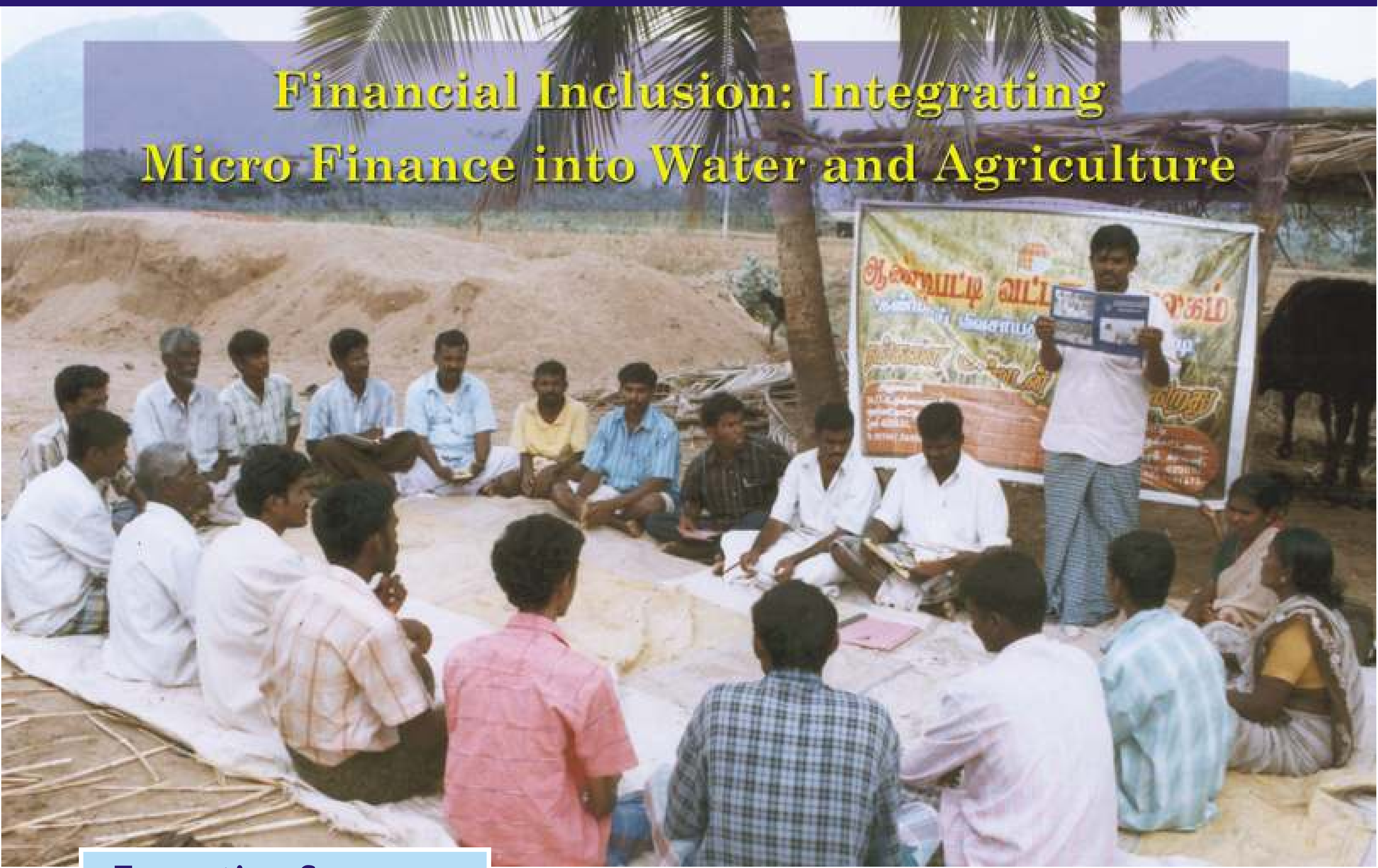
Policy Brief 2

Financial Inclusion: Integrating Micro Finance into Water and Agriculture



MFG meeting at Bodidasanpatti village, Andipatti Block, Theni District

Executive Summary

DHAN's experience in Integrating Micro Finance into Water and Agriculture

Micro Finance has emerged as a successful tool in alleviating rural poverty. Access to Micro Finance services helps the poor to expand their choices for livelihood opportunities and improve the quality of their life. The Self-Help Group–Bank Linkage programme pioneered by the National Bank for Agriculture and Rural Development (NABARD) and the contribution by Small Industries Development Bank of India (SIDBI) has accelerated and strengthened the Micro Finance movement in our Country. Micro Finance has had positive impacts on the poor such as (i) organising the unorganised and making SHG as a movement (ii) weaning them away from money lenders who were charging usurious interest (iii) facilitating the poor to diversify their livelihood options and (iv) addressing developmental issues. There is scope for further development by integrating Micro Finance into various sub-sectors such as Water Conservation, Agriculture, Coastal Zone Management,

Information and Communication Technology (ICT), Health, Education etc.

DHAN foundation has fourteen years of grassroots experience in rehabilitation of minor irrigation tanks and ponds through people-led water security movement called 'Vayalagam'. The Vayalagam programme focuses on conservation and development of water resources; it includes rehabilitation of minor irrigation tanks, water management for agricultural production, fish culture and other livelihood interventions. In order to diversify and sustain the activities of the Vayalagam movement, it introduced savings and credit component through Micro Finance Group (MFG) among the members of Vayalagam. MFG is the concept of Self-Help Groups, which are farm based including small farmers, marginal farmers and landless agricultural labourers. This paves a platform for proper maintenance of tanks besides enabling the members to pursue other income generating activities for their livelihood. Promotion of MFG encourages the weaker sections of society such as small, marginal and landless farmers to get engaged in livelihood activities, generated through timely support of credit for agricultural operations.

DHAN's experience in Micro Finance over a decade necessitates the integration of Micro Finance activities with various sectors and sub-sectors. Presently, 1634 MFGs are functional with 25,787 members, of whom 30 percent comprise landless women and agricultural labourers. The average size of a Vayalagam group is 14 members. The average monthly savings of the members range from Rs. 25 to Rs. 100 according to their earning capacity. These MFGs have been linked with Micro Finance Institutions such as Kalanjiam Development Financial Services (KDFS) a section 25 NBFC and Nationalised and Regional Rural Banks.

MFGs facilitate members to avail credit for infrastructure creation like farm pond and group loans for construction of drinking water ponds. An encouraging aspect of MFGs is the repayment of loans to the extent of 98 percent and above.

