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Editors

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Small Farmer: Credit Constraints—A Paradigm

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THE small farmer and agricultural labourers have very limited investment opportunities in rainfed regions. Any analysis aiming to explore the interaction of this class of farmers with various developmental efforts, must begin with the understanding of the initial resources management of small farmers. His capacity to manoeuvre the terms of exchange *vis-a-vis* various institutional agencies and informal sources offering credit, input and advice is highly limited by various factors forming an integral part of his internal cash flows. A paradigm presenting this aspect of small farmers' conditions has been given here (Fig. 1).

The capacity of a small farmer regarding converting available possible inputs with given advice into a profitable output depends on: (a) the sources of financial and material inputs; (b) the delivery mechanism of these sources; (c) the decision making options *vis-a-vis* allocation of resources in the given farm situation; (d) the sustenance of these investments; (e) the surplus produce left after providing for consumption, and its marketing (including transportation and price effects); and (f) repayment or re-cycling of the fund flow. If the economy of the farmer is in deficit the stages get modified depending upon the nature, extent and timing of deficit.

The small farmer due to risk and uncertain environmental conditions in rainfed regions, has a very precarious homeostatic balance supporting him in the society. In fact this balance often acquires a form of negative homeostatics due to heavy indebtedness, traditional technology, risk and drought effects in rainfed regions. This implies on the part of small farmer, a tendency to adjust against the sub-optimal level of input invest-

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terms, cost of repayment schedule and security. The money-lender may be the input supplier as well as the source of advice, with the result what farmer has to do, how and at what cost, has already been determined for him in the credit market. The product market may also get inter-penetrated by credit market, if the same person is also the purchaser of the produce of this small farmer.

The different sub-sets in the figure present various possibilities that confront the small farmer in different farm situations once he has got the credit.

In the case of the most ideal sub-set (entitled Most Regular-A), assuming that farmer gets whatever inputs he wants with supporting technological advice, he may utilise this opportunity to invest the credit in such enterprises as Crop, Animal Husbandry (A.H.), Minor Irrigation (M.I.), etc. After taking up any one or more enterprises, the farmer would market the produce, hoping to get enough surplus to pay back the initial credit he took from whatever sources. Obviously this will be the shortest cash flow cycle running into single run of the enterprise. However, those who are familiar with the farmers' condition in rainfed regions know that such an ideal situation rarely exists.

The possibility is that due to vagaries of nature the enterprise may fail, with the result he looks either for more credit so as to come back into the investment cycle or goes to some money-lender, big farmer or a trader from where he takes further credit to repay the original source. This is a case of pseudo repayment given in sub-set C. Further implications of this may be that he resorts to the asset disposal or takes to the labour work or simply migrates out.

The pseudo repayment also results if a farmer after having taken the credit prefers to clear his old debt which he owes to somebody else. When need arises he takes further credit from this new source to pay back the old source. Such cycle obviously leads farmer to a state of perpetual indebtedness and hardships.

Another path before a farmer could be that he consumes the credit obtained for any domestic or social purpose which again could be avoidable or unavoidable. The classification of his consumption need as avoidable or unavoidable is somewhat arbitrary because some of the consumption requirement that is seemingly avoidable becomes unavoidable for the farmer due to social or cultural pressures. For example having fixed the marriage of a daughter, small farmer even at the cost of certain loss on account of sub-optimal investment in the economic enterprise, may decide to celebrate the marriage and thus enter further deficit. Likewise health-house or other social considerations may force the farmer to consume the credit. At this stage after having consumed the credit, he may enter the investment cycle through saving of the wages plus some further borrowings so as to repay the credit from the original source. For this he may

