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INFORMAL CREDIT AND RURAL INDEBTEDNESS IN INDIA

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1. INTRODUCTION

Though financial liberalization and other public sector policies are on the way, a perusal at the sectoral deployment of credit in India in the post reform period witnessed subtle changes. Reforms and the evolving economic structure had a profound impact on the flow of bank credit to various sectors of the economy during the 1990s, 2000s and the current decade. Credit growth to agriculture during the 1990s slowed down to almost one-half as compared with the 1980s, though the trend was reversed beginning from 2002-03 as a result of concerted efforts made by the Reserve Bank and the Government to increase the flow of credit to agriculture. Credit to the industrial sector slowed down, *albeit* marginally, in the 1990s and the current decade as compared with the 1980s. On the face of these, a significant development during the current decade has been the rapid credit expansion to the household sector (personal loans) in the form of housing and other retail loans. To sum up, generally, the share of agriculture and industrial sectors in total bank credit declined between end-March 1990 and end-March 2005, while that of personal and professional services increased sharply (RBI, 2006).

According to the All India Debt and Investment Survey (AIDIS) 2002, the share of institutional agencies in outstanding cash debts of the households declined from 66.3 per cent in 1991 to 57.1 per cent in 2002, with a corresponding increase in reliance on informal channels of credit (RBI, 2006). Although, the share of institutional credit might have arisen on account of significant increase in bank credit to agriculture in recent years, concerns about inadequate access to credit in rural areas remain. Such a trend is disturbing, given the fact that credit market policies were aimed at increasing the efficiency, productivity and flexibility to provide access to credit to the agriculture, small scale industries and weaker sections of the society. The uneven pattern of sectoral distribution of credit in spite of increase in annual growth of credit and Credit-GDP Ratio, tend to study the trends and patterns in rural credit and rural indebtedness with reference to informal credit.

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Such a study is warranted since the policy reforms in India were aimed at eliminating the evil effects of informal credit The present paper is an attempt in this direction.

2. CRUMBLING DOWN OF THE PRE-REFORM FRAMEWORK

The biggest achievement of nationalisation was the reallocation of sectoral credit in favour of agriculture, small industries and exports, which formed the core of the priority sector. However, bank nationalisation created its own problems like excessive bureaucratization, red-tapism and disruptive practices of trade unions of bank employees. To quote RBI (2002): "after the nationalisation of large banks in 1969 and 1980, Government owned banks have dominated the banking sector. The role of technology was minimal and the quality of service was not given adequate importance. Banks also did not follow proper risk management systems and the prudential standards were weak. All these resulted in poor asset quality and low profitability. During this period, commercial banks in India functioned in a highly regulated environment characterised by administered interest rate structure, quantitative restrictions on credit flows, high reserve requirements under CRR and SLR etc. These restrictions among others resulted in low productivity and inefficiency, which in turn led to low/negative profits. Controlled interest rates in the financial sector due to inflation and was deemed to adversely affect the deepening of the financial system and the savings rate (D'Souza 1998).

The financial system has thus evolved in an environment of administered interest rates and maintaining stipulations on credit distribution. The deposit and lending rates of banks were fixed by a complex web of regulations. A substantial part of the credit was channeled to the Government and priority sectors at below market rates. The financial system was dominated by public institutions and there was hardly any competition. These government controls were intended to provide cheap credit to specific sectors and economic activities and to finance the budget constraints at relatively low cost. In order to meet these objectives, there was cross subsidisation in the financial system. An element of cross subsidisation implicit in an administered system of lending rates meant that some borrowers had to pay higher rates than others. The Indian financial system remained largely segmented due to an administered interest rate regime and direct credit controls, which prevented proper pricing of instruments. Since then, government raised resources from the banking system at interest rates, which were not market-related. In short, in the pre reform period, Government of India determined the quantum, allocation and price of credit, a situation referred to as *'financial repression'* in the financial system.

It is noted that the actual realisation of interest income in banks has been much lower because of the high level of non-performing assets (Rangarajan 1997). Government also imposed cash reserve requirements consisting of cash reserve

ratio (CRR) and statutory liquidity ratio (SLR). The supply of bank finance to corporate sector has to be viewed against this because if the reserve requirements is high, it could lessen the overall resources available to commercial banks for lending and vice versa. The negative implication of financial repression was evident from the fact that, by 1991, statutory preemptions under the CRR and SLR, on an incremental basis, reached a level of 63.5 per cent, and even of the balance 36.5 per cent, there were preemptions under the priority sector of 40 aper cent, export credit, food credit, and other formal and informal preemptions (Tarapore 1997). Thus it is argued that credit allocation under the financial repression regime resulted in distorted resource mobilisation by firms and restricted the freedom of intermediation of banks. The retail lending to more risk-prone areas at concessional interest rates has raised costs, also affected the quality of bank assets and strained their profitability. The inefficiency in the deployment of credit and deteriorating bank profitability also went hand in hand with inadequate capitalization and insufficient provision for bad debts by the banks (Government of India 1991).

