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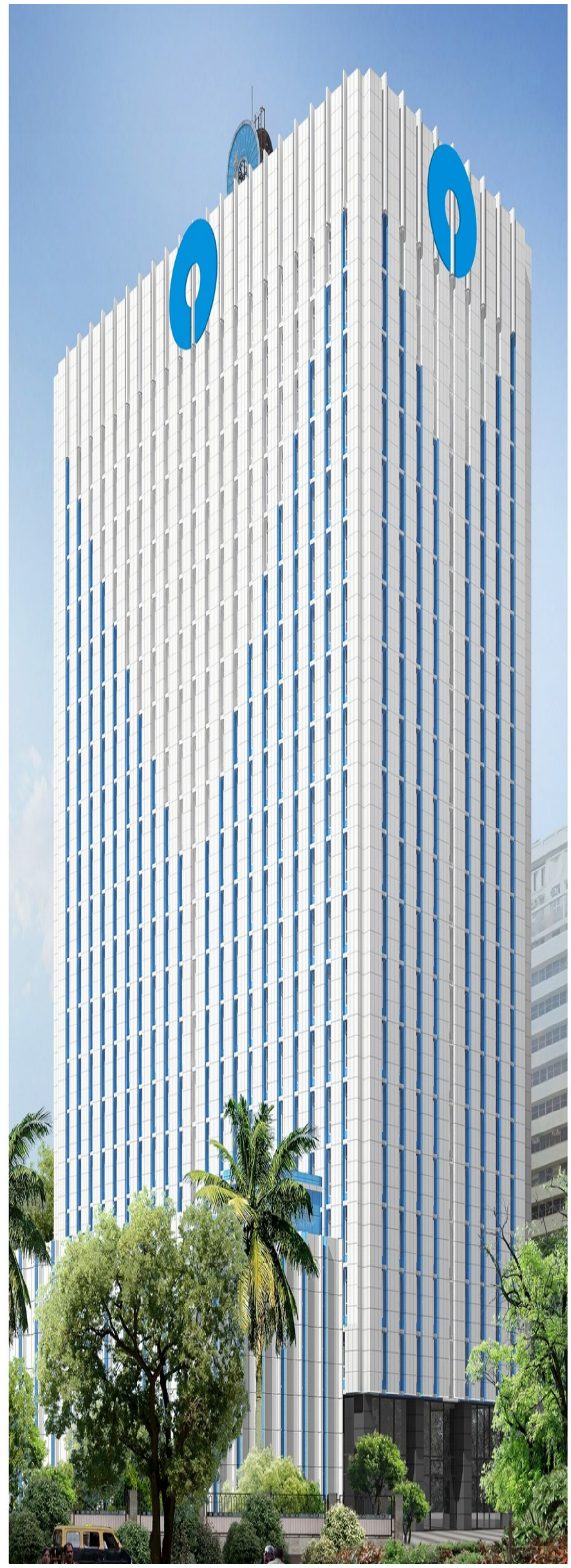

NOT LOAN WAIVER, BUT SIMPLE LOW HANGING FRUITS CAN SOLVE RURAL WOES

There are 8 States where assembly election is scheduled for next year. Considering the competitive populism policy followed across States, few other States may now decide to go for a farm debt waiver scheme. Under such circumstances, the states have only two option to fund the debt waiver scheme: (i) borrow from market; (ii) reduce capital expenditure.

We believe, given the lack of limited fiscal space available to states in terms of market borrowings as per the Fourteenth Finance Commission recommendations, states have to cut back significantly on capital expenditure, even after incrementally borrowing from the market. Our estimate shows that states like Madhya Pradesh, Rajasthan, Assam, Chhattisgarh and Karnataka will have to cumulatively cut Rs 78,453 crores in capital expenditures, if incremental revenue measures are not announced. The problem is that since such cut in Capital expenditure cannot happen in a single year, it will be spread over a period of time and hence settlement will also be delayed. This will only imply stuttering of credit flow as the relevant account will not be eligible for new loans. This will also imply farmers accessing informal sector for loans and hence higher indebtedness and may be another round of loan waivers.

We would also like to draw attention to another problem. **As per the existing norms of asset classification for agriculture advances, in case of an agriculture cash credit account a farmer has to repay the entire outstanding (principal along with interest) to seek fresh loans from the banks unlike other segments of cash credit business where if the borrower has cleared interest payments and ensured submission periodic stock statements, he/she would be eligible for enhancement/ renewal eventually continuing as a performing cash credit account.**

It would be in the benefit of all, *if the farmer is given renewal/ enhancement based on deposit of applicable interest to the bank and the submission of periodic stock statements (which may be linked to the yearly crop cycles) especially if the bank is satisfied with the farmer in terms of his/her land holding/paying capacity etc.*

If we align the NPA classification norms for KCC and crop loans for agri at par with other segments, we can also save as much as Rs 37,000 crore on being classified as NPAs. It would not only help the farmers but would also help the banks in saving capital on account of provisions made towards these otherwise avoidable NPAs!

