Bank Credit Utilisation by Agriculturists and MSMEs: An Empirical Study With Reference To Kerala

Dr. Suby Baby

Assistant Professor
Post Graduate and Research Department of Commerce, Nirmala College,
Muvattupuzha, Kerala, India.
Email: drsubynirmala@yahoo.com

Abstract

The paper examines the utilisation of bank credit by micro, small and medium enterprises (MSMEs) in the selected districts of Kerala. One of the cardinal principles behind sanctioning a loan is to use it for the purpose for which it was granted. However, diversions of credit for unspecified purposes are alleged to be diluting the objective of lending. Moreover, most of the bank officials are pressured by target oriented lending and to fulfil their target, most of the time, they relax the lending and utilisation norms. Eventually, it results in loan default and utilization gap. The empirical results show that a large majority of the borrowers (63.8%) utilized credit for the purpose for which it was sanctioned and the rest (36.2%) diverted the credit. Again, 38.2 per cent of the borrowers diverted 10 to 20 per cent of their loan amount and 33.6 per cent diverted 30 to 40 per cent. Further, 53.9 per cent of the borrowers, who diverted the loan, used the amount for unproductive purposes and none more than 7.4 per cent used it for productive purposes. This paper insinuates banks to cautiously design an efficient and effective mechanism to identify an eligible borrower and the point at which the borrower diverts the loan. Ensuring proper scrutinizing of the borrowers along with adequate credit flow and efficient monitoring machinery will definitely alleviate the chances of default, which rescue the borrower from the claws of insolvency and the bank from the snatch of over dues syndrome.

Keywords: Bank Credit Utilization – Credit Diversion – Credit Utilisation Gap – MSME Credit Utilisation – Credit Overdue

I. Introduction

Access to bank credit and its efficient utilization, especially by the agriculturists and micro, small and medium enterprises (MSMEs) are the essential pre-requisite for improving economic growth, poverty alleviation and social upliftment. A significant portion of Keralites (20.19%) are either in agriculture fields or in small industries sector (Kerala Economic Review, 2009). They are either depending on formal source of finance like commercial banks or informal sources of finance like private money lenders for their financial need. The

commercial banks in Kerala play a pivotal role in catering the financial needs of these sectors. But their access to credit is prone to problems due to the inability to arrange for collateral security and or third party guarantee. Again, there are divergent views as to the utilization of credit by these category borrowers. It is expected that all the borrowers utilize the credit for the purpose for which it was sanctioned. Though this is one of the cardinal principles behind sanctioning a loan most of them are not actually adhered this. Again, in order to fulfil the target oriented lending imposed on bank officials they fail to chalk out eligible borrower and eventually the concerned borrower makes divert the loan. This gradually results in wilful default and utilization gap. It is in this backdrop that the present paper has been prepared.

II. Objectives and Methodology

This paper focuses on the utilization of bank credit by agriculture and MSME borrowers of the public and private sector banks in Kerala. It examines whether the credits have been utilised by the borrowers effectively or not for the purpose for which they are sanctioned. The extent and purpose of credit diversion, and the steps taken by banks to avoid diversions are also discussed in the paper. The study has been done based on the perception of the borrowers and bank managers.

The study is empirical in nature. The data required for the study are collected from the borrowers (i.e. agriculturists and MSMEs) and managers in the public and private sector banks in Kerala based on structured interview schedules. All the public and private sector banks (except new generation and foreign banks) in Kerala constitute the universe for the study. Multistage Systematic Random Sampling technique was employed for selecting the sample. In the first stage, the State of Kerala is divided in to three zones – south, central and north – for selecting one district each representing these zones. The districts were selected by considering the volume of banking business and number of branches. Accordingly, Thiruvananthapuram (representing the south), Ernakulam (representing the central) and Kozhikode (representing the north) are selected. In the second stage, one bank from the public sector and one bank from the private sector are selected from each of the three sample districts based on the volume of business and number of branches. The State Bank of Travancore (SBT) and Federal bank were the banks in the public sector and private sector, respectively fulfilling the selection criteria in all the three zones in Kerala. Thus, State Bank of Travancore and Federal Bank constitute the sample banks.

