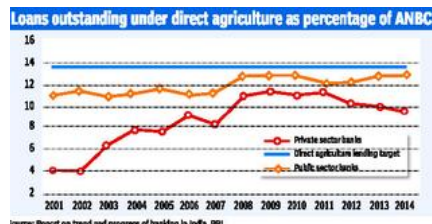


New lending norms will hurt small farmers

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The RBI has reintroduced 'direct' loans without curbs on 'indirect' ones, which defeats the purpose



Back-to-back droughts have prompted the Reserve Bank of India to go back to the policy of setting a direct agricultural lending target for banks. But lifting the cap on indirect lending may defeat the purpose, with damaging implications for agriculture.

Direct lending implies finance to individual farmers, including SHGs, for dairy, piggery, poultry and beekeeping, among other activities. It includes crop loans, investment credit, post-harvest credit and purchase of land by small and marginal farmers for agriculture purposes.

Indirect lending entails loans to agro and food processing units, finance for the purchase of agri-machinery, loans to NBFCs and for the construction of storage facilities, among other activities that require more capital than direct lending.

Confused flip-flops

In April this year, on the basis of recommendations of an internal working group set up to revisit existing priority sector lending guidelines, the RBI had announced fresh norms which abolished the distinction between direct and indirect agriculture lending, but set targets for loans to small and marginal farmers.

However, in its November 18 notification, the RBI directed banks to ensure that their overall direct lending to non-corporate farmers does not fall below the level of 11.57 per cent of adjusted net bank credit (ANBC) in the fiscal 2015-16. They were also advised to continue to reach the level of 13.5 per cent direct lending to the beneficiaries who earlier constituted the direct agriculture sector.

In view of the neglect of small and marginal farmers in direct credit, under the new guidelines a sub-target of 8 per cent of ANBC is recommended for small and marginal farmers within the agricultural target of 18 per cent of ANBC. This is to be achieved in a phased manner — 7 per cent by March 2016 and 8 per cent by March 2017.

Relaxing the stipulation that indirect credit to agriculture should not exceed 4.5 per cent of ANBC will incentivise indirect lending. Though an increase in indirect finance may be necessary to facilitate farming activities, it should not lead to an undermining of the latter. Domestic banks have been unable to achieve the target of 13.5 per cent of ANBC, existing over the years, for direct agriculture lending. This includes public sector banks, which have reported slippages since 2001.

Though the advances to direct agriculture by private sector banks has increased manifold — from 4 per cent of ANBC in 2001 to 11.3 per cent of ANBC in 2011 — it has remained well below the target of 13.5 per cent of ANBC.

In sharp contrast to this, the indirect lending percentage of ANBC was always above the cap of 4.5 per cent of ANBC except in 2012 and 2013. Indirect credit over and above 4.5 per cent is allowed to be taken into consideration in meeting the overall target of 40 per cent for priority-sector advances — providing an incentive to neglect direct lending.

Hence, notwithstanding the upper limit, there was an incentive to give indirect credit to agriculture. In the post-reform period, there has been a significant shift towards indirect lending to farmers. Of the total increase in credit supply between 2002 and 2010, more than one-fourth was contributed by indirect finance. Relaxing the requirement of 4.5 per cent of ANBC for indirect credit will worsen matters.

Priority lending tag

An RBI advisory committee had noted in 2004 that “indirect lending needs to be subject to certain limitations, lest banks neglect direct finance for agricultural production, which may jeopardise the goal of achieving annual growth of 4 per cent in agricultural production”.

Therefore, it is important to place a limit under indirect finance. Advances exceeding the limit should not be taken into consideration in meeting the overall lending requirement of 40 per cent under priority sector.

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