

Major Research Project
On
Causes for NPA in MSMEs and Agriculture Sector

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Declaration

I, Manish Rana, declare that my major research project report on “**Causes for NPA in MSMEs and Agriculture sector**” is my original work and no other individual or organization has the right on the report. This report has not been submitted to any other organization and the report has been prepared under the supervision of my mentor at Delhi School of Management, DTU.

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Acknowledgement

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Executive Summary

1.1 Background

MSMEs and Agriculture sectors are crucial sectors in terms of employment as well as to maintain economic regional balance in the country. For past several years, these sectors have been indulging in downturn in their working operations, specially, increasing NPAs in the sectors. Increasing NPAs in these sectors are also restricting the revenue of the involved banks in the process of Loan.

There are multiple reasons for which the obligators defaulted on their obligations. These reasons vary from unfavourable economic conditions to unfavourable weather conditions. Non-performing assets (NPA) occurs when the borrower defaults on obligation for more than 90 days.

The Gross NPA in PSBs accounted for INR 9.42 lakh crore by the end of the July, out of which INR 1.1 lakh crore belonged to agriculture and its allied activities. Likewise, MSME loans worth of INR 2.4 lakh crore have been disbursed by banks by January 2020, out of which 12.1% stood as NPA by December 2019.

1.2 Objectives of the Study

- To obtain potential causes in MSME and Agriculture sectors
- To understand the impact of NPAs in banks and economy as a whole
- To gather participants' view on NPA in the designated sectors

1.3 Scope of the Study

The significance of the project is to procure causes of NPA to make amendments in the process to tackle and reduce the threats of NPAs and to manage NPA in the best possible way.

The suggestions acquired from the participants' input play a key role to find loopholes and to make intuitive decisions to contain NPA.

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Non-Performing Asset

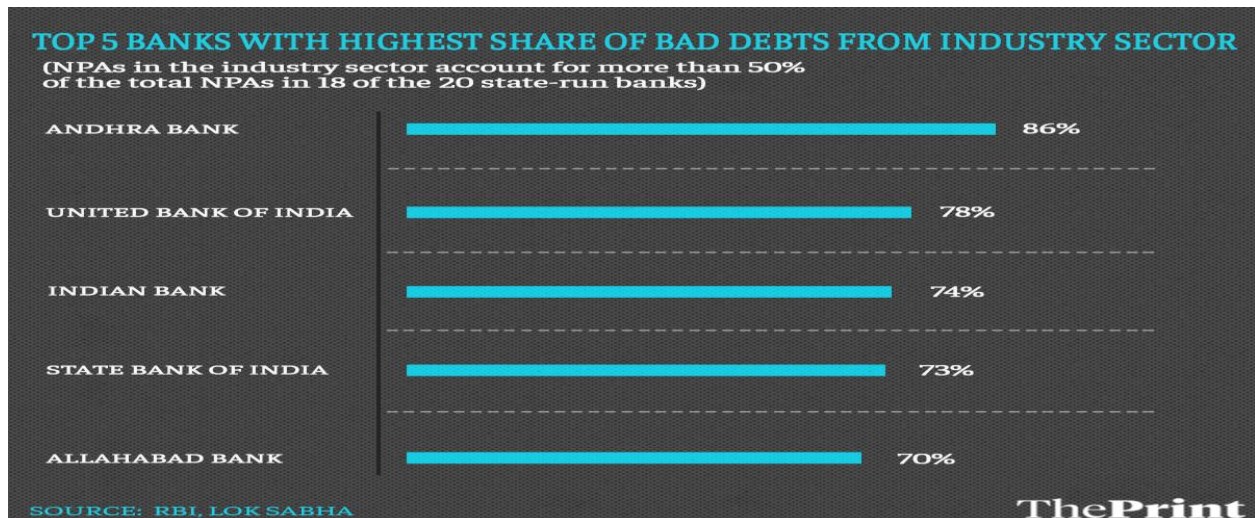
Non-Performing assets refer to the classification of loans and advances which are defaulted on the obligation. This arises due to arrear in loans when the principal or interest payment gets defaulted.

According to RBI, NPA is the asset, including all leased assets, becomes a non-performing asset when it stops generating income for a bank. An installment or an interest, which remains overdue for the period exceeding 90 days termed as an NPA.

For agriculture, an installment of the principal or the interest income remains muted for two successive crop seasons is termed as NPA.

In India, non-performing assets largely prevailed in agriculture sector where farmers are not able to pay the loan amount or interest accrued on the principal amount due to the losses which occur in case of floods or drought.

NPAs in the Industry sector accounted for over 50% of the total bad debts in 18 of the 20 state-run banks in 2018-19. Five state-run banks reported that bad debts from the industry accounted for more than 70% of their total NPAs. These banks include Andhra Bank, United bank of India Indian bank, SBI, Allahbad Bank.



Classification of Assets

Assets can be classified into four classes according to the state of the asset:

Standard Asset: the risk is nominal in this class of asset. It does not carry above than the normal risk and is not actually an NPA. In this class of asset, a bank receives interest income as well as principal amount in the obligated time. In such a scenario, accrued interest and the principal income exceed not more than 90 days.

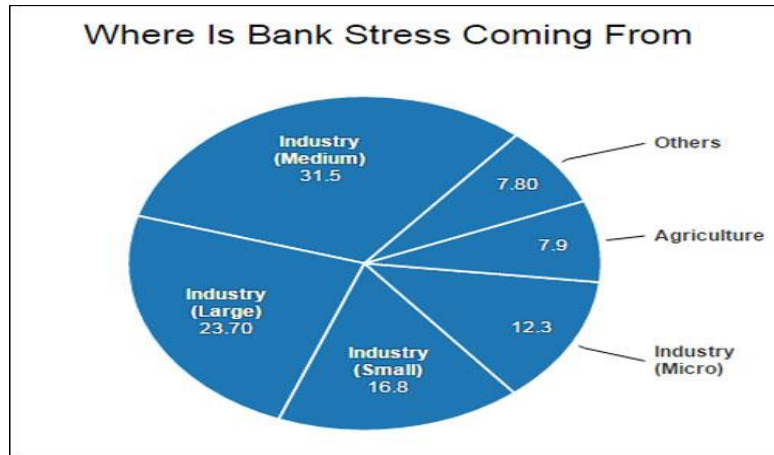
Sub-Standard Asset: When the asset remains NPA for below or equivalent to 12-month in a row can be termed as a sub standard asset. In this case, the total net worth of a borrower of the bank or a guarantor or prevailing market value of the security in the market is not sufficient to recover the loan amount. Such an asset well defines the credit weaknesses that jeopardize the liquidity in the market.

Doubtful Asset: An asset is defined as doubtful asset if the asset remains non-performing asset above 12 months. An advance designated as a doubtful asset carries all the inherent weaknesses as of sub-standard asset. There are three stages under this category: D-1, doubtful for 1 year, D-2, doubtful for 2 years and D3, doubtful for than three years.

Loss Asset: Any asset which is confirmed by a bank or external or internal auditors per Reserve Bank of India's inspectors the asset with no chance of recovering dues is the loss asset, and the amounts haven't been written off completely or partially. An optimism to recover the advances is lost in case of loss asset.

Reasons for NPA

NPA has been the key issue, impacting the banking sector to operate vehemently. The gross NPA reached 10.2% by September 2017 and the same reached around 11% by September 2018. According RBI, the gross non-performing assets pegged at Rs. 10.25L crores by 31st March 2018.



Source:

<https://tinyurl.com/y7sarlck>

Internal Factors

- Defective Lending Process
- Poor Credit Appraisal System
- Absence of monitoring the borrowers
- Managerial deficiencies
- Improper Industrial Visit

External Factors

- Uncertainty in the economy
- Change of Government policies
- Willful defaulters
- Diversion of Funds
- Natural Calamities
- Political Interference
- Unproductive Business
- Inability of Companies to cover their credit dues.

MSME

MSME(micro, small, medium enterprises) is the one of the branches of the Government of India, the incumbent executive body designated specially for the formulation and administration of all the rules related to the subject, and regulation of all the enacted laws associating with MSMEs in India.

MSMEs Development Act, 2006, is the act of the parliament of India. In a relation to this enacted act, if a purchaser fails on its obligation towards an MSME for 45 days, he/she will have to reimburse monthly-compounded interest rate at three times of the rate notified by the RBI.