There are 172 SBT branches and 128 Federal bank branches in the three selected zones in Kerala. In the third stage, for selecting the sample branches, 10 per cent from each zone of SBT and Federal bank are selected systematically. Thus, 17 SBT branches and 13 Federal bank branches constitute the sample branches. In the fourth stage, the sample borrowers are selected. For the intensive study, 300 agricultural borrowers (270 from SBT and 30 from Federal bank) and 300 MSME borrowers (208 from SBT and 92 from Federal bank) are selected conveniently by considering the proportion of the number of agricultural and MSME borrowers from the three zones of

17 branches of SBT and 13 branches of Federal bank. Thus, a total of 600 respondents are representing as borrowers for the study. All the branch managers of the selected 17 branches of SBT and 13 branches of Federal bank are respondents to represent the public and private sector commercial banks in Kerala. Data analysis is done using average, percentage, weighted mean and chi square test. The weighted mean is found to determine the relative order of preference of the respondents and the chi square test is applied to examine the variations in the opinion of the respondents with reference to the three zones of Kerala.

III. Results and Discussion

III. (A) Credit Utilisation

While sanctioning a loan, it is expected that all the borrowers utilise the credit for the purpose for which it was sanctioned. The utilisation of credit availed by agriculturists and MSMEs in the public and private sector banks in Kerala reveals that a large majority of the borrowers (63.8%) utilised the credit for the purpose for which it was sanctioned and the rest (36.2%) diverted the credit for other purposes. The chi-square test calculated separately for the public sector and private sector banks, and also between the sectors show a significant variation in the opinion among borrowers ($p < 0.05$) (Table 1).

Table 1: Credit Utilisation (Opinion of Borrowers)

Diversion/ Utilisation	Public Sector Bank				Private Sector Bank				Total
	South	Central	North	Total	South	Central	North	Total	
Diversion	69 (31.2)	89 (44.1)	33 (60.0)	191 (40.0)	18 (60.0)	6 (8.5)	2 (9.5)	26 (21.3)	217 (36.2)
Utilisation	152 (68.8)	113 (55.9)	22 (40.0)	287 (60.0)	12 (40.0)	65 (91.5)	19 (90.5)	96 (78.7)	383 (63.8)
Total	221 (100)	202 (100)	55 (100)	478 (100)	30 (100)	71 (100)	21 (100)	122 (100)	600 (100)

Figures in parenthesis are percentages to respective totals.
Public sector banks- Chi square (df= 2) = 17.655 p value = .000*
Private sector banks- Chi square (df= 2) = 35.520 p value = .000*
Public and Private sector banks- Chi square (df= 1) = 13.842;p value = .000*
* Significant at 5 per cent level.
Source: Primary data.

III. (B) Extent of Credit Diversion

Larger the amount of credit diverted, the more will be the chance of overdue. The extent of credit diversion given in Table 2 reveals that 41.9 per cent of the borrowers diverted up to 20 per cent of their credit and 34.6 per cent diverted between 30 and 50 per cent of their credit amount. While analyzing the sectors separately, 38.2 per cent of the borrowers of the public sector banks diverted 30 to 50 per cent of their credit whereas 84.6 per cent of the borrowers in the private sector banks diverted less than 20 per cent. The chi-square test results confirm that significant variation exist regarding credit diversion among the borrowers of public sector banks ($p < 0.05$). However, no significant variations exist with regard to extent of credit diversion among the borrowers of the private sector banks; and between the borrowers of the two sectors ($p>0.05$).

