# FARMERS LOAN WAIVER SCHEME AND INDIAN AGRICULTURE

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## ABSTRACT

The loan waiver scheme of the Union Budget 2008 had some serious flaws, and it was perfectly fine because the outreach of any government measure was limited, and some section of the society would be benefited more than the other. But the most important consideration was the fact that agriculture was facing a serious crisis and some productive measures had to be undertaken by the government in this regard. The Loan Waiver Scheme had a very limited number of beneficiaries, and with such huge amount of money the least to be expected by a government scheme was to reach a large number of people. It seems that the assumptions under which the Finance Minister developed this scheme were flawed, despite the comprehensive committee report of Dr R Radhakrishna on rural indebtedness. The loan waiver scheme targeted a selected group of farmers, and the problem was not with the small section of farmers being benefited, but the fact that the potential of such a huge amount of money was enormous and many more could have been benefited. As a long term solution, India needs special public investment to ensure sustainable development of the farm sector.

***Keywords:*** loan waiver, agriculture, bank

## INTRODUCTION

We all know about the loan waiver scheme of the Union Budget 2008, we know that there have been many farmer suicides in the recent past, and we also know that Indian agriculture is facing a crisis. Still, there is a lot of criticism about the loan waiver scheme which was designed to provide relief to the ailing rural economy and bring some respite to the distressed farmers.

This research paper tries to analyze the loan waiver scheme to figure out the problems in the scheme, and also to elaborate in details the pros and cons of the scheme. The huge amount of money that would be spent for this scheme has caught everyone's attention, and that is not the major concern of this paper. As we know, agriculture is of vital importance in Indian socio-economic framework, and with a large population dependent on agriculture, such a huge amount should not be a problem if it is able to provide some relief to the distress and needy farmers. This paper attempts to explore the potential of the huge amount of government resources spent on this scheme, and if the present use of money is its best possible use. But we must not forget that Indian agriculture is actually facing a crisis and some measures have to be taken to provide relief. This paper tries to find out the actual problems in Indian agriculture and to know if the present scheme solves some of these problems and then what steps should have been taken to address all these issues.

The major problem in agriculture today is of declining productivity and lack of adequate infrastructure. One reason for low productivity is the increasing cost and improper supply of inputs, which is the result of a under developed marketing network. Unless the farmers have an assured source of income, we can't expect them to get out of this vicious circle of indebtedness. Government policies should stress upon increasing the productivity in agriculture so that the farmers are able to generate enough income to repay their loans.

Agriculture currently contributes just about 15% to the national output and about 50% of the population directly or indirectly depends on it for employment.

Farmer distress is a real and pressing problem, as evidenced by the protests currently taking place in various parts of the country. In the recent past, widespread demands have been heard for farm loan waivers amid continuing agrarian distress.

**Drawbacks of loan waivers:**

- Firstly, it covers only a tiny fraction of farmers. The loan waiver as a concept excludes most of the farm households in dire need of relief and includes some who do not deserve such relief on economic grounds.
- Second, it provides only a partial relief to the indebted farmers as about half of the institutional borrowing of a cultivator is for non-farm purposes.

- Third, in many cases, one household has multiple loans either from different sources or in the name of different family members, which entitles it to multiple loan waiving.
- Fourth, loan waiving excludes agricultural labourers who are even weaker than cultivators in bearing the consequences of economic distress.
- Fifth, it severely erodes the credit culture, with dire long-run consequences to the banking business. According to RBI Governor Dr. Urjit Patel, farm loan waiver distorts wise credit culture of the banking industry and affects the national balance sheet.
- Sixth, the scheme is prone to serious exclusion and inclusion errors, as evidenced by the Comptroller and Auditor General's (CAG) findings in the Agricultural Debt Waiver and Debt Relief Scheme, 2008.
- .Seventh, the farmers who have the ability to repay loans on time are inspired to default on loan repayments with a hope of announcement of such schemes in future. Hence the money which could have been utilized in other developmental activities gets diverted in waiving loans, a part of which does not deserve to be waived at all.
- Eighth, waiver schemes strains the pocket of tax payers since the tax payers' money is utilized for waiving of loans.
- Lastly, schemes have serious implications for other developmental expenditure, having a much larger multiplier effect on the economy.