FISCAL SPACE AVAILABLE FOR STATES IN 2018-19 BASED ON 14TH FINANCE COMMISSION RECOMENDATIONS

- Once again, State Finance has drawn the limelight ever since some the States have announced to waive farm loans and how to fund this unallocated expenditure in the era of FRBM act. One important question is: **Are these States eligible for additional borrowing over and above the fiscal deficit target of 3% and what is the associated cost of it ?**
- As per Fourteenth Finance Commission Recommendations, all states are required to maintain fiscal deficit of 3% of their GSDP annually for the period of 2015-16 to 2019-20. Additional relaxation will be given to those states for market borrowing who are compliant to both necessary and sufficient criteria of fiscal prudence prescribed by the Commission.
- The Necessary Condition (NC) is that the States should have zero revenue deficit in the year for which the borrowing limit has to be fixed and in the immediately preceding year. The Sufficient Condition (SC) is (i) States' debt-GSDP ratio should be less than or equal to 25% in the preceding year and (ii) interest payment/revenue receipts (IP/RR) should be less than or equal to 10% in the preceding year. States meeting one or both of the above criteria are allowed a relaxation in their fiscal deficit targets by 0.25% or 0.50% of GSDP provided they meet the Necessary Condition.
- If a State is not able to fully utilise its sanctioned borrowing limit of 3% of GSDP in any particular year during the first four years of award period (2015-16 to 2018-19), it will have the option of availing the un-utilized borrowing amount only in the following year but within award period.
- In our previous report on State finance, out of the major 17 non-special category states in India, there were only seven states namely Bihar, Chhattisgarh, Jharkhand, Karnataka, Madhya Pradesh, Odisha, and Telangana, which satisfied both the SCs along with NC and were eligible to have a maximum GFD/GSDP ratio of 3.50% for FY18 whereas one state (Gujarat) satisfied only one of the SCs, therefore eligible to have a maximum GFD/GSDP ratio of 3.25% in FY18. As per their Budgetary documents FY19, the Fiscal Deficit (RE) figure reveals that out of the above eight States both Bihar and Odisha have availed the additional room in FY18 whereas remaining other six States have the option to avail the un-utilised amount in FY19.
- Interestingly for FY19, there are 10 States who have additional 0.25%-0.5% legroom in their fiscal space, based on the 14th FC conditions. Among these 10 States, Odisha, Chhattisgarh and Karnataka have additional room of 50bps for market borrowing over and above of Fiscal deficit of 3% whereas Sates like Gujarat, Jharkhand, J&K, Telangana, Himachal Pradesh, Madhya Pradesh & Goa are eligible for additional room 25bps over and above of 3% fiscal deficit target.

States Eligible for Additional Fiscal Space in FY19

State	RD 2018 (RE) %	RD 2019 (BE)	Debt/ GSDP (%) 2018 (RE)	IP/ RR (%) 2018 (RE)	NC	SC I	SC II	Relaxation on FD in 2017-18 (% of GSDP)	GFD 2018 (RE)	GFD 2019 (BE)
Andhra Pradesh	-0.5	0.6	28.4	12.0	×	×	×	×	3.4	2.60
Bihar	0.3	3.9	30.0	7.2	✓	×	✓		7.2	2.00
Chhattisgarh	1.0	1.2	16.3	4.8	✓	✓	✓	0.50	3.0	2.80
Goa	0.4	0.2	24.7	11.7	✓	✓	×	0.25	4.6	4.80
Gujarat	0.5	0.4	20.1	14.5	✓	✓	×	0.25	1.7	1.70
Haryana	-1.4	-1.2	27.4	17.0	×	×	×	×	2.8	2.90
Jharkhand	2.8	2.1	26.6	6.8	✓	×	✓	0.25	2.5	2.50
Karnataka	0.0	0.0	17.9	9.7	✓	✓	✓	0.50	2.8	2.90
Kerala	-1.9	-1.7	31.6	15.3	×	×	×	×	3.4	3.20
Madhya Pradesh	0.1	0.0	25.2	8.9	✓	×	✓	0.25	3.4	3.30
Maharashtra	-0.6	-0.5	17.4	13.0	×	×	×	×	1.8	1.80
Odisha	2.1	2.2	20.4	5.6	✓	✓	✓	0.50	3.5	3.40
Punjab	-3.1	-2.5	42.1	26.7	×	×	×	×	4.5	3.90
Rajasthan	-2.4	-1.9	33.2	14.7	×	×	×	×	3.5	3.00
Tamil Nadu	-1.3	-1.1	22.3	16.6	×	×	×	×	2.8	2.80
Telangana	0.2	0.7	21.0	10.3	✓	✓	×	0.25	3.2	3.50
Uttar Pradesh	1.4	1.8	25.0	9.9	×	×	×	×	3.1	3.00
West Bengal	-0.9	0.0	29.9	20.7	×	×	×	×	2.4	1.70
Assam	-8.1	0.8	18.4	6.7	×	×	×		12.7	3.00
Himachal Pradesh	-1.9	-2.1	36.6	13.6	×	×	×	×	5.4	5.20
Jammu and Kashmir	8.1	7.1	46.9	8.3	✓	×	✓	0.25	3.9	4.50
Uttarakhand	0.0	0.0	23.1	14.0	✓	✓	×	0.25	2.6	2.80

