CHAPTER II
CONCEPTS AND REVIEW OF RELATED LITERATURE

2.1 CONCEPTS

An understanding of the various concepts used in the study is no doubt essential for a meaningful scientific study. This enables the researcher to have a clearer understanding and perception of the problems under investigation, as important concepts used in the study are made clear and room for controversies and misunderstanding are avoided.

A concept very relevant and important for the present study is Efficiency. In general, it refers to the non-wasteful use of an input relative to its potential usefulness. Economic efficiency measures the money value of inputs and outputs. A production process is technically efficient, if it produces the highest possible output from its chosen combinations of inputs. The manner in which scarce resources are allocated to various sectors of the economy for productive uses is referred to as allocational efficiency. Tobin\(^{17}\) relates functional efficiency to the economic functions of the financial firms. In banking, the functional measures of efficiency are manifested in:

i. The allocational efficiency, as observed in the distribution of investible fund in a manner in which capital funds are allocated by the lending institutions.

ii. Collection or loan recovery performance, measured as ratio of performing to non-performing assets.

iii. Operational efficiency in the spread of interest i.e. difference between interest earning and interest cost.

However, under a regime of administered interest rate, operational efficiency cannot be effectively measured.

Johnson\textsuperscript{18}, while examining the problems of efficiency in monetary management distinguishes three aspects of efficiency measures, namely, (i) structural efficiency, (ii) efficiency in stabilisation policy, and (iii) efficiency in secular economic policy.

**Structural efficiency**, in the ordinary economic sense of the banking system, refers primarily to efficiency in the payment mechanism as well as the efforts taken to mobilise savings and allocate capital among competing borrowers. Macropolicies directed at keeping the economy on a desired course and correcting deviations from that course correspond to **efficiency in stabilisation policy**. Efficiency with respect to the choice of the desired level and observable trend of the major macroeconomic variables that reflect the economy's performance is viewed as **efficiency in secular economic policy**.

Bank efficiency is explained by Dimitri Vittas\textsuperscript{19} as a reduction in the interest spread between lending and deposit rates. Three types of operating ratios, viz. (i) operating asset ratio, (ii) operating income ratio, and (iii) operating equity ratio are considered as proxy measures of bank efficiency. Moreover, an important parameter for assessing bank efficiency is the range and quality of service rendered to clients. Angadi\textsuperscript{20} corroborates the view, that efficiency of a commercial bank is better assessed on the strength of its customer services. A measure of efficiency, related to the success of a rural branch of a bank, according to Varde\textsuperscript{21} is assessed on the role of the branch in promoting socio-economic development of the serviced area. The use of Efficiency in the present study is confined to the functional efficiency as attributed to loan recovery and the concomitant impediments to successful recovery as perceived by the borrowers. The size of the non-performing assets is considered a proxy measure of the degree of efficiency.

Closely connected with the concept of efficiency is that of non-performing assets. The level of non-performing assets (NPAs) provides an important measure of the performance of banks as it reflects on the quality of the loan portfolio. These assets per-se neither earn interest nor are they repaid on maturity. On the contrary, the lender banks incur expenditure in recovering the loan amount. Hence, non-performing assets are assets which do not directly contribute to the bank's


profitability. Meyer\textsuperscript{22} has suggested the plotting of a loan recovery profile to study the relationship between time and the percentage of the loan principal repaid. A comparison of the loan recovery profile for loans given in various years would reveal if a lender is more or less successful in collecting loans made in a particular year vis-a-vis another. This comparison also suggests whether or not there is a change in the borrowers behaviour regarding loan repayment. The loan recovery position is measured as a ratio of loan received, divided by loan due as well as previous overdues i.e.

\[
\text{Percentage of the loan portfolio in arrears} = \frac{\text{Loan Payment Received}}{\text{Loan Due + Previous Overdues}}
\]

The Narasimham Committee\textsuperscript{23} however, defines non-performing assets as assets that remain due for a period exceeding 180 days. For the purpose of provisioning, these assets are further categorised into four types:

1. **Standard Assets** are non-performing assets (NPAs) with irregularity for less than 180 days, and against such outstanding amount no provisioning is necessary.

2. **Sub-Standard Assets** are non-performing assets (NPAs) for a period of not more than two years. Provisioning to an extent of 10 percent of the outstanding amount is required.