Table 2: Extent of Credit Diversion (Opinion of Borrowers)

Extent of Diversion (%)	Public sector bank				Private sector bank				Total
	South	Central	North	Total	South	Central	North	Total	
< 20	21 (30.4)	24 (26.9)	24 (72.7)	69 (36.1)	16 (88.9)	5 (83.3)	1 (50)	22 (84.6)	91 (41.9)
30-50	46 (66.7)	20 (22.5)	7 (21.2)	73 (38.2)	1 (5.6)	1 (16.7)	-	2 (7.7)	75 (34.6)
> 50	2 (2.9)	45 (50.5)	2 (6.1)	49 (25.7)	1 (5.5)	-	1 (50)	2 (7.7)	51 (23.5)
Total	69 (100)	89 (100)	33 (100)	191 (100)	18 (100)	6 (100)	2 (100)	26 (100)	217 (100)

Figures in parenthesis are percentages to respective totals.
Public sector banks- Chi square (df =4) = 110.488 p value = .000*
Private sector banks- Chi square (df = 4) = 40.971 p value = .000*
Public and Private sector banks- Chi square (df = 2) = 5.162; p value = .0757*
* Significant at 5 per cent level.
Source: Primary data.

III. (C) Purpose of Credit Diversion

The borrowers may divert the credits disbursed to them for productive or unproductive purposes. The analysis of the perception of the borrowers in this regard reveals that 53.9 per cent of them have diverted the credit for unproductive purposes like clearing of old personal debts, meeting family recurring expenses, purchase of household assets, etc. This true for the two sectors independently and collectively (Table 3).

Table 3: Purpose of Diversion of Loan (Opinion of Borrowers)

Purpose of Loan Diversion	Public Sector Bank				Private Sector Bank				Total
	South	Central	North	Total	South	Central	North	Total	
Productive:									
Purchase of farm animals	1 (1.4)	15 (16.9)	-	16 (8.4)	-	-	-	-	16 (7.4)
Digging of wells	-	5 (5.6)	-	5 (2.6)	-	-	-	-	5 (2.3)
Meeting marketing expense	-	3 (3.4)	-	3 (1.6)	-	-	1 (50.0)	1 (3.9)	4 (1.8)
Meeting labour charges	-		1 (3.0)	1 (0.5)	-	-	-	-	1 (0.5)
Purchase of goods	1 (1.4)	2 (2.2)	-	3 (1.6)	-	-	1 (50.0)	1 (3.9)	4 (1.8)
Construction of farm building	-	8 (9.0)	-	8 (4.2)	-	-	-	-	8 (3.7)
Purchase of raw materials	-	4 (4.5)	1 (3.0)	5 (2.6)	-	-	-	-	5 (2.3)
Purchase of farm animals	-	12 (13.5)	-	12 (6.3)	-	-	-	-	12 (5.5)
Repair expenses	-	6 (6.7)	3 (9.1)	9 (4.7)	-	-	1 (50.0)	1 (3.9)	10 (4.6)
Unproductive:									
Family expenses	25 (36.2)	26 (29.2)	4 (12.1)	55 (28.8)	2 (11.1)	1 (16.7)	-	3 (11.5)	58 (26.7)
Clearing of old personal debts	48 (70)	30 (33.7)	22 (66.7)	100 (52.4)	11 (61.1)	5 (83.3)	1 (50.0)	17 (65.4)	117 (53.9)
Purchase of household asset	21 (30.4)	12 (13.5)	6 (18.2)	39 (20.4)	6 (33.3)	-	1 (50.0)	7 (26.9)	46 (21.2)
Social ceremonies	5 (7.2)	2 (2.2)	-	7 (3.7)	-	-	-	-	7 (3.2)
Others	3 (4.3)	1 (1.1)	-	4 (2.1)	-	-	-	-	4 (1.8)
Total	69 (100)	89 (100)	33 (100)	191 (100)	18 (100)	6 (100)	2 (100)	26 (100)	217 (100)

Source: Primary data.
Figures in parentheses are percentages to respective totals.

III. (D) Steps Taken for Avoiding/Reducing Credit Diversion

The analysis of the perception of borrowers regarding utilisation of credit (Table 2) clearly reveals that 34.6 per cent borrowers have diverted even up to 30 to 50 per cent of their credit amounts. Noticeably, 53.9 per cent of the borrowers who diverted their credit utilised the same for clearing of old personal debts (Table 3). The responses of the bank managers regarding the preventive steps taken to avoid/reduce the credit diversion are given in Table 4 (Page 42). The steps such as, 'insisting account only transaction', 'disburse only through dealers of assets' and 'minimum cash disbursement' are reported to be effective steps by the managers. In addition, 'frequent stock verification' and 'educating the borrowers' are also found to be initiated by manages.

