SMALL FARMER CREDIT WITH PARTICULAR REFERENCE TO NIGERIA

by

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To my brother, Paddy, who has spared
no effort throughout the course of
my education.

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INTRODUCTION

Most less developed countries (LDC's) of the world depend on agriculture for a significant portion of their national income. If such countries are to develop economically, the agricultural sector must contribute in a positive way to the general development process. The bulk of the farmers who are expected to contribute to this economic development are poor and live in rural areas. They depend mainly on their energy and nature's abundance in the soil. It is expected that these farmers will improve their productivity and that increases in their incomes will help stimulate industrial development by opening up new markets for consumer goods.

Increasing productivity of these small farms involves a number of interrelated factors. Among them, lack of capital is generally recognised as an important constraint. Larger farmers to some extent have access to commercial funds. Such opportunities bypass the small farmers who are often looked upon for most of the expanded food supply.

In an attempt to reach this group of farmers many governments have opened up small farmer credit programmes which undertake the provision of credit so that peasant farmers can utilize more or better agricultural production inputs than would otherwise be the case. Either a change in technology is involved or, as is sometimes the case, a farmer already using improved methods and inputs to a certain extent, is enabled to extend his use of improved technology.

The present work, which is based on literature review, looks at the difficulties involved in extending credit to these small farmers and suggests some ways of alleviating them. The first chapter deals with the economic environment in the LDC's. The need for and preconditions for a successful credit programme are presented in Chapter Two. Chapter Three examines the sources of credit and their difficulties. Chapter Four considers the policy issues involved in credit delivery while in Chapter Five the Nigerian Credit experience is discussed. Finally, Conclusions and Recommendations are treated in Chapter Six.

CHAPTER ONE

AGRICULTURAL SITUATION

1.1 PRODUCTION ENVIRONMENT

For quite some time the agricultural industry has been the major source of employment and the base for national economy for most developing countries. The per capita income for these countries is very low as most of the farmers who constitute a greater percentage of the working population operate on subsistence level (see Tables 1 and 2 on the following page).

The dominant development strategy adopted by many developing countries on attainment of independence in the 1950's and 1960's emphasized importation of industrial technology. They regarded the economic achievements in Europe or North America as synonymous with development, and industry as the key to progress. This policy has had negative results for agriculture; the nations' attention and resources tended to be concentrated on development of urban cities to the neglect of farming and the rural areas. The shortcomings of this "industrial import substitution" policy became apparent in the late 1960's and early 1970's. Now it has become clear that poor development of agriculture which means much to the nation in terms of employment opportunities as well as economic stability is a major constraint on national growth.

Rural-urban migration has become an important phenomenon in the social set-up of many developing countries. Biggs (1974) asserts that the push factors of low per capita incomes, and inadequate employment opportunities have generated massive outflows of people from rural areas. Furthermore, Wells (1971) emphasizes ". . . In areas or regions where the problem of hunger

Table 1

Total population, agric. population and population economically active in agriculture 1976

Country	Population		Economically active population		
	total	agric	total	agric	% in agric
			(thousands)		
Kenya	13,701	10,888	5,315	4,224	79.5
Nigeria	64,887	36,898	25,193	14,326	56.9
Chad	4,016	3,476	1,551	1,342	86.6
Burma	31,992	17,523	13,107	7,179	54.8
India	628,608	414,661	245,104	161,683	66.0
Pakistan	72,859	40,408	20,167	11,185	55.5
U.K.	55,970	1,291	25,871	597	2.3
Germany (Fed)	61,775	3,258	28,367	1,496	5.3

Source: FAO Production Yearbook 1977

Table 2

GNP and average annual growth rates 1976

Country	Amount US $	Real growth rates (%) 1970-76
Kenya	250	0.9
Nigeria	400	5.4
Chad	120	-1.4
India	140	0.5
Pakistan	180	1.1
U.K.	4,180	1.7
Germany	7,510	2.0

Source: World Book Atlas 1978

is most acute or at least a constant threat, ways and means must be found for increasing the agricultural productivity while at the same time maintaining in rural areas most of the current populations as well as a substantial portion of their annual increase over the years ahead . . . Whatever solutions are worked out in many of these countries must be built around small farmers and rural industries, as these rural populations are already moving to cities at a rate faster than they can be accommodated".

Income distribution statistics for developing countries are not easy to compile, and when available they are often incomplete. However, Healy (1972) indicates that it is quite common to find that the lowest 50 percent of the income earners receive between 15 - 20 percent of the total income, while the highest ten percent receive 40 and 50 percent. Hunter et al. (1972) have shown that in Brazil, Mexico and the Philippines the ratios of income controlled by the top 20 percent of income recipients to the bottom 20 percent varied between 10 to 1 and 25 to 1.

On the basis of the foregoing evidence, there can be no doubt as to the desirability of rural development programmes which will be basically agricultural.

1.2 AGRICULTURAL DEVELOPMENT

In addition to the factors examined above, those of improving economic conditions of farmers, creation of employment opportunities and equitable distribution of income, improved

agriculture has other roles to play in the development of less developed countries. These include:

a) increased food production to cope with the increasing population.

b) production of export crops which will earn foreign exchange.

c) provision of raw materials and market for local industries.

It is obvious that there is need for increased productivity if agriculture must fulfil the above functions. This additional output must come from the small holders who make up most of the farm population in these countries.

Fortunately, there is considerable potential for increasing agricultural output in the developing countries, including output from the small farm sector. This potential should be sufficient to provide the marginal additions to food output needed to keep pace with population growth over the next several decades. Realization of this potential requires more irrigation and better water control, more soil conservation and reclamation, and additional infrastructure such as roads and market facilities. It also means new crop varieties, more fertilizer and pesticides, better quality storage and food processing - plus careful planning for the introduction, management and control of this technology. Furthermore, the technology must be brought within reach of millions of small farmers.

Thus there is a general need for an evolution which depends, to a very large extent on the conversion of the millions of small farm units into more advanced types of enterprises which lay an increasing emphasis on market production. This conversion is one of the most difficult and complex problems developing countries have to face. It would be unrealistic to expect a rapid conversion of the numerous subsistence farms into economic units based on a fully fledged market production.

A number of factors combine to militate against this needed improvement. Invariably, inadequate supply of capital is one of the major limiting factors. Availability of capital in the countries is often a problem and even where it is available, ensuring that it reaches the small village farmers tends to be a bigger problem.

2.1 THE NEED FOR CREDIT

Internal financing forms for the small farmers are created by production processes in which family labour is the primary, and, in some cases, the only resource (in addition to land). Due to the size of the farms, and the low level of existing technology, the level of production, marketing and net income tend to be very low. Consequently, with consumption needs that are high relative to the level of income, these farmers cannot save and invest new capital in their farm business. Therefore little or no capital improvement, on which productivity increases are based, is possible.

To break this vicious circle there is need to inject not only technology and other agricultural services, but also capital into rural agriculture. "Financial credit is the most universal and flexible transferable form of economic resource", says Donald (1975), "with cash obtained via credit one can buy anything that is for sale". Thus where appropriate technology is available, acceptable and understood by the farmers, with an increased capital base, they will be in a position to adopt the technology. However, the major credit facilities elude them. These are available in the towns away from the rural villages. Besides, the farmers lack adequate collateral to offer as security for the institutional credit and usually have to resort to informal or private sources of credit.

In particular the need for increased supply of capital seems to arise from the following line of reasoning as given by

Ogunfowara et al. (1972):

> "(i) Many innovations in farming inevitably increase the capital requirements of farmers. The low rate of adoption of improved practices is partly due to the lack of adequate financial resources for implementing these practices.
>
> (ii) The bulk of the farmers produce at the subsistence level and there is usually small surplus out of which savings for future investment can be made.
>
> (iii) The seasonal nature of farm production and income generation creates a need for short and medium term loans for financing the production activities.
>
> (iv) The supply of loans may strengthen the farmer's position in the disposal of his farm produce instead of having the timing determined by urgent need for cash."