Source: RBI, SBI Research

AGRICULTURAL LOAN WAIVER AND STATE BORROWING

- There are 8 States where assembly election is scheduled for the next year. Considering the competitive populism policy followed across States, few other States may now decide to go for a farm debt waiver scheme. Under such circumstances, they have two option to fund the Debt waiver scheme: (i) borrow from market; (ii) reduce capital expenditure. Both the option, though in short term to bring some relief to State finance, but it has a long term impact on health of the economy.
- Historical trend suggest, States finance around 70-80% of their fiscal deficit through market borrowing. Apart from this additional eligibility to relax fiscal deficit beyond 3% may prompt some States to access market in case of meeting policies like agricultural debt waiver. Our estimate suggests, States like Chhattisgarh, Gujarat, Jharkhand, Karnataka, MP, Telangana, Odisha, Uttarakhand, J&K, Goa have extra room for additional market borrowing of Rs 35,774 crore in FY19. In FY18, all States have borrowed Rs 4,18,270 crore from market.
- Research shows that loan waiver never become a solution to farmer distress and it's benefit don't reach to the targeted person, due to various reasons such as lack of formal credit, identification of beneficiaries, etc. Past experience suggests that States like Tamil Nadu, Maharashtra, Karnataka, Uttar Pradesh, J&K, Punjab, Chhattisgarh, Andhra Pradesh, and Telangana who have in the recent past announced their own farm loan/debt waiver schemes are not successful in implementing it properly.

States having extra space in market borrowing in FY19

State	Amount (in Rs crore)
Andhra Pradesh	0
Bihar	0
Chhattisgarh	3571
Goa	214
Gujarat	7524
Haryana	0
Jharkhand	2247
Karnataka	9836
Kerala	0
Madhya Pradesh	2840
Maharashtra	0
Odisha	2282
Punjab	0
Rajasthan	0
Tamil Nadu	0
Telangana	6231
Uttar Pradesh	0
West Bengal	0
Assam	0
Himachal Pradesh	0
Jammu and Kashmir	429
Uttarakhand	599
Total	**35774**

Source: RBI, SBI Research

NEED TO ALIGN NPA CLASSIFICATION NORM FOR AGRI CASH CREDIT LOAN EXACTLY AT PAR WITH OTHER SEGMENTS

- The income from the agriculture depends upon the harvest of the crop. The marginal and small farmers do not have any other source of income other than the produce which is sold in the market to pay for their loan dues and to meet their subsistence expenses.
- As per the existing norms of asset classification for agriculture advances, in case of an agriculture cash credit account a farmer has to repay the entire outstanding (principal along with interest) to seek fresh loans from the banks unlike other segments of cash credit business where if the borrower has cleared interest payments, he/she would be eligible for enhancement/ renewal. This makes the farmers woes aggravated. Say for a loan of Rs 1 lakh, unless the farmer repays the Bank this amount along with the applicable interest, he/she would not be able to either roll-over or become eligible for fresh loan or enhancement. For a marginal farmer, it becomes difficult to lock his entire crop sales proceeds with the bank *(till the loan is processed)* to become eligible for fresh loan. It may also be noted that a typical cash credit account for any business apart from agriculture, requires only the interest to be serviced and the periodic submission of stock statements to remain as a performing cash credit account.
- It would be in the benefit of the bankers as well as the farmers, ***if the farmer is given renewal/enhancement based on deposit of applicable interest to the bank and the submission of periodic stock statements (which may be linked to the yearly crop cycles) especially when the bank is satisfied with the farmer in terms of his/her land holding/paying capacity etc.***
- As per the latest data of RBI the Agriculture NPA was Rs 60200 Cr as at Mar'17. Applying a threshold figure, NPAs on the industry level on account of KCC & Crop loan would be around Rs 27700 Cr for Mar'17. If we assume that the Mar'17 figure of Rs 60,200 Cr would have moved up to Rs 80000 Cr as per trends, the NPA ratio of KCC/Crop loan would be Rs 36800 Cr.
- If we align the NPA classification norms for KCC and crop loans at par with other segments, we would be thus able to save the aforesaid amount from being classified as NPAs. It would not only help the farmers but would also help the banks in saving capital on account of provisions made towards these otherwise avoidable NPAs.

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ABOUT US

The Economic Research Department (ERD) in SBI Corporate Centre is the successor to the Economic and Statistical Research Department (E&SRD). The latter came into being in 1956, immediately after the State Bank of India was formed, with the objective of "tendering technical advice to the management on economic and financial problems in which the Bank has interest and which required expert analysis".

After the first reorganization of the Bank, when specialized departments like Management Science, Management Information Systems, Planning and Market Segment Departments took over the statistical work of E&SRD, the Department was renamed as ERD.

However, with the ERD team now taking on multidimensional functionalities in the area of risk management, corporate analytics, strategy and so on, who knows, the time may have come to rename it again!

DISCLAIMER

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