MFGs also help to reduce the input cost to the farmers by providing quality seeds, seedlings and fertilizers produced/undertaken by their own federations.

In mitigating the risks related to drought, several infrastructure facilities like farm ponds and check dams are constructed with funds from NWDPRA, NABARD, NOVIB, WDF and ITC. Under the NWDPRA scheme, agriculture related activities like soil testing, organic farming, fodder cultivation, procurement of fertilizers; agroforestry and dryland horticulture are being promoted. Apart from this, Life Insurance to farmers has also been covered in MFGs through farmers' federations, with support from insurance companies.

Salient outcome of DHAN's experience through MFGs are presented below:

- Micro Finance Group formation (Farm based Self-Help Groups) is the best tool for the sustainability of the institutions promoted around small-scale water bodies.
- Participation level of the members is very high in planning, implementation and monitoring of the works.
- The Micro Finance activity keeps the members as a cohesive group to have a shared understanding among them. This helps them to resolve most of the conflicts related to water sharing.
- MFGs are capable of undertaking the repair, renovation and management of water bodies.
- This group acts as a common forum to update the knowledge on water management and information sharing on agricultural techniques.
- It involves landless farmers in decision-making.
- It ensures the availability of common fund for maintenance of small-scale water bodies.
- It helps to increase the economic status of the members.

There is tremendous potential for integrating Micro Finance with Water and Agriculture. For smooth integration, it requires suitable amendments to the existing policy framework on

Micro Finance and Agriculture sectors. DHAN Organised a one-day policy seminar to share its field experience with experts from various fields relating to Micro Finance and Agriculture on January 30, 2006 at MSSRF, Chennai. This policy brief includes the outcome of the policy seminar and also other research inputs.

This brief proposes the following recommendations to Reserve Bank of India (RBI), National Bank for Agriculture and Rural Development (NABARD), Commercial Banks and Agriculture Department. The recommendations are

- Commercial Banks and NABARD should come up with support to bankable projects like renovation and maintenance of small-scale water bodies. There is a huge requirement of soft loan with low interest rate to farmers. Long-term projects should be designed for farmers by the Commercial Banks. Policy direction and Operational details in this regard may be prepared and monitored by RBI.
- Rate of interest to farm loans through Self-Help Groups (SHGs) or Farmers' Micro Finance Groups should be lower than housing loans to ensure farmer's livelihood.
- To promote Micro Finance activities and to develop agriculture and small-scale water bodies, incentives to community organisations such as Farmers' federations and SHGs federations are needed from NABARD and State Government as promotional grants.

Summary of suggested changes in policies and practices in Micro Finance and Agricultural Sectors of Financial Institutions and Government Departments

Existing policies/guidelines and practices	Policy/Practice changes required
1. Reserve Bank of India	
Lending to SHGs as part of banks' lending to the weaker sections under priority sector. At present the usual practice is to give priority to women SHGs involved in farm and non-farm based activities. 90 percent of SHGs are exclusively women SHGs.	Equal importance and thrust have to be given to extend credit facilities through commercial banking institutions to the farmers (small and marginal), landless labour men groups and other groups from weaker sections of the society, involved in Micro Finance for agriculture and allied activities. Recognition of farmers men group (MFGs) under weaker sections will provide a wide range of opportunities to effectively deliver credit to the needy people.
Rate of interest to SHGs from Commercial Banks and RRBs is ranging from 9 percent to 11.5 percent.	The interest on farm loans to SHGs, MFGs as a group loan should be favourably considered, which has to be lower than housing loan.
The current credit delivery mechanism allocates 18 percent of Net Banking Credit (NBC) to Agriculture lending. But in practice it has been only upto 11.5 percent during the years 1995 to 2004.	The 18 percent allocation of NBC has to be strictly adhered to agriculture lending. The demand for agriculture credit is much higher than

Existing policies/guidelines and practices	Policy/Practice changes required
	what is granted. According to Tenth Five-Year Plan working group on Agriculture credit, less than 50 percent of the requirement has been provided towards credit to the farmers. Out of 40 percent of NBC for priority sector, the percentage for weaker sections under Micro Finance should be at least 25 percent instead of 10 percent.
Commercial Banks have to lend 10 percent of NBC to weaker sections but it has delivered only around seven percent.	Existing share of 10 percent allotted for the weaker sections has to be delivered strictly by the Commercial Banks under priority sector lending to meet the entire demand.
2. NABARD	
NABARD Rural Infrastructure Development Fund (RIDF) is expected to improve the credit absorption capacity in the areas concerned and provide the infrastructural support for agriculture production and development. Various activities under RIDF such as watershed development and minor irrigation projects have been included under Tranche RIDF IX and are executed through State Departments.	NABARD should be encouraged to support implementation of farm-based infrastructure only through farmers' groups recognised by the agencies supported under RIDF.
	Requisite capital support should be given to farmers' groups for pilot experimentation to collectively procure and market the farm produce. Infrastructure development credit should be supported along with suitable social security measures (similar to SBI Life Insurance for Home Loan).
3. Government of India, Rural Development Department	
Government of India–SGSY scheme: The SGSY guideline Para 1.7 and Para 1.8 stress and recommend the importance of irrigation facilities for increasing the irrigated area and project approach under micro irrigation.	Allocation of subsidy component for common property works such as those connected with minor irrigation tanks should be incorporated in the group economic assistance linkage also.

Existing policies/guidelines and practices	Policy/Practice changes required
Para 1.10 deals with the recommendation of consultation process for selection of important activities for assistance.	As per para 1.10 farmer groups should be included in the consultation process at district level (SGSY) consultation committee and block level committee for identification of activities in agriculture and allied areas.
National Rural Employment Guarantee Assistance (NREGA) scheme provides for taking up priority works in new ponds, renovation of existing ponds, ooranis, desilting of channels and irrigation tanks.	Gram Panchayat may suggest need based priorities and also prioritise ponds, ooranis renovation works under NREGA scheme that would ensure the benefits to poor, landless and farmers.
4. Commercial Banks	
Under the priority sector lending, SHGs are recognised by banks for lending to the weaker sections. Over 90 percent of SHGs are exclusive women groups.	Provide eligibility status to the small and marginal farmers including landless labourers having prudential track record in MF activity similar to SHG women members. Commercial Banks have to pitch in and facilitate MFGs to open bank account and provide linkage to sustain their economic development activities.
Out of the overall percentage of 40 percent for priority sector, only 10 percent is allocated to weaker sections. But the public and private sector banks deliver only around 7 percent and 1.4 percent, respectively.	Commercial Banks (Public and Private sectors) should strictly follow the stipulated target allotted for the weaker sections under priority sector lending.
	Commercial Banks should develop innovative loan products and joint experimentations with NGOs/ Federation of MFGs to provide marketing support to the farmers, e.g. regulated online credit to SHGs and MFGs. Venture capital funding is available to federation of MFGs for marketing. Projects like Oorani and drinking water pond development with community participation also needs to be brought under new loan scheme just like venture funding.

