Persistence of Informal Credit in Rural India: Evidence from 'All-India Debt and Investment Survey' and Beyond

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Narayan Chandra Pradhan*

Abstract

Rural credit markets in India is characterised by the coexistence of both formal and informal sources of finance and the market is fragmented. To discuss the informal rural credit issue and to maintain consistency with All India Debt and Investment Survey (AIDIS) data, this paper treats credit supplied by non-institutional agencies as informal while institutional agencies as formal sources of credit. It covers both 'All-India Rural Credit Survey 1951-52' (RBI, 1954) and 'All-India Rural Debt and Investment Survey 1961-62' (RBI, 1965) conducted by the Reserve Bank and four rounds of All-India Debt and Investment Surveys by 'National Sample Survey Organisation' (NSSO) of the Government of India from 1971-72 to 2002-03. In the absence of further survey data, to extend discussion on rural credit scenario including 'Micro Finance Institutions' (MFIs) beyond 2002, the paper has heavily drawn upon four recent official Reports: (i) Report of the Technical Group to Review Legislations on Money Lending (RBI, 2006), (ii) Report of the Task Force on Credit Related Issues of Farmers (GOI, 2010), (iii) 'Malegam Committee Report' (RBI, 2011), and (iv) Micro Finance Institutions (Development and Regulation) Bill, 2012 (introduced in Parliament on May 16, 2012). It is assessed that the share of rural informal credit in total outstanding debt has been certainly decreasing over the period from 1950 to 2002 with various financial inclusion initiatives of the Reserve Bank and legislations of the various state governments to regulate moneylenders. However, about two-fifth of the rural households' dependence on informal credit, even today, indicates further scope for financial inclusion in rural areas. This augurs well for new financial sector initiatives in the form of prompt and innovative policy responses to prioritise financial inclusion, financial education as well as financial literacy.

JEL Classification: E26, G21, G23, O17

Key words: rural credit, informal finance, microfinance, non-banking financial institutions

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I. Introduction

Before the First Plan began in 1951, almost all the financial needs of rural sector *vis-à-vis* agriculture were provided by the moneylenders. At that time, the Reserve Bank was very active in pursuing cooperative movements through a variety of initiatives. Despite all those efforts, the provision of credit through cooperatives and commercial banks were to the extent of about 4 per cent of the total outstanding debt as at end-June 1951. This finding of Report of the *All India Rural Credit survey* (RBI, 1954), AIRCS henceforth, had laid the foundation stone for furthering the role of institutional credit to rural sector through formal channel of cooperatives and commercial banks. The AIRCS[1] stated, *Cooperation has failed, but Cooperation must succeed* and recommended for credit delivery through *institutional* channel (throughout this paper, formal and institutional as well as informal and non-institutional are used interchangeably) in the areas of agriculture marketing, processing, storage and warehousing. The subsequent formation of 'Agricultural Refinance Corporation' in 1963, nationalisation of major commercial banks in 1969 and 1980 in second phase, setting up of Regional Rural Banks in 1975, and formation of National Bank for Agriculture and Rural Development (NABARD) in 1982 - all these efforts by the Reserve Bank were to institutionalise the credit channel for rural sector. In the 1990s and 2000s, the concept of micro-credit along with MFI- and SHG-Bank linkage models have evolved with the institutional support of the Reserve Bank and NABARD in order to help the poor in providing credit without collaterals (for a succinct description of rural credit scenario in recent years, one may refer to: Mohan, 2004; Reddy, 2006; Golait, 2007).

In recent years, the excessive reliance of borrowers on some or other forms of moneylender and informal/semi-formal sources and exorbitant interest rate charged by those entities have captured the attention of policy makers to downsize the informal sector finance. The Technical Group Report to review legislations on money lending (RBI, 2006) by the Reserve Bank had examined, *inter alia*, the functioning of moneylenders, linkages between money lending activities and formal credit channels, international practices in regulating money lending activities, and enforcement machinery for money lending and similar activities in the interest of rural households. The Report of the 'Task Force on Credit Related Issues of Farmers' (GOI, 2010) submitted to the Ministry of Agriculture in June 2010 had looked into the issue of a large number of farmers, who had taken loans from private moneylenders (and not covered under the loan waiver scheme). The report has mentioned: *In recent years, policy interventions have led to doubling of agricultural credit, but the limited access of small and marginal farmers to institutional credit continues to be a*

[1] AIRCS had also recommended for amalgamation of Imperial Banks into the 'State bank of India' as a special institution for rural credit delivery.

matter of concern. What is worrying is that the proportion of such farmers is increasing and they form more than four-fifths of the operational holdings".

The inadequate and untimely credit along with procedural hassles from formal institutions has been added to the problem of credit access by rural farmers. At the same time, micro finance institutions (MFIs) have been criticised for seeking higher interest rate and mostly confined to the states with fairly well-developed banking system and also competing for same target group. The performance of some of the public sector banks in rural and agricultural lending is also inadequate while that of the private and foreign banks is even lower, despite considerable expansion of the scope of priority sector lending (Reddy, 2006). These facts have motivated to a large extent to the enquiry about the persistence of informal sector finance in rural sector. To this end, we have covered the period from 1951 to 2002 on the basis of AIDIS Survey data and up to 2011 on the basis of three related reports (RBI, 2006; GOI, 2010[2]; RBI, 2011[3]). Our discussion on informal credit after 2002 relied on these Reports to draw certain linkages as well as policy implications. The Micro Finance Institutions (Development and Regulation) Bill, 2012 aims at providing a framework for the development and regulation of micro-finance institutions. The Bill has entrusted the Reserve Bank with the power to issue directions to all MFIs.

