CHAPTER V
CAUSES FOR INCREASE OF BANKS OVERDUES

Introduction

Banks are financial intermediaries. They mobilise deposits from the public mainly for the purpose of lending and investment and to earn profits from such operations. Keeping a part of deposits in cash and other liquid assets to enable the banker to meet his obligations towards the depositors, a large part of the funds are employed in income-earning assets like loans and investments. The funds of a banking institution may be classified into two categories, namely —

(i) the owned funds, consisting of paid-up capital, reserve fund, other reserves, etc. and

(ii) the borrowed funds, consisting of deposits of various types received from the depositors and borrowings from other banks. The borrowed funds, mainly the deposits of the public, constitute the bulk of a bank's funds.

At the time a borrower, especially a businessman or an industrialist, approaches a banker with a credit proposal, the banker generally investigates into all aspects of the borrower's business and also about his personal character, capacity and capital. In this task of financial appraisal of the credit proposal and the evaluation of the borrowers credit worthiness, the financial statements of the business are of great value to the banker. The two important financial statements are the balance sheet and the profit and loss account of the business. The balance sheet shows the financial position of the business at a particular point of time. The profit and loss account shows the
financial results of the working of an enterprise over a period of time. When these statements of the last few years are studied and analysed, significant conclusions may be arrived at regarding the changes in the financial position, the important policies followed and the trends in profits, etc. Analysis and interpretation of the financial statements has now become an important technique of credit appraisal. The financial statements are analysed and interpreted by different classes of persons from different angles. Though the basic technique of appraisal remains the same in all the cases but the approach and emphasis in analysis varies. As a lender and creditor of his borrower-customer, a banker is interested in assessing the solvency or the repaying capacity of the borrower as is evident from his financial statements. A banker is concerned with the estimation of the risks, if any, involved in lending the money to the borrower. A banker analyses and interprets the financial statements so as to evaluate:

(i) the financial soundness and stability
(ii) the liquidity position
(iii) the profitability or the earning capacity of the borrowing concern.

The role of the modern banker is that he should be a catalyst for social change. The increase in employment opportunities and the per capita income of a person and the economic progress or prosperity that is achieved in a particular place can be well related to a growth cycle.

Growth cycle vis-a-vis inflation

Lending leads to growth and growth contributes to surplus. Surplus creates savings and savings bring deposits. Deposits create
advances and advances in turn create deposits. In an unbanked area, where the economic activity is negligible, bank cannot expect deposits. On the other hand, the lending for productive purposes results in creation of growth infrastructure. Productive activities not only create employment opportunities but also creates additional surpluses and cash generation. This cash generation or income generation has to come to bank branch also, which will help the deposit portfolio of the branch.

While the growth cycle is welcome, there is another cycle which is the cycle of inflation. It is very vicious and disastrous not only to the community, but to banks also. Inflation causes high cost of living. While some people will take advantage of inflation and become rich overnight in speculative buying for which most of the people may become victim to rising costs and pushed to extreme losses and poverty. In times of inflation, the effective value of rupee goes down, from time to time, thus reducing the purchasing power of the people. At the same time the traders and industrialists push up the price of products and while the Government increases taxes, duties etc. to meet the financial outlays (the labourers will demand increases in wages). It becomes very difficult to hold back the running inflation. High cost inflation affects the savings as the people will be left with no funds after meeting the high cost, which inversely creates financial problems of credit institution.

While the growth cycle is expected to grow in arithmetical proportions, the inflationary cycle has the tendency to grow in geometrical proportion. The following example reflects some horrific features of inflation —
Money supply, i.e. X may be taken as currency supply which means actual money in circulation plus bank deposits. Resources, i.e. Y may be taken as resources available. Needs i.e. Z may be taken as demand from the Public. Demand for the purpose of this example has relevance to increasing population and increased needs on account of change in standards. In the above example, the "Resource" in the first stage is 1 and the "needs" is also 1. There is adequate resources to meet the needs. Hence, the first stage denotes the most ideal situation. In the second stage, the resources remain constant, whereas the needs have increased to 2, thereby creating an imbalance between resources and needs. This is a problem area causing concern to economists, society and the Government. If increase of resources is not possible, the only alternative for the Government is to increase the currency. The problem is solved artificially and on a temporary basis. Increase of resources proportionately may solve the problem permanently. In the third stage, the resources and needs remain constant. Since the problem is not solved properly in second stage, this has the boomerang effect further and to certain social pressure, a further increase in money supply is noticed, i.e. X is increased to 3. The incidence of inflation is high at this stage. In the fourth stage, it is a matter of relief that the supply