Prior to liberalization the instruments of control in the financial sector included various interest rates on deposits and lending being fixed by the central bank, high reserve requirements, quantitative credit restrictions, concessional interest rates for specified sectors along with cross-subsidisation, and restrictions on the scope of activities of financial institutions (D'Souza 1998). Financial markets were thus characterised by barriers to entry, control over pricing of financial assets, high transaction costs and restrictions on movement of funds from one market segment to another in the controlled regime.

It was in this backdrop that wide-ranging financial sector reforms were introduced in mid 1991. The first attempt to reform the financial sector was undertaken with the release of the Chakravarty Committee Report in 1985, which reviewed the working of the monetary system. Later, against the backdrop of the balance of payments crisis in 1991 and the macro-economic adjustment, the Narasimham Committee was appointed with a view to promoting a diversified and competitive financial system as part of the overall structural reforms. The recommendations of the Chakravarty and Narasimham Committee resulted in many new steps by the Reserve Bank of India to move away from direct monetary policy instruments to indirect monetary control. The pre-reform model of bank based financing thus began to crumble down by the early 1990s. With the structural reforms initiated in 1991, the need was recognised to orient the financial sector towards market-guided signals. The 1990s ushered in the first phase of financial sector liberalisation to coincide with the real sector deregulation. Liberalisation of financial sector means softening of allocative regulations and hardening of prudential regulations; moving away from the regime of administered rates towards market determined rates; and providing better access to money and capital

market to higher credit rated industrial clients with an aim of promoting efficiency. With this in mind, in the next section we analyse the policy changes that is likely to have had its impact on quantum, cost and instruments for the availability of funds for financing investment.

3. POLICY REFORMS AND SOURCES OF CREDIT

Financial sector liberalisation has shifted the focus of financial repression, from the 'control of financial products prices' to prudential regulation, supervision and promotion of competition' (Joseph *et al.* 1999). The thrust of these reforms was the deregulation of capital markets and banks, deregulation of interest rates, withdrawal of credit targeting and interest subsidies, introduction of stricter accounting norms in the banking sector and the integration of domestic financial markets with the international financial markets through external sector liberalisation of capital flows. The general approach of the liberalization was to open up the economy, give the market a greater role in price setting, and increase the private sector's role in development. It aimed at promoting a diversified, efficient and competitive financial system with the ultimate objective of improving the allocative efficiency of available resources through operational flexibility, improved financial viability and institutional strengthening (GoI 1991; 1993). It is expected that increased reliance on market forces for determining the cost and availability of funds.

In what follows we discuss policy changes pertaining to cost and availability of credit in various constituents of the financial markets. In the following sub sections, instead of giving a comprehensive discussion of Indian financial sector policies, we confine only to major aspects of the changes in policy regime that would have an impact on the credit availability.

3.1. Reduction in Reserve Requirements and Availability of Funds

Narasimham committee recommended that RBI should rely on open market operations increasingly and reduce its dependence on CRR. As a result, the CRR, which was 15 per cent in 1991-92, was reduced to 4.75 percent in 2003-04 (Table 2.1). Apart from the CRR, SLR provision has created a captive market for government securities, which increases automatically with the growth in the liabilities of banks. The base SLR that stood at 38.5 percent in 1990-91 has come down to a uniform level of 25 percent from 1997-98 onwards (Table 2.1). The expectation was that this would reduce the amount of cash balances of the banks with the RBI enabling them to increase their revenues through more investments. It suggests that these reductions will have implications for availability of credit. Along with these reductions, bank rate also met with a decline to which all other rates are aligned, but only after 1996.

3.2. Interest Rate Liberalisation – Declining Cost of Credit

Interest rate liberalisation formed an integral part of financial reforms. In 1991, with freeing interest rates, the structure of administered interest rate was dismantled (Reddy 1999). Almost all major interest rates have been set free with banks and financial institutions themselves determining their own minimum lending rates and 1-year deposit rates (table 2.2) except the saving deposit rate, which is set by the RBI. Government also reduced the volume and burden of directed credits, in order to increase credit to the private sector. Loan rates actually began to be liberalized in 1988, when the maximum rate on non-directed credit was turned in to a minimum. After 1992, the number of interest rate categories for different types of loans was reduced sharply, and most directed credit (priority sector credit) was gradually shifted to free rates. By March 1998, banks were allowed to set different rates for the same maturity deposits and set their own penalties for early withdrawal (Hanson 2004). Consequently, the nominal interest rate structure had undergone drastic changes with all the rates showing declining trend, especially after 1996. Till 1991-92 interest rates moved upward and started declining afterwards. The country has moved towards liberalized credit allocation mechanism and reduced control over interest rates by the monetary authorities. By 1997-98, most of the interest rate liberalization was complete. The implication is that reduction in interest rates will promote investment through greater access towards cheaper credit from financial institutions.