Industries are bisected in two categories, manufacturing industries and service industries. These industries are further carved up in micro, small and medium industries. In the manufacturing sector alone, capital requirements for micro enterprises are under 25 lakh rupees, for Small enterprises capital requirements swing from 25 lakh to 5 crore, and for medium enterprises, capital requirements vary from 5-10 crore rupees.

In service sector, capital requirements for micro industries are under 10 lakh rupees, 10-200 lakh for small industries and 2-5 crore rupees for medium industries.

In India, valuable contribution of MSMEs is exceptional in Indian economy. MSMEs generate greater than 48% of the total output in India and greater than 42% of India's total exports. MSMEs employ around 100 million in the country.

In the Indian market, MSME's lively growth can be seen as if Indian entrepreneurs are making remarkable proceeds in various industries such as precision engineering design, manufacturing, IT&ITES, retail, textile & garments, pharmaceutical, food processing, services and agro sector..

MSMEs not only serve the urban market but also serve to rural and outskirts areas, thus, making it possible to reduce regional imbalances and securing distribution of national income evenly.

Apart from employment, there are more than 6000 products already varying from traditional to high-tech utility items, which are manufacturing by MSMEs in India. These products include cotton textile, silk, beverages, synthetic products, jute, wood products, wood, electronic equipment, accessories etc.

Policies towards MSME and Evaluation of reservation policy of MSME

Review of Policies

- MSMEs can be seen as a major source of employment and equitable distribution of national income since the independence; still, the objectives of such policies pressuring the roles of MSMEs have not been realized yet.
- After the independence, the development in this particular sector has been noticeable, both in terms of programmes and in regions.
- Measures for the Policy include fiscal concessions, technical and marketing support, subsidized directed bank credit with exclusive productions by MSME.
- All the policy measures were in accordant with the other policy measures such as domestic investment and foreign trade policies which gradually became more stringent over the past years.
- Since the mid of the 1980s, the amendments in the tax system and the liberalization of import policies have been made.
- The shift in the policies of MSMEs emphasized on protection from the competition. Since then, the supports in policy measures in the 1990s and 2000s have been remarkable to the MSMEs to bridle the key challenges in terms of performance and competition in the market.

Evaluation

- Policies for keeping products for exclusive manufacturing in the small sector enacted in 1967 with 47 products were on board; the reserved list increased to 872 by 1984.
- The increased items were reduced to 830 in 1989.
- The stride of the reforms was expedited in 1992 and the average tariff rates were steadily lowered, number of quantitative restrictions was removed, and the domestic investment policies were realized.
- With the lapse of time, the items were reduced and brought down 605 in 2005.
- As polices became more liberalized, the items on the reserved list started getting import items from various countries, thus, resulted, competition from foreign enterprises.

Challenges to MSMEs

MSMEs control over 45% of the market share; still, this sector is surrounded by the number of challenges and does not get the deserved support from the respective governments or the centre government, banks and other financial institutions are also proving to be the hurdles in the growing path of MSMEs.

Key challenges include:

- Timely and adequate availability of banking finance
- Constraints on modernization and expansion due to financial stress
- Limited knowledge and capital
- Non availability of skilled labors at negotiated price

With the sustainable growth rate of around or above 10.1 per cent from 2015-2018, MSMEs reflect the ability of Indian entrepreneurs to innovate and to produce solutions despite resource and logistic problems existing in the country.

Having intense potential, this sector is unable to imbue in novel technologies, accessing to resources and other technological skills due to lack of funds and investors who are willing to invest in the sector.

Decelerate and liquidity crunch have driven the sector towards **NPA** inflictions which led the Finance Minister, Nirmala Sitharaman, to declare at ASSOCHAM anniversary celebrations event about the need of restructuring in the MSME sector which can be done without categorizing the loans as NPSs.

Keeping the issues in the view, the collaborative efforts are required to introduce MSMEs towards new developments and technologies and how these developments could be efficiently implemented by keeping them in the local norms such as the local languages and the other various modes at which the locals are comfortable with.

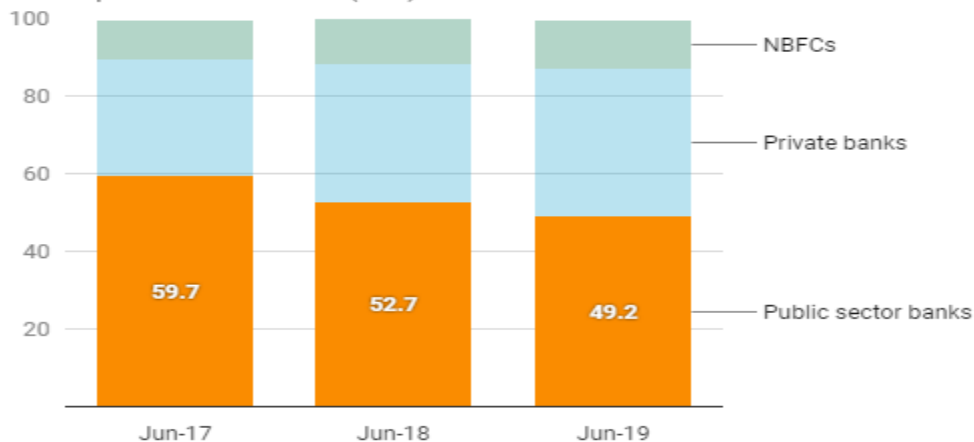
GST compliance is also a burden on MSMEs. There are multifold issues associated to labor, research & developments, and the infrastructure for MSMEs. A few new labor codes are already there in the queue and all the other interferences by the incumbent authorities must contribute equally important efforts to sensitize the state government and the local bodies not to impose undue compliance burden on them. Similarly, relaxation must be there for other codes to promote ease of doing business.

Causes for NPA in MSME

- **Competition:** Small and medium firms find it difficult to stay with the competition, thus, the chances of getting defaulted on the obligations towards load increase.
- **Management Inefficiency:** Inefficiency of the management of firms to boost the growth of the firms. This mismanagement arises the problems of sales of the products and services to generate revenue for the firms to pay back their dues.
- **Government Policies:** Unable to cope up with the sudden changes of the policies of the Government, such as demonetization or GST etc. These changes make it difficult for small and medium enterprises to stabilize the business.
- **Unskilled labors:** Lack of skilled labors at low cost is a big issue, which contribute to the growth of enterprises.
- **Capital Requirement:** Limited capital to adopt technological advances.

Public sector banks are the biggest source of MSME credit but their contribution is decreasing

Breakup of credit to MSME (in %)



Source: TransUnion Cibil • [Get the data](#) • Created with [Datawrapper](#)

Competition in the Market

Global Competition: Globalization has led to increase competition which can be reflected in the cost of labor, products and services. Range of products and services has also been multi folded since the inception of globalization. Brainwashing is another concept under globalization, where the skilled and great minds switch to other countries in the search of living a good life and finding good jobs for them. These activities have collectively increased the global competition in the market.

Exchange of Technology: Technology is one of the factors of competition and the resultant for quality of goods and services produced. Globalization has increased the speed of technology transfer and improvement. Capital intensive market requires rapid change in the technology to survive the threats and challenges from the market. The technologies in which competitive advantages can be achieved:

- Customer service
- Operations and processes
- Cloud computing services
- Supply chain management
- FinTech
- Database management and warehouse
- SAP management
- Software development
- Internet of things
- Artificial Technology
- Machine Learning

Knowledge Transfer: Knowledge is the key source of value production factor in the current environment. A good knowledge management system is the key competitive advantage for knowledge creating, sharing, and managing to achieve competitive position in the market.

Resource Based Competitive Advantage

Tangible Resource: Tangible assets include property, plants and equipment. Apart from PPE, labors are the important human resources, especially, in labor intensive firms. Many of the MSME firms are labor intensive due to high capital requirement to tackle the completion from the capital intensive firms and it also requires a good amount of investment in capital intensive firms. Thus, finding skilled labors at negotiated price is the biggest task for small and mid- sized companies, and getting the employees or worker at compromised price leads to inefficiency in management of the allocated tasks.