\textsuperscript{23} RBI, op. cit., 1991, p. 56.
3. **Doubtful Assets** are non-performing assets (NPAs) for a period of more than two years, but less than five years. Against such outstanding assets, a provisioning of 20-50 percent is needed; and.

4. **Loss Assets** are those non-performing assets (NPAs) for more than five years. Against the outstanding amount, cent percent provisioning is mandatory.

The recent report\(^\text{24}\) on Trend and Progress of Banking in India (1993-94), shows that at the end of March 1993, non-performing assets (NPAs) of public sector banks stood at Rs.39,746 crores, which formed 23.2 percent of the total advances. The non-performing assets (NPAs) of public sector banks, as at the end of March 1994, had been provisionally placed at Rs.39,553 crores, accounting for 23.6 percent of total advances.

The present study defines non-performing assets as those loans which the borrowers have either delayed repayment (i.e been delinquent) or have defaulted. \(^*\)It is measured as a ratio of demand to actual recovery. Recovery rate is defined as that part of total demand [i.e overdue demand + current demand] collected by the bank from borrowers [excluding any repayment made by government institutions on behalf of borrowers]. Demand means the aggregate of principal and interest during the accounting year under consideration, plus overdue from previous years, excluding demand for loans written off or rescheduled.

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A concept exclusively dealt with in the present study is Priority Sector. This sector has been a creation of government policy actions taken on the basis of certain economic, social, and political compulsions, and it serves as a conduit for the smooth flow of directed credit in consonance with the planned priorities. The concept of priority sector emanated following the adoption of social control in 1967, and was later formalised in 1972 by the Reserve Bank of India. The rationale for introducing directed lending is that if the banks are left to pursue their independent polices, credit would flow largely towards commercially profitable investments. Over the years, the scope of priority sector, which earlier was confined to agriculture and small scale industries, has undergone changes in sectoral coverage and targeted beneficiaries. The study adopts the Narasimham committee’s redefined version of the priority sector which comprises of the following segments:

1. Small and marginal farmers.

2. Tiny sector industry.

3. Village and cottage industries.

4. Small business and transport operators.

5. Rural artisans, and

6. Other weaker sections.

The concept of weaker sections was evolved by the Krishnaswamy
Committee\textsuperscript{25} in 1980 and later modified by the Ghosh Committee\textsuperscript{26} in 1982. As per the RBI\textsuperscript{27} guidelines, which is followed in this study, the weaker sections comprise of the following categories of beneficiaries.

1. **Small and marginal farmers with land holdings upto 5 acres, landless labourers, tenant farmers and share croppers.**

2. **Artisans, village and cottage industries enjoying credit limit upto Rs.25,000/-.**

3. **IRDP, and DRI beneficiaries; and**

4. **Beneficiaries belonging to SC/ST communities.**

As at the end of March 1994, advances of public sector banks\textsuperscript{28} to weaker sections aggregated Rs.12,779 crores, constituting 9.1 percent of their net bank credit, as against a target of 10 percent.

Short-run delays in repayments is referred to as **Delinquency**. High delinquency rates according to Vogel\textsuperscript{29} are attributed to the riskiness and low productivity of the economic unit or the unwillingness of the borrowers to repay, combined with the lack of forceful collection policies. Delinquency rate is measured as the total value of loans, with such payment of interest or principal

\textsuperscript{25} RBl, *Report of the Committee to Study the Role of Banks in Lending to Priority Sector and 20 - Point Programme*, Bombay, 1980.

\textsuperscript{26} RBl, *Report of the Committee to Study the Role of Banks in the Implementation of the New 20 - Point Programme*, Bombay, 1982.

\textsuperscript{27} RBl, 1993-94 (July-June), op. cit. p. 18.

\textsuperscript{28} Ibid, p. 18.

overdue as a percentage of the total value of loans outstanding. On the other hand, any violations of a loan contract, including failure to pay interest and repay principal that are due and payable, is an act of default.