3.3. Prudential Reforms and Institutional Strengthening

As part of financial liberalization, internationally accepted prudential norms relating to income recognition, asset classification, provisioning for bad and doubtful debts and capital adequacy norms etc., have been introduced. These norms are recognized world over and are considered fundamental in ensuring the soundness and solvency of commercial banks. A proper definition of income is essential in order to ensure that banks take in to account income, which is actually realized. Banks have now been given a clear definition of what constitutes a 'non-performing' asset and instructions have been used that no interest should be charged and taken to income account on any 'non-performing' asset. The definition of 'non-performing' asset is also being tightened over a time. Banks are now required to make provisions on advances depending on four types of classification viz., standard assets, sub-standard assets, doubtful assets and loss assets (Rangarajan 1997). The provisioning requirement ranges from 10 per cent to 100 per cent depending on the category of the asset.

In nutshell, the reform measures have been mainly directed towards removing the liquidity constraints of firms and industries in the corporate sector and making finance available at competitive rates. In the case of institutional strengthening, it has introduced a framework for strengthening the supervisory process and created

new institutions like the Board of Financial Supervision, Ombudsman and Debt Recovery Tribunals to make substantial improvement in terms of frequency, coverage, focus and tools of supervision. Recently, credit rating agencies set up at the initiative of financial institutions are operational in guiding the credit risk associated with debt instruments. Their indication of the relative capacity of a corporate entity to service its obligations within a specified time period and with reference to a particular debt instruments being rated, has great impact on the credit market.

3.4. Changes in Priority Sector Lending

Narasimham committee recommended certain changes in the norms of priority sector lending. The direct credit programme should cover a redefined priority sector comprising small and marginal farmers, tiny sector industry, small business and transport operation, village and cottage industries, rural artisans and other weaker sections with credit targets to be re fixed at 10 percent of aggregate bank credit. It was recommended that concessional interest to the redefined priority sector should be reviewed with a view to its eventual elimination, in about three years. At the end of every three year review should be made to see whether the directed credit programme should be continued.

Though the Narasimham Committee redefine the priority sector, so as to cover only the weaker sections and to reduce drastically the target for priority sector lending, what the banking authorities have done is exactly the opposite, though the result were not much different. No reduction was made in overall targets of the priority sector. But more items, which had till then remained outside the priority sector, were included under priority sector. The redefinition of the priority sector is as follows.

- There was a sub-target for agricultural advance, namely that indirect advances should not exceed one-fourth of the total agriculture advance. By including the indirect advances under the priority sector this sub-limit was later lifted. Financing and distribution of inputs for taking up allied activities up to Rs 5 lakh were thereafter to be treated as priority sector advance. All these stipulations reduced the scope of direct advances to the agriculture sector;
- All short-term advances to plantation crops, including tea, coffee, and rubber was included in priority sector advances irrespective of the size of holding.
- In the case of small-scale industrial units, the limit of investment in plant and machinery was raised in 1994 to Rs 60 lakh from Rs 35 lakh. Subsequently, it was further raised to Rs 1 cr.
- Existing credit limit of other priority sector advances was also raised, i.e., of retail traders from Rs 25,000 to Rs 2 lakh, of business entrepreneurs

from Rs 2 lakh to Rs 10 lakh, and of professional and self-employment from Rs 1 lakh to Rs 5 lakh.

- In October 1997, the scope of the priority sector credit to road and water transport operation was widened by increasing the number of eligible vehicles from 6 to 10.
- One of the housing loans given to weaker sections had been under the priority sector before 1994. But after 1994, all housing loans up to Rs 3 lakh (revised again to Rs 5 lakh) came to be considered priority advances.
- In addition, contributions made by public sector banks to Rural Infrastructure Development Fund and Khadi and Village Industries Commission also came to be treated as priority sector advance

The assumption is that, these reforms must have affected credit disbursement by commercial banks to priority sectors. Though the priority sector lending had nearly reached the target (of 40 percent) in 1990, it was continually declining since then till 1996. It is also seen that the CD ratio of banks was continuously declining since 1991. After 1996, the priority sector advances improved due mainly to the widening of the priority sector.