Existing policies/guidelines and practices	Policy/Practice changes required
Commercial Banks have realised the importance of the social capital, i.e. investing in promoting and nurturing SHGs by NGOs/ federation of SHGs/Civil society organisations. A few banks have started providing grant assistance to NGOs for this purpose.	Commercial Banks may consider allocation of some specific percentage of their profit to NGOs and CBOs for promotion and monitoring of SHGs and MFGs for farmers.
SHG loan document papers are designed and followed in accordance with individual bank's needs.	Uniformity of loan document in all banks would help the farmers to approach any bank.
5. Regional Rural Banks (RRBs)	
RRBs have strong rural branch infrastructure and rural orientation of the staff. RRBs are expected to primarily cover small and marginal farmers and landless labourers. The market share of RRBs in rural credit has remained at 8–9 percent right from their inception.	Strategic attention of RRBs is required to serve the credit needs of small farmers. RRBs should pay attention to serve the credit needs of small farmers also.
6. Primary Agriculture Co-operative Societies (PACS)	
Reform process has to be carried out for PACS based on the recommendations of Dr. Vaidyanathan committee.	After the reform process is undertaken based on the recommendations of Dr. Vaidyanathan committee, PACs should be involved in a big way to grant farm loans to farmers through farmers' groups.
7. Tamil Nadu State Rural Development Department	
SGSY scheme facilitates organisation of the poor into SHGs and provides credit linkage with financial institutions for economic improvement, infrastructure and marketing support.	Facilitation to form Micro Finance Groups among small and marginal farmers, landless labourers and women for economic assistance is required with revolving fund support.
Provision exists for implementation of special SGSY projects.	Specific provision is required to include common property works such as rehabilitation of tanks and ooranis under special SGSY projects.

Existing policies/guidelines and practices	Policy/Practice changes required
National Rural Employment Guarantee Assistance (NREGA) scheme provides assistance as per the priority works being taken up in new ponds, renovation of existing ponds, Ooranis, desilting of channels and irrigation tanks.	Gram Panchayat should ensure that benefits reach the poor and landless labourers by prioritising ponds, Ooranis' works under NREGA scheme.
8. Tamil Nadu State Agriculture Department	
Focus is given on formation of Farmers' interest groups and provision of technical information and other details like inputs, price, market situation and assistance for office automation and provision for Library.	The focus of farmers' interest groups should be widened to include Micro Finance functions, tank renovation and integrating innovative development products through appropriate capacity building and extension activities by Agricultural Department.
9. Academic Institutions	
No policy/practice exists to support activities that are bankable under MF programmes.	Specific provision is required to scientifically support MF activities that are bankable. Institutions of higher learning and advanced studies like IIT, IIM and School of Economics should be encouraged to take up studies to scientifically identify activities that are bankable under Micro Finance activities. These institutions should provide technical support to banks.

This brief proposes further Policy/Practice changes through process mechanisms among RBI, NABARD, Commercial Banks, State Departments, Academic Institutions and NGOs.

Policy Seminar on Integrating Micro Finance into Water and Agriculture at MSSRF, Chennai

Integrating Micro Finance into Water and Agriculture

I. Introduction

Tanks are an important source of irrigation in India, particularly South India. It covers about 17.65 percent of Net Irrigated Area (NIA). The total number of minor irrigation tanks in India accounts for about 465,355 of which many of them are in bad condition due to various reasons. But efforts are under way to restore them. DHAN foundation a pro-poor development organisation, working on poverty alleviation, has fourteen years of grassroots experience in rehabilitation of minor irrigation tanks and ponds through people-led water security movement called 'Vayalagam'. Vayalagam Tankfed Agricultural Programme (VTAP) of DHAN promotes community based nested institutions such as Vayalagam Water Users' Associations (WUA), Cascade Associations (CA) and Tank Federations (TF). So far, 1103 WUAs have been formed with 94,837 members comprising small and marginal farmers and landless labourers. The Vayalagam programme focuses on conservation and developmental works; it includes desilting of small and minor irrigation tanks, agricultural production, foreshore plantations and other livelihood interventions. In order to diversify and sustain the activities of the Vayalagam movement, it introduces Micro Finance component through Micro Finance Group (MFG) among the members of Vayalagam. This ensures proper maintenance of tanks and allows the members to pursue other income generating activities for their livelihood. Financial inclusion in agriculture takes care of livelihood needs in the rainfall scarce years. Promotion of MFG encourages small, marginal and landless farmers to go for livelihood activities through timely support of credit for agricultural operations. As such, the weaker sections of the society get benefitted.

II. Micro Finance & sub Sectoral Issues

Micro Finance has emerged as a successful tool in alleviating the rural poverty since mid 1980s. Access to Micro Finance services helps the poor to expand their choices for livelihood opportunities and improve their life. Micro Finance programmes in India are quite distinct in terms of perspective and also mechanism of delivery. Of late, India chose to advance the development perspectives through Micro Finance programmes rather than focusing on financial delivery alone. The Self-Help Group–Bank linkage programme pioneered by the National Bank for Agriculture and Rural Development (NABARD) and the contribution by Small Industries Development Bank of India (SIDBI) accelerated and strengthened the Micro Finance movement in our Country. As of March 2006, the SHG Bank linkage programme is one of the largest Micro Finance programmes in the world with 22.38 lakh SHGs throughout the country, in which, 90 percent of the SHGs have women as members. Certainly, Micro Finance has made many positive impacts on the poor (i) organise the unorganised, making SHG as a movement (ii) weaning them away from money lenders who are charging usurious interest (iii) to help the poor to diversify their livelihood options and (iv) address developmental issues. The sincere efforts taken by formal financial system and NGOs in promoting Micro Finance have made a positive impact. There is further scope of opportunities in the field of Development in integrating Micro Finance into various sub-sectors such as Water Conservation, Agriculture, Coastal Zone Management, Information and Communication Technology (ICT), Health, Education etc.