Most credit institutions in developing countries fail to operate on a viable or self-sustaining basis due to lack of proper evaluation and quantification of borrower's debt or repayment capacity. Von Pischke\textsuperscript{30} defines debt capacity to be borrowing power, which is created by the borrower's estimated future payment capacity and is equal to the amount of credit which this capacity can command in financial markets. For the lender, debt capacity concept permits exploration of a lender's evaluation of loan applications. Factors necessary for generating debt-capacity are risk reducing technologies, price policy, institutional reforms and financial flexibility. A simple quantified measure of the debt or repayment capacity used in the present study is represented as $R = Y - (E + L + K)$; where

\[ R = \text{Repayment Capacity}, \]

\[ Y = \text{Total Income}, \]

\[ E = \text{Total Expenditure}, \]

\[ L = \text{Pre-existing liabilities to be met within a year}, \text{ and} \]

\[ K = \text{Risk Allowance (Taken as 10 percent of the total income)}. \]

The debt capacity which is created can be also accepted as a proxy for economic development.

Viability and Profitability are concepts widely referred to in banking literature, which complement each other and are indispensable prerequisites for successful banking. The present study, in order to delve into the problems of delinquency and default, conceptualises viability to be a measure of sustainability in the flow of loanable funds through timely and effective recycling of credit. Non-recovery of loans or a rise in the quantum of non-performing assets curb the flow of funds and gradually erodes the viability and efficacy of the banking system. The central problem of finance being the risk associated with recovery of loans, effective loan recovery would also rest on the efficiency of the bank in assessing the borrower's credit risk. This in turn, would improve recovery and enable the bank to effectively recycle credit and remain viable. In the context of social banking, the viability of this activity can be conceptualised and measured as:

\[ V = f(E,R) \]

\[ V = \text{Viability of Social Banking.} \]

\[ E = \text{Collection efficiency of the Lender Bank or loan recovery management, and} \]

\[ R = \text{Borrower's repayment capacity} \]
2.2 MEANING OF SOCIAL BANKING

The term social banking is synonymous with development banking which, in its broadest sense, refers to any government intervention in financial markets with development objectives in mind. This includes leaning on the commercial banks to lend to priority sectors or to provide refinance facilities for rural farmers and micro-sector entrepreneurs to achieve developmental goals. Sandford identifies a social activity in the realm of economics with matters directly affecting the standard of living and quality of life. Sen affirms that social goals are rooted in ethical grounds and distancing economics from ethics will narrow individuals understanding of human beings and society. According to Copestake, a subtle difference underlying the philosophy of social banking, as distinct from commercial and development banking, is the explicit objective of equity being strapped along with the goals of economic growth and financial viability. The role of the state is to influence the allocation of credit by social class.

The present study considers social banking to be an economic activity, wherein there is a conscious and deliberate policy induced action of the central bank to direct loanable funds towards socially desirable investments. This action is primarily followed on the premise that social priorities should take precedence over

private gains, more so, in consonance with the social principles of equity and distributive justice. It is nonetheless imperative that banks adhere to the principles of solvency, liquidity and profitability to pursue social banking as a viable activity.

In conclusion, the conceptualisation of important issues that arise in the present study, not only relate the issues to the empirical study, but also contribute to an analytical understanding of the problem.

2.3 REVIEW OF RELATED LITERATURE

An essential part of this investigation is a critical examination of past studies on the causes of delinquency and defaults in social banking. More specifically, it is important to know what we have learnt so far from the widespread experiences of commercial banks with regard to default in loan repayment, more so after the advent of social banking.

2.4 DYNAMICS OF DEFAULT - AN ECONOMIC VIEW

Default enfeebles the borrower’s ability to repay and thus hinders the uninterrupted flow of loanable funds. The default problem is multifaceted encompassing economic, socio-cultural, political, legal and behavioural dimensions. Conventionally, factor resources are channelised and distributed in conformity to the economic philosophy which the country professes. In a market driven economy, motivated by profit earnings, the borrower’s creditworthiness is a precondition for loan disbursement. In contrast, the principle of growth with equity is adopted for the distribution of scarce capital resources in planned economies.
The political ideology underlying an economic system necessarily influences the lender-borrower relationship. Borrowers are normally categorised as wilful and non-wilful defaulters. The willingness to repay or otherwise would depend on a number of factors. In economies confronted with social and economic deprivation, it is naive to consider an act of default as necessarily wilful. Moreover, in doing so, one inadvertently overlooks the inherent weaknesses of the lender. It is therefore necessary to make an indepth examination of the underlying forces in the analysis of the default problem.