2.1.1 Types of Loans Needed

Agricultural credit is usually divided into three groups according to the length of time for which it is required. The groups are short-, medium-, and long-term loans. This classification has been described by Collingwood (1967), Miller (1977). It must, however, be emphasized that the divisions between the groups are by no means clear-cut.

Looked at from a different perspective, the need for credit among the small farmers can generally be divided into two - for productive and consumption purposes. For production, the credit funds are mostly spent on payment for labour and purchase

of basic farm inputs (seeds, fertilizers and chemicals)(see table 4). Others include purchase of basic tools - hoes, ox-drawn ploughs; water pumps in irrigation areas. Because the items purchased are small and seasonal, the credit required is short-term and seasonal too.

The purpose of production credit is to provide funds for the undertaking of some economic activity so that the borrower will have a higher net income after he has repaid the loan. On the other hand, credit used for consumption is static rather than dynamic since it does not increase the borrower's income or help him to repay the loan when it comes due. Nevertheless, provision should be made for consumption loans.

FAO (1975) argues that the objective of a credit programme for the small farmer should be to meet all his credit requirements including his genuine consumption needs.' Stickley (1976) has observed that limiting loans to productive purposes sometimes leads to situations which are difficult to defend. Baker (1973) also argues against excluding credit for consumption from small farmer credit. "In the organisation of the small farm it is difficult to and perhaps unrewarding to separate the household from the firm consumption'. . . Input requirements for the household are just as demanding as are input requirements for the firm . . ." Miller (1975) has shown that non-productive use of credit by the rice and maize farmers in Kwara and Western States of Nigeria accounts for more than 50 percent of total amount borrowed. This consumption part of credit appears to be most important during the period between planting and harvesting which makes it seasonal.

Results of many studies suggest that the volume of credit required per farmer is small (Table 5). This fact has led many workers to conclude that the administrative cost of lending to this category of farmer is very high (Section 4.2).

Therefore, even though there is an urgent need to increase the capital strength of small farmers, the credit required is short-term, seasonal and generally of small amounts per farmer.

2.2 ROLE OF CREDIT

One reason for the importance frequently attached to small farm credit as a vehicle for rural development in LDC's is the belief that the lack of small farmer access to institutional credit constitutes a critical constraint to the adoption of improved inputs and modern technologies which can lead to increased incomes and enhance rural welfare. Thus, if farmers are to adopt improved farming methods, such as the use of improved livestock, better seeds and pesticides, etc., they will require credit, especially short-term credit, to help them purchase these inputs.

Mosher (1971) states that "Most methods of increasing farm productivity involve the use of purchased inputs, and those farms near the subsistence end of the continuum from subsistence to commercial, produce little cash income out of which inputs can be bought". Rice (1973) summarizes the assumptions behind the conventional credit programme as being:-

"1. that farmers need credit to adopt new technology.

2. that they cannot get credit economically (if at all) from unscheduled private sources outside the programme.

3. that the provision of credit breaks the most important constraint of small farmers' progress."

As already stated, small farmers constitute the majority of farmers and consequently much more will be proportionally achieved if their contribution to agricultural production is improved. But lack of capital is a major constraint preventing the small farmer from increasing his farm productivity. Many research studies have demonstrated the potential effect of increased level of capital on agricultural production (Norman, 1970; Ogunfowara, 1972). They tend to show that when increased capital base is combined with improved technology, greater opportunities exist for larger volume of production and higher levels of farm income. Chandavarkar (1970) has emphasized that "one of the basic problems facing the less developed countries is the scarcity of domestic capital relative to the size of investment required to achieve high and self-sustaining rates of growth of national and per capita incomes."

While the above references are adequate in their own rights, agricultural credit is not a panacea for the solution of all problems of the small farmer and the developing countries. Small farmers can improve their productivity simply by good husbandry. In Western Kenya, field trials on farms and experimental stations have demonstrated that local maize yields

can be increased from 8.8 bags to 21.8 bags per acre (an increase of 162.5%) by good husbandry (Von Pischke, 1978).

The purpose of production credit is to enable farmers to purchase productive equipment and supplies. Credit is therefore less important to agricultural development than is the ready availability of such supplies and equipment at convenient nearby markets. But where effective and profitable production supplies and equipment are available, and where farmers have facilities for learning how to use them, production credit can accelerate the adoption of improved practices.

The farmers must show willingness and ability to use credit productively for farm development. As observed by Penny (1968) in Indonesia - "It is not capital or credit they lack, but the motivation to use resources for development. Until governments realise this point, and act accordingly, money will continue to be lent to farmers without a corresponding increase in production."

Therefore, while adequate arrangements are being made for small farmer credit, attention should simultaneously be paid to certain conditions which will enhance the usefulness of the credit. These conditions are examined in the next section.

2.3 PRECONDITIONS

An important policy question is whether credit should be used as a first tool to initiate development or whether other action

should precede it. Experience (FAO, 1975) indicates that credit can seldom be used to initiate more productive methods. Donald (1975) emphasizes that financial resources provide only part of the answer. Its use thus appears to be chiefly to extend the use of better technologies once these have already been introduced. There are, however, some basic preconditions for the effective and profitable utilization of farm credit. Donald summed them up in the following sentences "For the success of a credit programme more than money is needed. There must be a new technology, markets that can supply additional inputs and absorb additional output, institutions willing to lend to small farmers on terms the farmers consider attractive, and, perhaps most important, farmers willing to borrow, to invest and to repay loans." Some of the preconditions are discussed below.

For a credit programme to lead to greater output, there must be a desire on the part of farmers to invest more capital. Such a desire arises in a group of small farmers from the realization that there are profitable investments which they cannot undertake with their present holdings of capital. Such opportunities for investment arise out of a change in agricultural technology.

2.3.1 Viability of the Farming Unit

If within a given production structure farming itself is an uneconomic venture, then the chances of mounting a successful agricultural credit programme would be meagre, unless simultaneous measures are taken for reforming the production structure. Every farmer whether big or small, has to balance his total costs against total returns. His decision to invest would therefore depend on security of his expectations regarding costs and

returns. A viable credit programme can only be introduced if, at least in the long run, the returns exceed costs so that both principal and interest can be repaid with some profit margin.

What is often assumed profitable is, in fact, less so for the small farmer. A rigorous test of profitability for a set of improved practices in a district in India showed that over half of the demonstrations did not pay (Mellor, 1966). Oluwasanmi & Alao (1964) concluded that the farm credit schemes in Nigeria have only a limited effect so long as they are operated without due regard to the earning capabilities of the innovations being financed.

The need for adequate feasibility studies and investment appraisal cannot be overemphasized if the success of the credit programmes, which depend on the success of the individual farms, is envisaged.

2.3.2 Technology

Agricultural credit will be ineffective without a technology which is profitable to the farmer. Technology in farming is simply the way things are done; a given technology implies a given set of inputs or factors of production (Mosher, 1966). Thus, "traditional technology" means the particular way the traditional inputs of land, labour, seeds, organic fertilizer, hand implements, oxen and water are combined and used. 'New technology' is no more than a new set of inputs or factors of production which are different from the traditional set.

2.3.2.1 Traditional Technology Schultz (1974) has suggested that it is unprofitable to further expand the use of traditional technology. This implies that the farmers cannot significantly increase their farm production by either reallocating the resources at their disposal or by adding more of the traditional inputs (Mellor, 1966). A number of other studies have also reached this conclusion. For example, Eckert (1971) concluded that Pakistani farmers had achieved economic optimum levels of nitrogen use for native wheat varieties. Studies in Brazil also showed that it was not profitable to fertilize many existing crops (Meyer et al., 1973). This is primarily due to the very low production functions that exist for traditional practices. Thus it is not clear that any further expansion will increase a small farmer's net income commensurate with the added costs and risk involved in borrowing capital to finance such an expansion. Therefore it does appear, although not conclusively, that few profitable investment opportunities are available for small farmers when applying existing technology.

2.3.2.2 New Technology To assume that new technology is available or can be made readily available, if desired, to the small farmer is a great error. Worse still is the assumption that the new technology is always profitable where available.