<table>
<thead>
<tr>
<th>Stages of Economy</th>
<th>Money circulation</th>
<th>Resources (supply)</th>
<th>Needs (Demands)</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>X</td>
<td>Y</td>
<td>Z</td>
</tr>
<tr>
<td>I</td>
<td>1</td>
<td>1</td>
<td>1</td>
</tr>
<tr>
<td>II</td>
<td>2</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>III</td>
<td>3</td>
<td>1</td>
<td>2</td>
</tr>
<tr>
<td>IV</td>
<td>4</td>
<td>2</td>
<td>2</td>
</tr>
<tr>
<td>V</td>
<td>5</td>
<td>1</td>
<td>3</td>
</tr>
</tbody>
</table>
of resources has become 2, which is only due to social pressure and survival of the Government in power. This is sufficient to meet demands which is also 2. But the evil effects of inflation in third stage again results in increase of money supply (X) to 4. In the fifth stage, resources (Y) is 1. Probably the natural calamities like fire, flood, famine or wars or strike might have brought that situation. But needs never remain static. They grow more from time to time. Now need (Z) is 3. Apparently there is a lot of scarcity. Vested interest further create artificial scarcity. This has a revolutionary effect of bringing in further money supply. Thus money circulation (X) has been increased to 5. Thus in this stage, inflation is at its peak.

Resources in 5th stage is same as 1st stage. Needs in 5th stage is 3 times more than in 1st stage. Money supply in 5th stage is 5 times more than in the 1st stage. The additional money supply from 1st stage to 5th stage to the extent of 4 has come to bank. If the bank deposits at 1st stage is 100 crore. and at 5th stage, it is 600 crore, can it be said that the bank has achieved the deposit increase of 500 crore? Probably, no. The effective increase in deposit mobilisation is only 100 crore, as the other 400 crore increase is on account of incidence of inflation. Here the rupees value is 20 paise only in terms of its purchasing power.

In the above example, let us suppose the bank has mobilised 400 crore in the 5th stage, although there is an increase of 300 crore, the effect is that the effective deposits are lost to the extent of 100 crore. Borrowers who had availed finances earlier and set up the projects are at advantageous position to clear off the bank’s loan, whereas the borrowers at the time of inflation require more amount of
loan in order to meet high cost of materials etc. and ultimately find it difficult in repaying the bank's loan as well as the interest. As a result, there will be a mounting of overdues in banks. Moreover the borrowers are left with little money, in some cases no money, to repay the loan after meeting the daily requirements at a high cost (out of the money saved) to repay the loan. In view of these dimensions, it is not out of context to emphasize that modern banker will have to make a plan of positive approach towards making advance, instead of being merely security-oriented or rigidly relying on the character, capacity and capital of the borrowers.

Spread of advances

The four cardinal principles to determine the spread of advances are:
1. How to be safe;
2. How to meet the demand;
3. How to meet all cost; and
4. How to bring about the development in terms of achieving social objectives through priority sector advances and mass banking habits. It is not only the economic development of a person, but also of the community. Man individually and the project, both are important. The spread should be the ideal blend of social criteria and self-sustainance.