For purpose of our analysis of the 'informal credit in rural India', we capture the financial flows that occur beyond the scope of India's formal financial system of banks and non-banking financial institutions. The Report of the Task Force (GOI, 2010) was of the view that 'institutional finance' should include the following: (a) banks and other widely held financial institutions, whether they are public or private institutions; (b) state owned financial institutions aimed at financing the less privileged; and (c) user owned institutions such as SHGs and their federations and cooperatives – both Primary Agricultural Credit Societies (PACS), as well as new generation thrift and credit cooperatives registered under more liberal cooperative laws. Added to the above sources of finance are also not-for profit Non-Banking Financial Companies (NBFCs) and not-for-profit Non-Government Organisations (NGOs).

Although, formal and informal sector credit do not have similar lending methodologies (in terms of size, tenure, repayment schedule, collateral requirements, etc.), this study focuses on the trends of formal versus informal credit in rural India to examine the issues of 'access to' and 'demand for' credit, *ceteris paribus*. For this purpose, we capture the changing share of institutional and non-

[2] The Report of the Task Force (Chairman: Shri U. C. Sarangi) submitted to the Government of India has analysed the rural credit scenario based on visits to 45 villages across 17 major States during 2009-10, review of available literature, laws relating to moneylenders - maintaining continuity with data on AIDIS Survey.

[3] The 'Malegam Committee Report' had studied issues and concerns in the microfinance sector in so far as they related to the entities regulated by the Reserve Bank.

institutional credit agencies in the outstanding cash dues of the rural households and treat credit supplied by non-institutional agencies as informal, whereas, institutional agencies as formal sources of credit.

The rest of this paper is organised as follows. In Section II, we have discussed the background of the ‘All India Debt and Investment Survey’, both by the Reserve Bank and National Sample Survey Organization (NSSO) of the Government of India. The discussion on persistence of informal finance in rural areas, both All-India and State-wise along with credit agency-wise on the basis of data from various AIDIS Survey rounds is provided in Section III. Section IV has discussed the informal credit aspects in rural areas from three recent Reports as mentioned above. Section V concludes with major observations.

II. All India Debt and Investment Survey

(a) Surveys by the Reserve Bank

In order to study both the demand and supply sides of credit in the household sector, the Reserve Bank had conducted the ‘All-India Rural Credit Survey’ in 1951-52 and a result of the Survey was published in 1954. Information on assets, economic activities, particulars of credit operations and the incidence of indebtedness in the rural areas were collected to assess the demand for rural credit. Further, data on the extent and mode of operations of different credit agencies were also collected with a view to examine the supply side of the credit. The first Rural Credit Survey was followed up with a similar Survey in 1961-62 by the Reserve Bank. The scope of the survey was extended to include capital expenditure in the household sector and other associated indicators of the rural economy. The second survey was accordingly titled ‘All India Rural Debt and Investment Survey’ and results were published in 1965. Both the surveys by the Reserve Bank were conducted for rural areas only.

(b) Surveys by the NSSO

The National Sample Survey Organisation (NSSO) has been conducting All-India Survey on Debt and Investment, decennially, since its 26th round (1971-72) in both rural and urban areas. These surveys generate basic information on assets, liabilities and capital expenditure in the household sector of the economy. The All-India Debt and Investment Survey (AIDIS), which was carried out as part of the 59th round of the National Sample Survey (NSS) during January to December 2003 (latest in the series), was the sixth such survey conducted at the all-India level. These reports by NSSO gives the estimates of indebted households and the amount of debt classified by various aspects at the State and all-India level in both rural and urban areas. At present, the decennially conducted AIDIS is the only nation-wide enquiry providing data on household assets, indebtedness and capital expenditure.

The main objective of the AIDIS is to generate reliable estimates on assets, liabilities and capital expenditure of the household sector. The survey provides the details of household liabilities required for the formulation of credit policy of financial institutions and planning for development.

According to the AIDIS, the agency from which a loan was taken treated as the credit agency. The credit agencies were either 'institutional agencies' or 'non-institutional agencies'. The various agencies which were treated as 'institutional agencies' were: government, co-operative agencies, commercial banks including regional rural banks, insurance, provident fund, financial Corporation/institution, financial company and 'other institutional agencies'. The agencies which were treated as 'non-institutional agencies' were: landlord, agriculturist money lender, professional money lender, trader, relatives and friends, doctors, lawyers and other professionals, and 'others'. Of all the characteristics in AIDIS, credit agencies and terms and rate of interest of loans have been probed into more deeply than the rest, in view of their historical importance regarding the supply side and cost of loans, respectively.

III. Persistence of Informal Credit in Rural Sector – AIDIS Surveys

(a) All India Rural Credit Survey (1951-52)

Although, India inherited a basic network of credit cooperatives from the colonial era, the Reserve Bank's first decennial AIRCS 1951-52 (RBI, 1954) found that 92.8 per cent of rural households relied on informal financial sector (Table 1). The investigation extended over nearly 1,30,000 families having residents in 600 villages and all types of credit agencies in 75 selected districts. During 1951-52, an increase in debt was recorded in all the 75 districts (in 20 districts the increase in debt was below 50 per cent; in 31 districts the increase varied from 50 to 100 per cent; in 19 districts from 100 to 200 per cent; and in 5 districts the increase exceeded 200 per cent).

The moneylenders' continued dominance in the beginning of Plan period (around 70 per cent of rural credit) despite all measures to control them, suppress or supplant had led to the suggestion that '… *any realistic system of rural credit should seek to incorporate him in itself rather than compete with him or wishfully expect to eliminate him*'(RBI, 1954). Among creditors, the moneylender, and among moneylenders the professional moneylender dominates the rural credit scenario. The dominance itself has been made possible by the ineffectiveness of all attempts to organise a competitive agency for supply of rural credit. The first AIRCS had opined that the co-operatives were 'utter failure' in providing rural credit, but added they had a vital role in agricultural credit. Loans from relatives (virtually interest free) accounted for 14 per cent of the reported borrowings of cultivators. About 6 per cent of the total borrowings of cultivators were from traders and commission agents. The combined contribution of Government and Cooperatives was about 6 per cent of the total rural credit, each accounting for about 3 per cent. As for commercial banks, 1 per cent represented the insignificant part played by them in the direct financing of the cultivator. In 44 out of the 75 districts selected for the Survey, not a single pie was reported as having been borrowed by cultivators from a commercial bank.