Very often the new technology has not been locally adapted or tested under conditions similar to those faced by the farmer. Or, if shown to be physically better than the traditional, under local conditions such technology may be unprofitable. Tinnermeier (1974) has cited examples of profitable new

innovations in Zambia, Rhodesia, Mexico, Ethiopia and Columbia. On the other hand, his examples included failures or less than adequate results in some areas of India and the Philippines. Sacay (1973) found lower yields in rice during the dry season for the high yielding varieties as compared with the yields of the traditional varieties.

Therefore it should not be surprising to find slower rates of adoption of new techniques when additional risk is involved or when the technique is less profitable. Another cause of non-adoption could be the unavailability of technical and economic information on the use of the technology as was the case for fertilizer technology in wheat and corn production in Argentina (De Janvry, 1972).

Thus, to assume profitable technology is available especially to the small farmer, is very questionable. A small farmer is not always assured a profit above that found in using traditional varieties. The factors which determine proftability are many. These include "relative prices of inputs and products, land tenure arrangements, knowledge and skill of the farmer, risk, and the transportation and marketing systems" (Schultz, 1964). The type of technology required, therefore, must among other things aim at output increasing or cost-saving or both.

The added risks associated with new technologies are worth mentioning. Small farmers face a number of risks which can significantly affect the extent to which they adopt new technology. Since they cannot accept risks which might jeopardize

their families survival, their economic decisions attempt to reduce risk and to increase security. In fact Naidu (1964) argued that increased farm investment will take place only when risks are removed from the minds of farmers.

In conclusion one can say that when a new technology is understood by the farmers, perceived appropriate, and proved profitable in their situation, capital requirement assumes importance. In this circumstance, the absence of capital and credit would be an obvious bottleneck to the adoption of the new technology practices.

2.3.3 Extension Services

Because of the prevailing farming practices and social systems in developing countries, the establishment of an efficient extension service, adapted to the social and economic conditions of each country, is essential for agricultural development and rural progress. However, its effectiveness is often hindered by the farmers' lack of capital to implement the recommendations of the extension worker. On the other hand, to supply capital to the farmers without ensuring adequate utilization of labour and farm resources, often results in repayment defaults and large losses for credit institutions.

Both extension, credit and other relevant services all aim at one particulur purpose; to help the farmers increase their production and income in order to improve their living standards. Therefore the approach to successful agricultural development should be the integrated provision of these services to the

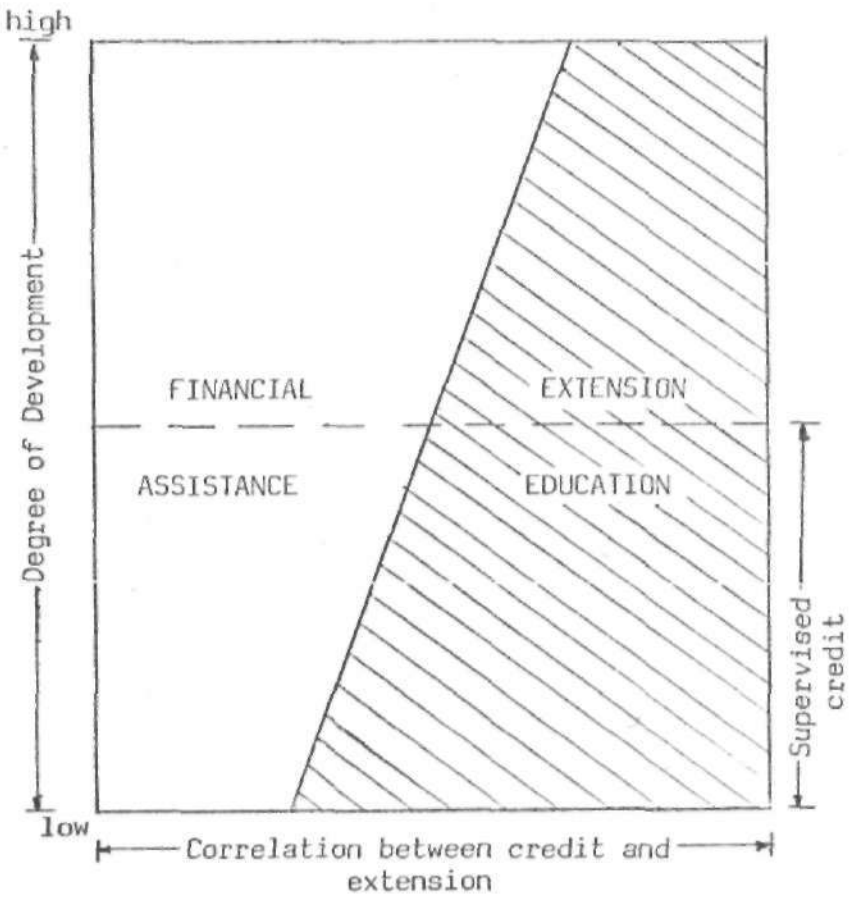
small farmers. In other words, to have an adequate impact on agricultural production, provision of credit should be accompanied by, and coordinated with, a sufficient amount of technical advice. According to Tinnermeier (1973), "Extension *is the mechanism by which the new technology is developed*, modified, carried and translated to the farmer in coordination with the provision of credit, when needed".

The tremendous success of the integrated approach between credit and extension has led to the concept of supervised credit. It has been defined by Belshaw (1959): "Supervised credit is a technical term to describe a particular system of credit provision aiming at improving both production and family living, which coordinates credit provision with extension services and aims at effective supervision, but usually goes further, for example, in making improved provision for marketing and other ancillary services".

FAO (1966) asserts that agricultural credit and agricultural extension, each in its own way, exercise great influence in the rural areas of developed countries when farmers have a high level of education and 'know-how'. But in the newly developing countries they should be properly coordinated, so as to render credit an effective instrument for promoting economic and social progress.

Figure 1

Relationship of credit and extension education in credit programmes for developing areas



The diagram shows the relative importance of credit and extension education in agricultural credit operations in developed and developing areas.

2.3.4 Input Supply and Marketing Facilities

Ideally, the new investments must be sufficiently profitable to overcome the small farmers' innate conservatism toward risky new ventures. And profitability depends upon the price and availability of inputs, and access to markets for sale of the products, and of course their prices. A credit financed expansion in the demand for inputs, not matched by additional supplies, will only produce a rise in prices, not an expansion

in output. Correspondingly, any fall in the price of the product in response to additional output will lower the profitability of innovation to the farmer.

When credit is provided in kind it is essential that the inputs (fertilizers, seeds, etc.) needed to adopt the new practice should be made available in the villages at the proper time and in the amounts required. FAO (1965) discussed the unsatisfactory handling of these factors. Since smallholders can seldom store their stock very adequately, delivery at too early a date often results in losses of seed and fertilizer. Delivery too late, is of course, pointless.

The adverse impact of markets on adoption of new practices is mentioned in a number of country studies - in Ecuador by Guzman (1973), in Ghana by Goodwin and Selly (1972), in India by Hendrix (1973) and in Malaysia by Long & Hoover (1973). In the end it is the economic and not the technical potential which determines profitability and that in turn depends upon the adequacy of markets.

This does not exhaust the list of precondition factors. But suffice it to say that, unless these preconditions for successful use of credit exist, or are being created, extending credit to small farmers may be a disservice. They may become burdened with debt obligations with little, if any, increase in their incomes from which to repay, while the lenders are faced with a difficult collection problem. Mosher (1966), who aptly labelled production credit an 'accelerator' rather than an

'essential', for agricultural development emphasized that where proper conditions already exist, well-managed production credit can give agricultural development a strong boost by accelerating the rate of adoption of improved technology by farmers. Galbraith (1952) adds, "At a certain stage in agricultural development agricultural credit clearly does become a strong force for further improvement - when a man with energy who lacks only the resources for more and more efficient production is enabled by the use of credit to eliminate the one block on his path to improvement".

CHAPTER THREE

SOURCES OF CREDIT

The major sources of farm credit supply can be classified into institutional and non-institutional (also regarded as private or informal).