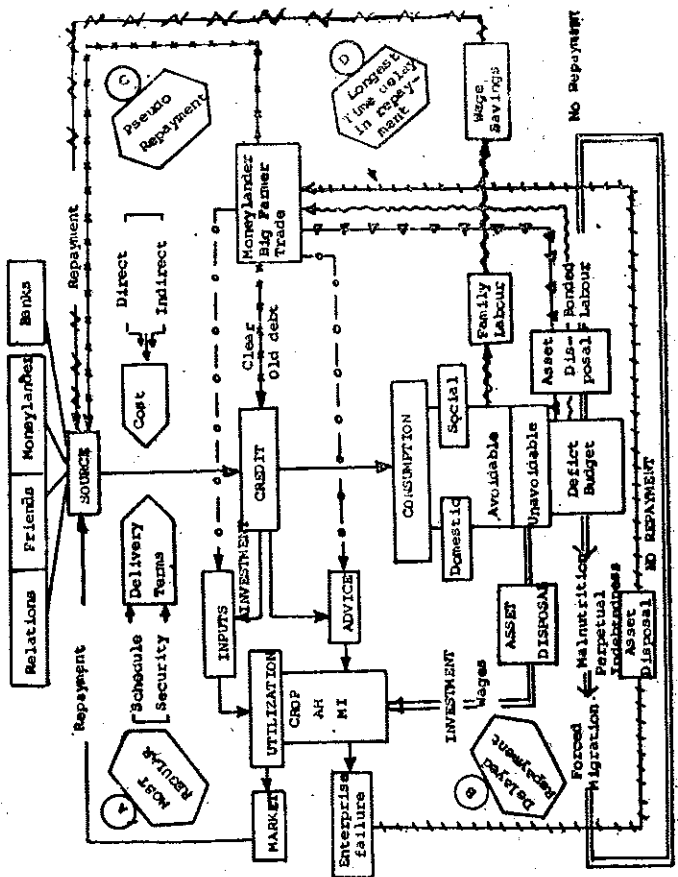


FIG. 1

ment so as to ensure lesser but certain production. Thus the paradigm describes different paths that different classes of farmers in different farm situations may have to take to survive in a given socio-economic context. It would be interesting to see which stages should attract maximum attention from the project planners and how.

It has been assumed that once a farmer decides to enter the investment cycle, he may succeed in getting some credit from say relations, friends, money-lenders or banks. Referring to Fig. 1, we note that the farmer, before getting credit, has to agree to certain delivery terms and pay certain direct and indirect costs. The delivery terms include repayment schedule security, collateral/coobligant, direct costs (the rate of interest, service charges and other expenditure) and indirect costs (the transportation expenditure of the borrower and coobligant, in arranging collateral and other terms for finally getting the credit). These costs also include the commitment of labour and other resources made by an individual or his family to the source of credit. The supervisory follow-up, extension, advice, input purchase obtaining various other services also cost the farmer something directly or indirectly. In the above process, he has to forgo several investment options depending upon the credit

have to dispose of some of his assets like livestock, etc. (also to supplement his savings to enter enterprise/investment cycle, asset disposal may take place). This cycle as mentioned in sub-set B would be a case of delayed repayment. However, he may also choose to forgo the opportunity of investment because of either lack of access to further inputs or because of reduced faith in future returns (or for some other reasons) and he may decide to invest his own and the family's labour at other's farms or public works to earn the wages. The savings from these wages would go to pay the original source. Obviously this is the case of longest time delay in repayment as shown in sub-set D.

In the same case there could be another possibility. Farmer finds that even after having taken the credit from the original source, the social or domestic need has not been met completely and due to deficit budget he resorts to borrowing from the money-lender, big farmer, trader, etc. Efforts to meet gap may include disposal of assets besides other pursuits (as mentioned earlier). In that case either he commits the family labour to this new source of credit leading to bonded labour in which case he may never be able to pay the original source (or for that matter even the new source) or he may through malnutrition, perpetual indebtedness choose to escape and migrate out leading again to no repayment to the original source at all.

There are several other possibilities, depending upon the extent of the deficit remaining after paying the old source, and entering of farmer either in investment cycle or wages and savings cycle. The possibilities are also there, for the farmer after having taken the credit from some new source to pay back the old loan so that not only inputs but also advice is taken from the new source only. Such a situation would have far reaching implications for the future decision making options of a small farmer *vis-a-vis* exploitation of his existing potential, resource base and human capital.

