General Studies-3; Topic– Indian agriculture: Issues

Farm Loan Waivers

1) Introduction

- Despite substantial increase in agriculture production and productivity levels over the years, farmers' indebtedness has not changed significantly.
- Farm loan waivers, is now seen as a necessary promise for electoral victory.
- After corporate bad debt, banks are worried about the next threat — farm loan waivers.

2) Present Status

- Since 2014, India has seen large-scale loan waivers as a populist device and a short-term tool addressing the plight of farmers.
- According to the National Bank for Agriculture and Rural Development (Nabard) All India Rural Financial Inclusion Survey (Nafis) 2016-17, 52.5% of agricultural households were indebted.
- Increasing allocations by Rs 1 lakh crore in every Union Budget over the past three years for the farm sector.
- But non-institutional credit still hovers around 40%, and the majority of small and marginal farmers rely on moneylenders.
- The primary reason for this persistent distress is the inability of farmers to get remunerative prices, due to the prevailing disconnect with the value chain resulting from market asymmetry, and lacking institutional and infrastructure support.

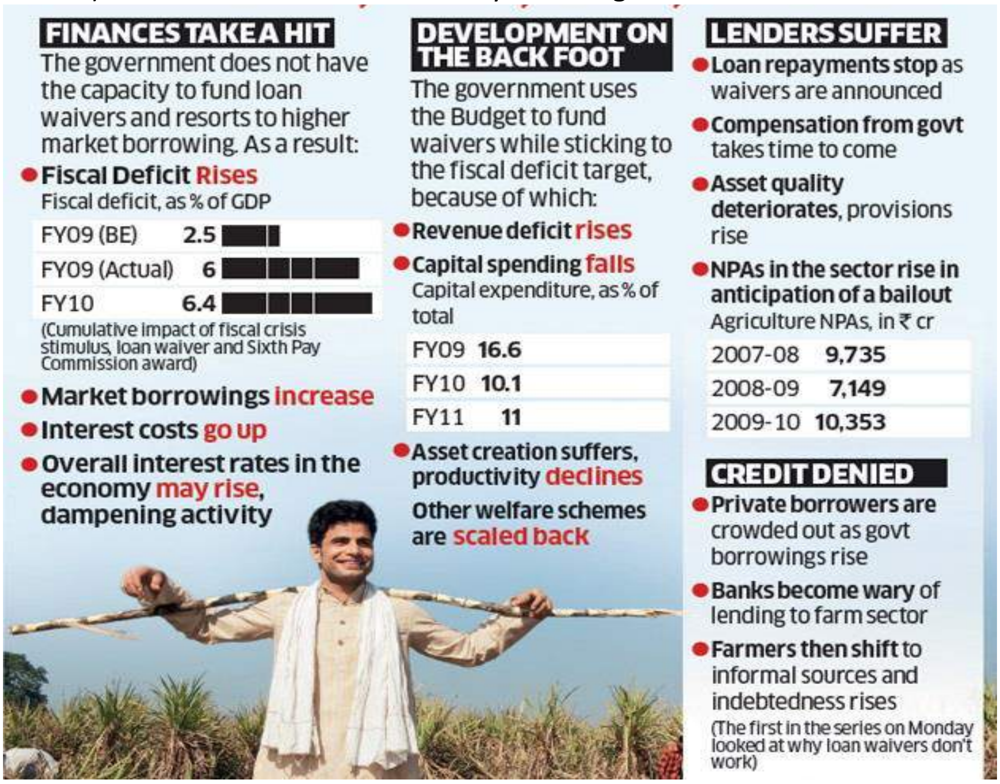
3) Arguments against Loan Waiver

- Study shows that farm loan waivers are not the answer.
- There are evidences on the ineffectiveness of the Agricultural Debt Waiver and Debt Relief Scheme (ADWDRS) of 2008.
- Loan waiver scheme did not have any positive impact on household savings, credit uptake from banks, or investments.
- Economic theory suggests that waiving debts via such a scheme will lead to debt overhang (essentially stagnated investments due to any new income being used largely for paying back old debts).
- A farm loan waiver benefits only farmers who have access to formal credit—commonly estimated at 30% of farmers.
- RBI Governor Shaktikanta Das said, Farm loan waiver adversely impacts the credit culture and the behaviour of borrowers.

4) Consequences

- Because the farmer knows that the loan will be waived in the future, she will prefer to default on the loan rather than work towards repayment.
- The RBI, in a report on state finances had cautioned against the propensity of waiving loans as they were increasing the fiscal deficits of the states.
- The RBI said that debt waivers can deflect the state from its fiscal consolidation path.
- If the waivers are not targeted efficiently the potential for these waivers contributing to inflationary pressures via higher fiscal deficits remains a key concern.
- Farm loan waivers have also resulted in a spike in banks' NPAs, in the agricultural sector.

- It has also pushed the farmers into borrowing from money lenders at an exorbitant interest rate — because banks become wary of lending to farmers fearing loan write-offs by the government.
- With loan waivers, capital investment takes a back seat, aggravating both demand and supply side constraints in the agriculture sector due to a likely fall in asset creation (irrigation, markets, power, etc) that is crucial for sustainability of the agriculture sector.



5) **Way Forward**

- Greater focus is required on enhancing farmer loan repayment capacity via smooth supply and value chains, and better price realisations.
- Monitoring of debt and ensuring appropriate governance mechanisms for new loans.
- The enforcement costs for this will likely be far lower than the huge fiscal burden associated with debt relief schemes.
- Encouraging adoption of appropriate crop insurance products that operate along pay-on-harvest lines.
- This has found to be effective in reducing farmer vulnerability in Kenya.
- A mix of policy interventions that are aimed at reducing farmer vulnerability and helping them save more for tomorrow so that they can invest in improving their agricultural productivity.
- Bold steps now have to be taken to allay the apprehensions of the farming community.
- An Income Support Scheme for small and marginal farmers might turn out be a viable solution.
- The cost of such a scheme will be around only Rs 50,000 crore a year -- or 0.3% of GDP. This is lower than the incremental debt waiver.
- Partial waivers or small loans waivers alone won't help.
- The Swaminathan Committee in 2004 had recommended farmers be allowed to fix the price for their produce on their own (cost of production plus 50% as profit), keeping local factors in mind.
- The government must focus on three things: crop insurance, better irrigation and subsidised seed and fertilisers.
- Alternative ways to help farmers in distress, such as raising the interest subvention limit for borrowers who repay on time.