4. INFORMAL CREDIT AND RURAL INDEBTEDNESS IN INDIA

The All India Debt and Investment Surveys from 1961 to 2002 in respect of number of indebted households, outstanding households' debt and outstanding debt per indebted household in rural areas showed in table 3.9. The number of indebted households, in absolute terms as well as percentage to total households, declined sharply from 43.1 million (62.8%) in 1961 to 31.8 million (41.3%) in 1971 and further to 18.2 million (19.4%) in 1981. Thereafter, however, number of indebted households and their percentage to total households, increased significantly to 27.2 million (23.4%) in 1991 and 39.2 million (26.5%) in 2002, but could not reach the level of 1961. Amount of outstanding households' debt progressively increased from Rs.27,89 crores in 1961 to Rs.22,211 crores in 1991 and further to Rs.1,11,468 crores in 2002. However, outstanding households' debt in terms of per cent of GDP at current market prices declined from 21.4% in 1961 to 6.3% in 1991 and then significantly rose to 9.4% in 2002. Debt per household also progressively increased from Rs.647 in 1961 to Rs.28, 443 in 2002 in nominal terms. However, in terms of 1999-00 prices, debt per household declined slightly from Rs.12, 629 in 1961 to Rs.12,356 in 1971 but significantly increased in 1981, 1991 and 2002 (table 1).

It is seen from table 2 that number of borrowing households from institutional sources marginally increased from 7.5 million in 1961 to 7.6 million (101.3%) in 1971, which however significantly rose to 8.9 million (117.1%) in 1981 and sharply to 18.2 million (204.5%) in 1991 and 19.8 million (108.8%) in 2002. As against this, number of borrowing households from non-institutional sources significantly

Table 1
Number of Indebted Households, Outstanding Households' Debt, Outstanding Debt per Indebted Household in Rural Areas

End- June	*Number in Million*	*Amount of debt (Rs. Crores)*	*Debt per household Rs. Nominal Terms*	*Period*	*Compound Annual Growth Rate (in % age)*
1	*2*	*3*	*4*	*5*	*6*
1961	43.1 (62.8)	2789 (21.4)	647 (12629)	1961-71	3.0 (-3.2)
1971	31.8 (41.3)	3752 (12.2)	1180 (12356)	1971-81	5.1 (-3.7)
1981	18.2 (19.4)	6193 (6.2)	3411 (14904)	1981-91	13.6 (4.3)
1991	27.2 (23.4)	22211 (6.3)	8166 (15105)	1991-02	15.8 (8.5)
2002	39.2 (26.5)	111468 (9.4)	28443 (25711)	–	–

Note: Figures in the brackets in Col-2 indicate number of indebted households as percentage to total households, in Col-3 indicated per cent of GDP at current market price, in Col-4 indicates at 1999-00 prices & in Col-6 indicates at 1999-2000 prices.
Source: All India debt and Investment Survey, NSSO (various rounds)

declined from 35.6 million in 1961 to 24.2 million (67.9%) in 1971 and steeply declined to 9.3 million (38.4%) in 1981, which, then significantly increased to 11.4 million (122.6%) in 1991 and sharply shot up to 22.9 million (200.9%) in 2002. The pattern has been that with the declining total number of indebted households from 1961 to 1981 and increasing from 1991 to 2002, the number of indebted

Table 2
Number of Indebted Households & Outstanding Household debt institutional and non-institutional sources

Credit Agency	*Number of Indebted Households (Million)*					*Outstanding Debt (Rs. in Crores)*				
Year	*1961*	*1971*	*1981*	*1991*	*2002*	*1961*	*1971*	*1981*	*1991*	*2002*
Institutional	7.5	7.6	8.9	18.2	19.8	413	1094	3794	14215	63648
	(17.3)	(24.0)	(48.8)	(61.5)	(46.4)	(14.8)	(29.2)	(61.3)	(64.0)	(57.1)
Non-Institutional	35.6	24.2	9.3	11.4	22.9	23760	2658	2399	7996	47820
	(82.7)	(76.0)	(51.2)	(38.5)	(53.6)	(85.2)	(70.8)	(38.7)	(36.0)	(42.9)
All Agencies	43.1	31.8	18.2	29.6	39.2	27890	3752	6193	22211	111468
	(100)	(100)	(100)	(100)	(42.7)	(100)	(100)	(100)	(100)	(100)
CAGR: Institutional	–	–	1.77	8.27	0.85	–	–	–	–	–
Non-Institutional	–	–	–	2.29	7.22	–	–	–	–	–
All Agencies	–	–	–	5.55	2.85	–	–	–	–	–

Figures in the brackets indicates percentage to the total, CAGR= Compound Annual Growth Rate
Source: Calculated from NSSO (various rounds)

households to non-institutional sources also declined from 1961 to 1981 and then increased between 1991 and 2002.