The situation described above presents only a brief sketch of some of the possible stages through which the small farmer has to pass before completing an economic run of an enterprise or investment. The various types of projects that are suggested in rain-fed regions very often ignore the micro level dimension of internal resource management by the small farmer. This leads to inappropriate evaluation of the success or failure of the project as well as inadequate monitoring of the possible projects outputs.

The fungibility of credit so described above points to the limitations, the existing project management and supervised agricultural programmes face in their endeavours to help the small farmer. At present we do not have sufficient data to say as to which sub-set or combination of sub-sets include the greatest proportion of small farmers in the arid regions. Perhaps this proportion would differ from situation to situation. However, we believe that an in-depth analysis of these paths would certainly help

in unravelling the dynamics of decision making at a small farm level in the specific social context of farmers in rain-fed regions.

The planned interventions for meeting the specific demands of farmers operating in different sub-set situations described will have to be differently designed. The philosophical understanding of consumption and production activities of marginal farmers as inseparable from each other will have to be clearly accepted. The 'basic needs' model which differentiates between above needs of rural poor obviously cannot make much headway in the present level of market interaction together with complexity of decision making options of small farmer and labour. The concept of projects as vehicles for injecting resources for rural development may thus have to undergo some definitional change. The public policies also will have obvious repercussion in different sub-sets of the paradigm at different stages. The institutional arrangements and the built-in flexibility *vis-a-vis* the access differential operating in rural regions will also need elaboration.

This framework presenting a rather different view of 'farmers rationality', offers interesting openings for exploring the innovative project designs that synchronise their internal process of delivery with the cash flow and internal resource management of small farmers.

Projects suiting the sub-set A will have to merely concern themselves with the internal efficiency of the delivery system of credit because as per the paradigm the farmer is able to get required input and advice (probably because of efficient markets) to generate enough surplus to pay back the credit. However, in sub-set B the projects will have to take into account the consumption needs of the farmer as well as additional credit need for any deficit remaining after unavoidable consumption. The schedule of repayment will also have to be flexible. In case of enterprise failure, the project will have to provide for the nursing finance as an on inherent constituent of the project design so as to sustain farmer's economy. The design will have to be different in high risk prone enterprises or regions where flexibility in repayment is essential to keep the farmer solvent. Likewise the project design for sub-set D and C will not only have to be differently oriented but also, the project package will have different constituents.

In Fig. 2 & 3 the dynamics of credit have been presented through 'credit crayons' of two farmers, Ram Avatar Singh and Gharsi. In case of Ram Avatar Singh, we observe that credit from eight different sources not only interacts strikingly but also widens the budget deficit apparently in an irrevocable fashion. The fungibility of credit makes the input tie ups meaningless when the distinction of source specificity is constrained by the peculiar internal resource management designed (or manoeuvred) by the farmer. To pay back Mini Bank dues, he borrows from Begraj whom he pays back after much delay. And this repayment doesn't get generated from his small plot of land alone. There is a definite (though it is difficult to quantify) contribution of other credit sources towards this. Likewise,