3.1 NON-INSTITUTIONAL CREDIT

Sources of private credit include personal savings, loans from friends and relatives, moneylenders, merchants, etc. In most developing countries the private or non-institutional sector is a very important source of credit. In a study of agricultural development programmes in Nigeria, Ijose (1972) found that private credit sources still dominate the small holder credit environment, forming about 88 percent of the total credit received by farmers. In the Western and Kwara States of Nigeria, Miller (1975) shows that the credit corporation provided only 2.9 percent of the credit used by 302 farmers in 1973, while friends and relatives supplied 57.8 percent, moneylenders 24.4 percent and traders/merchants supplied 14.9 percent. Commercial banks did not provide any loans to these farmers.

The All-India Rural Credit Survey shows that some 70 percent of loans in rural areas were supplied by moneylenders and only six percent came from co-operatives and government agencies (see Table 3).

The private sources of credit are usually criticised because of the interest rates which are generally high (some 20 - 100 percent per annum). In some cases there is a de facto agreement that the farmers' products will be sold to the lender. But despite the higher interest rates charged, many small farmers prefer to borrow from the private lenders. Farmers are of the opinion that private credit sources have the advantages

of being quicker, more personal and informal and above all, can be obtained next door without unnecessary red tape (see Nisbet, 1973).

Table 3

Sources of agricultural credit in India

Source	Percent of farmers borrowing
Professional moneylenders	45
Agricultural moneylenders	25
Relatives	14
Traders and Commission Agents	5
Government Agencies	3
Co-operatives	3
Consumers	1
All other sources	4
Total	100

Source: Reserve Bank of India
in J. Mellor, 1974

Some experts have noted some useful reasons for the successful operation of these non-institutional lenders. They believe it is easier administratively and more efficient economically. The points follow:

1. Lower risk premium

Because of proximity, the moneylenders have full details about the farmers in the area - as to character, previous credit transactions, farming activities, degree of entrepreneurial capacity, etc. Thus the moneylenders have a comparative advantage over formal institutions with regard to this differential

access to information. They are therefore able to choose for themselves the low risk farmers. Acquisition of this information would be very costly for an urban institutional lender.

2. Lower collection costs

Typically it is not as difficult for informal lenders to collect outstanding loans as it is for institutional lenders (Wharton, 1962). The informal lenders know the true financial condition of the borrower, where he can be found, who his relatives are, etc. He can apply indirect pressures through local religious, political and economic forces where collection becomes difficult. These facts combine to lower the costs of repayment collection.

3. Lower transaction costs

Bottomley (1963) and Long (1968) have shown that fixed and variable costs are typically lower for the non-institutional lender. He does not employ any staff or rent any office or purchase special equipment as do the institutions.

Disadvantages

Apart from the exhorbitant interest rates mentioned above, there are some other disadvantages of the non-institutional lenders.

There is an absence of supervision of the agricultural activities. The moneylender possesses no technical agricultural knowledge himself and thus cannot offer any. Consequently, there is no defined development goal inbuilt into the system for the economic improvement of the farmers. Nisbet (1971) also observed that "the informal lender could prefer to maintain

the economic status quo or actually to promote the decline of the client so that he might acquire real assets or accumulate labour services". Thus this system tends also to worsen the already sensitive problem of income distribution.

Although the disadvantages of the informal lenders are quite apparent, it will take many years before the institutional sector reaches large segments of the rural population. Informal lenders will therefore continue to be an important source of credit ready to serve them. To eliminate the informal lenders will be to reduce the little source of finance meanwhile available to many small farmers.

3.2 INSTITUTIONAL CREDIT

The institutional sources of credit include government agricultural development banks, cooperative societies, commercial banks. Government activities predominate in this sector because for some years now, many LDC governments have come to realise that rural economic development will often start with agricultural development. Thus in an attempt to help the farmers and to overcome some of the problems and inadequacies of the private lenders, many governments have established agricultural credit systems. A number of success stories have been recorded (Goodman and Selly in Ghana; Nnebe in Ivory Coast; Frederickson in Uganda). On the other hand quite a number of failures have also been observed too.

Government credit institutions have often been seriously criticised for untimeliness in delivery of loans and inputs,

unnecessary bureaucratic measures, inability of setting up effective repayment collection machinery, insistence on provision of collateral.[1] Nisbet (1971) in a survey of attitudes among farmers in Colombia found that, despite the higher interest rates, more preferred to borrow from the moneylenders than from the banks; their complaints were that institutional programmes involved too much "red tape", were too slow, too rigid as regards payments, etc. In a detailed study of the 'true' cost to the farmer of official credit in East Pakistan, Shahjahan (1968) concluded that a combination of application fees, travel and entertainment costs and loss of working days in getting loans made public credit as expensive as private borrowing. Nehman (1971) reached the same conclusion in his study in Southern Brazil.

Effort is therefore devoted in this section to looking at the criteria for success and the problems of credit institutions.

3.2.1 Criteria for Success

1. Clarity of objectives

Perhaps one of the first requirements for an effective institution is that its goals, procedures and evaluation criteria are specific and understood. Tendler (1973) has summarized the objectives of small farmer credit programmes under three broad categories:

> "One has to do with the economic efficiency of the activities financed by credit, a second with the ability of the programmes to serve a hitherto neglected portion of the rural population, and the third with the viability of the institution through which the programme funds are administered."

According to Brake (1973) the clarity of objectives is one of the reasons why 'project' type credit seems to have been relatively successful. With the project approach development objectives of the projects are generally clear. The same point is probably one reason why government agency credit is so often not successful. The purpose is less clear. The government personnel may see their objective as one of getting funds out into the rural areas without proper arrangements for collection of payment.

2. It is necessary to separate the welfare purpose from the credit purpose. A credit institution expects repayment; a welfare agency does not. Both functions have merits but attempting to include both in one agency may well destroy the institutions ability to perform the credit function.

3. There must be potential borrower benefits from the use of credit for a small farmer credit institution to thrive. Simply providing credit to small farmers is not sufficient to build a viable credit institution. Greater production leading to increased return is probably the main benefit.

4. The culture and society must be receptive to the credit concepts. If the culture accepts non-repayment of institutional debts as a norm or if there are no sanctions available against defaulters, credit institutions cannot be effective.

Therefore, if a credit institution must survive and thrive, it must be able to specify its objectives, make the funds available to the farmers at the proper time, help them increase

their income hence their repayment capacity and be able to recover the loans for further advances.

3.2.2 Organizational and Operational Problems of Credit Institutions

The organizational and operational inefficiencies are the basic reasons why small farmers opt to borrow from private sources. The causes of these inefficiencies are discussed below.

1. Structure - has two aspects

a) Bureaucracy:- A diffusion of decision making authority leads to inefficient operation - there is excess paper work on the one hand and multiple level decision on the other. Having so many different levels of decision making before loans are approved leads to untimely release of funds. It opens opportunities for political meddling in purposes and procedures of the institutions and results in high administration costs and inflexibility of programmes.

b) 'Top-down' implementation system

Generally the boards and committees of the institutions are composed of 'government people' who set the policies. There are hardly any instances where there is a clientele representation in any of these committees.

Rural cooperatives, and project type credit schemes (e.g. Gezira Irrigation Project) tend to be organized with a degree of local clientele-participation. These are generally schemes which have been looked upon as successful cases. The need for clientele participation is basically two-fold.

i) Communication - it permits a two-way communication

so that the clientele group can be heard on policy matters. Programme objectives and rationale can be interpreted to the group by one of their own.

ii) It helps make "their" institution "our" institution. 'They' start to become 'we' (Brake, 1973). This helps simplify the repayment problem.

One bad effect of the "top-down" implementation of the programme is that the institution's employees look to the top for support and reward rather than on the clientele for service and efficiency.

2. Problem of Personnel

The success of cooperative organizations in Western Europe has been partly attributed to the selection of specialist managers. In the LDC's too little time is spent in training by persons who are to become managers and supervisors. In some cases, top officials might be appointed on political grounds. In others civil servants are posted to manage these institutions. Ugoh (1973) in his criticism of this approach says "usually, a successful civil servant is one who can muster ten good reasons why no action should be taken on a matter". Under such circumstances one would expect anything but the best from these institutions.