The data of the All India Debt and Investment Survey (AIDIS) conducted by the National Sample Survey Organization (NSSO) revealed that between 1961 and 1981 the number of borrowing households as well as households borrowing from non-institutional sources continued to decline significantly and thereafter between 1991 and 2002, their number significantly increased. As against this trend, number of households borrowing from institutional sources, however, marginally increased between 1961 and 1981 and the increase was significant between 1991 and 2002. The percentage share of households borrowing from non-institutional sources in the total was higher than that of households borrowing from institutional sources in all decades except decade ended 1991. The percentage share of outstanding debt of households borrowing from non-institutional sources in the total outstanding debt continued to decline in all decades except decade ended-2002. The outstanding debt of households borrowing from non-institutional sources in terms of percentage to total outstanding debt was considerably higher than that of borrowing from institutional sources between 1961 and 1971, which then declined significantly between 1981 and 2002 (table. 2).

4.1. Share of Formal and Informal sources in the Rural Credit Market of India

Among the Non-institutional Agencies (NIAs), Professional Moneylenders are in the top position. Though the relative share of these groups varies over the years their grip over the Rural Credit Market has not been loosened. According to the All India Rural Credit Survey Committee (1954), the Share of NIAs in the total rural credit was 92.7 per cent in 1951-52. The percentage has come down to 81.3 in 1961-62 and to 68.3 in 1971-72 (Tab le3). The Cooperative Banks did not make much progress before independence in reducing the role of NIAs in the rural credit market. The nationalization of commercial banks and emergence of RRBs widened the branch network in rural areas thereby reducing the market share of NIAs has increased up to 42.9 per cent in the year 2001-02. The dominance of NIAs in rural credit market has remained as a factor to reckon with. The share of Institutional agencies in the Rural Credit Market increases from 7.3 per cent in 1951-52 to 66.3 per cent in 1991-92. It stood 57.1 per cent in the year 2001-02. However, still more than 30 per cent of the rural credit has to be sourced from Non-Institutional Agencies and as a result the performance of Institutional agencies in rural credit market has attracted lot of criticism from the planners, academicians and researchers.

Table 3 gives the distribution of outstanding debt of all rural households by source of credit. It can be observed that, the most remarkable performance was that of the commercial banks while the share of co-operative societies in the outstanding cash dues of cultivator households increased from 22 per cent in 1971

Table 3
Share of Institutional and Non Institutional Agencies in Rural Credit

Agency	*1951-52@*	*1961-62#*	*1971-72**	*1981-82**	*1991-92**	*2001-02^*
Government	3.3	2.6	7.1	3.9	5.7	5.3
Cooperatives	3.1	15.5	22.0	29.9	23.6	27.3
Commercial Banks	0.9	0.6	2.4	28.9	35.2	24.5
Others	00	00	0.2	0.5	0.7	00
All Institutional Agencies	7.3	18.7	31.7	63.2	66.3	57.1
Landlords	1.5	0.6	8.1	3.6	3.7	2.2
Agricultural moneylenders	24.9	36.0	23.0	8.3	6.8	8.1
Professional moneylenders	44.8	13.2	13.1	7.8	10.7	21.5
Traders & Commission Agents	5.5	8.8	8.4	3.2	2.2	3.2
Relatives & Friends	16.2	8.8	13.1	8.7	4.6	6.7
Others	1.8	13.9	2.6	5.2	2.6	1.2
Non-Institutional Agencies	92.7	81.3	68.3	36.8	30.6	42.9
All Agencies	100.0	100.0	100.0	100.0	100.0	100.0

Sources: 1. @ Report of the All-India Rural Credit Survey Committee, Abridged Ed., (1954), p-6
2. # All India Debt and Investment Survey 1961, Quoted by Tandon P.L., A Profile of Rural Indebtedness, Social Scientist, Vol. 1 6(4), 1988.
3. * Government of India (1998), Debt and Investment Survey, Report 420, p. 26.
4. ^ Compiled from various publications of NSSO (1998a, 1998b and 2005)

to 29.9 per cent in 1981, therefore dropping to 27.3 per cent in 2002, that of commercial banks rose to 35.2 per cent in 1991, after rising sharply to 28.9 per cent in 1981 from a meager 2.4 per cent in 1971.