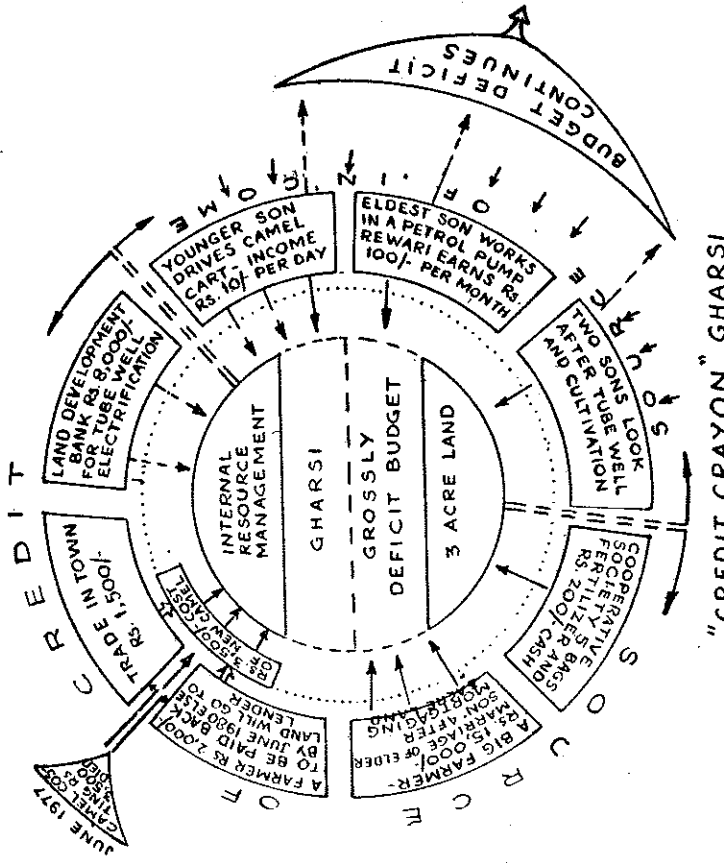


FIG. 3

institutional loan is consumed for meeting domestic needs, while kind component has been only apparently used. However, it may not be inferred from this that credit in kind always gets used (in fact it seldom does). Here the typical resource position of Gharsi has necessitated this adjustment on his part (Ref. Fig. 3).

A detailed look as to how the death of a camel triggers a chain of credit adjustments, may throw light on the credit constraints of a small farmer. Social customs have their own role in constraining the frame of adjustments as expressed through loan for marriage of Gharsi's son.

The pledging of loan and accompanying threat of foreclosure automatically predetermines Gharsi's priorities of investment as well as his risk taking capacity.

The 'credit crayons' (graphic details of credit receipt and repayment already made and/or potentially possible though presentation of internal resource management of small farmer, expressing not only credit constraints but also a total frame in which farmers' priorities are determined) are tools having definite bearing on the project design.

The risk taking capacity, not only for innovation but also for taking credit (and in investing it in ventures offering enough surplus to maintain