Intangible Resource: Intangible assets include Patents, Intellectual Property, Trademarks, Goodwill, Brand reputation etc. Intangible assets include intense capital require and highly skilled workers to generate fixed income for the firm thus able to repay all the loans at promised time. In case of MSMEs, they do not have enough capital and skilled labors to invest in intangible assets to compete in the market.

Human Resource: Human resource department is one the major department which is responsible for recruitment, employment and promotion. The HR department is the employee centered department, especially, for the development of employee benefits and wellness programme. The seven major functions of HR are:

- Selection and Recruitment
- Training development of employees
- Labor relations within and outside the organization
- Performance management in the organization
- Job design structure
- Managerial Relations
- Compensation and Benefits

A competent human resource management is an advantage for an organization to let the organization achieve it the vision and mission by acquiring skilled and talented employees. Human resource management must be aware of all the developments swinging in the market to provide an organization edge over others.

Banking Sector

Industry Profile

The industry for Indian banking came into existence in the initial decade of the 18th century as the first bank in India originated in 1786 and after that the Bank of Hindustan started to operate in the country. The earliest bank in India that is still operating and performing well is the State bank of India (Bhartiya State Bank) this bank was established as "State bank of Bengal" in Calcutta. The three banks Bank of India, State Bank of Bengal, and Bank of Hindustan then merged in 1921 to establish Imperial Bank of India, which after the independence of India, became the State Bank of India in 1956.

Banking industry is the industry that handles cash deposits, cash credits, investment schemes and other financial transactions. A bank is a different financial institution that receives deposits from the public and generates credit rather than just giving only credit and investment facilities like other financial institutions. Credit procedures could be done either by infusing directly or indirectly through the capital market. Banks play a significant role to maintain financial stability in the country; which is why banks are needed to regulate banks diligently.

Numerous countries have incorporated a banking system as "fractional reserve banking", it is the system where banks carry liquid assets to a fraction of their current liabilities. To ensure liquidity, the regulations have been laid out by RBI that banks have to maintain minimum capital requirements regarding the international set of capital standards.

There are total 10 public sector banks, 21 private sector banks, 46 foreign banks, 58 regional rural banks, 1539 urban cooperative banks, and 94,299 rural cooperative banks, in addition to cooperative credit institutions before 2014. By 31st March 2019, the number of ATMs in India had increased to 2,21,657 and is expected to increase to 407,000 by 2021.

The Reserve Bank of India (RBI) is the central bank of India, which control, monitors, and circulates the demand and supply of Indian rupee. Reserve Bank of India (RBI) is the regulator of the banking sector in India, which is responsible for creating guidelines for the banks in the country. Reserve Bank of India (RBI) regulates and controls all commercial banks and employed non-banking finance companies operating in India. RBI was established in 1935 under the Reserve Bank of India Act, 1934.

By Fiscal Year 2019, the total credit by the commercial banks surged around Rs 89 lakh crores and the total deposits grew to Rs 120.13 lakh crores. The Assets of public sector banks also stood at Rs 107.99 crore in FY18. The report published in the Union budget 2019-2020, stated that the provision coverage ratio of banks reached at its peak in the last 7 years.

Digital Revolution in Banking Industry

Banks had started utilizing Information Technology as the inception of personal computers recognized after then switched to Local Area Network (LAN) connectivity. The continuous improvement and advancement, banks started adopting the core platforms for banking system, thus the process of banking transformed to complete bank-banking system. CBS, core banking solution, is the system which allows banks to improve the support features to all the customers with an aim to embark on rectifying customer services whereby, customers can avail banking services from anywhere at any time. Other various principal banking platforms, such as Finacle, BaNCS, and Flexcube achieved recognition as customer management system in banks.

The computerization process popularized as the widening of the economy activities scopes by 1992. The cardinal motivation behind this turnover was increasing competition arising from the domestic and the foreign banks in the country. The Commercial banks also began to adopt digital services to stay sustainable in the race.

Banks have significantly improved their operating system in numerous ways by embracing new technologies such as E-banking; this system caused banks to reduce their operating costs and assisted in generating operating revenue via multiple sources. According to the obtained data, the operating costs of banks' transactions while performing branch-banking is reckoned to be in the bracket of Rs. 71 & Rs. 76, it is hovering around Rs. 14 to Rs. 15 for ATM, at most 2 rupee or less on online-banking and at most 1 rupee or less for mobile-banking. Increase in the number of customers has also remarkable due to the comfort in 'Anywhere-Banking' facility. Arrival of technologies has also declined the number human errors to an approximation. Now, it's feasible to obtain and to examine the information any time with the help of a strong reporting system.

Reserve Bank of India is a leading vehicle for banks to make them follow regulations and to give recommendations to stick to the objective laid by RBI. The commercial banks subsided in the country have started adopting technology using bank mechanization and automation by using MICR based cheque processing, implementation of Automated Teller Machine, inter-connectivity among bank branches, electronics funds transfer channels have resulted in achieving the objectives of anytime banking.

The Government of India is also vehemently endorsing digital transactions and planning to make India cashless economy. The launch and promotion digital payment wallets such as United Payment Interface (UPI) and Bharat Interface for Money (BHIM) by National Payments Corporation of India (NPCI) are significant attempts to transform the payment systems domain. UPI is an interface-friendly mobile application where customers can transfer funds instantly between accounts.

AGRICULTURE

The Agriculture sector is the one of the dominant contributing sectors in the wellness of the economy, which indicates a principal role in the economy. The agriculture sector alone employs nearly a half of the total workforce which have been employed in the other sectors and it significantly contributed about 16.9% in the GDP in the financial year 2015-16. In 2016, the agriculture sector and all its allied activities had accounted for roughly 15.45% of the gross GDP of the country.

As per the data published in 2014 by FAO world agriculture statistics, India is the world's largest producer for many agriculture outputs such as fruits like banana, mango, guava, papaya, lemon and vegetables like okra and milk, chickpea, major spices like chili pepper, ginger, fibrous crops such as jute, staples such as millets and castor seed. India is the 1second largest producer of wheat and rice, the world's major food staples.

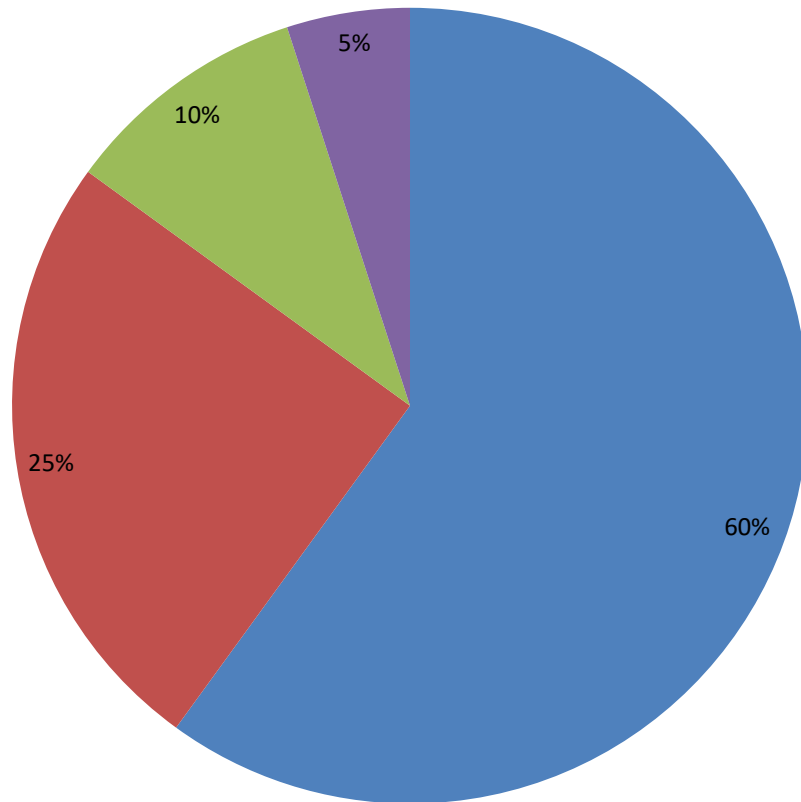
The production of food grains in India has been increasing every year and the consumption is also increasing proportionally, and India is among the top producers of several crops such as wheat, rice, pulses, sugarcane and cotton. India marks its presence in producing the highest quantity of milk and second highest in producing fruits and vegetables. In 2013, India contributed more than 23% to the world's total pulse-production, the highest for any country, around 21% to the rice production and 12% to the wheat production. It also accounted for about 24% of the total quantity of cotton produced around the world, apart from these contributions, India also bags the title for second highest exporter of cotton for the past several years.

