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ECONOMICS OF LOAN WAIVING CULTURE: EVIDENCE FROM INDIAN ECONOMY

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ABSTRACT

The loan waiver scheme of the Union Budget always has some serious flaws, but it is well known the outreach of any government measure is limited, and some section of the society would be benefited more than the other. But the most important fact is that agriculture is facing a serious crisis and some productive measures have to be undertaken by the government in this regard. The loan waiving scheme has a very limited number of beneficiaries, and with such huge amount of money the least to be expected by a government scheme is to reach a large number of people. Although these scheme have targeted a selected group of farmers, and the problem is not with the small section of farmers being benefited, but the fact that the potential of such a huge amount of money is enormous and many more could have been benefited. 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. This research article attempts to analyze the problems and suggest solutions to these issues.

KEYWORDS

GDP, fiscal deficit, loan waiving, productivity.

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INTRODUCTION

History of first ever nation-wide farm loan waiver started with the announcement in 1990 by Janata Party government led by then Prime Minister V.P. Singh and cost the government Rs 10,000 crore. Thereafter, on February 29, 2008 P. Chidambaram, the then Finance Minister under United Progressive Alliance government led by Prime Minister Man Mohan Singh provided Loan waiver to farmers was by the Central Government under Agricultural Debt Waiver and Debt Relief Scheme (ADWDRS), 2008. Under the scheme, direct agricultural loans disbursed by Scheduled Commercial Banks, Local Area Banks, Cooperative Credit Institutions and Regional Rural Banks between 1st April, 1997 to 31st March, 2007 to farmers, which were overdue as on 31st December, 2007 and remained unpaid up to 29th February, 2008 were eligible for Debt Waiver / Debt Relief. While Small and Marginal Farmers were entitled to cent per cent debt waiver, Other Farmers were given a rebate of 25 per cent of eligible amount, subject to the condition that the farmer pays the balance of 75 per cent. The UPA government had waived 1.3 per cent of GDP of farm loans in 2008. After that country witnessed more than half-a-dozen loan waiver proposals from various states in the last nine years. In 2014, Telangana waived Rs. 17,000 crores in loans to farmers and had identified to 36 lakh beneficiaries for a waiver of loans not exceeding Rs. 1 lakh to each family, while Andhra government identified 49 lakh families for a waiver of loans not exceeding Rs. 1.5 lakh per family. This scheme was aimed at benefiting farmers, who suffered in the cyclone Phailin that severely damaged crops. After Reserve Bank of India rejected a request for rescheduling of farm loans, a facility available only when drought is declared in a particular area, made by the Andhra and Telengana governments for the purpose of a loan waiver, the banks and RBI had successfully resisted attempts by the newly formed Telangana and Andhra Pradesh governments to force commercial banks to write off farm loans; both the governments had decided to repay farmers' loans in installments. Andhra Pradesh committed to repay the banks under its debt waiver scheme Rs. 22000 crore. Over nine years from 2008 to March 2017, the central and state governments waived Rs. 88,988 crore in loans to 4.86 crore farmers. The nationwide Rs. 52,000 crore loans waiver announced by the United Progressive Alliance (UPA) in 2008 occupies the bulk of this figure.

India now faces a cumulative loan waiver of Rs. 3.1 lakh crore ($49.1 billion), or 2.6% of the country's Gross Domestic Product (GDP) in 2016-17; according to calculation based on detailed analysis of the data. As demands for farm-loan waivers grows across Punjab, Haryana, Tamil Nadu, Gujarat, Madhya Pradesh, and Karnataka-after Uttar Pradesh; the states announced write off.

LITERATURE REVIEW

Sidhu & Gill (2006) have concluded in their research that reasonable certainty that farmers suicide is reported from those states of India, which are relatively more advanced and are front runners in commercial agriculture. **Kumar (2009)** emphasis that electoral considerations made this into an expansionary exercise that included massive increases in public outlays in support of employment guarantee schemes, farm loan waivers, pay commission rewards, and increases in food and fertilizer subsidies. **Burgess, Pande, & Wong, (2005)** concluded that expansion of State-led rural bank branch networks and direct lending to weaker societies has indeed helped in poverty reduction. **Das (2017)** concludes that the objectives of priority sector lending are found to be defeated because of fund mismanagement, easier access to loan (as if it is a free loan), increases willful default rate by borrowers. **Dinesh (2018)** mentioned in the study that the farming landscape is changing and that it is the large "smart" farmers who are getting benefited and that the small and marginal famers could not even afford the loan because of the high cost and difficulty in getting the loan, let alone getting a waiver. Their argument is that it might not be correct to link loan waiver as the reason for a political party winning an election.

OBJECTIVES OF THE STUDY

1. To understand banking and economic implications of loan waivers.
2. To make suitable suggestions to various stakeholders.