Water and Agriculture sector impacts larger population, which includes mainly the small and marginal farmers and landless labourers, requiring the basic life supporting system. Small and marginal farmers require timely credit for the purchase of agricultural inputs like seeds, fertilizers, organic manures, etc. whereas the landless labourers require employment opportunities throughout the year for their livelihood. To meet out these demands they borrow from the moneylender/retailer. They have to pay exorbitant rate of interest to the moneylender or have to sell their produce to the retailer at their doorstep for distress price. This has raised several serious issues relating to the provision of financial services and support to the weaker sections in Agriculture and Employment.

III. DHAN's Experience in Integrating Micro Finance into Water and Agriculture

DHAN's experience in Micro Finance necessitates the integration of Micro Finance activities with various sectors and sub-sectors. Financial inclusion, a recent debate holds good for sustaining development interventions in rural area. Our experience showed that financial inclusion of the under privileged was a remarkable success.

Micro Finance activity for the members of Vayalagam was attempted as a new frontier experiment by the programme during 2000–01. In the five years of its evolution farmers got convinced that Micro Finance would ensure their livelihood sustainability in the long run. During the year 2006, the programme team in 35 locations promoted MFGs either as entry intervention or as an intervention to review old associations. Presently 1634 MFGs are functional with 25,787 members of whom 30 percent comprising landless women and agricultural labourers. The average size of Vayalagam group is 14 members. The average monthly savings of the members ranges from Rs. 25 to Rs. 100 each according to their earning capacity. These MFGs get linked with Kalanjiam Development Financial Services (KDFS) and Nationalised and Regional Rural Banks.

In addition to credit access, MFGs have yielded credit plus benefits to the hitherto neglected sections of the society. MFGs common fund has been used in many ways, for conservation and development purposes such as contribution for the work, paying wage for labourers in maintenance of water resources, etc. MFGs also facilitated members to avail credit for infrastructure creation like farm ponds, group loans for construction of drinking water ponds and ensured repayment of the fund to cascade association/federation. An encouraging aspect of MFGs is the recovery of loans to the extent of 98 percent and above. This provides an alternative to the conventional way of bank lending where the Non-Performing Assets (NPAs) keep accumulating.

1. The Micro Finance experiences in Vayalagam Agricultural Development Programme (VADP) and Rainfed Farming Development Programme (RFDT) of DHAN Foundation – Highlights

1.1 MFG Linkage: KDFS is a Non-Banking Finance Company (NBFC) promoted by DHAN Foundation to provide Bridge Funding and to demonstrate to the banking system that the poor are bankable. The fact that KDFS alone has provided a credit support of Rs. 30.2 million to 704 MFGs in the last one-year and the repayment performance of 100 percent amply proves this point.

1.2 Bank Linkage: Vayalagam Micro Finance groups are being used as a vehicle for agricultural development. Another successful attempt by DHAN paved the way for State Bank of India (SBI), Mothagam Branch in Madurai to deliver credit of Rs. 35,000 for two MFGs in Silarpatti micro watershed. This credit linkage from bank to group strengthens the peoples' institutions at various levels. It helped to get timely credit for agricultural operations and investments on land improvement to the farming community. Some of the MFGs are involved in bulk purchasing of quality seeds and quality agricultural inputs. Cottonseeds were distributed to the MFG members in Kurayur and Pannikundu watershed of the Madurai district. The MFG meetings are used as the venue for training in improved agricultural practices and technology transfer through demonstration. Most of the members are aware of the crop diversification alternatives like medicinal plants and other agricultural related activities like Backyard Poultry with Broiler Chicks, rearing Telicherry Goats, Coir making and Vermicomposting, which are done through the Micro Finance group members.

2. Farmer's collective for inputs and marketing

Collective effort through Virumaniyendal TFA demanded fertilizer for cotton crop as loan under MFG account. Ramanathapuram District Tank Farmers' Federation purchased the required quantity of fertilizer from neighbouring registered retail merchant and supplied at the doorsteps of farmers by fixing a uniform rate. Later, it purchased from FARM AID Services (Madurai), regional wholesale trader which was facilitated by DHAN Business Development Services (BDS). It helped to get the required quantity of fertilizers at a lower price than the market rate.

In Ramnad region, a pilot initiative of Paddy procurement by avoiding the middlemen was attempted with the support of DHAN BDS. Similarly the wild herbs collection from the foot hills of Alagar hills at Kesampatti and Pulipatti watershed area has been successfully undertaken.

3. Social Security

Reducing the risk and vulnerability of the Vayalagam members is one of the main interventions to reduce the poverty of the members. All MFGs follow a norm that all the members of the group should insure their life before credit linkages of the group with bank or any other financial institution.

To illustrate, 2246 members of MFGs have insured their life under Birla Sun Life Insurance and 386 members have insured their life under Janashree Bhima Yojana scheme. Theni district tank farmers' federation designed their own insurance product for members. Insurance claim will help the bereaved family immediately after the death of a member. Advanced federations like Kottampatti and Theni tank farmers' federation are maintaining insurance revolving fund of Rs. 10,000/-.

4. Farm Ponds

Farm pond constructed at the individual marginal field provided successful crop and vegetable cultivation in the farm owned by the farmer. Over 150 farm ponds have been constructed under schemes like NWDPRA, Novib drought, ITC, Tsunami Agriculture interventions and NABARD-WDF. These infrastructures helped to mitigate the risks related to rainfall during the rain deficit years and resulted in follow-up crop with residual soil moisture during the normal rainfall seasons. Lack of impact assessment as well as process document to holistically assess the results of agriculture interventions remain as a big handicap, in creating databases.

In NWDPRA scheme, MFGs have predominantly utilised the credit for farm production systems such as soil testing, organic farming, fodder cultivation, alternative livelihood measures (like providing Broiler hen, supply of goats, vegetable cultivation). Especially in Madurai region, farmers were provided 15 tonnes of seed and 30 tonnes of fertilizers in addition to providing 38 farm implements through MFGs. About 24,000 plants/seedlings were planted under agroforestry and dryland horticulture.

5. Other Activities

Community Nursery: Punganur Federation has taken a piece of land and a water body on lease basis (Rs. 10,000 per year) and seedlings, namely tomato, Chilli and Brinjal were grown; and 50,000 seedlings were distributed from this nursery to watershed members and non-members in the mandal. In Punganur, one Primary Producer Group has been formed for Tamarind processing by involving seven members. This group sold 650 Kg of Tamarind at Bangalore @ Rs. 32/kg. Moreover, the stocks have been stored in a cold storage, awaiting price rise or expecting peak demand. Punganur Mandal also distributed 252 bags of groundnut pods to 158 farmers along with Trichoderma viridi a biological material for seed treatment. Rupees three lakh worth NPK fertilizers have also been distributed.

