

# **ARCs for Agriculture Loans**

This editorial is based on <u>"Farming Out"</u> which was published in Indian Express on 07/12/2021. It talks about the issue of bad loans in the agriculture sector and if creating an Asset Reconstruction Company (ARC) for the sector is a prudent way forward.

While farmers in India are struggling to get bank loans, as formal sector lenders have become even more risk averse amid the <u>Covid-19 pandemic</u>, the banks are challenged by huge <u>Non-Performing Assets</u> (<u>NPAs</u>) as they're unable to recover farm loans.

In this context, the <u>Indian Banks' Association</u> in a recently held meeting proposed the idea of floating an <u>Asset Reconstruction Company (ARC)</u> to improve the recovery from <u>bad loans in the</u> <u>agricultural sector.</u>

However, several issues exist with reference to setting up a single mechanism to tackle NPAs in the farm sector.

### **Agriculture and Bad Loans**

- Gross NPAs for Agriculture Sector: As per the RBI's Financial Stability Report, bad loans (gross NPAs) for the agricultural sector stood at 9.8% at the end of March 2021.
  - In comparison, they were at 11.3% and 7.5% for the industry and services sectors respectively.
- Issues Raised by Farm Loan Waivers: The announcement of farm loan waivers by states around elections leads to "deteriorating credit culture".
  - Since 2014, at least 11 states have announced farm loan waivers including Rajasthan, MP, Punjab, Chhattisgarh, Andhra Pradesh, Telangana, Maharashtra, Punjab and UP.
  - It creates a concern among banks regarding the rise of NPAs in the farm sector and leads to recovery challenges for the banks.
    - They often leave the banks reluctant to lend.
  - Loan waivers stress the budgets of the waiving state or central government.
  - Also, these waivers are poorly targeted, and eventually reduce the flow of credit
- Current Mechanism to tackle NPAs of Agri-Sector: At present, there is neither a unified mechanism to tackle NPAs in the farm sector nor a single law that deals with enforcement of mortgages created on agricultural land.
  - However, the recovery laws vary from state to state wherever agricultural land is offered as collateral.
  - Enforcement of provisions on mortgaged farm land is generally done through the Revenue Recovery Act of states, <u>Recovery of Debt and Bankruptcy Act</u>, <u>1993</u>, among other state-specific regulations.

### **Creating ARCs for Farm Sector**

 Recent Proposal: To improve recovery of bad loans in the agriculture sector, leading banks have made a pitch for setting up an ARC specifically to deal with collections and recovery of

#### farm loans.

- With a government-backed ARC having been recently set up to deal with bank NPAs to the industry, this idea has acceptability among banks.
- Arguments in Favour of ARCs for Farm Loans: As agricultural markets are dispersed, a single institution, as opposed to multiple banks, would be more suited to deal with collections and **recoveries** from farm loans, optimising the costs of the recovery.
  - Considering the absence of a unified framework to deal with the enforcement of mortgages created on agricultural land, there is a case for creating an effective mechanism for the recovery of dues.
- Arguments Against Creating ARCs for Farm Loans:
  - First and foremost, the requirement of the ARC is to have sufficient availability of funds to match the huge amount of the NPA market.
    - Even if sufficient funds are available with ARC, the **price expectation mismatch** between selling bank (s) and buying ARC and agreement on an acceptable valuation of the bad assets will also create a challenge for ARC.
  - As local banks have far greater presence on the ground than a single ARC, they are likely to be more capable of navigating the local terrain to recover their dues.
    - Local bank officials may be more successful in dealing with hundreds and thousands of these small borrowers than a single ARC.
  - As rural land markets are characterised by lack of clear titles and multiple **stakeholders,** ARCs specifically the farm sector is not an as prudent approach.
    - Moreover, even though land is a mortgageable asset, it is an emotive, political
  - There is also a possibility that since agriculture is a state subject, such an approach could risk being seen as encroaching on the rights of states.

## **Way Forward**

- Jision Observing the Success Rates of Other ARCs: The government has already set up such a framework (of ARCs) for the resolution of corporate sector loans that have turned bad.
  - Considering that doubts have been expressed over the effectiveness of the architecture of ARCs, a more prudent approach would be to assess its experience and then chalk the way forward.
  - Moreover, if there is indeed a need to provide for a similar framework for agricultural loans, then the same architecture could be employed.
- Alternatives to Help Farmers: There are also other ways to help farmers such as ensuring timely access to credit on more favourable terms.
  - A broader policy framework should be available to facilitate farming to become a more remunerative occupation.
- Easing the NPA Sale Procedure: It is utmost necessary for a rigorous and a realistic approach to pricing between the banks and ARCs.
  - Therefore, it is an urgent need for all stakeholders, including the regulator, to come together to make the entire process of NPA sale, resolution, recovery and revival fast and smooth.

#### **Drishti Mains Question**

Discuss the problem of bad loans that exists in the agricultural sector and what steps can be taken to mitigate the problem.

PDF Reference URL: https://www.drishtiias.com/printpdf/arcs-for-agriculture-loans