RESEARCH METHODOLOGY

Descriptive research method is used to gather preliminary information, observe the past agricultural loan growth in India, record the situations from a political and economic perspective and describe the implications of the loan waiver on the banks. Only Secondary data sources were used for the purpose of this study. Loan data and information related to NPAs, provisioning and write-offs etc. are collected from the official website of RBI and that of private and public sector banks. Annual reports of the banks are downloaded from the Annual Reports section of the bank's official websites that gave both descriptive and quantitative information. Research papers, journals and books were used to understand the concept better, particularly in the global context.

DISCUSSIONS

The implementation of the debt waiver would require the State to either ask for financial aid from the Centre, or issue bonds, just like the UP Government has planned via the Kisan Rahat Bonds (Mathew, 2017). However, the issuing of bonds would add on to the Governments' liabilities and the Centre has stated that it would not help shoulder the burden as it happens in case of Maharashtra Government (Unnikrishnan, 2017). This implies that the State would have to cut on its spending and chalk out a plan that excludes aids from the Centre. As a result, these loan waiving increase the public debt. Public borrowing involves transfer of purchasing power from individual to government and a subsequent retransfer of the same to the individuals from the government. Thus, public debt, in one sense, has the 'revenue effect', and, in another sense, has the 'expenditure effect'. This means that public borrowing produces different effects on the economy. However, the exact effects of borrowing will greatly depend on the sources of borrowed amounts.

Loan waiver scheme is a costly affair for bank and economy. The research has shown that the years after the waiver "witnessed a decline in the recovery rates by financial institutions, as farmers believed that they could default with impunity. It affected rural credit with defaults of such a high magnitude that it took the banks several years to recover from its impact. Although the scheme was implemented during 1990-91, the real impact may have been felt from November 1989 itself when various political parties started making promises that they would write off agricultural loans if they returned to power. A study has found concrete evidence that the loan recovery of PACS in Karnataka fell from 74.9 per cent in 1987-88 to 41.1 per cent in 1991-92." The CAG audit revealed lapses and errors raising which included inaccuracy of claims to an inclusion of ineligible beneficiaries to the accuracy of claims to reimbursement of the lending institution, all ranging serious concerns about the implementation of the scheme.

According to RBI the effect of loan waivers is as under:

- Farm loan waiver undermines an honest credit culture.
- It impacts credit discipline.
- It impacts incentives for future borrowers to repay.
- Waivers engender a moral hazard.

We need to create a consensus that such loan waiver policies are eschewed. Sub-sovereign fiscal challenges in this context could affect national balance sheets. Debt waivers also entail transfers from taxpayers to borrowers. On account of this overall government borrowing goes up, yields on government bonds also get impacted. Thereafter, it can also lead to crowding of the private borrowers as higher government borrowing can lead to increasing cost of borrowing for others.

Culture of loan waivers has proved as good politics but bad economics for Indian Economy. Politicians must put an end to the culture of loan waivers, normally offered as a part of pre-poll sops, as it does more harm to the system than offer any help. Research has shown how loan waivers disrupt credit flow and makes the recipients only better off in the short-run but worse off in the long term. It is suggested other measures such as loan restructuring for people affected by calamities as possible alternatives to loan waivers. Such waivers end up benefiting the wrong people instead of the intended recipients and added that such doles (in other forms) must be more targeted.

In India, agriculture is primarily dependent on monsoon rains. Since most of the farmers aren't rich, they invest heavily on crops by taking loans. A good shower brings good yields and repayment of the loan. If there isn't any rains or insufficient market demand, farmers are unable to pay the loan amount or interest. When there is a continuous monsoon failure, farmers are trapped, with no other option, the farmer are forced to commit suicides. So, farm loans waiver is a good step towards curbing the crisis. Besides, many farmers are force to flee from agriculture to find better career elsewhere, which could lead drop in agricultural yields. So in order to avoid such situations, farm loan waiver acts as a good initiative to attract and retain the farmers. Finally, most of the farmers borrow money from moneylenders who charge exorbitant interest rates and get trapped in a very problematic cycle of debt trap. Farm loan schemes and waivers will divert these farmers to borrow money from banks.

Loan waiver schemes disturb loan and credit discipline for the any financial system. Though waivers can be an attractive tool for retaining farmer's interest in agriculture and avoid fatal incidences, it could lead willful defaults among the farmers. If farm loan waivers are done more than twice, farmers will start to wait for the next loan waiver scheme, which is bad for the economy and agriculture. Besides, taxpayers are at a loss, because loans will be waived only with hard earned money of taxpayers. Rich farmers could take advantage of the situations and push to take loans even if there is no need, in the hope of the next loan waiver scheme. This will impact the poor farmers who are genuinely in need of loans for crops.