The purpose of advance or desirability of advance is very important now-a-days. The purpose of any loan should be productive and income generating. For the purpose of deposit mobilisation and to promote banking habits etc., reasonable small loans are being considered for consumption also. While the loans for production are for acquiring
durable articles like sewing machines, typewriters, fridge for hotels etc., setting up industrial units etc., consumption loans would involve financing for radio, fans, furniture, cycle etc. to individuals. Small loans are given depending upon the merits of each case. That is why, the rigidity in respect of productive purpose is relaxed to include reasonable consumption needs also, especially while assessing working capital needs. In case of small industries a provision is made for month's expenditure which include the proprietor's subsistence needs. In case of agricultural advances also, minimum expenses for family maintenance is also taken into account in addition to cost of manure, labour etc., while fixing scale of finance for each category of crop loans. Under social banking, persons below poverty line need a lot of sympathy and assistance. Sometimes, the loans given for certain productive purposes may also go for personal purposes like medical expenses, funeral expenses, marriage expenses, education etc. These are all social needs. Small personal loans are, however, necessary to make persons fit, skilful and sustaining and to develop potential in persons or community. If this is ignored, there are every chances that the loans given for productive purposes may be used for consumption purposes which adversely affects in the repaying capacity of the borrowers, thereby increasing the overdues in banks. Man is equally important as the project. If man fails, the project fails. So while assessing working capital needs, at the time of extending loans to the borrowers, banks must make a provision to include reasonable consumption needs also. While making an on the spot study in some bank branch situated in a rural area, in the district of Kamrup, Assam it is observed that — Some borrowers of the area after taking loan from the bank have cleared
off the old debt taken from the private agencies, such as money-lenders, mahajans etc. As they are paying interest to the agencies more than the commercial banks and as there is no way to get out from the clutches of the said agencies, the borrowers prefer to clear off the amount indebted to them (agencies). Moreover, there is every possibility of manipulation of the loan amount by the agencies. The borrowers are safe in this respects, while taking loans from the banks. So after clearing off the old debt, out of the bank's loan, there is little scope of repaying the bank's loan which ultimately increases the banks overdues. Under such circumstances, as far as possible, borrowers should be discouraged to take new loan to clear off the old debt taken from the private agencies and while making advances by banks, a careful scrutiny should be made in this regard.

Employment potential is also a test to consider financing a project. Project approach of lending is gathering momentum like irrigation project, house building complex, shopping complex, industrial complex etc. Viability approach is a test for considering finances for various developmental activities/schemes, to see how far such schemes are viable and whether all infrastructural facilities including good market and economic conditions are existing and the rate of return on investments is quite reasonable and commensurate.

Safety of advance is ensured by granting the advances to a reliable borrower who is prompt and trustworthy and who has capacity in utilising the loan amount. Adequate security, wherever necessary, insurance cover against losses of fire, flood, theft etc., credit guarantee for priority sector advances etc. are some of the factors in determining the safety of advances.
Profitability of advance is to ensure adequate income to cover up the bank's cost viz., interest rate, establishment charges, depreciation and bad debts. Lending rates of interest must not only be profitable, but also be flexible in the context of social banking. The interest rate should be fair enough to the risks involved in the advance and the capacity of the borrower. The capacity of borrowers like small and marginal farmers, small entrepreneur is very much less to pay exhorbitant rate of interest to bank. Interest is to be low in case of small borrowers so that they can maintain their daily requirements and repay the banks loan, out of the profit generated from the borrowed money. Interest rate is thus high or low depending upon the type of borrower, type of security, Reserve Bank of India directives etc. Concessional rate of interest is provided to export advances and sick industries in the national interest and perspective. The difference between the interest paid on deposits and interest received on advances (by banks) is known as 'SPREAD'. If the spread is unduly heavy, society has moral right to seek reduction of spread to give benefit to society. Therefore, social banking demands that the spread should be only that much to cover the burden. BURDEN is the difference between non-interest expenses (like salaries, rent, telephone charges, conveyance etc.) and non-interest income. When there is no adequate recovery of costs, it results a 'burden', which naturally covered by 'spread'. Cost benefit study of banks working in each area is drawing attention of banks now-a-days. Modern banking is changing the criteria and outlook on profitability.
Recovery of overdues

The major problems facing Indian Commercial Banks today are poor performance of recovery of their loans from both Industrial and Agricultural borrowers resulting in mounting overdues and their eroding profitability. In a sense, the two problems are inter-linked. Because locking up of funds for inordinately long period seriously hampers efficient turnover of credit which is primarily essential for larger production growth as well as for improving the earning capacity of banks. The industrial sector accounts for three times larger overdues than agricultural sector. Perhaps this may be due to entry of commercial banks in financing exclusively this sector during pre-nationalisation period. If we look back to financing of industrial sector by bank, the history is not very old. Prior to independence of the country, there were hardly any industry worth to name except textile and sugar.