In Chittoor region Jatropha (Bio-diesel) plant cultivation as demanded by DWMA has been undertaken by MFGs. In Punganur and Palamanur locations Jatropha seedlings were planted in 150 acres.

3.1 Case Studies

I. Case Study on on-lending Experience of Theni District Vayalagam Federation with Canara Bank in Tamil Nadu

i) By Canara Bank Intervention: Theni District Vayalagam Federation promoted by DHAN Foundation registered under Societies Act has been functioning in Theni District since 1998 with 112 Vayalagams and 118 MFGs. It covers 86 villages and 56 panchayats spread over seven blocks with a membership of 3350 small-scale farming and landless families. The federation is actively involved in tank renovation, water management and agricultural extension through micro financial activities. Initially none of the Commercial Banks came forward for the credit linkages because of the risk arising from the high rate of poor male members in the MFGs.

Kalanjiam Development Financial Services (KDFS) provided bridge loans of Rs. 5,000 to Rs. 50,000 to the Vayalagam MFGs to facilitate activities pertaining to water conservation and agricultural improvements. After seeing the repayment performances of the Vayalagam MFGs, Canara Bank provided Rs. 2.5 lakh and Rs. 10.00 lakh as first and second linkages and the bank understood the good impact on water conservation and improved agricultural operations.

Subsequently, Canara Bank provided loan facility to the federation and then the eligible Vayalagam MFGs were linked with the federation as on-lending process. The linkage particulars are given below:

(as on September 2005)

Sl. No.	Linkage particulars	No. of MFGs linked	No. of loans distributed	Total linkage amount (Rs.)
1	First linkage	9	47	2,50,000
2	Second linkage	27	189	10,00,000
	Total	**36**	**236**	**12,50,000**

ii) Leverage of on-lending: During the first linkage, the federation repaid to the bank whatever was received from the MFGs. But in the second linkage, the federation started revolving the loan amount with its member Vayalagams to meet their credit demand. After repaying the monthly demand to the bank, the remaining amount was distributed to the MFGs. The table below provides leverage details:

(as on September 2005)

Sl. No.	Linkage particulars	No. of MFGs linked	No. of loans distributed	Total linkage amount (Rs.)
1	MFGs linked first time	17	136	6,50,000
2	MFGs linked second time	7	73	2,20,000
	Total	**24**	**209**	**8,70,000**

iii) MFGs and Agriculture Development: It was found that 52 percent of the rural loan to the MFGs were utilised for preparation of land, input supply, labour wages, floriculture, horticulture and other agriculture based business. A total of 267 loans were provided to 60 MFGs across the district. This particular lending process helped the farmers to stop getting loans at higher interest outside. They could get quality inputs and could start cultivation at the right time, which gave them additional yield.

a. Five MFGs were allocated a sum of Rs. 94,600 to carry out rehabilitation of tanks and ponds and against this people's contribution, they could get grant for tank rehabilitation. The loan amount was shared by members and promptly repaid to the Canara Bank.

b. MFGs common fund can be diverted to improve common facilities such as cleaning of supply channel, repairing sluices and clearance of weeds etc. One MFG generated Rs. 12,300 by revolving Canara Bank loan on lending credit amount to their members by fixing interest spreads during their repayment. The MFG utilised this fund for cleaning the supply channel

iv) MFGs and other activities: Apart from the above agricultural activities, the MFGs have utilised the credit to create assets, development of small-scale businesses and to meet out their daily necessities of food, clothing, education, health care, up-gradation of houses and redemption of outside loans, which is given in the following table:

(as on September 2005)

Sl. No.	Purpose of the loan	No. of loans disbursed	Total linkage amount (Rs.)
1	Agricultural upliftment	267	9,72,600.00
2	Water conservation	5	1,06,900.00
3	Asset building	78	5,80,150.00
4	Business development	19	1,07,500.00
5	Others	76	1,02,850.00

v) Micro Finance and Institutional sustainability: On-lending process helped the federation to cover nearly 48 percent of the administrative expenses covering grading of MFGs, application generation, loan distribution, documentation, repayment monitoring and so on. It helped the federation to build solidarity among the members and Institutional sustainability to serve the members better.

II. CASE Study on Micro Finance for Water and Agriculture–DHAN's Experience in Ramnad District

Focus: This case study illustrates fertilizer and seed distribution through Micro Finance groups and the positive impacts.

Micro Finance–Age-old custom in villages: Micro Finance for men may look strange to many including bankers and bureaucrats. But men in villages have been practicing this concept since olden days through activities such as operating village common fund for social festivals, temple activities, providing support to individuals during time of distress etc. DHAN initiated MFGs in Vayalagam to sustain its activities through its MF intervention. The MF group consists of 15 to 20 members mainly farmers (both male and female members, but only one member from each family) and also includes landless agricultural labourers.

DHAN's intervention: Ramanathapuram District Tank Farmers Federation (R-TAFF) provided Rs. 20,000 as loan to Sirumaniyendal TFA to purchase fertilizers for cotton crop. The TFA paid 15 percent interest and repaid the loan in the same year (Year 2000).

In 2001, Sirumaniyendal TFA obtained credit from R-TAFF for Rs. 25,000/- to purchase fertilizers. The TFA had 3 MFGs. The TFA charged this loan to MFG account. The TFA repaid the loan through MFGs. The farmers felt that this process is much easier to get loan and make repayment if it is transacted through MFGs.

In 2002, R-TAFF, based on the previous two years experience, went ahead and planned fertilizer distribution on a mass scale.

i) It obtained fertilizer indent in advance

ii) Collected money from MFGs for the input cost in advance and arranged crop loan to MFGs from R-TAFF revolving fund.

R-TAFF initially purchased fertilizer at wholesale prices from registered retail merchant and later switched over to FARM AID SERVICES (Madurai wholesale dealer) and provided fertilizer at the doorsteps of the farmers.

Through these practices, the farmers gained 5.2 percent net profit because of the price reduction when buying at wholesale price. The farmers saved transport, loading and unloading charges as the fertilizers were delivered at the doorsteps. Vayalagam farmers got credit facilities as crop loan from R-TAFF. If this credit is not available, they will be driven to moneylenders.