Eight state governments have given farm loan waivers worth ₹1.9 trillion since April last year, amid massive farmer protests and promises made ahead of the recently concluded assembly elections in five states. It all began with Prime Minister Narendra Modi promising debt relief to farmers ahead of the Uttar Pradesh elections in February 2017.The Maharashtra government was next. It submitted to demands from farmer groups after they went on a strike. Together, Uttar Pradesh and Maharashtra promised to waive over ₹70,000 crore in farm loans, triggering a string of copycat announcements by governments in Punjab, Karnataka and Rajasthan. The latest round of farm loan waivers was announced after Congress formed governments defeating the incumbent Bharatiya Janata Party (BJP) in Chhattisgarh, Rajasthan and Madhya Pradesh. In total, ₹59,000 crore of waivers have been promised to farmers in these three states.

A more pertinent question is whether debt relief is the right solution to resolve farm distress, driven by drought, inadequate crop prices and falling incomes since 2014. Loan waivers are a band-aid solution, but necessary at times to provide some immediate relief. They help little to solve the fundamental problem of rising costs and falling profitability in agriculture. But it is an easy solution for politicians.

Ground realities of the ongoing farm loan waivers show many fault lines. Firstly, waivers are almost always conditional. In Punjab and Uttar Pradesh, for instance, the waivers were allowed only for small and marginal farmers, who own less than 5 acres. Secondly, governments usually set a cut-off date when they implement a waiver. Madhya Pradesh, for example, has set a cut-off date of 31 March 2018, when it approved a farm loan waiver earlier this week. This means farmers who availed crop loans in June or July for kharif planting will not benefit. Like all political parties, Congress, too, never said the waiver would be conditional. So, there is a degree of ambiguity built into all promises of debt relief.

In Uttar Pradesh, many honest farmers had repaid their loans before the government announced the waiver. Bank managers privy to information of an impending waiver also reissued loans in a way that deserving farmers were left out. A farmer leader with the Bhartiya Kisan Union. Malik added that compared to the promised waiver of ₹36,359 crores, the state managed to waive around ₹25,000 crores after more than 18 months. He suggested that a debt relief commission (Kerala has one) could help avoid these problems by restructuring and negotiating debts between farmers and lenders.

RECOMMENDED ALTERNATIVE SOLUTION FOR THE FARM LOAN WAIVING SCHEME: DEMAND SIDE AND SUPPLY SIDE

- Instead of creating more of government debt, efforts could be made increase yields, the framework for land leasing can be strengthened, which will not only allow consolidation, but will also give an opportunity to unwilling farmers to exit the sector.
- Also the idea of price deficiency payment should be highlighted. If the price of a crop falls below a predetermined threshold level, farmers can be compensated through cash transfers. Adequate safeguards need to be built in order to protect farmers against both production and price risks. Cooperatives can also be encouraged; these will help reduce risk and transaction costs.
- Central and state governments will need to work together in order to enhance the viability of the sector. This will require investment in practically every aspect of the farm economy, including irrigation, agricultural research, storage and marketing.
- It will also require policy decisions in other areas—foreign direct investment in multi-brand retail, which would lay the groundwork for cold- chain storage infrastructure—that support the sector.
- New research commissioned by Tata Trusts and Copenhagen Consensus for the India Consensus project, Rajasthan Priorities, which aims to identify policies for the state that will do the most social good relative to their costs across all sectors of government, shows waivers are extremely expensive while having a limited impact and other policies could help many more farmers for every rupee spent.

CONCLUSION

This paper made an attempted to bring our body of knowledge of agriculture loans and waivers from the banking and economic perspective. Only 15% of the marginal farmers (with less than 2 hectares of landholding) have access to formal credit, and loan waiver schemes typically cater to farmers who have availed of formal loans. In fact, previous waivers have led to banks reducing credit outlay for small farmers during their next loan cycle, thereby diminishing their chances of getting formal loans. Loan waivers actually do harm to the small farmers, as with less credit outlay from the formal sector, the small farmers increasingly have to depend upon the informal sector. The cost difference for loan rates between the formal and informal sectors vary between 30-45%, annually. Studies also point out small farmers use money saved from loan waiver for consumption activities and not to augment investment to increase agricultural productivity. This results in lower agricultural produce for small farmers during next loan cycles. On the contrary, the big and mid-size farmers (with more than 2 ha of landholding size) actually gain from farm loan waivers. With the small farmers receiving less money from banks, this incremental loan is actually made available for the big farmers who use it to buy farm equipment such as tractors and combine harvesters.

Loan waiver is not a permanent solution for agriculture until the fundamental problems are solved. Though it is instant temporary relief from debt preventing suicides, it largely failed on many occasions to contribute to farmers' welfare in the long term. Besides, there is always a question that to what extent this relief measure can help bring farmers out of indebtedness and suffering always remains a question. Since waivers in India are filled with lack of accountability and lack of proper monitoring reduces the effectiveness of the loan waivers. This coupled with the fact that not all the debt is formal, reduces their effectiveness even more. Since most of the working population of India is dependent on agriculture, loan waiver cannot be avoided. But a proper system of accountability and transparency of waiver will alone ensure the effective working of waiver scheme.

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