Results obtained from a study by Christen R. Peck³⁵ (1984) indicated that the borrower would default if expected return on defaulted loan was greater than expected return on repaid loan and would repay if it is not so. Although theoretically acceptable, a quantified measure of the opportunity cost is unreliable in an uncertain and risky environment. Default can be checked if the borrower is assured of adequate and sustained flow of credit from the lender. Needless to mention, timeliness is an essential quality of a good loan.

A study conducted by Wiggins³⁶ (1992) in Madurai region of Tamil Nadu revealed the fact that bad debts did restrict the ability of branches to recycle loans. There was a significant inverse correlation between new loans and overdues. However, the flow of funds was not affected since there was a strong presence of informal lenders.


Dale Adams (1987) has affirmed that defaults were logical outcome of using financial markets to allocate subsidies and to push development priorities. It would be impossible to create and sustain formal credit institutions if loan recovery rates were not increased substantially.

Mittendorf (1987) defined credit as a claim on resources and services. He pointed out that fungibility or interchangeability of credit was more often ignored by policy makers. Lack of management and operational skills also contributed to poor loan recovery. He reiterated that interest rate should not be used as a means of subsidy, but instead, greater emphasis must be laid on the earning capacity of the borrower to expand credit rather than rely on collateral. Von Pischke (1989) endorsed this view that the rationale for lending lay on the debt capacity of the borrower and was not related to credit needs. In addition to cash flows as the source of loan repayment, staff training, better accounting and controls would increase the efficiency of financial institutions.


2.5 MARKET AND RISK DIMENSIONS OF DEFAULT

a) Market

The financial markets of the Less Developed Countries (LDCs) are primarily dualistic. There exist a developed, sheltered, impersonal market along with a traditional, unorganised yet receptive private market. Tinnermeier\(^{40}\) (1977) had observed duality in the allocation of credit, in which there was a bias towards production credit to firms in relation to consumption credit to households. Moreover, Shaw\(^{41}\) (1973) and Virmani\(^{42}\) (1982) indicated that the rural financial market in developing countries are highly imperfect in so far as the markets are geographically as well as institutionally fragmented due to weak linkages between sub markets and multiplicity of interest rates. Rosenzweig\(^{43}\) (1978) has mentioned that the inter market differences in interest rates are at times greater than the cost of transferring funds among markets. These variations arose in response to difference in transaction, administrative and risk costs. McKinnon\(^{44}\) (1973) has inferred from his study on the capital markets of the LDCs that as a consequence of


market fragmentation, a potential farm entrepreneur, when devoid of physical resources, has limited access to external financing.

Braverman and Guasch\textsuperscript{45} (1986) have identified the following fundamental flaws pertaining to rural financial markets: i) lack of competitiveness among the formal lenders; ii) weak legal enforcement of contracts; iii) corruption and lack of accountability in the institutions; iv) poor dissemination of information; v) uncertainty regarding the ability of the borrowers to meet future loan obligations; vi) inability to monitor the use of funds; vii) lack of collateral, often due to land tenure arrangements or ambiguous property rights; viii) lack of coherent financial savings mobilisation programme and ix) high opportunity cost of capital in other sectors.

b) Risk

Another closely related problem in rural lending is the risk and uncertainty associated with subsistence farming and technological innovations. This has largely dissuaded formal credit agencies from enthusiastically participating in the rural financial markets. Risk is also related to the level of information possessed by the two contracting parties.

In Hodgman's\textsuperscript{46} (1960) equilibrium theory of credit rationing, it is assumed that risk is a function of the size of loan. The quantum of loan to be disbursed needed to be determined on the basis of the borrower's investment requirement and creditworthiness. The lenders are required to set credit limits in accordance with the repayment capacity of the borrowers. There is therefore, a perceived default risk attached to loans beyond the credit limits.