## LITERATURE REVIEW

Farmers in India take recourse to debt, both from formal and informal sources, not only to meet their investment needs but also to smoothen consumption in the face of adverse income shocks. At very high levels of debt, apart from the inability to repay it, the loss of creditworthiness no longer acts as a deterrent for non-repayment of loans, particularly those acquired through formal channels (Chakraborty and Gupta, 2017a). Debt relief/waiver schemes are, therefore, used by governments as a quick means to extricate farmers from their indebtedness, helping to restore their capacity to invest and produce. The costs and benefits of such debt relief schemes are, however, widely debated in the literature (Patel, 2017). Apart from adding to the financial stress of governments whose fiscal space may already be constrained, they may work against the borrowing farmers if lending institutions refrain from extending loans to defaulters by construing that they are likely to default again. Borrowers' expectation of repeated bailouts by the government may vitiate credit culture among farmers and may further constrict farm lending (De and Tantri, 2016).

Empirical research on agricultural debt waivers in India are mostly centred around the Agricultural Debt Waiver and Debt Relief Scheme (ADWDRS) 2008 of the Government of India (GoI), under which `Rs. 525.16 billion of agricultural debt issued by commercial and cooperative banks were waived. Past research found mixed evidence of the impact of ADWDRS on agricultural households. On the borrower's side, while debt relief was found to help reduce the overall household debt (Giné and Kanz, 2017; Kanz, 2016), there appears to be differential impact on distressed beneficiaries who benefit significantly from it compared to non-distressed beneficiaries whose loan performance worsens after the waiver (Mukherjee et al., 2017). Although agricultural debt waivers aim to increase investment and productivity of beneficiary households, empirical evidence does not support it (Kanz, 2016). Waiver impact on beneficiary farmers' consumption and savings indicates that while the level and pattern of consumption remained unaffected, there was a rise in precautionary savings in the form of increased investment in jewellery, likely due to anticipation of higher credit constraints in the post-waiver period (Mishra et al., 2017). There appears to be no evidence of improvement in the ex post repayment behaviour of the waiver beneficiaries. In fact, an expectation of similar debt relief in future generates moral hazard and strategic loan default, i.e., loan defaults become sensitive to the electoral cycle after debt relief (Giné and Kanz, 2017).

On the credit supply side, post-waiver lending slowed down in districts where the exposure to waivers was high, as banks shifted credit to observably less risky regions (ibid.). While this indicates improvement in efficiency of credit allocation post-waiver, on the flip side, restricted lending to backward districts could widen regional disparities. Difficulties in obtaining formal credit post-waiver could lead farmers to factor in future credit constraints and hence shift to informal sources of credit (Kanz, 2016). Consequently, loan waivers can have a dampening impact on lending by rural credit institutions (RBI, 2018).

# PROBLEMS WITH THE LOAN WAIVER SCHEME

While reading out the 'Debt Waiver and Debt Relief' scheme in his Union Budget 2008 speech, the Finance Minister showed special concern for the indebted farmers, and especially the small and marginal farmers. The opening statement of this scheme makes it clear that the Finance Minister has been working under the assumption that the main problem with Indian agriculture is of indebtedness, and small and marginal farmers are the people hit most badly by this crisis.

**Identifying the Target Group**

This is the most general perception about the scenario of Indian agriculture. Unquestionably, every scheme has to limit its reach, and even if the scheme aims to help the small and marginal farmers, the definition on the basis of the size of land holdings does not make much sense. According to Prof. MS Swaminathan1, in rain-fed, arid, and semi-arid areas, income from agriculture is very uncertain even for farmers having 4 or 5 hectares of cultivatable land and is closely dependent on the behaviour of monsoon. As Arindam Banik points out, "A small farmer with less land but assured irrigation may be financially better off than another farmer with much larger land holding but no assured irrigation."2 Sharad Joshi3 finds this idea of identifying the target group by measuring the size of land holdings having 'very little economic significance' and makes a point by saying "If agriculture is a losing proposition, the small holder should logically be a smaller loser than the larger holder."4

**Disappointing for the Farmers**

The role of the informal sector and moneylenders has been completely ignored in this scheme, and this will be dealt with more details in the next section. It is even more discouraging for those 'honest' farmers who have taken desperate measures to pay back their instalments. CR Sukumar 5 cites the example of a farmer couple who had no money to repay the bank loans due to monsoon failure, but rather than default, they borrowed from local a moneylender at a high cost and paid their loan instalments on time.