3. Accounting and Book-keeping Procedures

There is need for accurate and up-to-date records of the institutions' activities. The records will help in measuring efficiency, avoiding high rate of default and planning future

transactions. Brake asserts that "Book-keeping needs to be systematized so that the institution can differentiate between loans that are simply past due and those that are likely to be uncollectable."

4. Co-ordination and Co-operation

If the credit institution does not, itself, provide farm inputs, technical assistance and supervision, arrangements should be made with agencies which provide them. Lack of such arrangements may be part of the reason for untimely availability of inputs. Things work well where this cooperation exists but there could be a battle between the credit institution and extension agency or technical supervisors, for example. In some cases the other service agencies may not have reached such an advanced stage to be efficient.

5. Untimely Release of the Loan

This is a perpetual problem in most institutions. Obviously, funds for fertilizer and other inputs do little good if received months after the planting date. Having the credit approval decision at local level can help to alleviate this problem since the local manager is more accessible to prospective borrowers. He can recognise their problem when they complain that they need their seeds and fertilizer at planting time. But if all he can say is that he sent the application to the main office one month earlier, the farmers will lose faith in the programme.

6. The Cost of Small Farmer Credit

This major issue is discussed in section 4.2. Therefore only remedial approaches open to institutions will be mentioned here.

a) Institutions could charge interest rates commensurate with the risks and costs involved.

b) Loans could be made available to groups instead of individual small farmers.

c) The overhead costs of supervision and technical assistance could be separated from the credit costs and regarded as a cost of development policy. This is a social function and can therefore be subsidised.

d) Simplification of the system.

7. Repayment of Loans

This is one of the greatest problems facing the institutions and has been discussed in detail under section 4.4.

3.3 CO-OPERATIVES

Group credit has been broadly defined as:

> "non-individual credit in which funds for productive purposes are extended to groups of farmers joined together in some sort of associations, cooperatives, credit unions, users' societies, etc., and where such organisations play a role in the securing, managing, using and repayment of such funds." (Miller, 1977)

Because of the difficulties of reaching the small farmers in the villages, and the high administrative costs of making and

supervising small loans to individual farmers, various forms of group loans have been tried in developing countries. Credit Cooperative organisations have been successful in most countries of Europe e.g. Raiffeissen Cooperative organization of West Germany, Swedish Federation of Farmers Cooperatives. Some credit administrators have believed that such measures mean automatic success in the LDC's.

Examples are not lacking in LDC's where cooperation has been successful. "In Bangladesh the belief was that Comilla[1]-type cooperatives are the only viable vehicle for fostering significant progress among small farmers and that any service provided for small farmers - certainly credit - should come through cooperatives". (Stepanek, 1973). Goodman & Selley have clearly shown how the Agricultural Development Bank of Ghana has through special group and cooperative credit schemes for specific crops - maize and rice - achieved significant improvements in the production of these crops. Nnebe (1972) has demonstrated that in Ivory Coast, the CENAPEC has through the promotion of agricultural crops achieved an "increased agricultural production and better commercialization of products."

However, it should be recalled, as one of the pioneers among the developing countries had to admit, after some 50 years of cooperative effort, that cooperative credit as a mass movement failed. This failure was mainly due to the fact that Western policies and methods had been copied instead of having been

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[1] Comilla - a cooperative organization in Bangladesh.

adapted to the prevailing rural socio-economic pattern. (All India Rural Credit Report vol. II, 1955). Miracle (1972) has also asserted that " . . . little more than a handful of the several hundred cooperatives that have been attempted in LDC's have been successful. There are a number of reasons for this strikingly poor record but essentially in LDC's cooperatives have typically been attempted in situations where the necessary preconditions did not exist."

Thus an enormous amount of effort and money could be saved, and development of agricultural cooperatives and agricultural credit could be much faster, if the authorities in many LDC's could avoid the mistakes already recognised elsewhere.

3.3.1 Potential Advantages

The general advantage of group loans is that they are a method by which farmers who would not otherwise get institutional credit are enabled to do so. But more specifically the advantages include:

1. There is an opportunity for reduction of supervising and administrative costs. Having to deal with just one person or one committee rather than a large number of individual borrowers is a very pertinent factor in reducing costs. In a Malawi development project it has been estimated that making loans on a group rather than on individual basis would lower the interest charge required to break even on the credit operation from 23 percent to 13.5 percent (Alexander & Scott, 1974).

2. Loan repayment rates may be improved through the group's

responsibility for repayment, its ability to apply social pressure on delinquent members and the facility with which the group may be able to deduct loan repayments from the proceeds of marketing the borrowers farm products. S. Ugoh (1973) has clearly demonstrated this possible advantage.

3. The group also may constitute an effective organization through which deliveries of inputs could be made in larger lots, products marketed more profitably and education programmes on improved practices for wise use of the loan could be conducted. "Cooperatives which combine credit and the supply of farm requisites to their members with the marketing of their produce represent a highly satisfactory method of extending loans to farmers at a minimum risk." (FAO, 1964).

3.3.2 Criteria for Success of Group Loans

Group loans should be an effective method of providing small farmers with the necessary capital to adopt proven agricultural techniques leading to increased economic return. But, inspite of the potential advantages of group loans, their success is by no means assured. Some conditions could be cited as necessary for success.

i) There should be a viable group, or the potential to form one, which can work together, for the achievement of their common economic and social interests. Groups formed primarily for the purpose of obtaining a loan are less likely to succeed.

ii) There should be competent management and just and able leadership within the group to

administer a loan fairly and honestly, and to keep adequate records of disbursement and repayments.

iii) Access to profitable technology should be assured. The need for availability of necessary inputs and knowledge of how to use them cannot be overemphasized.

iv) Enterprises for which loans are granted should be economically viable so as to ensure returns permitting repayment of the loan and also profit to the farmer.

v) There should be proper arrangements for the marketing of the products and collection of the repayments at the time the products are sold.

vi) Jack Dublin (1973) suggests that "perhaps the single most important contribution cooperatives can make under these circumstances, is to help motivate poor farmers to find new ways of using their own resources with whatever assistance they can get from their governments to develop sound credit programmes."

This statement has some relevance to the basic principles of adequate cooperative spirit - that of some people coming together to help themselves through their own joint effort. Total dependence on government support will likely lead to failure. FAO (1965) emphasizes that " . . . as a result, the interest of the members in the well-being of their cooperative

societies is more often than not, relatively weak or even non-existent and their preparedness to make sacrifices for the economic interests of the group is usually still weaker. For the same reason, mutual supervision which is the cornerstone of the credit societies of the Raiffeissen[1] type does not play an important role either."

Actually, a difficulty exists in setting a limit to the extent of state control, guidance and finance of co-operatives. On the one hand, in the early years of cooperative development the control is necessary; on the other, the continuous and prolonged dependence of cooperatives on the government is bound to retard the growth of the spirit of self help.

It is stressed that, in their desire to achieve rapid success in the establishment of cooperatives, the governments should not neglect the combining of such a short-term policy with a long-term policy of organising, from the outset, adequate cooperative propaganda, education and training which, in due time, should produce an independent and self reliant movement.

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[1] Raffeissen is the national cooperative organisation in West Germany.

CHAPTER FOUR

POLICY ISSUES

4.1 SUBSIDY

In most countries of the world farmers routinely benefit from some kind of government subsidy. Subsidy has become one of the strategic issues in developing policies for small farmer credit in consideration of how much if any subsidy to this activity is justified and how much should be applied.

There are two avenues for subsidy - direct and indirect subsidies.

4.1.1 *Direct Subsidy*

This involves "an alteration to the price structure of a farmer's actual transactions"(FAO, 1975). These include the prices paid by the farmer for inputs and for credit (in this case the price paid is the interest charge) and the price received by the farmer for his produce.

4.1.1.1 Low Interest Rates (Subsidized Credit) This is probably the easiest to apply of the direct subsidies. Unfortunately in most circumstances it is also the type which has most disadvantages. I have therefore chosen to consider interest rates in much greater detail than other aspects of subsidy; in addition it is one of the most topical issues in credit programmes.

One of the most important differences among various classes of lenders is the disparity in the rates of interest charged on loans. The most prominent feature is the high rates charged by some informal lenders and the very low rates that formal lending institutions charge.