Table 1: Break-up of Institutional and Non-Institutional Rural Credit

(Per cent)

	1951	1961	1971	1981	1991	2002
Institutional Agencies	**7.2**	**14.8**	**29.2**	**61.2**	**64.0**	**57.1**
Government	3.3	5.3	6.7	4.0	5.7	2.3
Co-op. Society/bank	3.1	9.1	20.1	28.6	18.6	27.3
Commercial bank incl. RRBs	0.8	0.4	2.2	28.0	29.0	24.5
Insurance	--	--	0.1	0.3	0.5	0.3
Provident Fund	--	--	0.1	0.3	0.9	0.3
Others institutional agencies*	--	--	--	--	9.3	2.4
Non-Institutional Agencies	**92.8**	**85.2**	**70.8**	**38.8**	**36.0**	**42.9**
Landlord	1.5	0.9	8.6	4.0	4.0	1.0
Agricultural Moneylender	24.9	45.9	23.1	8.6	6.3	10.0
Professional Moneylender	44.8	14.9	13.8	8.3	9.4	19.6
Traders and Commission Agents	5.5	7.7	8.7	3.4	7.1	2.6
Relatives and Friends	14.2	6.8	13.8	9.0	6.7	7.1
Others	1.9	8.9	2.8	4.9	2.5	2.6
Total	***100***	***100***	***100***	***100***	***100***	***100***

*: includes financial corporation/institution, financial company and other institutional agencies.

Note: Percentage share of different credit agencies to the outstanding cash dues of the households as on 30th June.

-- denotes not available.

Source: All India Rural Credit Survey (1954); All India Debt and Investment Survey, Various Issues.

AIRCS (RBI, 1954) pointed out that "*agricultural prices during the Survey year witnessed a stagnation followed by a steep decline for the first time in a period over ten years*". However, a large part of the working funds borrowed by subsistence farmers seems to be related to *consumption* rather than production. The problem turned into more complicated one due to the socio-economic structure of the village with its characteristics of caste and inequality. Other factors that might have aided to the trend towards an increase in debt were relatively large incidence of drought, famine and inclement seasonal credit.

As our description built upon statistical data analysis and survey of literature, the brief about significance of informal credit agencies in supplying credit to rural areas during 1950s can be summarised as follows: *Moneylenders* were dominant not only due to their effective adaptation to rural areas, but also the ineffectiveness of any other competitive agency. Traders and Commission Agents were in direct contact with the cultivators and much of this financing was really in the nature of advance payment for purchase of products. The indigenous bankers were financier of trade and also traders themselves as well as finances moneylenders. Commercial banks were more interested in rural areas more for the purpose of getting deposits rather than financing either agriculture or cottage industry.

(b) All India Rural Debt and Investment Survey 1961-62

In this second Survey by Reserve Bank, the outstanding loans owed to agriculturist moneylenders accounted for about 46 per cent of the aggregate outstanding of all rural households, nearly double the share compared to first Survey. The share of outstanding loans owing to professional moneylenders was next highest though their share declined constituting 15 per cent of the aggregate outstanding. As per the Survey findings on all-India basis (Table 1), the share of cooperatives was at 9.1 per cent, 'others' at 8.9 per cent, traders and commission agents at 7.7 per cent, relatives at 6.8 per cent and government at 5.3 per cent in the total outstanding debt. The shares of landlords and commercial banks in the aggregate outstanding were negligible at 0.9 per cent and 0.4 per cent, respectively. This fact signifies the continuance of informal finance in rural India that might have prompted the nationalization of commercial banks in 1969 in the first phase.

The State-wise position in respect of outstanding loan owed to different credit agencies is provided in *Appendix Table 1*. It can be ascertained that the outstanding loans owed to agricultural moneylenders constitute 74 per cent of the aggregate outstanding of the rural households in Bihar, about 64 per cent each in Andhra Pradesh and Madras and about 60 per cent in Mysore. Their share was very low in Jammu & Kashmir (7 per cent) reflects low dependence on agriculture and Gujarat (9.8 per cent) due to higher share of cooperatives (20.3 per cent). On the other hand, the share of cooperatives was below 5 per cent in Bihar (0.9 per cent), Rajasthan (2.0 per cent), and West Bengal (4.1 per cent). For other states, it varied between 7 – 14 per cent. The share of professional moneylenders in the aggregate outstanding was the highest in Orissa (37.3 per cent) followed by Rajasthan (35.3 per cent), Madhya Pradesh (31.0 per cent), and Uttar Pradesh (24.5 per cent). It was very low in Mysore (1.4 per cent), Jammu & Kashmir (5.4 per cent), and Kerala (5.6 per cent) and varied between 6-15 per cent in other states. The share of Government in the aggregate outstanding was about 19 per cent in West Bengal and Maharashtra, 15 per cent in Assam and 12 per cent in Orissa. In all other States, it was 5 per cent or less.

The first three categories of informal lenders – landlords, agricultural moneylenders, and professional moneylenders – are not necessarily distinct from one another depending on the locality. But generally speaking, landlord moneylenders extend credit to tenants; agricultural moneylenders primarily deal with agricultural labourers and small farmers; and professional moneylenders service a wider range of customers and may register themselves as companies, partnerships, and trusts (Ghate, 1992). Those in the fourth official category, 'traders and commission agents' are also known as indigenous bankers. In contrast to professional moneylenders who lend their own money, indigenous bankers broker funds between banks and their clients, who tend to be traders rather than farmers. One of the important reasons for continued dependence on moneylenders is that the formal credit delivery structure has not stretched to the villages despite its penetration (Ghate 1988). The formal credit delivery channels also lack the personal bonds that moneylenders enjoy with the borrowers. Borrowers obtain their loans more promptly from non-institutional sources.

