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Farm Loan Waiver – Boon or Bane?

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INTRODUCTION

Farm loans are loans taken from the banks by the farmers for agriculture requisites and production. When there is a poor monsoon or natural calamity, farmers fail to repay their loans. So the centre or the state government take over the liability of farmers and repay the banks. For example, in 2008, crop and investment loans were completely waived for marginal and small farmers (those with less than 2 hectares of land ownership) and other farmers were only given a 25% reduction. The first recorded instance of granting loans to peasants in medieval India dates back to the regime of Muhammad-bin-Tughluq (1325-51) so as to ameliorate the distress suffered by villagers. However, faced with rebellion and famine, these loans were written off by Firoz Shah Tughluq, the subsequent ruler. There have only been two nationwide loan waiver programmes in India after Independence: in 1990 and 2008.
The first nationwide farm-loan waiver in independent India was implemented in 1990 by the VP Singh-led government. It cost the exchequer Rs 10,000 Crore. In 2008, the Agricultural Debt Waiver and Debt Relief Scheme, implemented by the UPA government, involved an outgo of Rs 71,680 crore. Since then, there has been a wave of such schemes by different State governments. From 2016 to 2018 six state governments have declared farm loan waivers of upto Rs1, 19,000 Cr. In this article, the authors have discussed the merits and demerits of farm loan waiver.

Arguments in Favour of Farm Loan Waiver

The Agriculture sector in India has been fighting with many issues — fragmented land holding, depleting water table levels, deteriorating soil quality, rising input costs, low productivity. But the single most problem is the vagaries of the monsoon. Output prices of the produces produced by the farmers are often not remunerative. Farmers are often forced to borrow to manage expenses. Also, many small farmers in India are not eligible for bank credit; they borrow at exorbitant interest rates from private sources. When nature rides roughshod over debt-ridden farmers in the form of erratic monsoon and crop failures, they face grim options. Indebtedness is a key reason for the many farmer suicides in the country. Loan waivers provide some relief to farmers in such situations. Many farmers are leaving farming due to better money making alternatives. If this situation continues, there will be serious food scarcity. To prevent this situation, the government needs to gain the trust of farmers. Thus Farm loan waiver is perceived by the ruling government the easy option. Another big reason of farm waiver is that many farmers borrow money from moneylenders at high-interest rates and get trapped in a never ending cycle of debt. Farm loan waivers help to divert these farmers to borrow money from banks instead of money lenders.

Arguments against Farm Loan Waiver

Loan waiver sends a negative signal to the market. Honest farmers who had taken loans earlier and had repaid using their savings, they feel cheated. It disrupts credit discipline. Loan weaver encourages farmers to turn into willful defaulters in hope of next loan waiver scheme, which is bad for economy. The focus of loan weaver schemes is on mainly small and marginal farmers. This ignores the dominant role of moneylenders and informal credit sources in the rural economy. The farmers who take loans from such sources are not benefitted from such schemes. Loan waiver schemes increase the fiscal deficit of the state as the gross expenditure of the concerned state government exceeds the gross revenue which in turn causes low credit ranking for the state and so the cost of borrowing increases for the state. In certain cases it was seen that rich farmers took heavy loans even if there was no need, in the hope of the next loan waiver scheme. This impacted the farmers who are genuinely in need of loans. Loan waivers not only increase the fiscal deficit and interest burden of the states but also limit its ability to undertake productive capital expenditure in the agriculture sector. It affects the long term growth in the sector. Providing loan waive in some states encourage farmers from other states to demand loan waiver even if they don't need them. There is also a political angle to this. Loan waivers are used as a tool for politicians to gain vote banks in all elections and prevent them from coming up with the long lasting solution. Constant occurrence of such populist actions lead to risks of impaired credit discipline and weak risk-reward for banks and reduced credit availability for borrowers. Farm loan waivers affect credit-off take and induce further stress on banks. The farm sector nonperforming assets (NPAs) account for 16% of the bank's advances under the priority sector lending as of October 2018. The State Bank of India (SBI), the country's largest lender, its NPAs stood at 6.4% before June 2017 when farm-loan waivers were announced in UP and Maharashtra. By September 2018, this rose to 11.4%, according to a report by Macquarie Research. Further announcement of farm loan waivers by selected governments can only worsen the situation of already beleaguered banks. Repeated occurrences of loan waivers hurt the credit culture in the country. Public sector banks are the worst affected because of their high exposure to agriculture and farm loans. Studies done by the Kolkata based Indian Statistical Institute and the World Bank have showed that loan waiver is not a solution to Indian agriculture mess. The institute's 2013 study showed increase in loan repayment default after the Central government announced farm loan waiver of Rs 60,000 crore in 2008, a year before general election. Honest farmers repaying the loan also turned defaulters after the waiver, the study said. In a study named "The Economic Effects Of A Borrower Bailout: Evidence From An Emerging Market" by Xavier Giné and Martin Kanz of the World Bank, the authors said schemes like loan waiver can affect agriculture output in medium to long term as banks may get more selective in extending credit. The authors also opined that there is no evidence of greater investment, consumption or positive labour market outcomes in areas where debt relief led to a significant reduction of household debt. A 2015 ICRIER paper said the massive write-off of loans in 2008 took its toll on the banks, increasing the non-performing assets of commercial banks threefold between 2009-10 and 2012-13.

CONCLUSION

In the present situation, farm loan waivers act only as a temporary solution to the problems of farmers and it will not make them free from issues like decreasing farm income, debt trap or crop failures. In this context, there is a need for creative engagement through which the surplus workers in the farming sector can be taken away to more productive sectors and farming can be made more profitable and sustainable for all the people. Measures to reduce input costs will help the farmers to avoid debt trap. Direct cash transfer is a better option than debt relief to incentivize the farmer and enable them to meet pre-operative expenses – and is proactive rather than reactive in nature. Returns on cultivation should be ensured through an appropriate minimum support price (MSP) on farm products and/or reducing input costs. There has been a demand to raise the MSP of all commodities to 1.5 times the cost – as recommended by the Swaminathan Committee. While loan waiver schemes are like a band-aid on a wound, it is the larger agrarian distress that demands urgent policy attention. Unless there are steps to raise productivity, reduce costs of cultivation by providing quality inputs at subsidized rates, provide remunerative prices following the recommendations of the Swaminathan Commission, ensure assured procurement of output, expand access to institutional credit, enhance public investment for infrastructural development, institute effective crop insurance systems and establishment of affordable scientific storage facilities and agro-processing industries for value addition, farmers will continue to be bonded to low-income equilibrium and will repeat the debt traps.

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