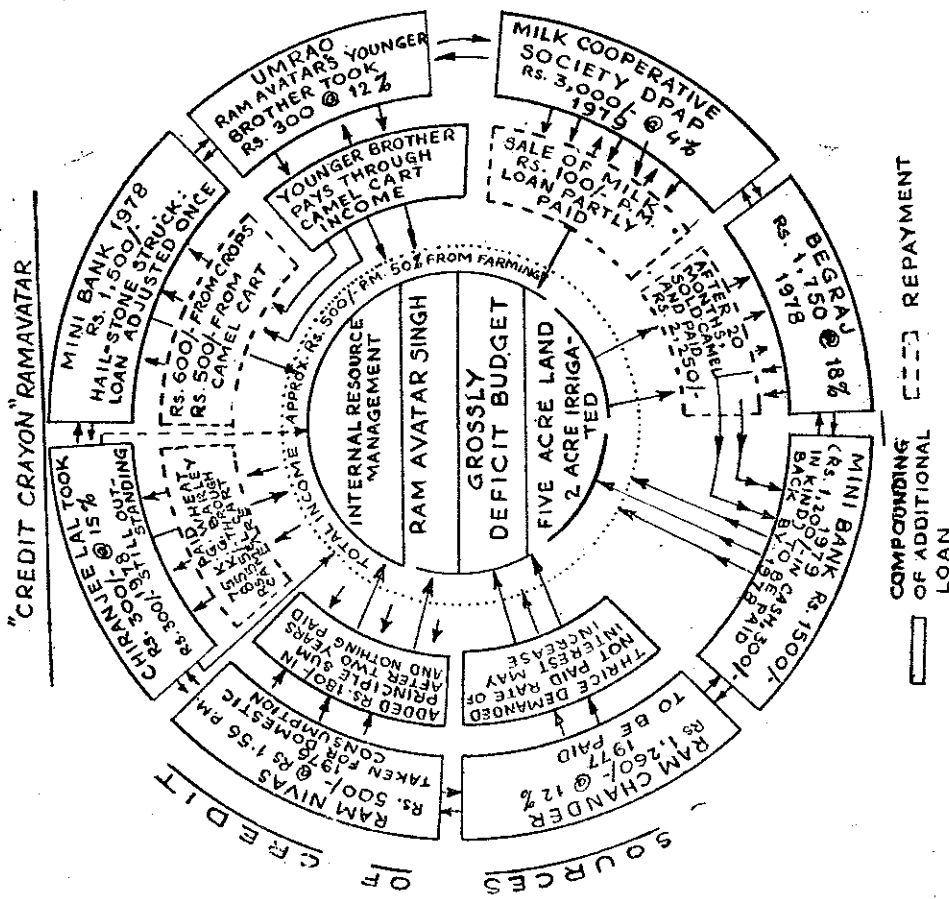


FIG. 2

the income of his younger brother who further raises a loan from a friend goes largely to liquidate the liability of Mini Bank wherefrom he borrows again. Compounding credit due to default can further be seen in case of loans from Ram Nivas, and Ram Chandra. This complicates all the more farmer's calculation for resource utilization (Ref. Fig. 2).

Despite substantial payment of dues of Chiranjee Lal in cash and kind the principal amount remains intact. Further, the payment of Mini Bank due in 1978 does not take place from the income from crop alone. Income from camel cart is also used by the farmer to liquidate it.

Interchangeability of credit source, use and recycling mechanism make the task of agricultural project designing very complicated. In case of Gharsi, credit network depicts the fact that entire cash component of the

farmer's homeostatic balance) and utilising it, is reflected as function of hosts of constraints in which drought economy puts a small farmer.

Thus, the interventions through the Project for ameliorating the condition of Gharsi or Ram Avatar Singh can't be conceived in isolation of their real credit contexts. And these contexts are modified, at times defined, by technological innovation, their spread and input supply support system besides farmer's own resource base. The ecological dimension of regional endowment in relation to each individual, breeds in him, a specific developmental potential. To exploit this, unique efforts are required at each farmer's level.

Traditional project design strategies don't provide for any such micro level relatedness between the project objectives and individual resource context.

Looking at the vast multitudes of small farmers who have to be helped, the complexity of task can be well anticipated. This paradigm clearly brings out that manipulations of the internal variables of project components would not, in any way, increase the correspondence between project performance process and internal dynamics of small farmers resource constraints.

Neither, reliance on efforts for improving the efficiency of market structures alone, nor pursuits of greater effectivity of existing institutional network in social context, constitute the complete realm of desired strategy.

The explorations towards administrative arrangements in the given planning framework, would suffer from several major limitations. They would imply pursuits of acceptability/desirability/feasibility/optimality and contextuality of various alternatives in segregated market framework. Flexibility, in the process would often be a casualty in the name of better small farmer care. Thus discussion on the project design and policy package can take place dispassionately only when some of the assumptions held dear are questioned:

- That of difference between consumption and production needs of small and marginal farmers whose major resource is labour.
- The manipulation of internal variables like interest rate, etc., only when repayment schedule and composite (port folio) financing may be better instruments for accommodating small farmer resource constraints.
- Policies for collective handling of needs of big and small farmers through single institutional channel.
- No discrimination between defaulters of different hues. Similar categorisation in this context is one single most important absurdity of institutional efforts to reach small farmer.
- Conventional banking through somewhat unconventional institutions

distorts all the more credit climate.

—Similar policy frame for catering to differently endowed regions and classes of farmers for different credit purposes projects, etc.

The implications for project design have direct bearing on the indices of monitoring the project performance *vis-a-vis* target group. Obviously the appraisal of project, both economic and social, will require basically different methodology than adopted hitherto. It is believed that typologies so described can be explored further to provide deeper insights for developing theory of rural development.

Needless to mention that the paths described here are only indicative and not exhaustive, for the regional dimension of diversity and disparity will have to be appropriately documented to make it comprehensive. However, the focus on small farmer's internal resource management can provide effective alternative to functional, sectoral and regional approaches to project design. The earlier approaches applied in developed societies have not proved to be replicable in developing societies. □