(c) All India Rural Debt and Investment Survey 1971-72 to 2001-02

At the outset, it may be mentioned that the Survey results of 26th round (1971-72), 37th round (1981-82), 48th round (1991-92) and 59th round (2002-03) of AIDIS are comparable across the Agency-wise and State-wise over the period. In order to compare the progress of formal and informal finance after the bank nationalization and to provide an overview of the flow of credit to rural areas in terms of credit agency-wise, we have analyzed these Survey results in a comparative manner and State-wise separately. It is important to note that there are problems in using data from these surveys given the sharp reduction in sample size of households and villages, especially in the 37th round in 1981-82. It may further be mentioned that, the estimates of household debt starting from 48th round in 1991-92 are based on both cash and kind, whereas before that it was based on cash debt.

From Table 1, it can be assessed that the informal/non-institutional finance was gradually declining during the 1960s, was very nearly broken during the 1970s, with the *institutional* agencies making steady inroads into the rural scene. The share of *institutional* credit agencies in the outstanding cash dues of the rural households at the all-India level increased from 29 per cent in 1971 to 61 per cent in 1981 and then the pace of increase was arrested rising to 64 per cent in 1991. During the following decade, the share declined by about 7 percentage points and reached 57 per cent in 2002. It seems that credit cooperatives, commercial banks, and other formal financial sector programs in rural areas have not displaced informal sources of credit, altogether. The 2002 AIDIS survey revealed that 43 per cent of rural households continue to rely on informal finance, which includes professional moneylenders, agricultural moneylenders, traders, relatives and friends, and others.

Institutional agencies (All-India Level)

From Table 1, it can be observed that, the most remarkable performance was that of the commercial banks while the share of co-operative societies in the outstanding cash dues of cultivator households increased from 20.1 per cent in 1971 to 28.6 per cent in 1981, therefore dropping to 27.3 per cent in 2002, that of commercial banks rose to 29 per cent in 1991, after rising sharply to 28 per cent in 1981 from a meager 2 per cent in 1971. It appears that the large number of branches that was set up by various commercial banks in 1970s and the subsequent introduction of rural banking schemes have driven the commercial banks to assume the role of principal credit agency in rural areas. It may be of interest to note that the share of government departments in the outstanding cash dues of cultivator households, after showing a decline from 7 per cent in 1971 to 4 per cent in 1981, again rose to 6 per cent in 1991 and dropped to 2 per cent in 2002. As a whole, at the all India level, among the *institutional* credit agencies, the co-operative societies and the commercial banks were the two most important agencies in the rural sector. These two agencies together, shared 91 per cent of the entire amount of debt advanced by the *institutional* agencies, accounted for 52 per cent of the outstanding cash debt, with *co-operative societies* (27.3 per cent) accounting for a greater share than the *Banks* (24.5 per cent) in 2002.

The gradual increase in the share of formal institutional credit in agriculture witnessed some reversal during 1991-2002 mainly because of a pull back by commercial banks. This disquieting trend is, in part, due to a contraction in rural branch network in the 1990s, and in part due to the general rigidities in procedures and systems of institutional sources of credit (Subbarao, 2012).

Non- Institutional agencies (All-India Level)

The combined share of all the *non*-institutional credit agencies in the outstanding cash dues of cultivator households recorded a sharp decline of 32 percentage points during 1970s but the decline got arrested in the 1980s – the fall being just of about 3 percentage points but increased to 43 per cent subsequently. The decline is found to be the steepest for the credit agency ‘agricultural money lenders’, whose share came down to 6 per cent in 1991 from about 9 per cent in 1981 and 23 per cent in 1971. However, the share of ‘professional money lenders’ has reported a rise to about 9 per cent in 1991, after registering a fall to 8 per cent in 1981 from about 14 per cent in 1971. Subsequently, the share has jumped to about 20 per cent in 2002. Relatives and friends appear to be gradually losing their importance as a source of credit. From 14 per cent in 1971, their share fell to 9 per cent in 1981, and dipped further down to about 7 per cent subsequently. As a whole, among the *non-institutional* agencies, *professional money lenders* were the main source of credit. Among the *non-institutional* credit agencies, money lenders – both *professional* and *agricultural* – in that order were found to be important sources of finance in rural areas, their respective shares being 19.6 per cent and 10.0 per cent. The share of *relatives and friends* was 7 per cent of the cash dues of rural households.

State-level Changes during 1971 to 2002

The State-level estimate indicates that of the total outstanding cash dues, the share of *institutional* agencies had increased marginally during the 1980s in most of the states, after having increased substantially during the 1970s (Table 2). However, the role of the *institutional* agencies, as judged from their share in the outstanding cash dues, varied from state to state. A snapshot of this variation in 2002 shows that in the rural areas, *institutional* credit agencies accounted for 85 per cent in Maharashtra, followed by Kerala (81 per cent), Himachal Pradesh and Orissa (74 per cent each) and Jammu & Kashmir (73 per cent). In contrast, not even 50 per cent of the debt was contracted through the *institutional* credit agencies in the rural areas of Andhra Pradesh (27 per cent), Rajasthan (34 per cent), Bihar (37 per cent) and Tamil Nadu (47 per cent).

Table 2: Share of Institutional and Non-Institutional Agencies in Outstanding Cash Debt of Major States in Rural Areas

(Per cent)

Major States	Institutional				Non-Institutional			
	1971 (26th)	1981 (37th)	1991 (48th)	2002 (59th)	1971 (26th)	1981 (37th)	1991 (48th)	2002 (59th)
Andhra Pradesh	14	41	34	27	86	59	66	73
Assam	35	31	66	58	65	69	34	42
Bihar	11	47	73	37	89	53	27	63
Gujarat	47	70	75	67	53	30	25	33
Haryana	26	76	73	50	74	24	27	50
Himachal Pradesh	24	75	62	74	76	25	38	26
Jammu & Kashmir	20	44	76	73	80	56	24	27
Karnataka	30	78	78	67	70	22	22	33
Kerala	44	79	92	81	56	21	8	19
Madhya Pradesh	32	66	73	59	68	34	27	41
Maharashtra	67	86	82	85	33	14	18	15
Orissa	30	81	80	74	70	19	20	26
Punjab	36	74	79	56	64	26	21	44
Rajasthan	9	41	40	34	91	59	60	66
Tamil Nadu	22	44	58	47	78	56	42	53
Uttar Pradesh	23	55	69	56	77	45	31	44
West Bengal	31	66	82	68	69	34	18	32
All India	**29**	**61**	**64**	**57**	**71**	**39**	**36**	**43**

Source: All India Debt and Investment Survey, NSS 59th Round, Report No. 501.