FAO (1975) maintains that in many direct programmes the interest rate charged on seasonal loans should be of the order of 25 to 30 percent, if all the costs involved are to be covered. But the interest rates in small farmer credit programmes are very much lower than this and, indeed, are often lower than the rates charged in other sectors of the economy.

Several arguments have been advanced in order to justify this policy. The grounds for justification include:

i) that small farmers have been exploited by various types of lenders who charge exhorbitant rates of interest, pay low prices for products purchased and ask high prices for inputs sold (Wharton, 1958).

ii) that traditional farmers need special inducements to use highly productive inputs, and that only highly subsidized credit will induce them to adopt modern technology.

iii) that low interest rates are a mechanism for income transfer to small farmers.

The above arguments have been dismissed in the following criticisms:

a) Where interest rates are lowered in an attempt to displace the informal lenders to the advantage of small farmers, the larger farmers who have better political, social and economic relationships with the institution officials tend to benefit more than the small farmers.

> "Subsidized credit which is captured by larger farmers creates conditions for the further exploitation of the small farmer, to the extent that its beneficiaries will use the funds borrowed from the lending agency to buy additional land and to displace small farmers in the purchase of scarce inputs." (Gonzalez-Vega, 1973)

This situation is also applicable to cases of subsidized inputs.

b) Reluctance on the part of a farmer to borrow and adopt new technology might be due to:

i) absence of appropriate technology;

ii) lack of profitability derivable from the technology;

iii) unavailability of certain inputs, existence of a bottleneck or the absence of a market for the product.

These obstacles might reflect imperfections that will not be removed by an expansion in the volume of credit. The distribution of credit at subsidized rates of interest might induce farmers to accept the 'gift' and to use the funds for consumption but it will not make the missing technology or market available. Rates of default will then be very high and the programme will fail.

c) The use of credit as a mechanism for income transfer is very inefficient. The perception by the farmer that he is dealing with a 'welfare' programme designed to transfer resources to poor farmers will induce reluctance to pay even if he could. While the credit programme by its very nature expects repayment, the welfare aspect of the programme induces non-payment.

Negative Impact of Low-Interest Rate Policies

As a mechanism for improving access of small farmers to credit, a policy of low interest rates presents several disadvantages some of which will be discussed.

1. A policy of low interest rates actually reduces the total volume of credit flowing into the small farm sector. This is because the policy means a relatively low return to the programmes, which are thus forced to continually rely on government and other outside sources of funds to subsidize the small farmer credit and cannot themselves compete efficiently for funds.
2. At the rate of interest set, there are more potential clients willing to borrow than those who could be satisfied with the institutional resources available.

Some sort of non-price mechanism for rationing them becomes necessary. The lending institution is forced to 'select' according to some arbitary set of criteria the beneficiaries of the credit programme. Often this leads to favouritism and corruption.

> "The high scarcity value of the limited resources that are being distributed at a price well below equilibrium generates the conditions for a black market price and leaves the lender vulnerable to pressures by the stronger farmers." (Gonzalez-Vega)

3. Low interest rates aim at reduction of the importance of informal lenders. In most LDC's it will take many years before the institutional sector reaches large segments

of the rural population and informal lenders will continue to be an important source of credit ready to serve them.

4. Low interest rates could induce the lending agencies to overemphasize their reliance on collateral requirements as criteria for selection. Collateral requirements restrict access to credit to only those who, prior to applying, own sufficient assets acceptable to the credit agency, i.e. to the wealthier members of the community.

4.1.1.2 Subsidies on Inputs The subsidization of inputs appears to be an attractive measure. It is adequate to popularize the use of new inputs and technologies by demonstrating clearly their productivity and profitability and encouraging the farmers to adopt them.

It may sometimes be useful to reduce the cost of inputs for a limited period of time. This has the effect of reducing risk of the innovation to the farmer and also reduces working capital requirement during the introductory phase. Sometimes a government may decide to subsidize farming in a particularly disadvantaged area or region, as is popular in the West European countries, through this means.

However, because subsidies on inputs suffer from many of the disadvantages associated with subsidized interest rate, there is need for carefulness in administering them. There is likely to be allocative problem because of the need for rationing.

4.1.2 Indirect Subsidy

By this approach, the government offers subsidy in disguise

to the farmers by provision of services such as education, research, advisory services, profitable technology, necessary infrastructure, etc., etc. This method does not suffer from many of the disadvantages of direct subsidy. Donald (1975) has highlighted this point:

> "These do not in themselves distort market forces but tend to assist them. They tend to reach target groups of small farmers with greater certainty. To be sure, the extension agents do have a tendency to spend more time with large farmers than small farmers, but this weakness is in some degree remediable. And generally speaking, services do not involve governments in such large and unpredictable expenditures as do market subsidies or the provision of public capital."

While it may be claimed that subsidized services are likely to prove more productive than subsidies in support of low interest rates, this does not mean that services are the only vehicle appropriate for subsidy or that they can accomplish what is needed in isolation.

4.2 THE COST FUNCTION OF CREDIT DELIVERY

In view of the disadvantages of the specially low interest rates, there is need to set a level that will lead to a successful credit programme. Successful, with respect to viability of credit institutions and a programme in which a small farmer is placed in a position where he can improve his income and standard of living. For an objective consideration of the interest rate, the costs of running the programme

deserves attention.

4.2.1 Opportunity Cost of the Resources Loaned

The prevalence of alternative development programmes in developing countries makes the opportunity cost of small farmer credit very high. However, this is seldom apparent to credit institutions. Institutional lenders usually receive funds at a rate which is already subsidized, either through special facilities at the central bank or from international agencies.

> "Public credit agencies customarily obtain their lending funds from their governments at concessional rates ranging from zero to, perhaps, 4 percent." (Donald, 1975)

The opportunity cost is more evident to informal lenders. When a moneylender lends a pound to a farmer, he has to be satisfied that he does not have a better use for it. This opportunity cost is equal to the return that the moneylender could obtain in alternative investments, after risk and administration costs are taken into account.

Differences in private opportunity cost, however, should not obscure the fundamental fact that the social opportunity cost of capital is very high in LDC's. If only for this one would expect much higher rates of interest than those currently quoted.

4.2.2 Administrative Costs

These are the expenses related to the process of granting, supervising and collecting the loans. These expenses usually

take the form of wages and salaries, purchase of supplies, materials and equipment, and transportation.

A low volume of operations at a given lending office which cannot fully utilize its capacity to administer loans increases average costs. Generally, the larger the loan, the lower the costs per pound or dollar loaned. The amount of paper work and time spent in processing a loan is more or less the same for loans of different sizes. Loans officials are frequently required to spend more time with the small and illiterate farmers who cannot fill in their application forms correctly, while large farmers more familiarised with banking practices require far less attention. Equally expensive are the visits to the farms - a greater number of visits are required for the numerous small farmers.

In addition, the cost of gathering information about the farmers can be described as administrative. This tends to be higher for institutions than for moneylenders who are already familiar with the farmers.

Bottomley (1963) concludes that:

> "As long as individual farmers remain small operators with relatively petty needs, and perhaps, intermittent reluctance or inability to repay, they will go on borrowing in small amounts each of which will require time to negotiate and recover, and the administrative costs of each dollar loaned will continue to be high."

4.2.3 Costs resulting from Losses due to Defaults and Delinquency

The risks that every lender has to consider include

a) objective risks - deriving from events that might make it impossible for the farmer to pay back the loan and which are not within his control e.g. a flood or death.

b) personal risks - that depend on the farmer's ability to produce income - his entrepreneural capacity - as well as on his character and attitude towards repayment. These are the types of risks which the lender can reduce through proper selection.

There is thus a tradeoff between administrative costs and losses due to default. The collection rate will be higher the more carefully the agency selects and supervises its borrowers but this entails high administrative costs.

Definitely, if all due considerations were to be given to the costs involved in administering a loan, the rate of interest would be pitched too high. While FAO (1975) estimates 25 - 30 percent, Donald puts it at 22 - 35 percent, World Bank 19 - 22 percent and Long (1973) at 60 percent.