Mounting overdues in the banking system—public sector, co-operatives and Regional Rural Banks has to be approached taking into consideration not only unsatisfactory recovery performance in terms of percentage, but also the absolute amount which has been locked and not available for further loaning to accelerate further economic development. To show the magnitude of the problem of overdue in banks, figures of the amount of overdues of Scheduled Commercial Banks for the State of Assam and on All India basis are shown in the Table 5.1 given in next page.
Table 5.1

(Amount in Rs. lakh)

<table>
<thead>
<tr>
<th>As on</th>
<th>No. of offices</th>
<th>Outstanding credit</th>
<th>Overdues</th>
</tr>
</thead>
<tbody>
<tr>
<td>Assam</td>
<td>31.3.93</td>
<td>1251</td>
<td>132673</td>
</tr>
<tr>
<td></td>
<td>31.3.97</td>
<td>1271</td>
<td>185237</td>
</tr>
<tr>
<td></td>
<td>31.3.98</td>
<td>1276</td>
<td>197823</td>
</tr>
<tr>
<td>All India</td>
<td>31.3.93</td>
<td>62774</td>
<td>16346729</td>
</tr>
<tr>
<td></td>
<td>31.3.97</td>
<td>63550</td>
<td>27840100</td>
</tr>
<tr>
<td></td>
<td>31.3.98</td>
<td>64218</td>
<td>32407900</td>
</tr>
</tbody>
</table>

2. Statistical tables relating to Banks in India, 1997-98, Reserve Bank of India.

The amount of overdues as on 30th June, 1984 on all India basis was 131900 lakh which is increased to Rs. 3452105 lakh as on 31.03.98. The mounting of overdues from industrial sector are mainly due to incidence of sickness caused by various factors and in agriculture due to natural calamities and wilful defaults. Due to mounting industrial and agricultural overdues, commercial banks are facing the problems of recycling their funds, thereby affecting their profitability as well as the economic development of the nation. The Government of India and the Reserve Bank of India both are quite seized with the problem from the beginning and have been issuing policy directives/guidelines to banks and other financial institutions to effectively deal with the problem of mounting industrial and agricultural overdues. It is significant and encouraging that now the leading commercial banks too are taking initiative in bringing about discussions on the problems of recoveries of loans. Ultimately, it is the branches of commercial banks, which are facing the problems at the grass root level, in enforcing the Reserve
Bank guidelines in actual practice.

<table>
<thead>
<tr>
<th>Items</th>
<th>As on 31st March</th>
</tr>
</thead>
<tbody>
<tr>
<td>Total advances</td>
<td>169340</td>
</tr>
<tr>
<td>Total NPAs</td>
<td>(23.2)</td>
</tr>
</tbody>
</table>

Note: Figures in bracket indicate per cent share in total advances

Source: Statistical tables relating to Banks in India, 1997-98, Reserve Bank of India

Overdues due to industrial sickness

Industrial overdues of commercial banks could be defined as that part of their total advances/credit given to industrial units which have become sick after availing of the advances and hence the recovery of principal as that of interest is rendered difficult. It will be useful to describe here the term 'sickness'. This term is generally used loosely to describe a wide variety of ailments suffered by industrial units. For example, it is described as poorly managed unit, unit without adequate resources, unit where assets are less than liabilities, unit which suffers continuous fall in production, unit which is unable to meet its statutory liabilities. Sickness has other connotations as well. For example, a decline in demand owing to customers dissatisfaction or high prices can initiate a chain reaction leading to cancellation of orders, which in turn, means poor capacity utilisation.
leading the unit to the path of sickness. In view of such various
descriptions of sickness, the Reserve Bank of India had advised the
banks that the unit may be identified as sick if (a) it has incurred
losses for the previous year and in the judgement of the concerned bank,
is likely to incur cash losses for the current year as well as the
following year and (b) it has an imbalance in its financial structure
such as current ratio is less than 1:1 and debt equity ratio is also
worsening. Such unit would invariably have a working capital loan which
is not in a position to repay. A prime feature of such unit is that it
works much below the break-even point on a continuing basis or fails to
generate internal surpluses to meet its own requirements and depends on
external aid for its survival.