During the periods 1971 to 2002, the states do not reveal any uniform pattern in the share of *institutional* agencies in total debt. Compared to 1991, the picture had changed in some of the major states (Table 2). Of the 20 major states in the rural, as many as 15 have shown a fall in the share of *institutional* agencies, notable among them are Bihar, Punjab, Haryana and West Bengal, where the fall in percentage share from 1991 values had been to the tune of 36, 23, 23 and 14 percentage points, respectively. On the other hand, 13 major states out of 21 had registered a rise in the share, which, barring a few with marginal to moderate rise, can be described as sharp to spectacular (The detailed State-wise and Agency-wise position is provided in Appendix Tables 2-5).

IV. Recent Reports on 'Informal Credit Related Issues'

In the absence of survey data beyond AIDIS 2002 (published in December 2005), we have heavily drawn upon three recent Reports (RBI, 2006; GOI, 2010; RBI, 2011) that were also based on the sample surveys and extended the AIDIS data. The Report of the Task Force on 'Credit Related Issues of Farmers' (Chairman: Shri U. C. Sarangi), submitted to the Ministry of Agriculture, Government of India, looked into the issue of a large number of farmers who had taken loans from private moneylenders, but not covered under the 'Agricultural Debt Waiver and Debt Relief Scheme' of 2008. The Task Force Report has observed that "…*more disquieting feature of the trend was the increase in the share of moneylenders in the total debt of cultivators. There was an inverse relationship between land-size and the share of debt from informal sources. Moreover, a considerable proportion of the debt from informal sources was incurred at a fairly high rate of interest*". About 36 per cent of the debt of farmers from informal sources had interest ranging from 20 to 25 per cent. Another 38 per cent of loans had been borrowed at an even higher rate of 30 per cent and above, indicating the excessive interest burden of such debt on small and marginal farmers. The continued dependence of small and marginal farmers on informal sources of credit such as private moneylenders was attributed to constraint in the rural banking network and services arising out of financial sector reforms. Rigid procedures and systems of formal sources preventing easy access by small and marginal farmers, vied with the easy and more flexible methods of lending adopted by informal sources. The Task Force members came across situations where farmers were borrowing at the rate of five to ten per cent per month.

The identification of farmers indebted to private moneylenders is difficult. Such loans in most cases have no formal records and identifying and authenticating the debt from moneylenders may lead to problems of moral hazard (GOI, 2010). According to the Report, credit needs of small and marginal farmers are not only growing but are getting diversified due to increasing commercialization and modernization of agriculture. Simultaneously, for a variety of other needs, farmers incur considerable expenditure, resulting in increased borrowings. Adequacy, timeliness, affordability and convenience are factors that influence farmers, and for that matter, all borrowers, in their choice of creditors. Given that a single source may not to be able to satisfy all their credit needs, many farmers approach both formal and informal sources. Invariably, those who cannot afford any collateral are forced to borrow from informal sources. The Task Force reviewed the debt swap schemes of banks and revealed that these schemes had limited success as farmers were reluctant to disclose the name of the money-lenders, apprehensive in disclosing debt and some had even repaid the existing debt out of their Kisan Credit Card limits. Even though the Task Force came across some good debt swap schemes, bankers reported difficulty in taking these to scale and also reported that there was little guarantee that farmers would not ever again borrow from moneylenders.

Based on a review of the existing laws on money lending in the country, the 'Technical Group to Review Legislation on Money Lending' (RBI, 2006) has observed: "…*in spite of there being a legislation, a large number of moneylenders continue to operate without license, and even the registered moneylenders charge interest rates much higher than permitted by the legislation, apart from not complying with other provisions of the legislation. Signs of effective enforcement are absent*". The Report recommended legislative reforms to streamline the activities of moneylenders through suitable mechanism of incentives and disincentives. In this regard, Jeromi (2007) attempted to analyse the working of moneylenders in Kerala based on a sample survey, and mentioned that the existing legal provisions and regulatory and supervisory mechanisms are inadequate to protect the interests of both depositors and creditors in rural Kerala.

The growing commercialisation of Indian agriculture has encouraged the rise of trader-moneylender, as the formal sector finance is inadequate to meet the growing credit requirements of agriculture. The Task Force (GOI, 2010) noted that the moneylender today comes in many forms – as an outright lender, as a supplier of inputs/consumer goods, as a for-profit non-banking finance companies (NBFCs) including the for-profit MFIs, as a buyer of produce, and as an owner of the land on which the farmer is dependent. The sheer numbers of moneylenders, easy access to them, and their intricate relationships with the borrowers coupled with limited access to formal institutions made it difficult for borrowers to complain against them.

Micro Finance Scenario

Microfinance sector in India has progressed remarkably since 1990s and this sector has been acting as an important ally in expanding *financial inclusion* in rural areas (NABARD, 2012). Reserve Bank provides guidelines to banks for mainstreaming micro-credit providers, *inter alia*, stipulated that micro-credit extended by banks to individual borrowers directly or through any intermediary would be reckoned as part of their priority sector lending. However, no particular model was prescribed for micro-finance and banks have been extended freedom to formulate their own models or choose any conduit/intermediary for extending micro-credit. Though, there are different models for microfinance provision, the self-help-group (SHG)-Bank Linkage Programme has emerged as the major microfinance program in the country. It is being implemented by commercial banks, regional rural banks (RRBs) and cooperative banks. The gathering momentum in the microfinance sector has brought into focus the issue of regulating the sector.