However, interest rates should not be pitched very high simply to avoid the disadvantages of low interest rates or to cover all the costs of loan administration. For example, full costs of actual defaults should not be covered by lending charges. In principle it would be far better to reduce defaults than to charge the repaying borrowers for the cost of their neighbours delinquencies.

The rate of interest could be left at the ruling bank rates but then adequate steps should be taken, for example, 1)

to reduce the risks involved in small farm agriculture by proper supervision and improved technology and 2) to set up efficient collection machinery.

4.3 RURAL SAVINGS

The level of capital formation in agriculture depends on the level of production of goods and services over the level of consumption. The extra income which is saved can then be used for further production.

Volume of production depends on the farmers' capacity to produce which in turn depends upon the level of technology, skill, motivation, level of education and other socio-economic factors. Among small farmers in the developing countries, the negative effects of most of these factors prevail resulting in little or no marketable surplus over consumption needs. Therefore the level of capital formation is very low and has led to a great deal of reliance on finance from outside the sector.

Clery (1975) has shown that owned capital constituted 85 percent and 89.5 percent of the total investment of UK agriculture in 1970 and 1975 respectively and the tendency is towards higher owner equity. In view of the key role of capital formation in agricultural and industrial development, it is surprising that LDC's governments have given so little attention to the promotion of savings in the rural areas. Penny (1968) has emphasized, "The main tasks of government bent on development are to mobilize capital, in both the agricultural

and non-agricultural sectors and to ensure that it is used in the most economic way, on and off farm."

Part of the assumption for this negligence which has been questioned by Adams (1973) is that small farmers do not have the capacity or the inclination to save, or if they do, the amount would be too small to justify the effort. Adams concluded that the data available are "strongly suggestive that substantial voluntary savings capacities do exist among farmers in the LDC's."

4.3.1 Importance of Savings

Savings are important for small farmer credit in several ways:

i) Rural savings are a potential source of loan capital.

ii) The incorporation of rural savings component in a credit programme can help to tie farmers to the programme fostering feelings of identification with the institution and a stake in its success.

iii) The stimulation of savings habit can make an important contribution to development generally, especially in rural areas where the demand always outstrips the supply.

It is generally accepted that development in the long term involves a transfer of resources (land, labour, capital) from agriculture to the industrial and service sectors of the economy. However, it is a matter of debate and of consideration of individual cases, whether the rural sectors should immediately

provide resources for urban development.

4.3.2 Need for Savings Institutions in Rural Areas

Cash savings by small farmers help continued development primarily by increasing the volume of funds available for investment. This is true whether the money is invested directly by the income earner or whether it is deposited in a credit institution.

Despite the possibility of direct investment of savings and the importance to the farmer of a contingency reserve fund, savings institutions have an important role to play in rural agriculture.

1. They provide a means by which monetary capital transfers can take place between sectors and within the rural sector. Deposits by cash surplus farmers are loaned to others who may have investment opportunities beyond their immediate capital resources.
2. An institution provides a safe facility for those depositors who already wish to save.
3. The existence of an institution may itself be an encouragement to savers.
4. Integration of saving and lending activities in same institution in a rural area, tends to change the farmers' attitude to that of commercialization.

4.3.3 Linking Savings with Credit

Where a credit programme is integrated with savings, it often results in a strongly based cooperative society. The

integration enables the society to raise funds quickly for the members and to generate repayment capacity. One recent example of an apparently successful credit/savings linkage is the cooperative savings scheme in Kenya (von Pischke, 1975). Also the renowned Comilla rural development projects in Bangladesh put great stress on savings as well as credit. Khan (1974) speaking on this issue said, "I look attentively at the response to the discipline of thrift deposits and repayment of loans. A cooperative movement depends on these two disciplines - thrift and repayment of loans. The cooperatives must accumulate their own capital. They cannot depend exclusively on money borrowed from the State Bank. And the cooperatives must repay the loans they borrow . . . simply to organise cooperative societies for distribution of loans is easy enough. The real test of their future strength is in the record of repayment."

4.4 LOAN REPAYMENT

Credit normally is used synonymously with borrowing and both terms imply that the transfer of funds from the lender to the borrower is temporary. Loan repayment is assumed. Small farmers consistently have delinquency problems which means either they can repay the loans but do not want to, or they are unable to repay the loan when it comes due without placing themselves in a worse condition compared with their status before the loan was obtained.

As has been indicated earlier, the informal lenders do not have much difficulty in collecting their payments. They can apply religious, social or traditional legal pressures; the loan

can also be repaid either in cash or kind.

Credit institutions face major problems in loan collection. In an ideal situation a government credit programme for small farmers should function as follows: the government or central bank loans money to a credit institution which in turn lends the funds either directly or through cooperatives to small farmers. The farmers use the funds to purchase productive inputs which are combined with family labour to produce more output. The additional output is sold and the proceeds are sufficient to repay the loan and leave the farmer better off. The payments received from the farmers by the institution are sufficient to regenerate lending capacity, to cover administrative costs and to pay the interest on the government loan. Such a programme consumes no resources; the money committed simply constitutes a revolving loan.

However, between the model and reality, something often goes wrong. There may be no increases in agricultural production following the credit programme in many cases. And because of a high rate of default the funds pledged by governments to agricultural credit do not regenerate themselves, nor does the interest received cover costs.

4.4.1 Causes of Non-repayment

The high incidence of default raises a number of questions concerning i) the economic criterion used in the granting of loans; ii) the accuracy with which farm plans and budgets which form the cornerstone of supervised credit programmes are prepared;

iii) the timing and procedure of debt collection and iv) farmers ability to produce and their attitude to repayment of debts to government agencies.

However, the following factors can be identified as some of the causes of delinquency (and eventual default).

a) Capacity and will to repay.

b) Overlending.

c) Inadequate technical assistance.

d) Political influence.

e) Natural disaster.

Capacity and will tn repgy

Tinnermeier and Finn (1975) observed in their study of the Plan Costa programme in Peru, that "farmers cultivating a relatively small area (less than 3.5 ha) showed higher delinquency rates than farmers cultivating larger farms (3.5 to 30 ha)". The poorer repayment performances of small farmers is undoubtedly related to their higher subsistence needs relative to farm income. Because of the size of their holdings, only small amounts of loans will invariably be granted them as was demonstrated by Ijose & Abaelu (1973) that almost 90 percent of loans granted by WNACC to small farmers were less than £40. The marginal return of such loans may not be able to supplement the farmer's subsistence needs and still leave him with enough to repay both capital and interest.

On the other hand, farmers tend to regard government loans as a hand out or their own 'cuts' of 'national cake'. They,

therefore, tend to develop an attitude of non-repayment particularly when they discover that the more influential members of their community have not paid back their loans.

Overlending

Two aspects of the method used to calculate loan size may tend to encourage overlending. First, where the loan size is calculated on the basis of the cost of all inputs, including labour, even when the farmer intends to supply all or most of the labour himself. Second, cost and revenue estimates may be based on the operations of the better farmers and, as such, tend to be high for the average borrower. An average farmer who receives a loan based on the above methods of calculation may find the loan above his immediate requirements. Where he cannot put part of it into productive use, he still has to pay for such part from the income of the productive part of the entire sum.

Inadequate technical assistance

Adequate technology has been stressed as one of the vital conditions of the success of credit programmes. Donald (1975) in a review of 'Spring Review Studies' showed that only a few projects provided profitable new technology, and these were programmes with high levels of loan repayments.

Much as one would accept the principle of repayment, its chances are increased if, the credit leads to increased output. In other words, if the loan beneficiary is helped, with improved technical assistance, to increase his output and income, his ability to repay becomes enhanced. In the case of FAID as reported by Ugoh (1973) it would appear that once they got an

acceptable security, they did not care whether the credit led to an increase in the beneficiary's output or not.

Political interference

Where political influence is allowed to interfere with the granting of agricultural credit, the credit institutions are often faced with difficult repayment problems. In Nigeria, Osuntogun indicates that some loans were made without any technical analysis of borrowers farming operations and even without clear cut identification of such borrowers as farmers. The Coker Commission of Inquiry into the affairs of certain statutory corporations in Western Nigeria, reported that many so-called farming loans went to board members, petty traders, and others who were anything but farmers. In a few cases, loans were even applied for and granted to dead persons. In such circumstances there can be no follow-up, and could result in losses of reasonable amounts of money. Frederickson (1973) reports that in Uganda such interference has led to the writing off of 130,000 dollars in bad debts.