Clifton\textsuperscript{47} (1969) in his analysis of the role of agriculture in economic development has highlighted the risk and uncertainty associated with technological innovations, while Bessell\textsuperscript{48} (1975) has affirmed that there is both financial and social risks attached to rural lending. Vogel's\textsuperscript{49} (1981) study in Costa Rica brought to light features of high delinquency attributed to the riskiness and low productivity of agriculture and Christen R. Peck\textsuperscript{50} (1984) had argued that the decision of a borrower to default on contracted loan obligations was essentially a decision which took place in an uncertain risky environment. Hence, the key determinants of borrowers default are (a) Probability that the borrower would receive an adequate and long-term flow of credit from the lender (b) Willingness of the lender to enforce negative sanctions on delinquent borrowers. Huppi and Feder\textsuperscript{51} (1990)


\textsuperscript{49} R.C. Vogel (1981), op. cit. pp. 60-61

\textsuperscript{50} R. Christien Peck (1984), op. cit. p. 46.

perceived that large farmers who offered collaterals are less risky than small farmers. Besides, servicing large loans entailed lower administrative cost per unit of loan. They therefore advocated group lending - a form of joint liability - for reducing the risk of default among small farmers.

2.6 SOCIO-CULTURAL AND ATTITUINAL DIMENSIONS OF DEFAULT

All economic transactions are embedded in a particular cultural and institutional setting which influence the nature of transactions. In other words, there are social and cultural elements encompassing any credit relationship.

A study by Gillette and Uphoff\(^{52}\) (1973), on the socio-anthropology of less developed countries of Latin America indicated that repayment was a function of socio-cultural factors. Nicholson\(^{53}\) (1973) while commenting on the Indian Panchayat Raj System pointed out that credit programmes tied to new labour intensive production practices were likely to upset seasonal labour supply due to rituals and social customs. Furthermore, the principles of social organisation influenced the behaviour expectations of the farmer and thereby conditioned his attitude towards the credit agency.

\(^{52}\) C. Gillette and N. Uphoff, The Credit Connection: Cultural and Social Factors Affecting Small farmers participation in Credit Programs, Centre for International Studies, Cornell University, U.S.A.

By applying the discriminant function analysis George et al\textsuperscript{54} (1984) classified borrowers into defaulters and repayers of the loans on the basis of socio-economic characteristics. The results have revealed that factors such as literacy, income from other sources, adoption quotient, cropping intensity, personal attitude towards factors such as work, thrift, credit and indebtedness as well as the rural power structure influenced the farmers use of credit and their willingness to repay.

Muthayya and Prasad\textsuperscript{55} (1984) in their study covering five Indian states and 400 IRDP beneficiaries, stressed on the attitudinal factors which when guided by moral and ethical values greatly influenced the repayment of loans. Bhattacharyya\textsuperscript{56} (1994) evaluated the performances of formal credit institutions operating in a backward rural district of West Bengal, and attributed poor performance to wrong identification of borrowers and the lack of motivation and poor attitude of bank personnel. Further it was also found that in Third World Countries, the informal lenders operated within the milieu of the rural society and hence commanded a close rapport with the rural borrowers. Contrary to this, the formal lenders, being predominantly urban oriented, often functioned in a manner quite alien to the rural community.


2.7 INSTITUTIONAL DIMENSIONS OF DEFAULT

Mydral\textsuperscript{57} (1968) in his pioneering study on poverty commented that the local village level power structure was elitist and biased towards its own privileged members. Tendulkar\textsuperscript{58} (1983) had observed, that the complex socio-political power structure acted as a constraint on the successful implementation of developmental programmes sponsored by credit institutions. He further stated that the inequitable working of the Indian economic and social institutions was largely responsible for the inadequate percolations of the benefits of economic growth. A large number of formal credit institutions were not only vulnerable to political pressures, but too often succumbed to them. Narayana\textsuperscript{59} (1992) had attributed loan delinquency to inappropriate risk management and over politicisation of rural credit.

Blair\textsuperscript{60} (1973) confirmed that profligacy in lending had led to a situation where economic ends were often functions of political factors. It was also observed that rich farmers, who failed to repay were not penalised, because the political costs were too high. Added to this, debt forgiveness programmes were quite frequent, and borrowers tended to default with impunity and came to regard loans as grants.


The pattern of land ownership and its distribution among the rural community determined to a large extent, the success of credit programmes. Land, which is a fixed asset, can be considered as an ideal collateral. In many developing countries property rights to land are poorly codified and hence limits its usefulness as collateral. Property rights are residual control rights over a set of assets. Enforcement of repayment is constrained by the poor development of property rights. Rights to land are often usufructual and have limited possibilities for transfer to others.