There are several factors which decide the agricultural productivity in various ways. These factors include the availability & quality of factors of production of agriculture and the inputs required for agricultural activities such as land, water, seeds and fertilizers, accessibility to agricultural credit and crop insurance, assurance of remunerative prices for agricultural produce, and storage and marketing infrastructure, among others. This report provides an overview of the state of agriculture in India. It discusses factors related to the production and post-harvest activities in agriculture.

Agriculture industry not only employs the livelihood for the farmers and the laborers in agriculture sector, the industry also inspects food security for the nation. The Food and Agricultural Organization (FAO) of the United Nations defines food security as a situation where all people have physical and economic access to sufficient, safe and nutritious food that meets the dietary needs for the healthy lifestyle.

NPA CLASSIFICATION IN AGRICULTURE

■ FUND DIVERSION ■ INTENTIONAL DEFAULTERS ■ NATURAL HAZARDOUS ■ UNAWARENESS ■



Natural Hazardous

Weather is the most important contributor for agricultural activities and a farmer is highly dependent on weather for the productivity of crops. There are several climate change impacts which affect crops which are followed as:

- Temperature variation
- Changing Rainfall Patterns
- Hailstones
- Hailstorms

Two popular crops Dhaan(rice) and wheat are planted in summer and winter respectively. Intense heat in summer, especially, in June and July results in damage of the crop, dhaan(rice). To avoid this calamity, a farmer has to spend extra sum of money for water to avert this disaster. Similarly, a sharp decline in temperature blooms wheat crops in winters.

If farming is the only source of income for a particular farmer then adverse climate change forces the farmer unable to pay its due on time and if the climate change costs a heavy damage then it may take a good amount of time by a farmer to pay its debt or sometimes unable to pay back its dues.

Though the facility of insurance claim is already included in Kisan Credit Card (KCC), farmers are still unaware about this facility and those who are aware of this facility, they do not know where to report loss and how to avail this facility. These barriers do not allow farmers to recover their losses.

A. Temperature Variation:

One of the major reasons for temperature variation is ozone, nitrous oxide, methane, green house gases, nitrous oxide etc which are significantly impacting agriculture and warming the environment rapidly. Increasing Global warming causing crops die due to intense heat if not watered sufficiently. A continuous supply of water is required to keep the crops alive, which costs farmers to strain their pockets.

At the same time in winter, farmers have to spend additional money for keeping the crops off the failure from steep decreasing in temperature. The steps to protect crops in winter include:

- Splashing water on soil to generate heat evaporation to ward off crops from freezing.
- Burning woods and cow dungs to set off frozen environment around crops.
- Covering the field. It is the most expensive method to protect crops from extremely cold environment.

B. Chang in Rainfall Patterns

Heavy Rainfall:

It is a natural process which is beyond the control of any human intervention. Heavy rainfall greatly impacts the production of wheat and other crucial grains like corn and millet (bajra).Eradication of crops from heavy rainfall causes farmer to bear the monetary loss.

Abnormally high amount of rain can leach nutrients, especially, nitrogen from the soil. Nitrogen added to the soil in the form of granular fertilizer which is vulnerable to leaching. If this occurs, farmers either have to incur additional cost of reapplying fertilizers or experience the reduction of crop yield associated with nutrient deficiency.

In case of flooding, crops submerge in water resulting in devastating losses. The foliage of submerge plants will quickly begin to die because submerged leaves are not able to exchange atmospheric gases mainly carbon dioxide and oxygen.

While the heavy rainfall helps cut the cost of irrigation for wheat crop, these are set to affect the output of oilseeds and mustard.

Low Rainfall

Below average monsoon with expectations of erratic rainfall induced by climate change, aggravates farm distress particularly in drought ridden regions. Soybean, groundnuts and pulses are the major rain-fed crops that are affected if the rain deficiency prevails.

Managing the problem of low rainfall is nearly possible through Irrigation but irrigation requires large amount of energy making it expensive for every farmer. Salinization and waterlogging of soil are serious problems associated with irrigation. Scarcity of water in drought hit areas makes irrigation impossible and wreaks ultimate failure of crops.

C. Hailstones

Hailstones are accompanied by heavy rainfall. They are solid particles, when fall on crops, result in completely destruction of crucial crops such as rice, millet, wheat etc. This is indeed a heavy loss to a farmer. Productivity of soil also reduces due to excessive and large amount of hailstones.

Heavy hailstones also disfigure composition of soil and cause farmers to invest extra time and money to shape the soil again.

D. Hailstorms

It is a natural hazard. The impact of hail on crops depends on the size of hailstorms and the growth stage of the crops. According to a media report, more than 124000 hectares of farmland spread over 1,086 villages in Maharashtra was affected by unseasonal rains and hailstorms in February 2018.

Unyielding hailstorms bend and break plants and strip them of leaves and bark thus destroy the hard work of farmers. Around 100000 hectares of crops like wheat, gram, peas, lentils, oilseeds, mustard etc were damaged in Uttar Pradesh in 2018.

Similarly, in April 2019, Kota region of Rajasthan, which is prominent wheat belt in the State, reported the loss between 20% and 50% due to heavy rains and thunderstorms.

Political Interference and Government Decisions

Loan waivers announced by state government and central government are likely to cause spike in non-performing assets in agriculture. This political interference allows farmers to draw back from their promising dates of repaying loan which results in increase rate of interest and further increase in the loan amount, after waiting for years for loan waive if a farmer unable to receive Loan waiver then the farmer becomes a **willful defaulter**.

A wilful defaulter is the borrower of the loans, who has been defaulted in meeting repaying obligations within stipulated time despite having the capacity to repay.

Loan waiver scheme is prevalent during elections in the country whether it is state elections or general elections. Promises by political leaders towards loan waiving create a chaos among the banks which have disbursed a large amount of farm loan as these loans become NPA after a certain period of time. Recovery of NPA takes a huge effort from a bank as it requires a good amount of time and money to conduct schemes like **one time settlement scheme mela** and **Lok Adalats**.

In 2017, the Uttar Pradesh government's loan waiver of Rs 36,359 crore in agriculture had increased non-performing assets and NPAs from agriculture and other allied activities had steadily soared from 3.4% of aggregate banking loans in March 2011 to more than 6% by the end of 2017.

Similarly, a large chunk of farmers are waiting for loan waiver under PM Kisan scheme. Recently, the government has initiated the Pradhan Mantri Kisan Samman Nidhi, effective from February 1, 2019, to keep the expenses associated with agriculture and its allied activities. Under this scheme, the government distributes a payment amount of Rs 6,000 per year in three equal statements of Rs 2,000 to all the beneficiaries.

Government Decisions

Unusual decision like **Demonetization** creates turmoil among farmers, though it has a short term impact on the economy; it records a significant impact on agriculture, especially, on small and marginal farmers. A farmer still heavily depends on physical currency notes rather than digital currency or online transactions. After demonetization, due to lack of cash, farmers were unable to purchase seeds and fertilizers ahead of rabi season. At the same time, selling of agriculture outputs became extremely difficult for farmers.

Demonetization also affected big farmers as they had to pay wages to the laborers working on their fields.

Farmers were unable to purchase quality seeds from market. They were using old seeds from last year's harvest. This slightly affected good yield of crops. The farmers, who were into cultivating fruits and vegetables, were badly hit as they needed cash on for their operating costs on regular basis to purchase inputs like pesticides and fertilizers and to transport & to sell their harvests in the market.

Farmers were unable to withdraw more money from their banks until they repaid their dues. This mismatch snowballed NPA in agriculture.

Even after the good production of fruits and vegetables, there was a decline in demand because of the crunch of high currency notes and the only mode of trading was low currency notes which consumers were unwilling to use. This caused farmers to collect a good amount of sum even after a fruitful production.

Even National Seeds Corporation failed to sell quintals of wheat seeds because of cash crunch. This resulted in the low production of wheat even ahead of good monsoon.