Up-scaling: A farmers group is formed either from TFA or MFG consisting of 50 to 100 farmers. Each member contributes certain amount as share capital. This group collects the indent from farmers in advance and arranges storage of fertilizers after bulk purchase. The group sells the fertilizers to the needy. The federation facilitates the group and appoints a person as business associate. The federation collects all the indents from the groups and maintains accounts regarding share capital and helps in bulk purchase and distribution. The selling price is fixed as per government norms.

At the end of the season, the net profit after meeting the administrative expenses is distributed to groups as dividends based upon the share capital.

Fertilizer and seeds through TFAs: The federation also arranges quality seed distribution (cotton and groundnut) making bulk purchase and distributes them to TFAs and MFGs. Seven TFAs could save Rs. 40,000/- because of the bulk purchase. Seven TFAs and five MFGs could save Rs. 34,000/- when fertilizers were procured at wholesale prices.

Conclusion

- Farmers are interested in getting the fertilizers through their MFGs
- Local banks are now interested to extend credit facilities to MFGs for their agricultural activities
- As the credit now is timely, the planning and execution of agricultural activities are smooth.

IV. Sectoral Policy Analysis

i) Current Credit Delivery Mechanism– Priority Sector and Micro Finance

Priority sector lending is aimed at providing credit to hitherto neglected sectors viz., agriculture, small scale industries and the weaker sections of the society. It acts as a social control over banks on credit delivery mechanism. Under priority sector lending, it is mandatory for the banks to achieve 40 percent of their Net Bank Credit to the needy sectors of the economy and weaker sections of the society. Out of 40 percent of Net Bank Credit, sub-targets have been spelt out precisely for the Commercial Banks for adoption.

The targets and sub-targets set under priority sector lending for domestic and foreign banks operating in India are furnished below:

The priority sector targets the following:

1. Agriculture
2. Small scale industries
3. Small road and water transport operators
4. Small business
5. Retail trade
6. Professional and self-employed persons
7. Organisations sponsored by State for SC
8. Education
9. Housing
10. Consumption loans
11. Sites lending
12. Food, plant and machinery
13. Venture capital funding.

Particulars	Domestic banks (both public sector and private sector banks)	Foreign banks operating in India
Total Priority Sector advances	40 percent of NBC	32 percent of NBC
Total agricultural advances	18 percent of NBC	No target
Small Scale Industries (SSI) advances	No target	10 percent of NBC
Export credit	Export credit does not form part of priority sector	12 percent of NBC
Advances to weaker sections	10 percent of NBC	No target

{Note: NBC denotes Net Bank Credit}

The targets mentioned above have not been achieved in the past. Even after 36 years of priority sector lending, it is observed that certain important sectors in the economy suffer from inadequate credit flow. For example, 18 percent of NBC has been assigned to agriculture but the actualisation ranges from 11.4 percent in 1995, which has increased marginally to 11.5 percent in 2004. These unmet target funds are parked in Rural Infrastructure Development Fund (RIDF), which impinges on the direct lending to agriculture. It creates severe repercussions for the development of agriculture sector, which is already in a bad shape, when compared to the developed countries. In a mandatory lending requirement of 18 percent of the priority sector of agriculture, the Commercial Banks should proactively consider the Micro Finance Group as potential groups with good business propositions and support community based organisations like federations and watershed associations to facilitate the eligible groups for lending.

Other sectors under the priority sector lending also meet the same end. The Commercial Banks are supposed to lend 10 percent of Net Bank Credit to weaker sections. But during 2001–2004, public sector banks and private sector banks have delivered around 7 percent and 1.4 percent, respectively. It should be noted that the Tenth Five-year plan working group on agriculture credit estimated that requirement of credit per annum is Rs. 144,000 crore. The amount disbursed in 2001 was Rs. 60,000 crore which was less than 50 percent of estimated credit demand. Under the existing credit delivery mechanisms, larger share allotted for the weaker sections has to be delivered as envisaged.

The definition of weaker section in priority sector under RBI guidelines has also been revised and accordingly, the weaker sections in priority sector are now defined as:

a. Small and marginal farmers with land holding of 5 acres and below and landless labourers, tenant farmers and sharecroppers.
b. Artisan, village and cottage industries with individual credit requirement not exceeding Rs. 50,000/-
c. Beneficiaries of the Swarnajayanti Gram Swarojgar Yojana (SGSY).
d. Scheduled Caste and Scheduled Tribe.
e. Beneficiaries of the Differential Rate of Interest (DRI) Scheme.
f. Beneficiaries under Swarna Jayanti Shahari Rojgar Yojana (SJSRY).
g. Beneficiaries under the Scheme for Liberation and Rehabilitation of Scavengers.

Recognition of SHGs under weaker sections provide a wide range of opportunities to effectively deliver the credit to the needy, since credit delivery to the weaker sections through self-help groups is more acceptable in reaching the targets with high loan recovery. Already efforts have been made on this line, but a special emphasis is required for credit delivery to SHG. They will achieve twin purposes. First, it really percolates and reaches the very poor segments in the society. Second, unlike NPA accumulation in other sectors of the economy the SHGs ensure high percentage of loan recovery. Looking into the categories listed under weaker sections, loans were already provided through SHGs under SGSY, SJSRY schemes etc. If necessary changes are made under weaker sections under priority sector lending it will enhance the quality as well as quantity of credit delivery and its use. Banks should strictly follow the stipulated target of 10 percent for the weaker sections under priority sector lending. The above discussion clearly shows that there should be requisite changes in the operation of the present form of priority sector lending.

RBI's credit policy on priority sector lending predominantly supports government's macro economic strategies. Even though the present guidelines are elaborate and appreciable, Reserve Bank of India should proactively make required changes to ensure effective utilisation of priority sector lending. RBI should provide eligibility status to the small and marginal farmers comprising landless labourers having prudential track record in Micro Finance activity similar to SHG women members. This will help farmers to avail timely credit for agriculture and allied activities through commercial banking institutions without collateral security. In turn, Commercial Banks have to pitch in and facilitate such MFGs to open bank account and sustain their economic development activities with Micro Finance fundamentals. Along this line, maintenance of softer interest regime is important to satisfy the high aspirations of the farmers. In the prevailing softer interest regime, corporate clients are seeking loan from banks at the interest rates between 6.5 percent and 7 percent, individual home loans between 7 percent and 9 percent. On the same lines Farmer's expectations can be fulfilled through favourable interest rates ranging from 6 to 6.5 percent, which should be given to MFGs as group loan.

