Reforming Loan Waivers - Kerala Model

Why in news?

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Union government is discussing a scheme to waive outstanding farm loans.

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What is the NPA status of Farm loans?

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- NPAs in agriculture remained stable at around 4 to 5% between 2011 and 2015.
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- This was despite the fact that agricultural growth averaged just 1.5% between 2011 and 2015.
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- The rise in agricultural NPAs between 2009 and 2011 was due to the "general economic slowdown" after 2009 and the introduction of new norms in the "system-wide identification of NPAs".
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- Agricultural NPAs began to rise again after 2015, it was real, policy-induced and a direct consequence of acute agrarian distress that spread across rural India after 2015.
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- In particular, the demonetization of November 2016 aggravated already brewing agrarian distress by sucking cash out of the rural areas, crashing output prices and disrupting supply chains.
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What are the issues with loan waivers?

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- Loan waivers have "reputational consequences"; that is, they adversely affect the repayment discipline of farmers, leading to a rise in defaults in future.
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- Earlier debt waiver schemes have not led to increases in investment or productivity in agriculture.
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- After the implementation of debt waiver schemes, a farmer's access to formal sector lenders declines, leading to a rise in his dependence on informal sector lenders, in other words, waivers lead to the shrinkage of a farmer's future access to formal sector credit.
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- Majority of small and marginal farmers are not proportionately included.
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- The latter are forced to rely on informal sources, particularly moneylenders, for much of their credit needs.
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- As a result, the benefits of loan waivers accrue disproportionately to large farmers while only marginally benefiting the small and marginal farmers.
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Why do farmers need more than loan waivers?

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- In India there have only been two nationwide loan waiver program in India after Independence: in 1990 and 2008.
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- Farmers are most disciplined in their repayment behavior, In September 2018, agricultural NPAs (about 8%) were far lower than in industry (about 21%).
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- Furthermore, agricultural NPAs were on a continuous decline between 2001 and 2008.
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- There is no evidence to argue that the 2008 waiver led to a rise in default rates among farmers.
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- The lowest of all NPAs after 2001 was recorded in March 2009 (2.1%), which was just after the implementation of the 2008 scheme.
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- The reason was the government's cleaning up of the account books of banks.
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- Once this was complete, it was totally expected that NPAs would rise again to settle at a slightly higher level. This was exactly what had happened: agricultural NPAs rose and settled at about 5% by 2011.
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- For two reasons, the rise of agricultural NPAs, from 2% to 5%, is no evidence for indiscipline in farmer repayment behavior.
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Why at times Loan waivers are significant?

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- Loan waivers do not promote investment or raise productivity, it is a bit absurd because nowhere has investment or productivity figured as the official objectives of these schemes.
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- After every waiver, banks become conservative in issuing fresh loans to beneficiaries, as they are perceived to be less creditworthy.
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- In India firms have always received debt waivers, though they are tactfully termed as “loan restructuring” or “one-time settlements”.
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- Just as for firms, farms also need a reduction of debt burden, followed by fresh infusion of credit, when their economic cycle is on a downturn.
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- The demand for loan waivers in India is absolutely logical when viewed from such a standpoint.
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What union government can learn from Kerala?

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- The solution to address farmer distress lies in carefully designing waiver schemes that ensure universal coverage for small, marginal and medium-sized farmers while covering both the formal and informal sources of debt.
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- The Kerala Farmers’ Debt Relief Commission Act, 2006 is an excellent model in this regard.
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- This scheme defines debt as “any sum borrowed by a farmer from the creditor”, with the creditor defined as “any person engaged in money lending, whether under a license or not”.
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- The commission’s mandate included the right “to fix, in the case of creditors

other than institutional creditors, a fair rate of interest and an appropriate level of debt, to be payable…”
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- That is, the commission could waive, reschedule or reduce any debt on a need-basis after a detailed hearing of both the parties.
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- Legislations such as Kerala’s are blueprints to design comprehensive, inclusive and less-leaky loan waiver schemes in other States.
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- Apart from this steps ‘to raise productivity, reduce costs of cultivation by providing quality inputs at subsidized rates, provide remunerative prices needs to be taken.
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Source: The Hindu

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