IV. Conclusion

The empirical analysis made above confirms that majority of the borrowers have utilised the credit for the purpose for which it was sanctioned. Regarding the diversion of credit, majority of the respondents have diverted below 20 per cent of their credit for unsanctioned purposes. Alarmingly, large majority of the borrowers who diverted their credit utilised it for unproductive purposes such as clearing of old personal debts, meeting family expenses, purchase of house hold assets, etc. 'Insisting account only transaction', 'disburse only through dealers of assets' and 'minimum cash disbursement' are the main steps taken by bank managers to prevent/reduce the diversion of credit. Thus, the above results confirms that, regardless of sectors, credit diversion for unproductive purposes by borrowers are considerable and further measures should be taken by the lenders to minimise it to the extent possible. Identifying eligible borrowers and assessing the magnitude credit requirement through strict adherence to lending norms are keys to overcome the situation. Also, pre-disbursement and post-disbursement monitoring should be strengthened further to avoid the credit diversion or to ensure its effective utilisation.

References

Basu, P (2006). "Improving access to Finance for India's Rural Poor", Washington D.C: The World Bank.

Chaudhry Kamran Naseer (2010). "Agriculture-credit is critical for the flood-hit farmers' subsistence", Business and Finance Review, Vol.5 (2), January.

Government of Kerala (2009).*Economic Review*, State Planning Board, Thiruvananthapuram.

Hans,V.Basil (2006). "Towards A Vibrant Indian Culture", *Kissan World,* Vol 33(2), February, pp. 18-20.

James Manalel (1994). "Role of incentives in the development of small scale industrial units   in Kerala", *Ph.D Thesis*, Cochin University, Cochin.

Prasad, C.S (2006). "Micro, Small and Medium enterprises financing in India: Issues and concerns", *Cab Calling*, July-Sept 2006, pp 35-40.

Press Trust of India (2009). "20-PSU banks fail to meet farm sector lending target till November", *The Economic Times*. Retrieved from

http://economictimes.indiatimes.com.

Rahji, M.A.Y and S. B. Fakyode (2009). "A multinomial logit analysis of agricultural credit rationing by commercial banks in Nigeria", *International Research Journal of Finance and Economics*, Issue .24, Nigeria.

Singh, S. K and Singh, S (2009). "Use of institutional credit for sustainable agriculture production" *GCRA*, International Conference on communication for development in the information age: Extending benefits of technology for all, Banaras Hindu University, Varanasi.

Table4: Steps for Avoiding/Reducing Credit Diversion (Opinion of Bank Managers)

Particulars	Public Sector Bank									Private Sector Bank									Total		
	South			Central			North			South			Central			North					
	N	M	R	N	M	R	N	M	R	N	M	R	N	M	R	N	M	R	N	M	R
Minimum cash disbursement	8	3.3	3	6	3.1	3	3	3.0	3	3	3.0	3	6	3.0	3	4	3.0	3	30	3.1	3
Frequent stock verification	8	5.3	5	6	5.8	6	3	5.3	5	3	5.6	5.5	6	5.6	6	4	5.5	5.5	30	5.5	6
Insist account only transaction	8	1.1	1	6	1.6	2	3	1.3	1	3	1.0	1	6	1.3	1	4	1.5	1.5	30	1.3	1
Close follow up	8	3.6	4	6	3.8	4	3	4.0	4	3	4.0	4	6	4.0	4	4	4.0	4	30	3.8	4
Educate the borrowers	8	5.6	6	6	5.1	5	3	5.6	6	3	5.6	5.5	6	5.5	5	4	5.5	5.5	30	5.5	5
Disburse through dealers of asset	8	1.8	2	6	1.3	1	3	1.6	2	3	2.0	2	6	1.6	2	4	1.5	1.5	30	1.6	2
Others	8	.00	-	6	.00	-	3	.00	-	3	.00	-	6	.00	-	4	.00	-	30	.00	-

Source: Primary data.
Note: N= Number M=Mean R= Rank.