Advances to be treated as overdues

The Reserve Bank of India has clearly listed the following
categories of advances, which should be treated as overdues —
(1) Where loan has remained unpaid though due for repayment
(2) All advances irrespective of their nature, viz., loans, overdrafts,
cashcredits etc. which have been recalled by the bank but not repaid.
(3) In the case of term loans, the amount of instalments which have
become due and remained unpaid.
(4) Advances which are treated as bad/doubtful of recovery and
inrespect of which suits have been filed.
(5) Entire amount of advances to sick industrial units which are not
considered potentially viable
(6) Borrowal accounts irrespective of their nature, viz. overdrafts,
cashcredits etc., where the interest has not been paid and where
there are practically no operation or excess drawings over the drawing power/drawing limit continuously for a period of six months or more i.e. stagnant accounts.

For studying indepth causes of sickness in industry, one has to examine both external and internal factors. Among external factors, government policies regarding industry, international market, industrial relations are pertinent. Immediately after independence, banks entered into planned growth era, wherein the role of industry became imminent. Apex financial institutions started providing term loans, while working capital was provided by the commercial banks. Banks followed the pattern of cash credit limit for industry in a similar fashion as they were used to finance trade and commerce prior to independence. Cash credit system had several draw backs for which some reformation were to be made. There were hardly any set of norms for financing working capital. Reserve Bank of India constituted a study group under the chairmanship of Mr. P.L. Tandon to study the pattern of financing of industry by the banks and recommended modifications necessary for meeting genuine credit needs of industry. Further Chore Committee was constituted to make further refinement from the angle of operations at the commercial banks level. The norms suggested by Tandon/Chore Committee if applied to already financed unit, it clearly bring out lot of diversion of funds and excess financing. If these funds could be released and channelised properly into investments, a much higher industrial growth could be achieved.

Credit flow to Small Scale Industry (SSI) Sector

In the case of Small Scale Industries the picture is quite different. Such units face different kinds of problems like change in
the Government policy, non-payment of dues, taxation, custom duties etc. which are external factors for sickness of industry. Internal factors for sickness are lack of managerial skill, financial discipline, obsolescence, industrial relations, poor marketing intelligence etc. Generally, big industries and/or public sector undertakings, take undue long time to pay the dues of small scale units. This results into heavy burden of interest on small scale unit.

In order to help small/medium scale industries to collect their bills in time, IDBI is contemplating to organise factorisation, perhaps establishment of factors might mitigate some problems of the small scale/medium scale units. Several other steps are contemplated to assist sick small scale units through nursing programmes. This will go a long way to improve the atmosphere of small scale industrial units.

Another important point for sickness in small scale unit is obsolescence. Small scale industry cannot afford sophisticated consultants as compared to big industries. Apex financial institutions like IDBI, IFCI and some commercial banks have organised technical consultancy cells for appraisal of projects and provide monitoring support to some extent. These consultancy cells may help in overcoming the problem of overdues in due course of time with better projects and proper technical support.