Further, Commercial Banks should come forward to provide loans to bankable components in water resources development like farm ponds, deepening of drinking water ponds, community wells, desilting of supply channels, fishponds, thrashing floor, farm implements and rural godowns as a group activity. The term of repayment of loan should be flexible particularly during drought and flood affected years or even rescheduled.

ii) SGSY and Micro Finance

Under SGSY, mostly the women members are benefitted. There is no such emphasis given to MFGs engaged in agriculture and allied activities. But beyond doubt, DHAN's experience in watershed development programmes through community participation provides ample scope for the promotion of MFGs where part of the SGSY component can target MFGs. The efficiency of the credit delivery mechanism can be ensured and enhanced by following group approach, instead of individual approach, since credit widening and credit deepening takes place. The additional role can be assigned to block committee and district committee to ensure credit support for the minor irrigation tanks. To improve Credit Performance Ratio (CPR) lending to MFGs under group economic assistance to be emphasised.

Scope: The above consideration can be taken into account in the existing programme. The SGSY Guidelines document of the Ministry of Rural Development gives ample scope for accommodating the above recommendations. Para 1.7 deals with on-farm activities for providing irrigation facilities to increase the irrigated areas of the rural poor towards their sustainable income. Para 1.8 recommends project approach under micro irrigation, instead of spreading the investment in a scattered manner. DHAN exactly does the same through watershed approach with community participation, under which MFGs are formed to carry out other activities.

Para 1.10 deals with the recommendation of the consultation process; the committee may identify about 8 to 10 activities, which may be addressed in the order of preference, in which MFGs can be very well accommodated as an important activity under SGSY.

Allocation of subsidy component for common property works such as those connected with minor irrigation tanks should be incorporated under Group Economic Assistance Linkage

iii) RIDF and Micro Finance

The scope for lending loans has been widened by including NGOs, SHGs etc., under RIDF since 1999. Various activities under RIDF, such as watershed development and minor irrigation projects have been included under Tranche RIDF IX. DHAN's successful experience in maintenance of the water bodies through community participation provides windows of opportunities to park and utilise the RIDF funds effectively. Further, MFGs can be formed under the umbrella of water user associations mainly to diversify and sustain the existing activity.

In the era of globalisation, our agriculture sector is thrown open to highly competitive world market. To withstand competition, fundamentals of agriculture need to be strengthened particularly, the infrastructure. Our agriculture sector suffers heavily from inadequacy of infrastructure facilities, such as storage, marketing etc. On this front, NABARD should be encouraged to take necessary steps to implement the Micro Finance activities by all the agencies supported under its RIDF. In order to avoid exploitation by middlemen, requisite capital support should be given to farmers' groups for pilot experimentation to collectively procure and market the farm produce. Later, infrastructure development credit should be supported along with suitable social security measures like Life Insurance for Housing loans by SBI.

Recent development in Micro Finance sector is mainly on the quality concerns of the existing MFGs. In the process of upscaling SHGs as well as diversifying its activities quality checks such as transparent accounting system and avoidance of duplication of members will give a professional outlook. These standards have to be maintained to win the confidence over the mainstream lending institutions. This needs studies in different ecosystems to scientifically support the activities that are 'bankable' under Micro Finance activities. Commercialisation of agriculture is utmost important to withstand the global competition emerging after liberalisation. There is an urgent need to incorporate the value addition of farm produce and efficient water use equipments that can be supported through farm credit to MFGs. The academic institutions should lend their support to accomplish these tasks. Continuous research input on bankable Micro Finance activities is essential through the academic and research institutions like Agricultural Universities and Engineering Institutions. The Non-Governmental Organisations and Registered Community Based Organisations have a great role to promote process and monitor the functioning of MFGs. They should be provided with sufficient promotional grant assistance to carry out the above activities effectively.

iv) Crop Insurance and Micro Finance

Agricultural activities are exposed to both controllable and uncontrollable risks. Controllable risks can be mitigated with the use of technology, effective monitoring and appropriate usage of inputs. The seriousness of the problem is felt more in rainfed agriculture where majority of the farmers are small and marginal. Erratic rainfall in the rainfed regions underlines the importance of the existing and new water conservation structures. Safeguarding the farmers from frequent crop failures and ensuring an assured income is essential for sustaining their livelihood. The cost incurred in the crop cultivation has to be met through crop insurance. But the existing crop insurance schemes lack strength in their application in the eyes of the experts. The existing crop insurance scheme, launched in 1999–2000, in the form of National Agricultural Insurance Scheme (NAIS) has come under strict scrutiny. First, it covered both uncontrollable and controllable risks. Second, the total claims disbursed were six times more than the total premium. Finally, high administrative expenses coupled with inordinate delays in claims settlement (since each claim had to be individually assessed) made the scheme unsustainable on long-term basis. This led to instances where farmers received the claim amount after twelve to eighteen months, defeating the very purpose of insurance.

To revamp the whole agricultural insurance scheme, some pragmatic steps have to be taken. Though there are many practical difficulties in the existing system, yet it is possible to streamline the procedures and turn the tide in making the insurance a successful tool for sustaining the livelihood of the poor farming community. Introducing an agency model into the existing insurance scheme will make the tool more effective. Further, instead of an individual approach for insurance, a group approach can be followed, which can act as 'checks and balances' so that it reaches the needy people. Constructing or evolving an appropriate tool to measure the crop failure on a location specific approach will make the insurance component a meaningful one. A thorough pilot study at the field level taking into account the above measures may strengthen the existing form of insurance delivery mechanism. Convergence of farmers, bankers and government departments pertaining to the insurance sector and those closely working with the needy, like NGOs, is essential to make the present form of insurance tool easily accessible to all the stakeholders.

V. Policy Seminar

The integration of Micro Finance with water and agriculture will benefit all the mainstream agencies like the Central and State governments, Banks and the academics. For smooth integration, it requires suitable amendments to the existing policy framework on Micro Finance. Such sharing will help to suggest policy changes to provide the farming community timely and adequate institutional credit to enhance farm production on a sustainable basis. In this background, DHAN Foundation laid the platform and organised a policy seminar on integrating Micro Finance in water and agriculture. It shared the long field experiences with experts from various fields relating to Micro Finance sector. The deliberations of the policy seminar with further research inputs helped us to bring this policy brief.