The Malegam Committee Report (RBI, 2011) was constituted to study issues and concerns in the MFI sector in the wake of Andhra Pradesh micro finance crisis in 2010. The Committee, *inter alia*, recommended (i) creation of a separate category of NBFC-MFIs; (ii) a margin cap and an interest rate cap on individual loans; (iii) transparency in interest charges; (iv) lending by not more than two MFIs to individual borrowers; (v) creation of one or more credit information bureaus; (vi) establishment of a proper system of grievance redressal procedure by MFIs; (vii) creation of one or more "social capital funds"; and (viii) continuation of categorisation of bank loans to MFIs, complying with the regulation laid down for NBFC-MFIs, under the priority sector. The recommendations of the Committee were discussed with all stakeholders, including the Government of India, select State Governments, major NBFCs working as MFIs, industry associations of MFIs working in the country, other smaller MFIs, and major banks. The Reserve Bank has accepted the broad framework of regulations recommended by the Committee Report.

The The Micro Finance Institutions (Development and Regulation) Bill, 2012 envisages that the Reserve Bank would be the overall regulator of the MFI sector, regardless of legal structure. The Reserve Bank has provided the views on the Bill to the Government of India. The aims of the Bill are to regulate the sector in the customers' interest and to avoid a multitude of microfinance legislation in different states. The proper balancing of the resources at the Reserve Bank to supervise these additional sets of institutions besides the existing regulated institutions could be an important issue. Requiring all MFIs to register is a critical and necessary step towards effective regulation. The proposal for appointment of an Ombudsman will boost the banking industry's own efforts to handle grievances better. Compulsory registration of the MFIs would bring the erstwhile money-lenders into the fold of organised financial services in the hinterland who had been acting as MFIs hitherto.

V. Concluding Observations

The key findings from the above analysis is that informal credit has certainly declined as a percentage of total debt, and both professional and agricultural moneylenders have reduced their share over time. Informal/non-institutional finance was gradually declining during the 1960s and was nearly broken during the 1970s with the institutional agencies venturing into the rural areas with nationalization of major commercial banks and setting up of regional rural banks with initiatives of the Reserve Bank. The decline in the share of moneylenders reflects in part the Government's efforts to register and regulate professional moneylenders.

At the all India level, among the institutional credit agencies, the co-operative societies and the commercial banks were the two most important agencies in the rural sector. These two agencies together shared 91 per cent of the entire amount of debt advanced by the institutional agencies, accounted for 52 per cent of the outstanding cash debt, with co-operative societies (27.3 per cent) accounting for a greater share than the Banks (24.5 per cent). Of the 20 major states in 2002, as many as 15 have shown a fall in the share of *institutional* agencies, notable among them are Bihar, Punjab, Haryana and West Bengal. The above facts indicate that the cooperatives, commercial banks, and other formal financial sector programs in rural areas have not displaced informal sources of credit altogether as 43 per cent of rural households continue to rely on informal finance in 2002.

The most important reason for continuation of informal rural credit market is that the existing financial institutions tend to restrict their lending activities to more risky field of lending to the agricultural sector. Those in the rural credit market prefer to use informal sources of credit despite the fact that the interest rates are much higher. Informal sources do not insist on punctual repayment as banks or cooperative societies do. Usually, it is possible to obtain loans for such purposes as marriage and litigation only from informal sources. There are generally no intricate and complicated rules governing the granting of loans by the village moneylenders. And informal sources are willing to lend money more freely without collateral and on the borrower's mere promise to repay.

As reported in Malegam Committee Report, the impact of microfinance on the lives of the poor is inconclusive. The micro surveys create fears that in some cases microfinance has created credit dependency and cyclical debt. The analysts expressed doubt as to whether lending agencies have in all cases remained committed to the goal of fighting poverty or whether they are solely motivated by financial gain. This augurs well for the regulation of microfinance as a tool of financial inclusion and greater well being of the society.

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Appendix Table 1: Outstanding Cash Debt of Major States as on June 30, 1962 – Credit Agency Wise (AIDIS 1961-62) (Per cent)									
States	**Government**	**Cooperatives**	**Commercial Banks**	**Landlords**	**Agricultural Moneylenders**	**Professional Moneylenders**	**Traders and Commission Agents**	**Relatives**	**Others**
1. Andhra Pradesh	1.6	7.3	0.6	0.3	64.0	9.9	10.7	2.0	3.6
2. Assam	15.5	8.3	--	0.3	35.5	14.6	6.4	11.9	7.6
3. Bihar	4.2	0.9	--	0.1	74.0	12.1	2.8	3.5	2.3
4. Gujarat	3.3	20.3	0.1	0.1	9.8	8.1	16.0	19.2	23.2
5. Jammu & Kashmir	0.3	9.2	0.2	2.1	7.0	5.4	23.1	19.5	33.2
6. Kerala	4.5	9.1	4.0	3.1	16.2	5.6	5.2	14.7	37.8
7. Madhya Pradesh	4.2	11.4	0.1	0.3	37.7	31.0	9.7	3.0	2.7
8. Madras	2.8	9.3	1.4	0.2	63.7	6.7	6.1	3.0	6.7
9. Maharashtra	18.8	27.5	0.1	0.8	17.6	8.7	3.5	12.4	10.6
10. Mysore	4.1	11.4	0.6	1.1	59.8	1.4	7.0	5.8	8.8
11. Orissa	12.0	14.4	--	1.0	22.4	37.3	3.8	2.8	6.5
12. Punjab	3.6	7.1	--	6.7	48.6	12.8	2.9	10.5	7.8
13. Rajasthan	2.5	2.0	--	0.2	29.2	35.3	15.0	4.7	11.1
14. Uttar Pradesh	3.0	7.8	0.2	0.1	42.5	24.5	5.2	8.0	8.8
15. West Bengal	19.2	4.1	0.1	1.0	31.8	7.4	7.0	12.6	16.9
All India	**5.3**	**9.1**	**0.4**	**0.9**	**45.9**	**14.9**	**7.7**	**6.8**	**8.9**
Source: All India Debt and Investment Survey, 1961-62 (RBI, 1965).									