It reveals from the Table 5.3 that bank lending to SSIs increased from Rs. 12,968 crore at the end of Dec., 1988 to Rs. 38,109 crore at the end of March, 1998 registering a growth of Rs. 25,141 crore. In percentage terms the advances for SSIs remained between 14.5% to 17.5% of net bank credit during the year 1988 to 1998.
Table 5.3
Credit flow to SSI Sector from Commercial Banks

<table>
<thead>
<tr>
<th>As on last day of</th>
<th>Amount outstanding to Small Scale Industry (in crore)</th>
<th>Net Bank Credit (in crore)</th>
<th>Percentage of total Small Scale Industry advance to net bank credit</th>
</tr>
</thead>
<tbody>
<tr>
<td>Dec., 1998</td>
<td>12,968</td>
<td>79,598</td>
<td>16.3%</td>
</tr>
<tr>
<td>Sept., 1989</td>
<td>14,535</td>
<td>91,272</td>
<td>16.0%</td>
</tr>
<tr>
<td>March, 1990</td>
<td>15,969</td>
<td>1,01,178</td>
<td>15.8%</td>
</tr>
<tr>
<td>March, 1991</td>
<td>17,513</td>
<td>1,20,374</td>
<td>14.5%</td>
</tr>
<tr>
<td>March, 1992</td>
<td>17,398</td>
<td>1,12,160</td>
<td>15.5%</td>
</tr>
<tr>
<td>March, 1993</td>
<td>17,388</td>
<td>1,32,781</td>
<td>14.6%</td>
</tr>
<tr>
<td>March, 1997</td>
<td>31,175</td>
<td>1,89,684</td>
<td>16.4%</td>
</tr>
<tr>
<td>March, 1998</td>
<td>38,109</td>
<td>2,18,218</td>
<td>17.4%</td>
</tr>
</tbody>
</table>

Source: 1. ICSI- Herald October, 1994

Banks sometimes ask for repayment of loan instalment when the unit financed is still in gestation period and generation of adequate revenue is yet to take place. In many cases, shorter repayment period involves higher amount of repayment instalment, which the borrower might find difficult to meet out of the incremental income, hence default in repayment, thereby increasing the amount of overdues in banks. Infrastructural facilities like transport (for marketing) electricity (for SSI), health facilities (for allied agricultural activities), water and such other inputs play significant role in providing adequate and regular income to the borrower. But, there is every reason to believe that in some of the areas, financing is done without said facilities for their subsistence. This leads to decrease in the flow of income of the
beneficiary which affects the repayment capacity of the borrowers. Instances have come to light where entrepreneurs have been striving to get their unit declared as sick so that they may avail of the incentives under the pretext of revival of their units. Indeed these units might have diverted their funds for speculative purposes. Sickness seemingly suits them well, hence default in repayment of bank loans. At times the local authorities happen to declare in public meetings that banks loans given to poor people are subject to write-off and bankers have been vested with such powers. This type of declaration is made with the intention to get favourable mandate from the audience or for some other political motive. Loud promises are given at such meetings to get the recovery of banks loans rescheduled or truncated which breeds default in repayment on the part of the loanees.

Agricultural Credit

Ever since the emergence of commercial banks in the rural banking scene under the multi-agency approach for providing institutional credit to the agricultural sector in a big way, there has been phenomenal expansion of bank credit to the agriculture and allied activities.

When the commercial banks took to rural financing, they had practically no experience, no adequate base and field-level machinery to undertake the activities on a massive scale. The system and procedures of lending were also not conducive to mass banking. But in its dynamic endeavour to promote social banking in consonance with the objectives of nationalisation the banking system has taken all these limitations and constraints into stride and surged ahead by enlarging the flow of credit
to the agricultural sector at an accelerated pace. The quantitative target laid down in this respect by the monetary authority has also been a major propelling factor.

Table 5.4

Scheduled Commercial Banks Credit to Agriculture (All India)

<table>
<thead>
<tr>
<th>At the end of</th>
<th>Amount (in crore.)</th>
</tr>
</thead>
<tbody>
<tr>
<td>July, 1969</td>
<td>162</td>
</tr>
<tr>
<td>March, 1985</td>
<td>7,657</td>
</tr>
<tr>
<td>March, 1993</td>
<td>22,060</td>
</tr>
<tr>
<td>March, 1996</td>
<td>27,488</td>
</tr>
<tr>
<td>March, 1997</td>
<td>32,434</td>
</tr>
<tr>
<td>March, 1998</td>
<td>34,304</td>
</tr>
</tbody>
</table>