All the affects mentioned above forced small and marginal farmers to take loan from third party at higher side of the interest for inputs like pesticides and fertilizers as comparison to the interest given by banks. **Farmers also had to give vegetables and fruits on credit for which they did not receive money on time.** This increased burden of loan on farmers which reflected in the form of NPAs.

FUND DIVERSION

Low interest rates under Kisan Credit Card(KCC), pegged at 7%, attract farmers to take loan under KCC for their personal needs too. This allows farmers to take advantage of KCC to divert fund.

Kisan Credit Card (KCC)

It is a credit providing system started by the government of India to fulfill the credit requirements as working capital of the farmers in a convenient and hassle free manner. The scheme designed to cater the entire country by institutional credit involving commercial banks, RRBs and cooperatives have received a broad acceptability among bankers and farmers for the smooth implementation of the scheme. Interest rate for the loan under KCC is 7%, whereby if a farmer pays his/her dues within a year then he/she only has to pay only 4% rather than 7%.

Objectives

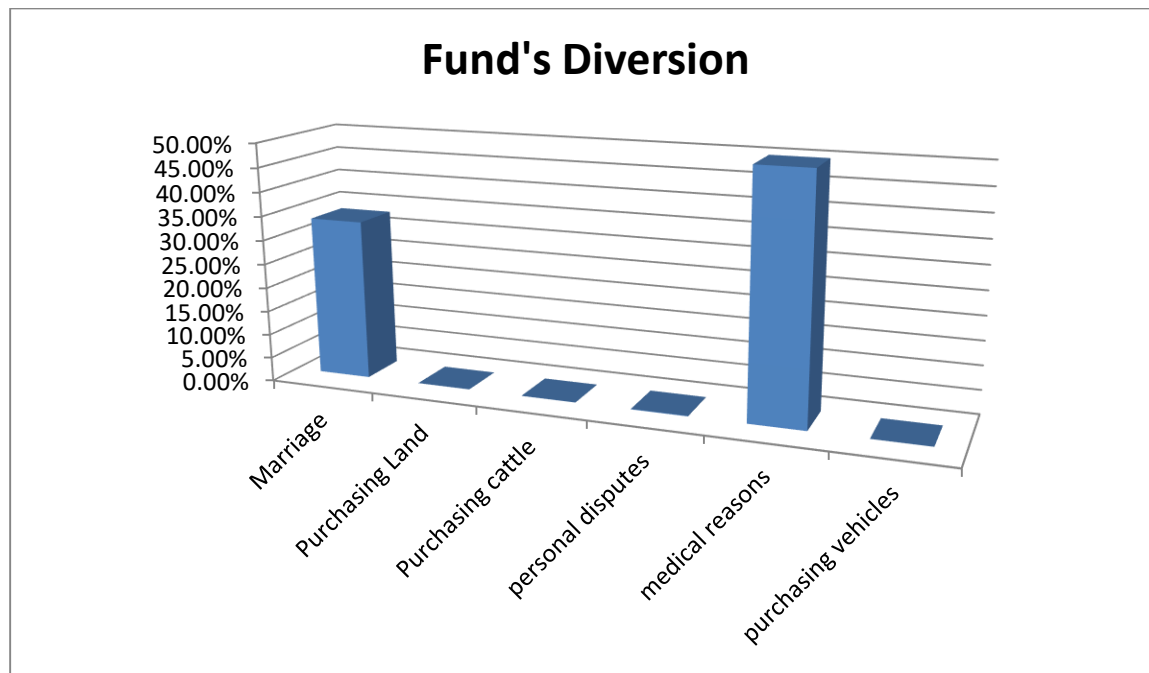
- To cover the short-term credit requirements.
- Cover expenses post harvest
- Provide loan for marketing
- Household requirements
- Net working capital requirement for the sustenance of farm equipment and its allied activities.
- Credit required for investment in agriculture and allied activities such as fertilizers, sprayers, dairy animals for agricultural output etc.

Eligibility

- All the farmers indulge in agricultural activities
- Tenant farmers working in agriculture fields
- Self help groups or joint liability groups of farmers including tenant farmers

Funds Diversion Includes

- Funds taken for Marriage
- For purchasing a piece of Land
- For purchasing cattle
- For resolving personal disputes
- For medical reasons
- For purchasing vehicles



Funds taken for Marriage

A farmer uses the funds for the marriage of his/her daughter or son or brother/sister etc. It might be the case that the farmer uses the fund into his/her own marriage. It is the second most prevalent reasons among diversion of funds.

Purchasing a Piece of Land

Purchased piece of land is generally used for farming or to give that piece of land on rent. In case of rent, a farmer is not always able to receive rent on time or sometimes it is difficult to find a potential occupier for the rent. These limitations from the investment make farmers unable to receive the return on time in order to pay his/her dues.

Purchasing Cattle

Cattle are used for labours connected with farming such as tilling, irrigation and carting. Cattle are one of the important sources of income for farmers. Cows and Bulls are popularly used in tilling and other agricultural activities to reduce human effort and to increase productivity.

Personal Disputes

Personal disputes are usual in rural areas. Most of the disputes are related to land. Such disputes occasionally take a violent turn which lead to police cases. Additional expenses in lawsuits are generally bore with the help of loan under KCC.

Medical Reasons

It is the major reason for the diversion of funds. In case of emergency, a farmer has no other options than taking loan from a bank. To obtain money in a timely manner and at low interest rate a farmer always opts to obtain loan under KCC. Some popular medical reasons include:

- Heart operation
- Road accidents
- To bear the expenses of expensive operations and medicines

Sometimes, diseases such as malaria, dengue etc, require special treatments which are only available at different cities, especially in urban areas. These cost a farmer additional expenditures.

Purchasing vehicles

It is not a common activity, but, sometimes; a farmer uses the money taken from bank as a loan to cover the remaining amount for purchasing a vehicle. Rather than taking a vehicle loan at higher rate, a farmer chooses loan under KCC.

KCC seems the most profitable source of fund when it comes to take loan at low interest rate.

UNAWARENESS

Lack of awareness among farmers regarding obtained loan under KCC plays a significant role towards increasing NPA. Not all farmers are adequately literate to understand the messages they receive regarding loan as the messages are in English following which they do not turn up in the bank within the promised time period.

Although it is told to farmers in very beginning while disbursing the loan that after paying all the dues they have to fill a renewal form which is mandatory, there are still some farmers who do not fill renewal form after paying their full dues and subsequently, their accounts fall under NPA accounts after a certain period of time.

But, it is not always the case of lack of awareness, sometimes; farmers show delinquency in filling renewal form and consequently, pay the price in the form of accrued interest on the obtained loan.

Many farmers do not know where and whom to report for insurance claim after the natural calamity. This lack of awareness results in forfeiting the recovery amount. As there is a limited time period for insurance claim, which is only 48 hours in case of destruction of crops, a farmer is not able receive insurance claim even after visiting the bank as the farmer is not able to fulfill the formalities within the time he/she still does not know that it just 2 days.

Communication Error

It is a rare case where it is difficult to find the farmer who took a loan from a bank. A marginal farmer, with no mobile phone, and who also does not mention the name of his/her father along with no exact address while filling documents for KCC, is generally difficult to track. In this case, the only way to track him/her is to visit the village he/she lives in and to ask the Sarpanch about the person by his/her name.

Lack of supervision

All the farmers are informed before disbursing the loan that they have to pay the loan within 1 year to avoid higher interest rate or to pay whole amount within two harvest seasons and they also have to fill a mandatory renewal form after paying all the obligations, still there are some farmers who do not remember the terms and conditions and they lack in fulfilling some formalities such as not filling of renewal form, not remembering the last date of repaying loan etc. The Timely renewal of the advances under KCC makes farmers eligible for the automatic increase of 10% in their KCC loan limits.

To tackle such cases, a sincere supervision might help which may include a text message every month and calling farmers in the last month of the loan repayment so as to keep them informed.

There is also a big clause here. It is difficult to contact most of the farmers through text or calling as the registered number with the bank is either not in service or Invalid and sometimes; the number is wrong number.