Appendix Table 2: Outstanding Cash Debt of Major States as on June 30, 1972 – Credit Agency Wise (AIDIS 1971-72) (Per cent)							
States	**Government**	**Cooperatives**	**Commercial Banks**	**Money Lenders (Agr. & Prof.)**	**Landlords & Traders**	**Relatives & Friends**	**Others**
1. Andhra Pradesh	2.2	9.4	1.9	46.8	23.3	12.6	3.9
2. Assam	23.5	10.6	0.0	19.7	11.6	27.0	7.6
3. Bihar	5.9	4.4	0.4	55.7	19.1	12.6	1.9
4. Gujarat	6.0	37.8	3.0	11.9	21.0	18.1	2.2
5. Jammu & Kashmir	12.7	7.8	0.0	11.5	34.6	32.4	1.0
6. Karnataka	8.4	15.9	5.3	38.8	20.0	9.6	1.9
7. Kerala	4.7	25.3	13.2	16.1	7.6	23.0	9.8
8. Madhya Pradesh	4.0	26.0	1.1	45.8	15.5	5.7	1.9
9. Maharashtra	11.7	54.3	1.3	9.7	8.9	12.6	1.5
10. Orissa	8.9	20.1	0.7	39.1	11.9	13.0	6.3
11. Punjab & Haryana	5.2	24.0	3.1	27.1	24.4	13.7	2.5
12. Rajasthan	3.9	5.0	0.5	49.6	23.6	12.3	5.1
13. Tamil Nadu	5.7	14.6	1.6	44.5	15.9	14.4	3.3
14. Uttar Pradesh	8.4	13.2	1.3	50.3	11.1	12.8	2.9
15. West Bengal	14.7	13.8	1.2	28.1	14.0	25.2	3.2
All India	**6.7**	**20.1**	**2.2**	**36.9**	**17.3**	**13.8**	**3.0**
Source: All India Debt and Investment Survey, 1971-72 (RBI, 1977).							

Appendix Table 3: Outstanding Cash Debt of Major States as on June 30, 1982 – Credit Agency Wise (AIDIS 1981-82) (Per cent)											
States	**Government**	**Cooperatives**	**Commercial Banks**	**Insurance**	**Provident Fund**	**Landlords**	**Agriculturist moneylenders**	**Professional moneylender**	**Traders**	**Relatives**	**Other Sources**
1. Andhra Pradesh	2.2	20.0	18.3	0.1	0.0	10.9	14.6	9.7	4.8	7.6	10.5
2. Assam	2.0	6.0	16.0	0.0	6.0	--	2.0	4.0	2.0	34.0	28.0
3. Bihar	9.3	8.3	29.4	0.0	0.0	11.3	18.6	4.9	1.5	11.3	4.4
4. Gujarat	1.9	53.8	14.3	0.0	0.0	2.7	1.1	1.7	6.5	16.4	0.4
5. Haryana	6.2	22.7	46.6	0.3	0.0	2.2	5.2	8.9	0.6	6.3	1.0
6. Himachal Pradesh	6.8	41.6	25.8	0.0	0.0	0.6	4.2	4.2	1.1	13.9	1.4
7. Jammu & Kashmir	4.8	7.6	31.2	0.0	0.0	--	1.2	0.4	27.6	12.8	3.6
8. Kerala	2.4	26.5	48.8	0.4	0.0	2.2	6.1	3.4	0.9	7.3	1.0
9. Madhya Pradesh	5.8	34.0	37.1	0.4	1.4	0.1	0.1	3.6	1.4	11.8	4.1
10. Maharashtra	2.1	32.7	31.2	0.0	0.0	2.5	6.2	15.7	4.6	4.2	0.8
11. Mysore	3.9	54.8	26.8	0.9	0.1	0.8	1.3	1.3	0.7	7.3	2.0
12. Orissa	7.7	46.7	27.5	0.0	0.0	0.9	1.2	1.2	3.5	2.0	4.6
13. Punjab	7.5	21.4	43.8	1.0	0.4	2.8	4.8	4.8	5.0	5.7	2.4
14. Rajasthan	0.6	16.3	23.6	0.3	0.0	4.9	9.5	9.5	4.9	12.3	10.3
15. Tamil Nadu	2.6	27.8	12.9	0.5	0.6	4.7	15.1	15.1	4.2	9.7	8.7
16. Uttar Pradesh	4.9	21.0	29.0	0.0	0.0	2.5	14.3	14.3	2.8	9.2	3.1
17. West Bengal	7.1	23.6	32.4	0.3	2.4	1.0	4.8	4.8	5.4	14.8	3.0
All India	**4.0**	**28.6**	**28.0**	**0.3**	**0.3**	**4.0**	**8.6**	**8.3**	**3.4**	**9.0**	**4.9**
Source: All India Debt and Investment Survey, 1981-82 (RBI, 1987).											