It appears that the large number of branches that was set up by various commercial banks in 1970s and the subsequent introduction of rural banking schemes have driven the commercial banks to assume the role of principal credit agency in rural areas. It may be of interest to note that the share of government departments in the outstanding cash dues of cultivator households, after showing a decline from 7.1 per cent in 1971 to 3.9 per cent in 1981, again rose to 5.7 per cent in 1991 and remained somewhat stable at 5.5 per cent in 2002. As a whole, at the all India level, among the *institutional* credit agencies, the co-operative societies and the commercial banks were the two most important agencies in the rural sector. These two agencies together, shared 91 per cent of the entire amount of debt advanced by the *institutional* agencies, accounted for 52 per cent of the outstanding cash debt, with *co-operative societies* (27.3 per cent) accounting for a greater share than the *Banks* (24.5 per cent) in 2001.

The gradual increase in the share of formal institutional credit in agriculture witnessed some reversal during 1991-2002 mainly because of a pull back by

commercial banks. This disquieting trend is, in part, due to a contraction in rural branch network in the 1990s, and in part due to the general rigidities in procedures and systems of institutional sources of credit (Subbarao, 2012).

The combined share of all the *non*-institutional credit agencies in the outstanding cash dues of cultivator households recorded a sharp decline of 32 percentage points during 1970s but the decline got arrested in the 1980s – the fall being just of about 3 percentage points but increased to 43 per cent subsequently. The decline is found to be the steepest for the credit agency 'agricultural money lenders', whose share came down to 6 per cent in 1991 from about 9 per cent in 1981 and 23 per cent in 1971. However, the share of 'professional money lenders' has reported a rise to about 9 per cent in 1991, after registering a fall to 8 per cent in 1981 from about 14 per cent in 1971. Subsequently, the share has jumped to about 20 per cent in 2002. Relatives and friends appear to be gradually losing their importance as a source of credit. From 14 per cent in 1971, their share fell to 9 per cent in 1981, and dipped further down to about 7 per cent subsequently. As a whole, among the *non-institutional* agencies, *professional money lenders* were the main source of credit. Among the *non-institutional* credit agencies, money lenders – both *professional* and *agricultural* – in that order were found to be important sources of finance in rural areas, their respective shares being 19.6 per cent and 10.0 per cent. The share of *relatives and friends* was 7 per cent of the cash dues of rural households. A major reason for increase in the overall household debt and the increase in the share of households indebted to non-institutional sources between 1991 and 2002 was attributed to a significant increase in current farm expenditure and household expenditure in rural areas. The household expenditure of rural households included many items for which households found it difficult to obtain loans from institutional sources.

4.2. Back to Informal Credit– Financial Reform Questioned

The analysis of institutional lending to agriculture proved that reforms have failed to accelerate credit flow to the farm households. This is reflected in the changes in the composition of borrowing in rural areas since 1991. The data on the sources of credit reveals that the debt of households is on the rise with a significant amount emerging from the non-institution (informal) sources. The relative share of institutional sources of credit increased from 53.3 per cent to 57.2 per cent 1991-92 to 2002-03, showing an improvement in the institutional sources of lending. However, this impression is lost when we compare the composition of the sources of credit for rural areas and urban areas because in the case of the latter, the contrast is striking since there is sharp increase in the share of institutional agencies. The share of institutional credit in the urban areas has increased from 59.9 per cent in 1991-92 to 75.7 per cent in 2002-03 (Table 4).

Table 4
Share of institutional and non-institutional sources in cash borrowings (in per cent)

Agency	*Rural*		*Urban*	
	1991-92	*2001-2002*	*1991-92*	*2001-2002*
Institutional Agencies	53.3	57.2	59.9	75.7
Co-operative societies/bank	25.7	28	21.9	22
Commercial banks	20.7	22.7	16.3	30.6
Non-institutional agencies	42.3	42.8	37.4	24.2
Land lord	3.9	0.6	0.3	0.2
Agricultural Money lender	8.1	9.6	0.6	0.6
Professional money lender	13.3	20.6	14	13.3
traders	4	2.9	3.5	1.3
Relatives and Friends	8.9	7.4	13.9	7
Others	4.2	1.7	5.1	1.8

Source: NSSO, All India Debt and Investment Survey (AIDIS), NSS 59th Round, 2006, No. 502

Regarding non-institutional credit (informal credit), the share of professional money lenders in the rural sector increased from 13.3 per cent in 1991-92 to 20.6 per cent in 2002-03, while the share of professional money lenders and landlords in the urban sector came down. On the aggregate, while the share of informal credit has remained the same in the rural sector, its share has gone down sharply in the urban sector. This suggests that in the rural credit scenario, the domination of non-institutional credit dominates with professional money lenders as an important source of rural households.

4.3. Indebtedness of Cultivator Households

As in the case of total households, the contraction of formal banking is reflected in the composition of credit by sources of farmer households. The analysis reveals certain trends that require immediate attention. The share of non-institutional credit, though declined to 30.6 in 1991 from a very high level of 92.7 per cent in 1951, regained its importance in the post 1991 period. Informal credit reversed by increasing to 38.9 per cent in 2002 with money lenders contributing a major share in it. On the other hand, the share of institutional credit came down from 66.3 per cent in 1991-92 to 61.6 per cent in 2002-03. With the share both cooperative societies and commercial banks declined (Table 5).