VI. Recommendations and Way forward

Policy changes required at different levels are given below:

a) Reserve Bank of India

- The farmer and other landless labour men groups from the weaker sections, if involved in Micro Finance activity, should be made eligible to avail credit for agriculture and allied activities through commercial banking institutions
- Guide Commercial Banks to facilitate approved MFGs to open bank account
- Interest on farmer loans through MFGs should be fixed at 6 to 6.5 percent and it should be considered as a group loan
- NABARD should be encouraged to support Micro Finance activities by all the agencies supported under RIDF, WDF, VVV and innovative emerging schemes.

b) Commercial Banks

- Proactively consider eligible MF groups under priority sector lending of 18 percent towards agriculture and allied activities of the MF groups
- Provide loans to MFGs to support agriculture and infrastructural development such as farm ponds, deepening drinking water ponds, community wells, desilting of supply channels, fish ponds, farm implements, rural godown etc.
- Innovative pilot project support with grant and loan mix
- Incorporate Social Security (like SBI Life for Housing loans) with infrastructure development credit
- NGOs and community based organisations may be encouraged with promotional grant assistance to process and monitor MFGs
- Provide adequate capital as loan MFGs to procure collectively and market farm produce eliminating middlemen.

c) Agriculture and Rural Development Departments of State Government

- Existing support to SHGs should be widened to incorporate changes in the guidelines, to allow watershed association to act as a nodal agency to avail credit to the groups by facilitating bank linkage
- All Government developmental activities to be integrated with Watershed Associations
- Eligible small and marginal farmers and poor women should be allowed to form Micro Finance groups and supported with revolving fund assistance
- Consideration of loan and grant mix for new and innovative development products.

d) Academic Institutions

Academic Research Institutions like Agricultural Universities and Agricultural Engineering Institutions should be encouraged to take up studies to scientifically support activities that are bankable under Micro Finance activities.

e) RRBs

- Strategic attention of RRBs is required to serve the credit needs of small farmers
- RRBs should pay attention to serve the credit needs of small farmers.

f) PACS

- After the reform processes are carried out based on the recommendations of Dr. Vaidyanathan committee, PACS should be involved in a big way to grant farm loans to farmers through farmers' groups.

Way forward

DHAN Foundation should initiate discussion with the following Institutions/Departments based on the Recommendations described in Section VI of this brief.

- Reserve Bank of India
- NABARD
- Commercial Banks, RRBs and Primary Agriculture Cooperative Societies
- Agriculture and Rural Development Departments of Central and State Government
- Academic and Research Institutions
- NGOs

DHAN Foundation would be involved in developing guidelines, operational procedures and bankable products jointly with RBI, NABARD and Commercial Banks. DHAN Foundation would be interested in piloting bankable products for common property resources in collaboration with banks.

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Abbreviations

TCA	–	Tank Cascade Association
CPR	–	Credit Performance Ratio
DWMA	–	District Water Management Agency
ICT	–	Information and Communication Technology
ITC	–	Indian Tobacco Company Ltd.
KDFS	–	Kalanjiam Development Financial Services
MFGs	–	Micro Finance Groups
NABARD	–	National Bank for Agricultural and Rural Development
NAIS	–	National Agriculture Insurance Scheme
NBC	–	Net Bank Credit
NBFC	-	Non-Banking Financial Corporation
Novib	–	Netherlands Organisation for International Development Co-operation
NPAs	–	Non-Performing Assets
NREGA	–	National Rural Employment Guarantee Act
NWDPRA	–	National Watershed Development Project for Rainfed Area
RBI	–	Reserve Bank of India
RFDT	–	Rainfed Farming Development Theme
RIDF	–	Rural Infrastructure Development Fund
R-TAFF	–	Ramanathapuram District Tank Farmers Federation
SBI	–	State Bank of India
SGSY	–	Swarna Jayanthi Gram Swarojgar Yojana
SHGs	–	Self-Help Groups
SIDBI	–	Small Industries Development Bank of India
SSI	–	Small Scale Industries
TFA	–	Tank Farmers Associations
VTADP	–	Vayalagam Tankfed Agriculture Development Programme
VVV	–	Vikas Volunteer Vahini
WDF	–	Watershed Development Fund
WUA	–	Water Users Association

A traditional source of irrigation and village ecosystem

Why this Policy Brief?

DHAN Foundation is involved in Natural Resources Management focusing mainly on Community based Development and Management of Water Resources in South India. The initiatives taken so far have reached several villages through rejuvenating water bodies benefitting thousands of families. By working closely with the community, DHAN has gained valuable experience over the past two decades. DHAN believes that for better management of water resources, certain changes in the present policies and practices are needed. Hence it has now been decided to come out with Policy Briefs to disseminate the changes needed in specific sectoral issues. This will facilitate Administrators and Field level Organisations in their attempts of better management of scarce water resources.

Policy Brief–2 focuses on the issues related to access to financial services for small and marginal farmers and landless labourers. The brief deals about the experience of DHAN Foundation in integration of Micro Finance into small-scale water bodies and agriculture and identifies the role of community organisation in access to savings, credit and insurance. It emphasis the attention needed by RBI, NABARD, Commercial Banks, RRBs on Micro Finance, access to small and marginal farmers, policy and practice changes. This brief is planned to carry forward the attention of Rural Development Department, Agriculture Department of Central and State Government, RBI, NABARD, Commercial Banks, RRBs, NGOs and community for making changes.

About DHAN Foundation

DHAN Foundation is a grassroots development organisation and was initiated with the objective of bringing highly motivated and qualified young professionals to the development sector for new innovations in development programmes and for upscaling development interventions to eradicate poverty. The Foundation works towards bringing significant changes in the livelihood of the poor through innovation in themes and institutions.

The approach of the Foundation is to promote people's organisation and their networks aiming at improving the livelihoods of poor communities by organising development works around themes. These people's organisations would sustain themselves and excel in long run. Presently DHAN Foundation is working on the themes namely Community Banking, Conservation of tanks, Information and Communication Technology for Poor, Rainfed Farming and Panchayats.

About the Centre for Policy and Planning

The Centre for Policy and Planning of DHAN Foundation provides support to the programmes and institutions of the DHAN Collective so that they evolve, develop and modify their policies and fulfill their aims. It shapes the sectoral policies to practice at the grassroots. DHAN Foundation as a member of many policy-making bodies on Micro Finance and Water Conservation strongly advocates pro-poor policies. The Centre takes up policy study and initiating research on Micro Finance, Water Conservation, Rainfed Farming, Panchayat Raj Institutions and Disaster Mitigation. As a resource centre, it organises many capacity building events and training programmes for bankers, government officials and representatives of NGOs within and outside the country.

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