator poverty.

4. **Improper Utilization of Loans:** Another issue is the mismanagement of loans by farmers, who sometimes use them for non-productive purposes. This misuse worsens the financial situation, undermining the goal of supporting agricultural productivity.
5. **Inefficient Administration:** Cooperatives and commercial banks often suffer from poor administration, which results in inefficiency and corruption. These organizations frequently fail to serve the farming community effectively, focusing more on personal gains rather than the welfare of farmers.
6. **Mounting Overdues:** The agricultural sector has seen an increase in overdue payments, partly due to the economic slowdown. This has set an unfavorable precedent, further hindering future agricultural development. Loan cancellation efforts must be taken seriously to avoid worsening the situation.
7. **No Provision of Consumption Loans:** Due to the seasonal nature of farm income, farmers require loans not only for production but also for purchasing durable goods. Unfortunately, this facility is mostly available in urban areas, forcing farmers to borrow from moneylenders, who exploit them with high-interest rates.
8. **Low Contribution to Development:** Agriculture's low productivity has resulted in a minimal share in overall economic development. Limited adoption of modern technologies has also hindered growth. Commercial banks tend to favor industrial and trade investments over agriculture, leaving wealthy farmers to benefit disproportionately from available loans. Poor farmers continue to rely on unscrupulous moneylenders, and cooperative loan disbursements are often skewed in favor of the affluent.
9. **Lack of Rural Savings:** Rural savings in India are insufficient to meet the demand for credit in rural areas. This necessitates the mobilization of external financing sources. However, rather than focusing on mobilizing rural savings, efforts should aim at making them feasible and accessible.
10. **Prevalence of Private Agencies:** The role of private agencies in providing rural finance remains dominant, but there is a need to replace them with more formal sources of credit. While institutional credit can be either private or public, continuing to rely on professional moneylenders as the primary source of rural finance will not address the challenges effectively.

Suggestions to Improve Agricultural Finance: Enhancing institutional lending to the agricultural sector and modernizing the system is crucial for fostering growth. The following recommendations can help improve agricultural finance:

1. **Repayment of Loans:** The government must take decisive action to facilitate suitable repayment facilities and provide necessary support to institutional credit agencies in recovering loans. This would allow credit institutions to extend additional loans to farmers, ensuring a more sustainable credit cycle.
2. **Reduction in Regional Imbalance:** To address disparities between rural and urban areas, it is essential to establish more bank branches in rural regions. Additionally, banks should prioritize lending to small and marginal farmers at lower interest rates to ensure equitable access to financial resources.
3. **Provision of Consumption Loans:** To protect rural residents from exploitation by moneylenders, cooperatives and commercial banks should offer consumption loans. Once freed from the oppressive practices of moneylenders, farmers will be more likely to sell their produce at market prices, thereby improving their farm income.
4. **Coordination of Credit Agencies:** Efforts must be made to improve coordination between cooperative societies and commercial banks. By working together, these institutions can more effectively meet the needs of the rural agricultural community. This collaboration could also encourage farmers to adopt modern and sustainable agricultural technologies.
5. **Proper Utilization of Loans:** To ensure loans are used effectively and contribute to increased crop productivity, each financial institution should establish a dedicated unit to monitor the proper utilization of loans [13]. This unit should closely oversee the loans to ensure they are used for their intended agricultural purposes, helping to maximize the impact of the financial support.