The small and marginal farmers began to really marginalize and the result of reforms appears have been one of driving the poor against the clutches of the money lender. Total debt of farmer households was estimated at Rs. 1.12 lakhs crore in 2003, of which rupees 65 thousand crore was from institutional agencies and Rs. 48000 crore from non-institutional agencies. Private money lenders accounted for 29,000 and traders 6000 crore. About Rs. 18000 crore debt from non-institutional sources, a major portion of which was from money lenders, carried

Table 5
Share of Borrowing – Cultivator Households (in per cent)

Sources of credit	*1991-92*	*2001-02*
Non-institutional	30.6	38.9
Of which money lenders	17.5	26.8
Institutional	66.3	61.1
cooperative societies	30	30.2
commercial banks	35.2	26.3

Source: NSSO, All India Debt and Investment Survey (AIDIS), NSS 59th Round, 2006, No. 502

an interest rate greater than 30 per cent (Government of India, 2006). The analysis calls an urgent need to relieve the farmers from private money lenders lending on high interest rate by revamping the institutional credit delivery system. The percentage share of cultivator households and their share of borrowings from institutional sources in the total progressively increased from 1961 to 1991, but significantly declined between 1991 and 2002. Of the 89.33 million farmer households estimated in 2003 about 43.42 million (48.6%) were indebted. In other words, more than half (45.91 million) or 51.4% had not accessed debt either from institutional or non-institutional sources. A large proportion of them might have been financially excluded.

Table 6
Distribution of outstanding debt of rural Dalit and Non-Dalit households by source of credit (1992 and 2002), (in per cent)

Type of Source	*Dalit households*		*Non-Dalit households*	
	1992	*2002*	*1992*	*2002*
All formal sources	61.1	44.8	64.6	59.0
Cooperatives	15	18.3	22.9	28.8
Commercial banks	34.6	21.6	33.6	25
All informal sources	36.6	55.2	31.9	41.0
Landlords	8.5	2.3	3.1	0.7
Agriculturist moneylenders	8	15.1	6.8	9.2
Professional moneylenders	10.4	27.6	10.5	18.4

Source: NSSO (1998 and 2006).

According to the AIDIS, in 2002, more than half of the total debt outstanding of Dalit households in rural India was from informal sources (Table 6). The share of formal sources in the total debt of Dalit households was only 44.8 per cent, much lower than the corresponding share (59 per cent) for non-Dalit households. Among formal sources, the largest share of debt of Dalit households was owed to commercial banks, followed by cooperatives. Among informal sources, professional moneylenders were the single most important source of debt for these households.

Table 7
Percentage of rural Dalit and non-dalit/non-adivasi households reporting at least one loan outstanding from formal and/or informal sources (1992 and 2002)

Type of Source	*Dalit households*		*Non-Dalit and Non-Adivasi households*	
	1992	*2002*	*1992*	*2002*
All formal sources	17.1	11.9	15.8	14.3
All informal sources	11.2	17.0	9.9	16.1

Source: NSSO (1998 and 2006)

An inter-round comparison of the AIDIS data from 1962 onwards shows that, with regard to the share of formal sources in the total debt of all rural households, there was a distinct break in the overall trend after 1992. The share of formal sources, commercial banks in particular, rose steadily between 1962 and 1992, and then fell between 1992 and 2002 (Table 7). The rise in the share of formal sources was particularly striking between 1972 and 1982, the period following the establishment of the policy of social and development banking. Separate data on Dalit households are not available from the AIDIS rounds before1992. Nevertheless, the data do indicate that Dalit households in rural areas gained new and often unprecedented access to formal sector credit. The Integrated Rural Development Programme, which "channelled funds on a hitherto unprecedented scale for creating supplementary incomes amongst the relatively poor in rural areas all over India" (Guhan 1986) – was the most important means of such access. Between 1992 and 2002, as was the case with all rural households, the share of formal sources in the total debt of rural Dalit households declined. However, the decline for Dalit households was greater than for non-Dalit households (Table 7). Debt from formal sources as a percentage of the total debt came down by about 16 percentage points between 1992 and 2002 for Dalit households as compared to five percentage points for non-Dalit households. Thus, in the 1990s, Dalits suffered more than others from the cutbacks in formal credit to rural areas. AIDIS data also show that, between 1992 and 2002, the number of Dalit households reporting at least one outstanding loan from formal sources fell by about five percentage points. The corresponding fall for non-Dalit households was only about one percentage point (Table 7).