Since many farmers borrow from the moneylenders in order to repay their bank loans, it would be very unfair for these farmers to be excluded from the relief scheme. It would be like penalizing the farmers who have been making prompt repayments of their debts honestly. In Sharad Joshi's words, "whether a farmer owes money to the moneylender or to the bank is entirely a matter of accident."6

Moreover, as MS Murty7 (former MD, State Bank of Mysore) points out, the farmers who have invested out of their savings rather than borrowings would be deprived of the benefit of this scheme. Also, the scheme covers only crop loans, and farmers who have invested in infrastructure would be discriminated against even though they have to pay back the loans out of crop yields only. Such farmers would continue to be defaulters and it is very important to make them eligible for fresh loans, so that they can repay the outstanding debt from their income out of new crop yield.

The most important aspect of the indebted farmers is their ineligibility to get fresh loans. The beneficiaries of the loan waiver scheme were eligible for fresh loans only after June 30, and they still could not apply for loans for the kharif season. Further, Ashwin Parekh says that it has not been made clear as to who would provide fresh loans to these farmers in future, because if they approach the same bank, "the present process of risk management would straight away deny them admission."8

## DISCOURAGING FOR THE BANKING SECTOR

According to RBI Governor Dr. Urjit Patel, farm loan waiver distorts wise credit culture of the banking industry and affects the national balance sheet. The farmers who have the ability to repay loans on time are inspired to default on loan repayments with a hope of announcement of such schemes in future. Hence the money which could have been utilized in other developmental activities gets diverted in waiving loans, a part of which does not deserve to be waived at all.

"I have decided not to repay my loan instalment this time. Who knows there could be a similar waiver again in view of elections in the state next year?" 9 These are the words of a farmer quoted by CR Sukumar in his article in Mint. Later in the same article, he quotes the deputy manager of Deccan Grameena Bank, Manjulapur. The deputy manager says, "We will be losing that healthy status (of around 98% recoveries) now with not more than 5% recoveries during this season, with farmers preferring not to repay in anticipation of a debt waiver scheme in the near future, in the backdrop of ensuing assembly elections in the state."9

The loan waiver scheme has certainly created a moral hazard situation in the banking sector, with increasing rate of non-repayment. PT Kuppuswamy, the chairman and CEO of Karur Vysya Bank told Mint10 that many farmers were shifting accounts from their banks to nationalized banks. The cause of this trend was the farmers' anticipation of a loan waiver in the present election year, and also their fear that they might not get a write off in a private sector bank.

In 1990, there was a loan waiver by the VP Singh government, and it took almost nine years for banks to recover from this scheme worth Rs10000 crore. There was a decline in agricultural loans from cooperative societies and commercial banks soon after the scheme was declared. The main reason for this decline was the fact that the government took some time to write off these loans, and meanwhile those individuals and societies that still had over-dues could not access fresh credit. This scheme had made people unenthusiastic about repaying their loans in anticipation of future write-offs, and the major reason for banks to violate priority sector and other guidelines was the 'unethical socio-political environment created against the discipline of loan repayments.'11 The situation seems to be very similar to the one that exists now.

## CONCLUSION

According to Prof. Raghuram Rajan, former Governor, RBI, *loan waivers not only inhibit investment in the farm sector but put pressure on the fiscal of states which undertake farm loan waiver*. In every state election during the last five years, loan waiver promise made by one political party or other. The recently concluded assembly election in five states, agriculture loan waiver and increasing minimum support price (MSP) of cereals was again part of manifesto of some of the political parties. Waiver may not be a solution to the put an end to the ever increasing problems faced by the agrarian population as in spite of a good harvest; they do not reap benefit of a fair price in the market. Their situation still remains vulnerable and the cost of waiver poses a heavy burden on the treasury of states and as well as centre. As a long term solution, India needs special public investment to ensure sustainable development of the farm sector. Problems like reduction in irrigated land, reduction in level of water-table, ground water pollution have become a cause of concern.

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