Literature Review

MSMEs and Agriculture sectors are two most significant and dominant sectors responsible for contributing remarkably in the economy. Both the sectors contribute a large chunk of the total contribution in creating regional economic balances. These sectors contribute largely in:

- Employment generation
- GDP
- Standard of living
- High disposable income
- Growth in economy
- Attracting FDIs
- Attracting FIIs
- Utilization of resources
- Generating income for state governments

The advances in Agriculture sector are diversified in various agriculture allied activities such as poultry, crops cultivation, crops protection equipment, fishery, livestock rearing, dairy etc.

Likewise, the advances in MSMEs are diversified for the development of products and services to cater the market needs.

NPA in agriculture continues to woe banks as the banks are unable to recover the dues within the duration of repayment and sometimes the assets become loss assets such that those assets become bad debts. Schemes like Lok adalat and One time settlements schemes are meant to negotiate with the farmers to repay their dues at negotiates price.

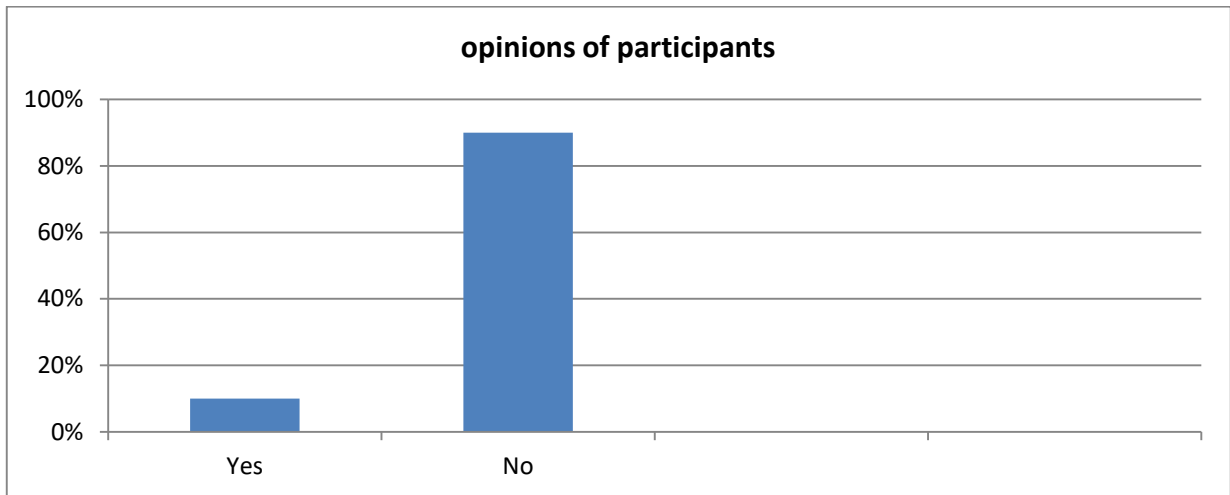
The major reasons for NPA in MSMEs are disruption in the existing technology and unwanted downtrends in the market. The MSMSs are not financially strong to withstand the competition from the domestic renowned enterprises and foreign enterprises.

Government intervention is the need-of-the-hour to protect the interest of MSMEs and to release stimulus package to guard the sector which employs nearly half of the employees in the country. The interest rate and other schemes must be cyclically announced to boost the enthusiasm in the sector and to realize the potential in making cutting edge products and services through which the sector is able to survive the competition.

Questionnaire

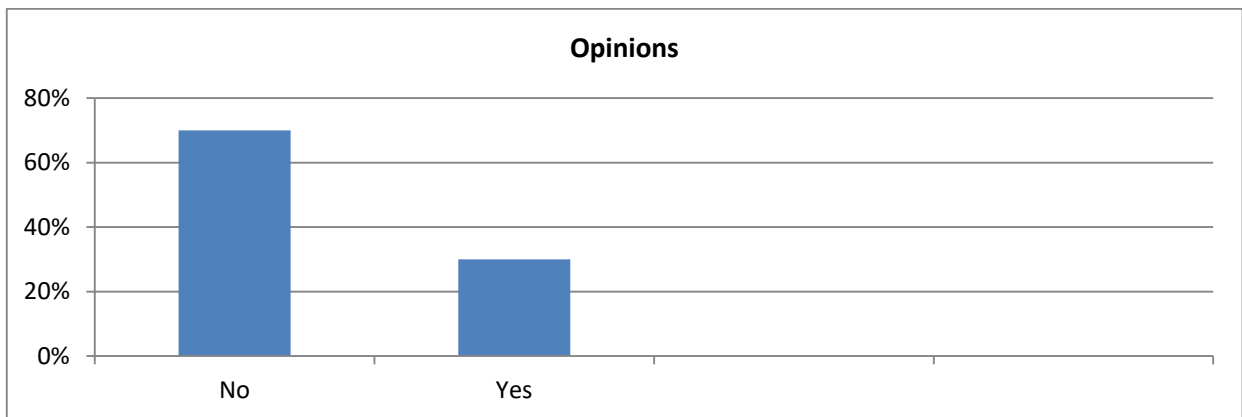
Q1. Does the total cost to a borrower, in terms of interest rates, processing fees, legal charges, supervision charge and follow up etc charges, very high that it might result in NPA?

Answer:

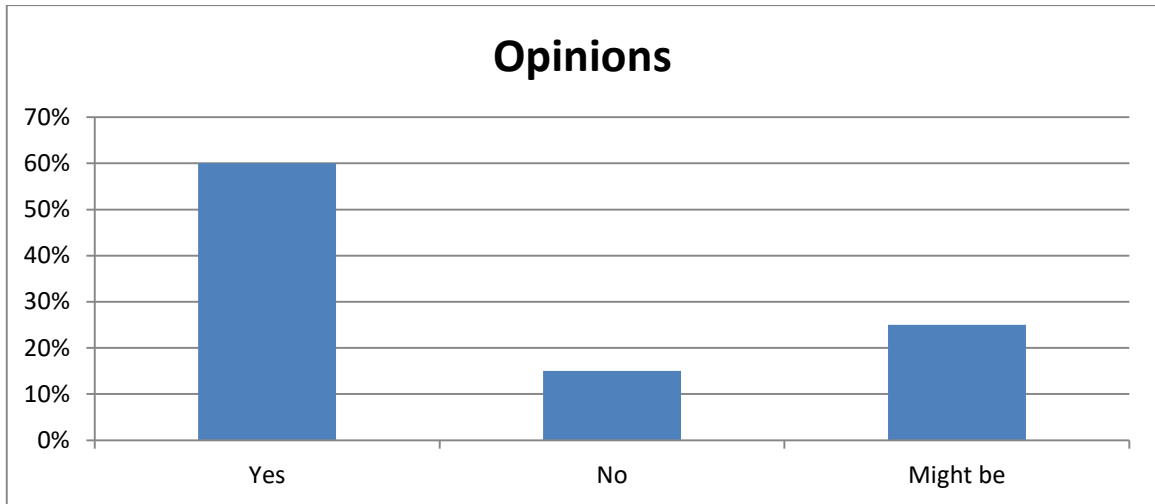


Q.2 does the lack of timely communication regarding repaying loan result in NPA?

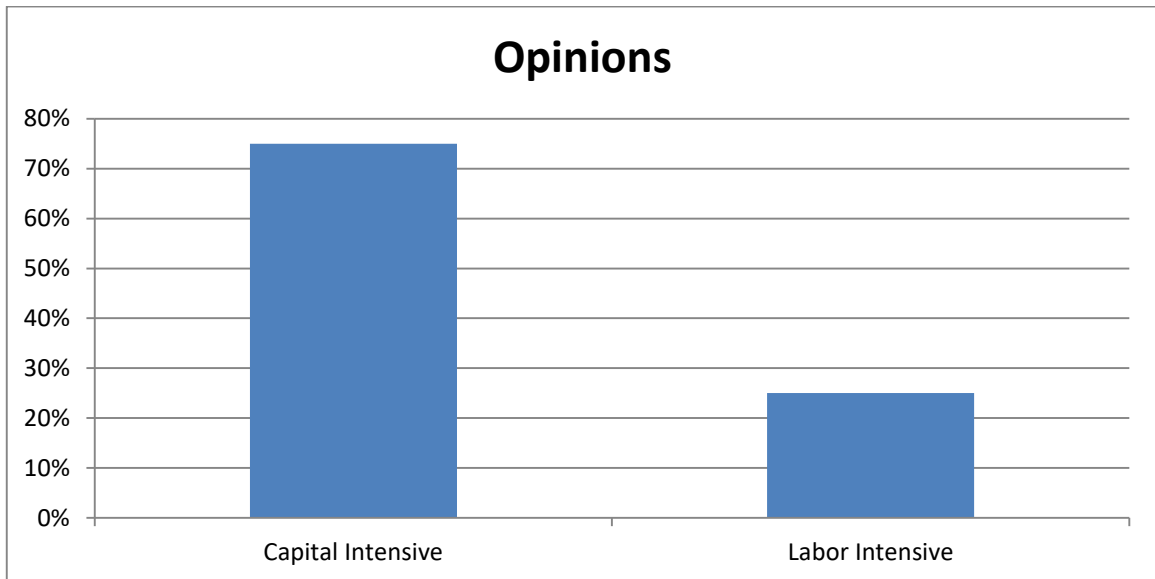
Answer:



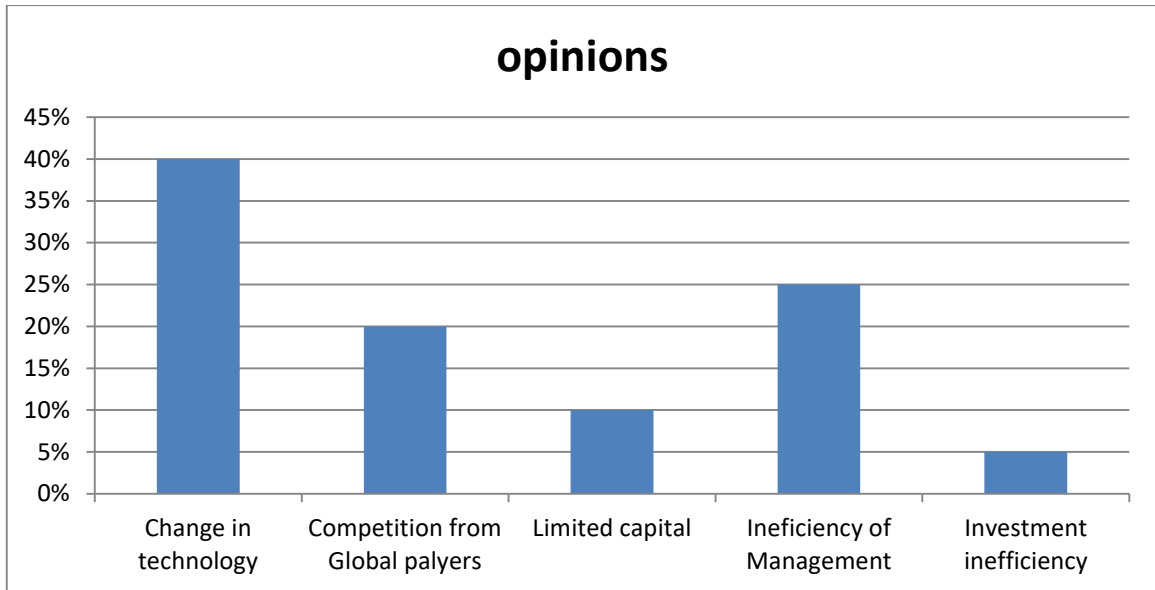
Q.3 does the global competition lead to increase in NPA?



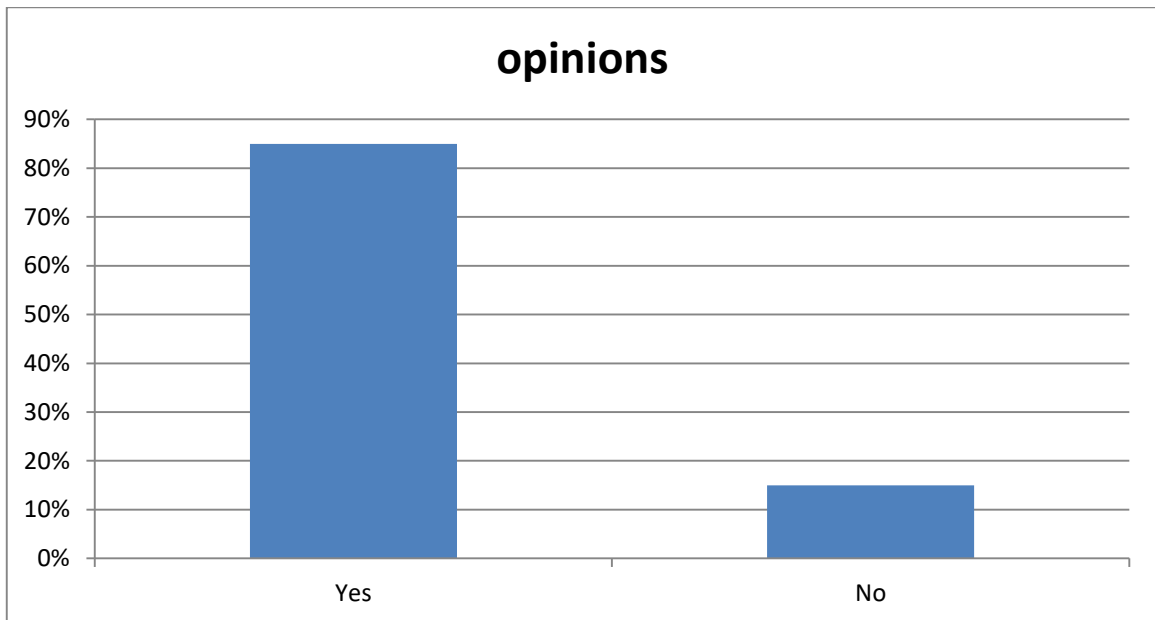
Q.4 which one is the more vulnerable to NPA, capital intensive firms or labor intensive?



Q.5 what are the reasons for high NPA in capital intensive firms?

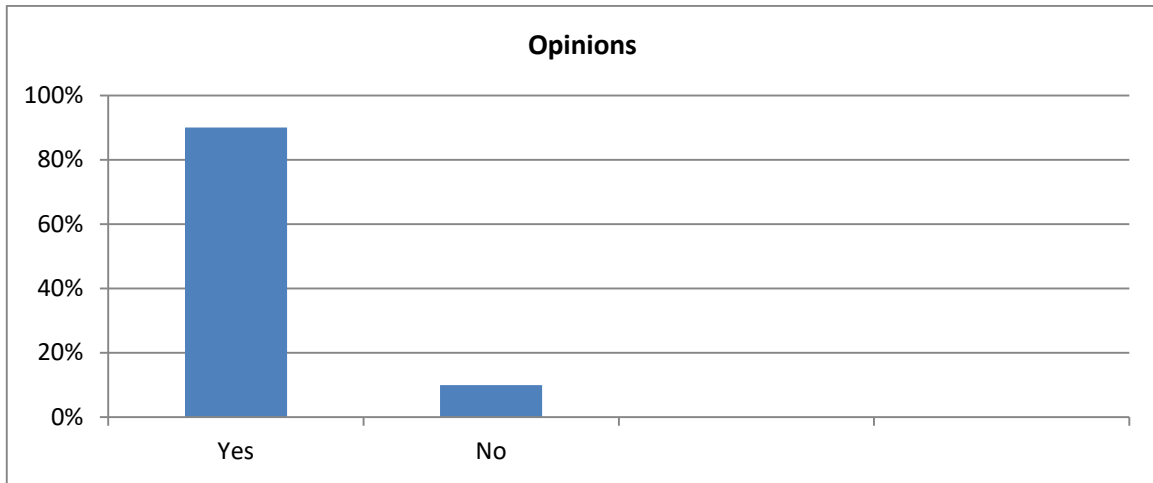


Q.6 does negligence from a bank play a significant role in “Bad Debts”?