Prior to liberalization the instruments of control in the financial sector included various interest rates on deposits and lending being fixed by the central bank, high reserve requirements, quantitative credit restrictions, concessional interest rates for specified sectors along with cross-subsidisation, and restrictions on the scope of activities of financial institutions (D'Souza 1998). Financial markets were thus characterised by barriers to entry, control over pricing of financial assets, high transaction costs and restrictions on movement of funds from one market segment to another in the controlled regime. As far as the banking sector is

concerned, financial liberalization made it market-determined in the pretext of increasing the efficiency and profitability of the system to compete with the rapidly growing foreign private banks in the country. However, the deprivation of different sectors and sections in terms of access to credit is evident in the post liberalization period.

The State-level estimate indicates that of the total outstanding cash dues, the share of *institutional* agencies had increased marginally during the 1980s in most of the states, after having increased substantially during the 1970s (Table 8). However, the role of the *institutional* agencies, as judged from their share in the outstanding cash dues, varied from state to state. A snapshot of this variation in 2002 shows that in the rural areas, *institutional* credit agencies accounted for 85 per cent in Maharashtra, followed by Kerala (81 per cent), Himachal Pradesh and Orissa (74 per cent each) and Jammu & Kashmir (73 per cent). In contrast, not even 50 per cent of the debt was contracted through the *institutional* credit agencies in the rural areas of Andhra Pradesh (27 per cent), Rajasthan (34 per cent), Bihar (37 per cent) and Tamil Nadu (47 per cent).

Table 8
Share of Institutional and Non-Institutional Agencies in Outstanding Cash Debt of Major States in Rural Areas (Per Cent)

Major States	*Institutional*				*Non-Institutional*			
	1971 (26th)	*1981 (37th)*	*1991 (48th)*	*2002 (59th)*	*1971 (26th)*	*1981 (37th)*	*1991 (48th)*	*2002 (59th)*
Andhra Pradesh	14	41	34	27	86	59	66	73
Assam	35	31	66	58	65	69	34	42
Bihar	11	47	73	37	89	53	27	63
Gujarat	47	70	75	67	53	30	25	33
Haryana	26	76	73	50	74	24	27	50
Himachal Pradesh	24	75	62	74	76	25	38	26
Jammu & Kashmir	20	44	76	73	80	56	24	27
Karnataka	30	78	78	67	70	22	22	33
Kerala	44	79	92	81	56	21	8	19
Madhya Pradesh	32	66	73	59	68	34	27	41
Maharashtra	67	86	82	85	33	14	18	15
Orissa	30	81	80	74	70	19	20	26
Punjab	36	74	79	56	64	26	21	44
Rajasthan	9	41	40	34	91	59	60	66
Tamil Nadu	22	44	58	47	78	56	42	53
Uttar Pradesh	23	55	69	56	77	45	31	44
West Bengal	31	66	82	68	69	34	18	32
All India	29	61	64	57	71	39	36	43

Source: All India Debt and Investment Survey, NSS 59th Round, Report No. 501.

During the periods 1971 to 2002, the states do not reveal any uniform pattern in the share of *institutional* agencies in total debt. Compared to 1991, the picture had changed in some of the major states (Table 8). Of the 20 major states in the rural, as many as 15 have shown a fall in the share of *institutional* agencies, notable among them are Bihar, Punjab, Haryana and West Bengal, where the fall in percentage share from 1991 values had been to the tune of 36, 23, 23 and 14 percentage points, respectively. On the other hand, 13 major states out of 21 had registered a rise in the share, which, barring a few with marginal to moderate rise, can be described as sharp to spectacular.

5. CONCLUSION

Though agricultural suicides are going on for more than a decade, the Government of India has intervened adequately, except the programme of 'debt relief' in 2008. The government has failed either to regulate the activities of informal money lenders in the rural credit market or revamp the credit system in accordance with the needs of the poor rural farmers. In failing to design support credit programmes to ensure adequate credit, the Government is not upholding the rights of farmers and their family to an adequate standard of living. The burden of indebtedness in rural India is very high, and falls mainly on the households of rural working people. The exploitation of this group in the credit market is one of the most pervasive and persistent features of rural life in India, and despite major structural changes in credit institutions and forms of rural credit in the post-nationalized and post-liberalized period, Darling's statement (1925), that "the India peasant is born in debt, lives in debt and dies in debt," still remains true for the great majority of working households in the countryside. Under the duty to protect, the Government of India must ensure that third party actors like (private money lenders, private businesses, private banks etc do not interfere with the enjoyment of the right to credit. As a prerequisite to this, states must revamp the rural credit delivery system by orienting its goals through state participated policies.

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