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**RESERVE BANK OF INDIA**

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## **RBI Working Paper Series 5 / 2013: Persistence of Informal Credit in Rural India: Regulatory Policies Need to Recognise Changing Rural Landscape**

The Reserve Bank today placed on its website a Working Paper titled "[Persistence of Informal Credit in Rural India: Evidence from 'All-India Debt and Investment Survey' and Beyond](#)" under the RBI Working Paper Series. The paper has been authored by Dr. Narayan Chandra Pradhan.

Rural credit market in India is characterised by the coexistence of both formal and informal sources of finance and the market is fragmented.

The paper chronicles 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. 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 and that of institutional agencies as formal sources of credit. 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.

The paper makes an attempt to assess the share of rural informal credit in total outstanding debt which has been 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 indicates further scope for financial inclusion in rural areas.

Major findings of the paper are:

- 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; the pace of increase was arrested subsequently to 64 per cent in 1991. During 1990s, the share declined and reached 57 per cent in 2002.
- The period of distress in agriculture in the 2000s is also identified with a relatively declining contribution of cooperatives in agricultural credit, and with RRBs not showing substantial increase in agricultural credit, indicating the urgent need to ensure increased access to agricultural credit for small and marginal farmers.

- Rural borrowers prefer to use informal sources of credit despite the fact that they charge much higher interest rates. This is perhaps because informal sources do not insist on regular repayment as banks or cooperative credit societies do. Usually, it is possible to obtain loans for such purposes as marriage and attending to litigation only from informal sources and without collaterals.
- There is a need for regulatory policies to recognise the changing rural landscape, adapt to new realities and bring in suitable changes as many of the informal players are not included in the existing regulatory framework on money lending.

This calls for financial sector initiatives in the form of prompt and innovative policy responses to prioritise financial inclusion, financial education as well as financial literacy.

The Reserve Bank of India introduced the RBI Working Papers series in March 2011. These papers present research in progress of the staff members of the Reserve Bank and are disseminated to elicit comments and further debate. The views expressed in these papers are those of authors and not those of the Reserve Bank of India. Comments and observations may kindly be forwarded to authors. Citation and use of such papers should take into account its provisional character.

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Director