2. Statistical tables relating to Banks in India, 1997-98, Reserve Bank of India

But this development has not been without blemish. One of the most serious lacunals that has crept in the horizon of rural banking is the growing delinquency in the repayment of agricultural credit. Without going into the conceptual and methodological issues relating to calculation of overdues and the little difference that it would make in the overall picture, there can be no two opinions about the enormity of the problem of agricultural overdues. For the past several years, more than half of direct loans falling due for repayment were not repaid. In short the percentage of recovery to demand of direct agricultural advances of public sector banks which has been hovering around 50 to 53 per cent can in no way be considered adequate to maintain a high level of credit deployment in terms of disbursals.
Overdues in Agricultural Credit

Growing overdues of agricultural credit have indeed emerged as one of the major areas of weakness of the banking system. In fact, serious concern is expressed in all quarters, i.e. the banks themselves, the Reserve Bank of India and the Government regarding the poor recovery of loans. It is really a problem for the banking institution to fulfil the task of social objectives, unless repayment of past loan improves. At the meetings of chief executives of banks convened either by the Union Finance Ministry or the Reserve Bank of India from time to time, the subject of recovery of banks loans, among other important matters, receives sharp focus and banks are advised to take effective measures to improve the situation.

It is generally recognised that when credit is provided for creation and better utilisation of assets, it should generate sufficient income to enable the borrower to repay the banks loans. The money lent, thus would ultimately flow back into the banking system. But in the case of our banking system, the experience is rather disconcerting. The inadequate recovery of loans only inhibits the ability of the banking system to recycle the funds as the withholding of payment of bank’s dues by a section of agricultural borrowers means that other agricultural borrowers are denied the benefits of borrowing from the banking system.

The lack of recovery of its dues also cripples the credit institution’s capacity to draw refinance from the NABARD. The eligibility criteria for banks to avail refinance from NABARD is linked with their recovery performance. The eligibility is calculated on the basis of percentage of overdues to demand in respect of direct advances.
for agriculture and allied activities which include direct long, medium and short term loans. The linkage of refinance with the level of overdues essentially suggests the urgency and importance of improving recovery performance. Availing of World Bank assistance by NABARD also has bearing on recovery performance of banks. All in all, poor recovery dries up loanable resources of banks and in the process slows down the flow of credit to the rural sector which is quite inconsistent with the concept of development banking. "The basic concept of development is that credit is consciously used as a lever of development."

It is true that banks can recover some portion of the bad debts from the Deposit Insurance and Credit Guarantee Corporation of India (DICGCI). But, to avail of this facility, they have also to pay substantial sum to the DICGCI by way of premium. In the final analysis, this tantamounts to transfer of funds from one pocket to another of the same owner, that is, the Government. This, therefore, does neither basically alter the recovery scene nor make any real change into the problem of overdues. Large overdues of agricultural loans, together with that of the industrial finances, have made serious inroads into the profitability of the banking system which is under severe strain due to variety of factors. All this, underlines the paramount need for tackling the vexed problem of overdues in the most effective manner.