Appendix Table 4: Outstanding Cash Debt of Major States as on June 30, 1992 – Credit Agency Wise (AIDIS 1991-92)

(Per cent)

State	Government	Cooperatives	Com. Banks	Landlords	Agr. & Prof. Moneylenders	Traders & Com. Agents	Relatives	Others
1. Andhra Pradesh	2.6	12.4	15.4	15.4	36.0	8.6	1.3	8.3
2. Assam	5.6	15.5	9.1	0.0	25.8	35.9	4.8	3.3
3. Bihar	6.9	20.1	36.9	1.8	16.2	3.9	5.4	8.8
4. Gujrat	5.8	41.4	35.6	0.0	0.2	9.1	6.9	1.0
5. Haryana	2.4	23.0	43.5	7.8	12.6	4.1	2.1	4.5
6. Himachal Pradesh	3.9	21.7	32.9	0.4	4.1	30.7	1.6	4.7
7. Jammu & Kashmir	4.9	9.1	43.0	2.0	2.2	3.1	17.0	18.7
8. Karnataka	5.0	22.1	42.7	3.3	10.1	4.0	2.7	10.1
9. Kerala	22.7	45.6	19.1	0.0	2.8	1.6	4.0	4.2
10. Madhya Pradesh	3.6	21.2	44.5	2.1	22.1	2.1	8.0	3.6
11. Maharashtra	5.1	45.4	27.2	0.8	6.7	1.1	9.5	4.2
12. Manipur	9.2	13.1	0.4	0.0	2.3	42.0	31.4	1.6
13. Meghalaya	67.4	23.2	0.0	0.0	0.0	0.0	9.4	0.0
14. Nagaland	21.0	7.3	27.0	0.0	3.3	0.0	40.3	1.1
15. Orissa	7.1	21.5	44.2	0.3	12.6	1.6	3.6	9.1
16. Punjab	2.5	20.1	55.3	2.0	3.7	6.9	7.9	1.6
17. Rajasthan	3.9	6.6	25.4	3.1	37.3	14.2	0.5	9.0
18. Sikkim	25.7	12.2	50.7	0.0	4.2	4.0	1.2	2.0
19. Tamilnadu	3.3	17.5	32.5	4.2	22.1	9.1	6.3	5.0
20. Tripura	26.5	12.8	49.9	0.0	1.9	2.6	6.1	0.2
21. Uttar Pradesh	7.2	14.2	44.8	1.6	15.7	4.3	9.2	3.0
22. West Bengal	11.8	20.1	41.5	0.1	5.9	3.5	8.6	8.5
All India	**5.7**	**18.6**	**29.0**	**4.0**	**15.7**	**7.1**	**6.7**	**2.5**

Source: All India Debt and Investment Survey, 1991-92.

Appendix Table 5: Outstanding Cash Debt of Major States as on June 30, 2002 – Credit Agency Wise (AIDIS 2001-02)

(Per cent)

States	Government	Coop. Society/ Bank	Commercial Bank	Insurance	Provident Fund	Financial Instn.	Financial Company	Other Institutional Ag.	Landlord	Agriculturist money lender	Professional moneylender	Traders	Relatives and friends	Others
Andhra Pradesh	0.7	11.7	13.3	0.4	0.0	0.0	0.8	0.4	3.3	27.7	29.7	5.0	1.5	5.6
Assam	15.4	5.2	23.0	0.1	7.3	2.2	0.8	3.9	0.2	2.4	23.8	1.4	12.4	1.9
Bihar	2.3	6.2	27.0	0.2	0.0	0.1	0.1	0.6	1.1	18.7	27.8	1.4	7.4	7.1
Chattisgarh	2.5	23.9	56.5	0.1	1.1	0.0	0.9	0.2	1.2	1.4	6.6	1.2	3.5	0.7
Gujarat	2.9	40.1	22.4	0.0	0.1	1.2	0.2	0.5	0.0	0.3	8.0	3.9	20.5	0.0
Haryana	0.4	22.7	25.7	0.0	0.0	1.0	0.0	0.0	1.3	15.0	26.5	1.4	3.0	2.9
Himachal Pradesh	4.5	25.1	40.3	0.0	0.7	0.2	2.3	0.5	0.2	0.2	3.0	0.5	17.6	4.8
Jammu & Kashmir	0.7	11.0	60.9	0.0	0.0	0.0	0.0	0.0	0.0	0.8	0.0	0.0	26.5	0.0
Jharkhand	10.5	9.5	46.9	0.0	3.3	0.0	0.1	0.3	0.7	3.5	13.6	0.7	10.7	0.2
Karnataka	1.2	35.3	28.9	0.1	0.0	0.8	0.0	0.3	1.8	9.5	14.0	2.0	5.0	1.0
Kerala	4.8	46.2	23.0	0.5	0.1	5.2	0.2	1.3	0.0	0.1	7.8	0.1	9.1	1.6
Madhya Pradesh	0.9	33.6	23.8	0.1	0.0	0.0	0.1	0.1	0.3	9.8	21.1	3.3	1.8	5.1
Maharashtra	1.0	60.3	20.9	0.8	0.3	0.7	0.3	0.5	0.1	2.4	4.0	0.3	6.6	1.8
Orissa	1.4	29.3	31.8	0.0	1.6	9.5	0.0	0.4	0.1	4.4	18.2	0.1	2.4	0.7
Punjab	1.1	19.0	28.6	0.1	0.0	1.2	6.3	0.2	2.6	16.5	7.8	1.5	13.9	1.4
Rajasthan	0.6	11.8	21.0	0.0	0.0	0.1	0.2	0.0	0.5	16.8	32.1	10.6	4.5	1.7
Tamil Nadu	2.8	23.8	17.2	0.9	0.6	0.1	0.4	0.9	0.6	4.2	42.2	0.6	4.3	1.4
Uttaranchal	1.4	12.2	44.9	0.0	0.0	0.1	0.0	0.0	0.0	1.9	12.8	0.1	25.3	1.3
Uttar Pradesh	2.5	11.7	38.6	0.0	0.1	0.1	0.1	2.8	0.5	9.3	20.2	1.5	9.9	2.7
West Bengal	11.9	14.0	35.6	0.2	2.0	2.7	0.3	0.8	0.4	2.1	10.8	2.9	14.2	2.1
All India	**2.3**	**27.3**	**24.5**	**0.3**	**0.3**	**1.1**	**0.6**	**0.7**	**1.0**	**10.0**	**19.6**	**2.6**	**7.1**	**2.6**

Source: All India Debt and Investment Survey, 2001-02.