Sanderatne’s\textsuperscript{61} (1978) study on the Sri Lankan economy indicated that the defects in the agrarian structure were the basic causes for defaults. Mosely\textsuperscript{62} (1986) attributed market imperfection to (i) ill defined property rights, and ii) weaknesses in the judicial system. In recent times, it had been observed that the formal lending institutions in LDCs were apprehensive about the potential viability of the rural borrowers, given the uneconomic farm size and abysmally low level of factor productivity. Added to the uneconomic farm size, a large number of them were fragmented and hence they were economically unviable. Rao\textsuperscript{63} (1970)


and Bhaduri64 (1982) were of the view that as a prelude to agrarian reforms, the credit delivery system needed to be strengthened. Needless to say, productivity, farm size and asset ownership patterns are crucial determinants of the borrower’s repayment potential.

b) Infrastructure and Manpower

The success of formal lending would also depend on the efficient working of a closely knit infrastructural support system. Von Pischke and Dale Adams65 (1983) on examining the determinants of the repayment capacity referred to the availability of basic infrastructure such as transport, communication, power, a well organised marketing and distribution network as essential prerequisites. Desai66 (1989) has asserted that improved inter-linkages between the agricultural production unit and the related input supply, in addition to the marketing and processing units, could bring about higher levels of productivity and income generation. With higher loan recovery and consequent higher recycling of funds, the viability of rural financial institutions can be improved.

64. A. Bhaduri, "The Role of Rural Credit in Agrarian Reform with Special Reference to India", Economic Bulletin for Asia and the Pacific, No. 33, 1982, pp. 104-111.
Shete (1992) while commenting on loan recoveries in developing countries opined that if the quantity of lending was to be improved, additional manpower, in the initial stages, will have to be made available along with organisational innovations like formation of self help groups to act as links between credit agencies and the borrowers.

Maharjan et al. (1983) conducted a study in Nepal and came to the conclusion that loan supervision and collection were essential procedures in loan repayment. Dhabal and Bhattacharya (1989) analysed the repayment performance of a branch of a regional rural bank in Bankura District of West Bengal and confirmed that repayment of loan basically depended on the ability and intention of borrowers to repay. They also inferred that improper deployment of loans coupled with lax supervision deterred borrowers from repaying the loan.

To cite Binswanger et al., (1985) "Given the low level of communication and transport infrastructure in third world countries, transaction costs were potentially very high, especially in rural areas, where the population was more widely dispersed". This had been one of the major reasons for the reluctance of


many formal financial institutions to expand their branch networks outside large urban centres.

2.8 THE INDIAN EXPERIENCE

The Khusro Committee\(^\text{71}\) which reviewed the Agricultural Credit System in India, had listed the following reasons for poor loan recovery.

a) **Defective loan policies and procedures.**

b) **Emphasis on completing targets.**

c) **Disbursement in loan melas to non-viable borrowers and activities; and**

d) **Ineffective supervision**

A study sponsored by NABARD\(^\text{72}\) and organised by the National Institute of Rural Development in Chengalpattu District of Tamil Nadu, attributed default mainly to informal borrowings, financing of non-viable schemes and delays in disbursement of loans. An observed phenomenon had been that repayment was not always a function of surplus net income alone, but also due to borrower’s attitude towards repayment.

C.V. Nair\(^\text{73}\) (1991) in his paper presented at the National Seminar on Rural Credit, inferred from his analyses that overdues were neutral to the classes of

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borrowers. There was apparently no significant relationship between overdues and size of holdings as well as the size of branch staff. Besides, no significant relationship between quantum of loan and overdues existed. However, relationship was established between overdues and literacy levels, value of crops and agroclimatic conditions.

Anil Gupta²⁴ (1991) after examining the supply side issues pertaining to rural banking in India, had drawn attention to the inadequate follow-up of the use of loans and the inability to discriminate between genuine and wilful defaulters, as reasons for poor recovery. These lapses he has attributed to manpower constraints and insufficient upgradation of skills of bank officials, together with a mismatch between banking technology and the nature of work. It is also inferred that, over financing could be as serious a reason for default as under financing.

Vyasulu and Rajasekar²⁵ (1991) from their field studies, emphasised that the structural deficiencies within the banking system coupled with political interference in the functioning of banks were the major causes for growing overdues. A disturbing factor reported was the problem of inadequate and untimely loans, particularly in the case of small and marginal farmers.