Factors responsible for overdues

Starting from the Study of Datey Committee relating to co-operative over dues more than two decades back, quite a useful study have been made to identify the factors responsible for poor recovery of loans and suggest measures to rectify the deficiency. The studies
conducted at the instance of committee on Agricultural Lendings by Commercial Banks (CALCAB) have identified number of factors which have given rise to high level of overdues in most of the branches covered by the study. These factors are classified into two broad categories, viz. internal and external. The internal factor are those for which the concerned branch/bank is responsible by way of faulty systems/procedures followed in identification/selection of borrowers, deficiencies in the processing of loan applications, lending policies, disbursement procedures and supervision of end-use of credit. Other factors such as wilful default, natural calamity, infructuous investment, which are beyond the control of the branch/bank are considered to be external factors. A wilful defaulter is defined as one whose surplus of income over consumer expenditure is adequate for loan service. The studies point out that wilful default originates in and is abetted by socio-political and psychological forces. The wilful defaulters are not even scared of legal action. Unlawful default, on the other hand, is generally caused by erosion of farm income due to drought, theft, fire and incomplete/infructuous investments. Underfinancing of investment has also been identified as one of the causes of unwilful default. Among the external factors, while the two factors viz. (1) those who repay their dues whether or not they generate additional income. (2) those who donot generate additional income because of unforeseen circumstances and have no means to repay their dues, would deserve sympathetic treatment by way of, say, re-phasement of loan repayments and other concessions, the wilful defaulter to be dealt with seriously.
Due to stipulations of shorter repayment period, the incremental income accruing to small farmers in several cases has not been sufficient to repay the loans within the period prescribed by banks. This is identified as one of the major factors for the rising trend of overdues under term lending. In the light of the findings of the studies and based on the economics of various schemes approved by it, NABARD has specified the schedule of term loan repayment period, including the gestation period that would be necessary to be given to small farmers in respect of various investments. The banks have, however, been given the discretion to vary the loan repayment period within the range indicated on the basis of case by case appraisal, but the period so stipulated should not be less than the minimum period prescribed in this respect. While these are all steps in the right direction, the banks have yet to find real solution to the problem of wilful defaults for which even legal action does not seem to be adequate and effective. Even the enactment of laws by the State Government, on the lines of model bill recommended by Talwar Committee, has made little difference in the overall situation as the concept has not yet percolated down at various levels of the State Government machinery. Moreover, an expensive and time consuming recovery process through legal measures does not appear to be conducive to mass banking. The wilful defaulters, however, stand on a different footing and taking legal action against such borrowers will in no way be inconsistent with the philosophy of development banking. Under the existing system, suits through civil courts are long drawn process and at best result in only partial recovery. What is more, even if decree is awarded, execution of the same becomes a time
consuming affair. The period of limitation of documents is another major problems faced by the credit institutions (banks).

Insufficient infrastructure, including man-power available with the branch managers is also reported to have come in the way of ensured repayment of bank dues. In fact, pre-sanction appraisal and post-sanction follow-up do enhance the viability of the schemes financed and the proper end use of credit. Post-sanction follow-up is in the form of monitoring which could ensure mid-term course corrections in the implementation of the assisted programmes. In some cases, beneficiaries were not aware of the technique of managing the assets provided to them. Hence they could not optimally utilise the assets. In fact, this underlines the need and importance of imparting specific training programme to the beneficiaries, which would boost up their income levels. This lacuna has been contributing its share to the poor repayment of bank dues.

Ambitions Credit Targets

The ambitious targets for extending credit fixed without proper modality and undue pressure exerted for their achievement before the close of the financial year from the senior executives of banks and other agencies involved in the process, makes the branch managers lend, while hardly sufficient time is available for conducting survey and study at pre-sanction stage. Further, sponsoring of applications in bulk by the developmental agencies at fag end of the financial year to commercial banks for achieving the targets also contribute to haphazard lending. The bank managers resort to lending half heartedly which is most likely to go astray. Banks are seen organising mass lending
functions and loan melas to disburse loans. Since adequate time is not available with the banks for organising the Credit Camp with proper pre-sanction appraisal etc., the unwilling takers of loan fall to turn out to be willing repayers. Availability of quality inputs in adequate measures is the pre-requisite for success of any venture. But, it is often seen that the borrowers availing loan from banks are not linked with any regular source of supply of quality inputs. Low quality pumpsets, poor quality animal-feeds, has many a times, led to failure of the units.

1 "Reserve Bank of India has directed the public sector banks to appoint senior executives in the rank of General Managers to look after the agricultural advances. The Governor, Reserve Bank of India has directed the bank chiefs to raise farm credit by over Rs. 2500 crore in 1996-97 over the previous year's level. The flow of credit to the agricultural sector which was Rs. 8225 crore in 1994-95 was increased to Rs. 10,192 crore in 1995-96 registering a 23.2 per cent growth. Despite that, most of the banks failed to reach the stipulated 18 per cent target of agriculture lending."

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