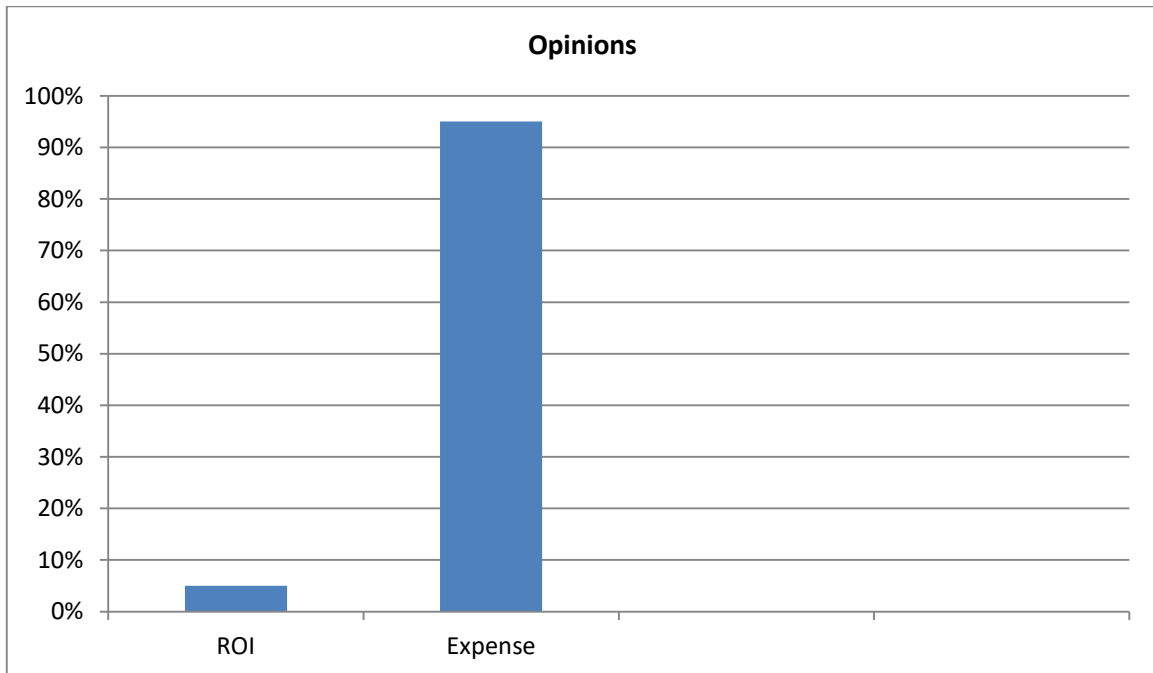
Q.7 is the time span of one year sufficient to meet obligations?

Answer:

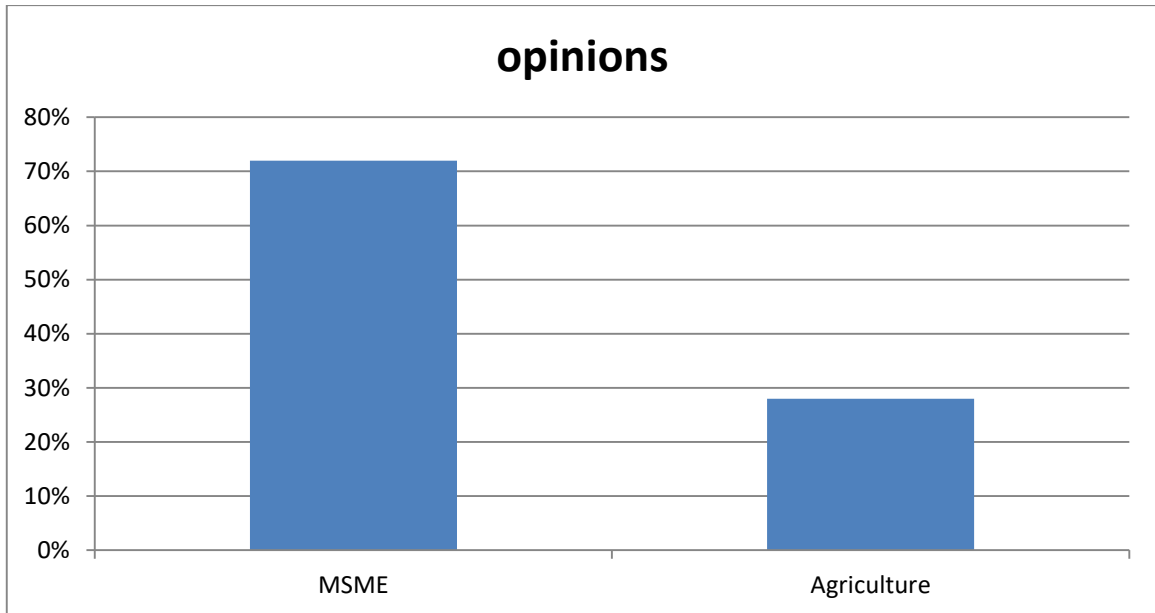


Q.8 is the diversion of fund worthy enough to get good return on investment? Or is it just only expense and not return on investment?

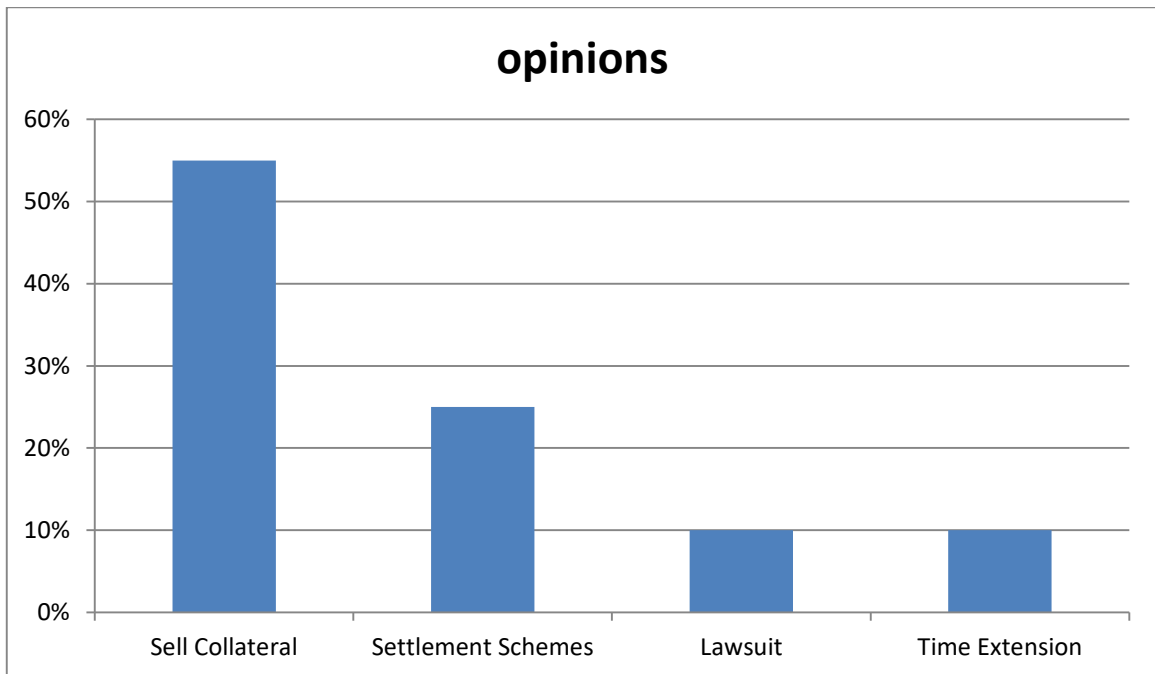
Answer:



Q.9 in which sector, the likelihood of NPA is high, MSME or Agriculture?



Q.10 what steps should banks take to tackle “Bad Debts”?



Conclusions

- Intense competition from large foreign companies making difficult for small and medium companies to thrive in the market.
- Government regulations for capital requirements and recruiting skilled labors at negotiated price are still a challenge for MSMEs.
- Delayed payments, liquidity and inventory issues, loss in business, change in regulation, competitive **factors** and change of business model are some major reasons for NPA in MSMEs.
- In agriculture, according to the data obtained from the participants, the most prevalent reason for high NPA was turned out to be the diversion of fund.
- In case of diversion of fund, the amount was majorly meant for expense rather than investing.
- Competent farmers, who were capable enough to pay back their obligations, did not meet the deadline of their obligations due to political interference and waited for several years for loan waiver which resulted in Advances Under Collection Account (AUCA).
- A periodic awareness camp at bank branches might enlighten farmers about the consequences of NPA accounts and the benefits of paying their obligations on time. It might also be done occasionally at various villages apart from one time settle scheme and Lokadalat.

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