While estimating the demand for credit, Dantwala\textsuperscript{76} (1989) had remarked that the major obstacles to poverty alleviation were on the demand side of credit. Availability of credit needs to be converted into access or entitlement to credit by the poor. Centrally determined target approach to rural financing had to be replaced by a more demand driven mechanism for credit delivery. The emphasis on credit delivery, according to him, must be more on the quality, rather than the quantity lent. In a nutshell, making the poor creditworthy is to make them more productive.

Deliberating on the second generation problems with regards rural credit, Mujumdar\textsuperscript{77} (1989) while summing up a discussion on rural institutional credit, highlighted the paradox of declining share of agriculture to GDP vis-a-vis increasing share of institutional credit as due to mis-allocation and mis-utilisation of funds.Binswanger and Khandker’s\textsuperscript{78} (1992) econometric results of the impact of finance on the rural economy suggested that commercial banks expansion in India has had an overall positive effect on non-farm employment output and rural wages, even though the supply-led approach to agricultural credit had failed to generate viable institutions and agricultural employment. The costs of the policy to the government had been high, as portfolio losses associated with poor repayment had to be borne by the government.


\textsuperscript{77} N.A. Mujumdar, "Summaries of Group Discussion, Subject II - Institutional Credit - Rural" \textit{Indian Journal of Agricultural Economics}, Vol. 64, No. 1, January-March 1989, pp. 20-23

Shukla\textsuperscript{79} (1985) in her observations on agricultural overdues had voiced concern about the mismatch between the time fixed for recovery of loans and the time when farmers could actually repay the loan. On examining the problems of rural credit confronting RRBs, Sheet and Karkal\textsuperscript{80} (1989) had reiterated that there was a mismatch between income generation and repayment schedule. Apparently there were flaws in the systems and procedures practised by lending institutions. Poor fund management, low level of labour productivity and escalating fixed capital expenditure were internal factors affecting the viability of regional rural banks. Singh\textsuperscript{81} (1986) had referred to the bias shown towards large farmers in the disbursement of institutional credit. This was largely because farm size, farm assets and output influenced the allocation of institutional credit.

The finding of a study conducted by Desai et al\textsuperscript{82} (1989) in Malpur taluka, a backward district of Gujarat, showed that for the rural farm households there was a higher share of the use of informal sources of credit. Although the households were potentially viable, their demand for and supply of financial services were observed to be small.


\textsuperscript{80} N.B. Shee and G.L. Karkal, "RRBs : Problems and Perspective of Rural Credit", \textit{Prayag}, Vol. 18, No-2, April - June 1989, pp. 131-211.


In a study of the factors affecting small farmers access to institutional credit in rural Orissa, Sarap (1990) had stressed on the defective bureaucratic and procedural measures pursued by the formal institutions, as factors responsible for raising the effective borrowing rate of interest and thereby dissuading the small borrowers from approaching these institutions.

2.9 SUMMARY AND CONCLUDING REMARKS

The above review of literature could be summed up as follows. Default is inextricably tied to a myriad of factors which are either internal or external to the lender-borrower contractual framework.

Constraints such as ill-defined and ambiguous property rights, weak legal contracts, market inefficiencies, a pro-rich socio-political power structure, inequitable asset ownership and entitlement, besides blatant outside interference in the working of credit institutions, although exogenous in nature, are significant causes for mounting defaults.

Due to legal restrictions on the functioning of banks, it is found that the lender banks do not have the freedom to frame and pursue lending policies which are flexible and conducive to the needs of the borrowers. There is, implicitly an element of compulsion on state owned banks to transact business, very often, not in conformity with the principles of sound banking.

The studies and reports reviewed do suggest that defects such as the multiplicity of interest rates; defective credit policies and improper selection of beneficiaries; inadequate follow-up and monitoring of the use of loans; apathy of the bank staff towards social banking; are, to some extent, due to state intervention in the working of banks. Under the existing conditions, lender banks consider the dispensation of credit as a social obligation, while borrowers who avail institutional loan, deem it to be a government grant.

It is therefore evident, both from the empirical findings and observations of researchers, that the problem of default and delinquency need to be examined and understood in its entirety.