



## AGRICULTURE LOANS - ECONOMY

**NEWS:** Why some banks are under the RBI's lens for demanding gold surety for small-value farm credit

### WHAT'S IN THE NEWS?

#### RBI's Stance on Regulatory Compliance

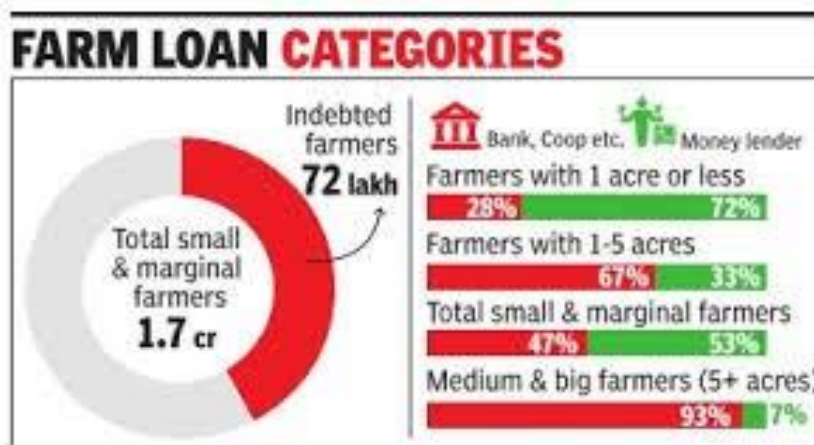
- **Expectation of Compliance:** The Reserve Bank of India (RBI) expects regulated entities, especially banks, to follow regulations strictly.
- **Consequences of Non-Compliance:** Banks pushing regulatory boundaries often face scrutiny and potential corrective actions from the RBI.

#### Recent Inspection Findings on Priority Sector Lending (PSL)

- **Inspection Focus:** The RBI recently conducted an annual inspection focusing on the Priority Sector Lending (PSL) portfolios of banks, especially old-generation private sector banks.
- **Issue Identified:** Inspectors noted irregularities in the classification of small agriculture loans (up to ₹1.6 lakh) under PSL, raising questions over their compliance with regulatory norms.

#### PSL Classification and Collateral-Free Loan Requirement

- **Collateral-Free Mandate:** Agriculture loans up to ₹1.6 lakh are mandated to be collateral-free as per RBI rules.
- **Violation Detected:** Certain banks were found to be taking gold as collateral for small loans to small and marginal farmers (SMFs), which disqualifies these loans from PSL classification.



#### Potential Impact on Banks

- **Reclassification Risk:** If these loans lose their PSL classification, affected banks would have to make alternative arrangements to meet PSL targets.
- **Options for Shortfall:** Banks may need to purchase PSL certificates or invest in low-interest instruments like NABARD's Rural Infrastructure Fund to compensate for PSL shortfalls.



## Overview of Priority Sector Lending (PSL) Requirements

- **Mandated Lending:** PSL aims to direct bank credit to sectors deemed essential, including agriculture, MSMEs, exports, education, housing, and renewable energy.
- **Lending Targets:** Domestic scheduled commercial banks are required to allocate 40% of their Adjusted Net Bank Credit (ANBC) or Credit Equivalent of Off-Balance Sheet Exposure (CEOBE) to PSL.

## Focus on Small and Marginal Farmers (SMFs) in PSL

- **SMF Sub-Target:** SMFs, comprising over 80% of India's farming households, are prioritized in PSL, with a 10% lending target out of the 18% overall agriculture target.
- **Definition of SMFs:**
  - **Small Farmers:** Landholding between 1-2 hectares.
  - **Marginal Farmers:** Landholding up to 1 hectare.
  - **Includes:** Landless agricultural laborers, tenant farmers, oral lessees, and sharecroppers.

## Increase in Collateral-Free Loan Limit

- **Revised Limit (2019):** The RBI raised the collateral-free agriculture loan limit from ₹1 lakh to ₹1.6 lakh in response to rising agricultural input costs and inflation.
- **Scale of Finance Example:** For Rabi onion crops in Maharashtra, a small farmer with 1.5 hectares could secure a collateral-free loan ranging between ₹94,249.5 to ₹1,42,734, based on local scale of finance assessments.

## Differences in Agricultural Lending Between Private and Public Banks

- **Private Sector Challenges:** Private sector banks often lack the expertise of public sector banks in extending collateral-free loans to SMFs and prefer using collateral like gold for added security.
- **Regulatory Stipulation:** While collateral (e.g., gold) is permissible for agricultural loans above ₹1.6 lakh, it cannot be used for loans below this threshold as per RBI rules.

## RBI's Enforcement Process

- **Steps for Addressing Non-Compliance:**
  - **Initial Action:** RBI first requests the banks to take corrective steps upon detecting regulatory violations.
  - **Escalated Measures:** If banks fail to comply, they face penalties or business restrictions until corrective actions are taken.
- **Message to Banks:** RBI stresses that even minor PSL classification rules, such as for collateral-free small agriculture loans, must be adhered to in both letter and spirit.



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## RBI's Vigilance and Accountability

- **Regulator's Commitment:** The RBI continues to monitor banks closely, emphasizing strict compliance with its guidelines to ensure fair and effective lending practices across the banking sector.
- **Unwavering Oversight:** RBI's inspection underscores its attention to detail, reinforcing that no regulatory deviation will go unnoticed.

**Source:** <https://www.thehindubusinessline.com/specials/current-account/mislabelled-agri-loans-face-culling/article68852869.ece#:~:text=Why%20some%20banks%20are%20under,for%20small%2Dva,lue%20farm%20credit&text=The%20Reserve%20Bank%20of%20India,tend%20to%20get%20into%20trouble.>