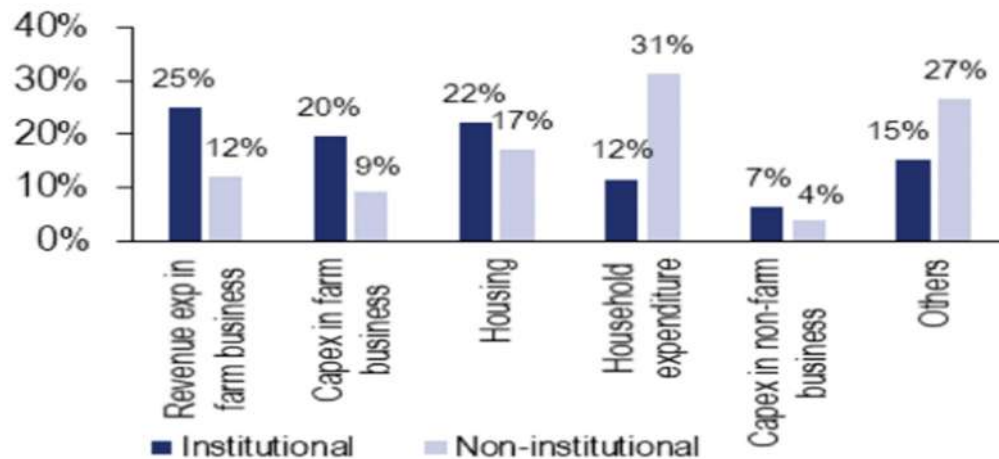


Fig 2 Purpose of Agriculture loan

Sources: All India Debt and Investment Survey 2019; PRS.

Suggestions to Improve Agricultural Finance: Enhancing institutional lending and modernizing the agricultural finance sector are critical for its growth and sustainability. The following suggestions are put forward to address these needs:

1. **Repayment of Loans:** The government should take robust measures to ensure suitable repayment facilities are available and extend the necessary support to institutional credit agencies in recovering loans. This will enable credit institutions to provide additional loans to farmers, promoting financial continuity.
2. **Reduction in Regional Imbalance:** To bridge the gap between rural and urban areas, new bank branches should be established in rural locations. Additionally, banks should be encouraged to offer loans primarily to small and marginal farmers at reduced interest rates, ensuring equitable access to financial resources.
3. **Provision of Consumption Loans:** To protect rural communities from the exploitation of moneylenders, cooperatives and commercial banks should step in to provide consumption loans [14] Once farmers are free from the manipulative practices of moneylenders, they will be more inclined to sell their produce at fair market prices, thereby boosting their income.
4. **Coordination of Credit Agencies:** Efforts must be made to better coordinate the activities of various cooperative societies and commercial banks. Through such collaboration, these institutions can more effectively serve the needs of the rural

agricultural community, encouraging farmers to adopt advanced agricultural technologies and practices.

5. **Proper Utilization of Loans:** To enhance crop productivity, financial institutions should establish dedicated units to ensure loans are used appropriately. These units should closely monitor the usage of loans to ensure they are invested in productive agricultural activities, leading to higher returns and more efficient farming.
6. **Suitable Representation of Farmers:** Small and marginal farmers should be better represented in the management of cooperative institutions. Having these farmers actively involved in decision-making will foster greater responsibility and ensure that the loans and financial products offered align with the needs of their community.



Fig 3 Flow of institutional credit available by agricultural sector (in Rs lakh crore)

Sources: Agricultural Statistics at a Glance (2021); PRS.

6. Conclusion

In conclusion, Agricultural finance is a critical component of India's rural economy, addressing the financial needs of farmers for various agricultural activities, including production, processing, and marketing. This paper highlights the challenges faced by farmers in accessing finance, such as high risks, lack of collateral, and limited cooperation among stakeholders. The complex and unpredictable nature of agriculture makes it difficult for farmers, particularly smallholders, to secure loans from formal financial institutions. Despite efforts by the government and financial institutions to enhance accessibility, issues such as complicated loan procedures, inadequate infrastructure, and misuse of loans remain prevalent. Institutional sources of agricultural finance, including cooperative societies,

regional rural banks, and commercial banks, play a significant role in providing financial support. However, non-institutional sources like moneylenders and traders continue to dominate, particularly in areas where institutional credit is limited or inaccessible. These sources, while providing immediate relief, often impose exorbitant interest rates, exacerbating the financial challenges faced by farmers. To improve the agricultural finance landscape, several recommendations are proposed. Enhancing institutional lending, reducing regional imbalances, and offering consumption loans are crucial to ensure equitable access to finance. Moreover, fostering better coordination among credit agencies and monitoring the proper utilization of loans can help boost agricultural productivity. The active involvement of small farmers in the decision-making processes of cooperative institutions is also essential for ensuring that financial products are tailored to their needs and used effectively. Ultimately, by modernizing the agricultural finance system and addressing the systemic challenges, India can provide sustainable financial support to farmers, fostering growth in the agricultural sector and contributing to the overall economic development.

Future Scope

- Ensure adequate credit facilities and infrastructure support for underserved regions.
- Promote financial education to help farmers understand loan terms and manage funds effectively.
- Develop specialized financial products, such as consumption loans with flexible terms, for small farmers.
- Utilize digital platforms and fintech solutions to improve financial inclusion in remote areas.

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