Natural disaster

Natural environment and general standards of farming are still very prone to natural disaster. In the tropics, the rainfall regime sets a great limitation on farming. Droughts minor and major, occur from time to time and yields are affected to a greater or lesser degree depending on the degree of severity of the drought. With little or no crop insurance among the small farmers, any such incident could render them incapable of meeting their repayment terms. In research work carried out in four districts in India during drought periods, ICRISAT (1976-77) reports

"Compared to predrought years, indebtedness increased - by more than one-half in two districts, nearly tripled in the third and more than tripled in the fourth".

Crop and livestock diseases, and ill health or death of the farmer or a member of his family (source of labour supply) are yet another source of objective risks. With poor disease control, one could expect that, once in a while, an illness could seriously deplete the farmer's repayment capacity.

4.4.2 Security and repayment capacity

It has been argued that credit institutions should regard repayment capacity as the foundation of agricultural credit and as far as possible help build the farmers repayment capacity. To this end Binns (1952) has warned that those agricultural credit institutions which depend mainly on land as security will sooner or later be faced with the choice between becoming the owners of large areas of land, which they may find difficult to administer and selling them at, perhaps, a loss.

For short- and medium term loans security of landed property may not be required. But depending on circumstances, e.g. the amount involved, security should be necessary. As far as long-term credit is concerned experience (FAO, 1965), has shown that security of real estate is indeed, indispensable. It is difficult to see how credit institutions could provide long term credit of some 10 - 20 years or more, without having any other guarantee, for the due recovery of principal and interest, than the honesty of the borrower and the fact that, for the time being, he has a sufficient repayment capacity.

On the other hand, it is also true that the provision of long-term credit on the single consideration that the evaluation of the security offered by the applicant shows a sufficient surplus value, is as serious a mistake. Granting credit without ascertaining that the borrower has sufficient repayment capacity must unavoidably end in undesirable consequences for both the debtor and the creditor. Nevertheless, it lies in human nature to attach undue importance to tangible matters as compared with abstractions like repayment capacity.

4.4.3 Remedies

A general climate favouring repayment should be set as a strategy by a credit institution. In economic terms, the importance of technology, supervision and the improvement of farm productivity and income stand out conspicuously. If there is a favourable prospect it can not only raise incomes to enable repayment, but will enter into the reactions of farmers by giving them a stake in the success of a credit programme. The loss of access to new loans for delinquents will have more impact if farmers can see gains from the continued use of credit. Socially, the farmers can identify with such a successful programme and can feel it is theirs.

FAO (1975) aware of the extent of non-repayments in different countries have considered the following measures useful:

1. Repayment of loans should be linked as closely as possible to the marketing of borrowers' produce.
2. Independent internal supervision and auditing designed to

inform the responsible directors regularly on the situation regarding arrears in repayments of capital and interest on loans.

3. Direct, frank and constructive discussions with borrowers on ways of gradual reduction of overdue balances.
4. Prompt action against the deliberate defaulters.

Donald (1975) has suggested 'hard' and 'soft' approaches for the repayment disciplines. The 'hard' approach includes such measures as (1) and (4) above as well as denial of any further credit until previous debts are paid, threat of or actual forfeiture of collaterals, exclusion from advantageous markets for input purchases and product sales. 'Soft' approach concerns item (3) above which implies friendly, sympathetic consultation, with concession offered in some cases. Such concessions may include willingness to wait for various time periods until the borrower is better able to make payments, and having no further interest charges for the period of delinquency.

CHAPTER FIVE

NIGERIAN EXPERIENCE

5.1 USE OF CREDIT AMONG SMALL FARMERS IN NIGERIA

The general picture with respect to the use of credit funds among small farmers in Nigeria is shown in Table 4 below.

Table 4

Use of credit by 302 farmers in Western and Kwara states in 1973 (Miller) and by 95 farmers in Western State of Nigeria 1974 (FAO)

Farm use	Percent of total funds borrowed	
	(Millers)	(FAO's)
Hired labour	36.6	22.1
Fert., chemicals, seeds, insecticides	7.8	21.1
Cattle rearing	2.0	
Hoes/cutlasses	0.3	
Tractor hiring	0.8	
Miscellaneous	1.0	
	48.5	43.0
Non-farm use		
School fees	20.7	5.3
Ceremonies	11.5	31.6
Others	19.3	20.1
	51.5	57.0
Total	100.0	100.0

Sources: L.F. Miller (1975)
FAO (1974)

The two sets of figures show that the non-farm needs of the farmers exceed their farm needs. Among the farm items for which the borrowed funds are used, farm wages and the purchase of seeds, fertilizers, etc. constitute more than half the expenditure.

Tables 5 and 6 on the following page give an idea of the level of borrowing of these farmers.

Table 5

Distribution of the size of loans obtained by small maize farmers, Western and Kwara States, 1973

Size of loans ₦	% of loans
4 - 20	26.4
21 - 50	31.4
51 - 100	32.9
101 - 300	9.3
	100.0

Source: Miller (1975)

(₦1 = £0.78)

Table 6

Size distribution of loans made by 22 of the Local Loans Board in W. Nigeria 1957-1961

Size of loans £	% of total borrowers in each size group
20	57.7
21 - 40	31.6
41 - 60	4.5
61 - 80	3.4
81 - 100	2.8
	100.0

Source: Ijose & Abaelu (1972)

The following facts are apparent from the above figures:

1. The borrowings of the farmers are still very low in terms of size - most of them are below £100.
2. A greater percentage (above 50%) of the borrowed funds are used for non-farm activities.

With very many farmers requiring small loans, a greater proportion of which is used for non productive purposes, it will be extremely costly for any government institution to meet their

needs. An attempt to push out the private lenders from the financial market would lead to either not reaching the small farmers with credit or reaching them only at a loss to the nation.

The government institutions reach most of the farmers through cooperative societies and Ministeries of Agriculture via the on-lending scheme. As payment of labour wages and purchase of basic farm inputs are the major sources of farm expense; efforts should be directed towards cooperative supply of these inputs instead of direct cash dispensation. Labour costs and demand can be reduced significantly by organisation of machinery pools for hiring. This approach will create viable cooperative societies whose ultimate aim would be the supply of inputs and services to the members and the marketing of their products.

5.2 SOURCES OF CREDIT

5.2.1 Private Sources

Private lenders constitute the most significant source of farm credit for small farmers in Nigeria. Ijose (1971) noted that private credit sources still dominate the small holder credit environment, forming about 88 percent of the total credit received by farmers. Vigo (1958) stressed the importance of friends and relatives "there is an obligation among kindred and neighbours to help the needy and this makes the raising of small interest-free loans easy and fairly common". Table 7 (p. 60) also emphasizes the importance of private sources.

These data (Table 7 below) showing an almost complete reliance on informal sources of credit, point to a major deficiency in the institutional infrastructure serving these farmers. Present informal lenders are serving a useful purpose and will doubtlessly continue to be important sources of credit particularly in supplying the loans for non-farm purposes.

Table 7
Sources of credit

	% of total borrowing			
	Galletti (1958)	Ijose (1971)	FAO (1972)	Miller (1975)
Friends and relatives	50	7.7	57.8	25.3
Moneylenders	7	5.0	24.4	12.6
Traders/merchants	21.5	-	14.9	28.4
Credit corporation	-	8.2	2.9	8.4
Commercial banks	-	0.9	-	-
Own savings	-	31.3	-	-
Deferred payments to labourers	-	44.0	-	-
Cooperative unions	-	-	-	23.2

Sources: 1. Galletti, Baldwin, Dina (1958)
2. Ijose & Abaelu (1971)
3. FAO (1972)
4. Miller, L.F. (1975)

But they can hardly be expected to provide either a major increase in credit supply to farmers or loans on terms needed to finance a widespread adoption of new technology - because as Ogunfowora et al. (1972) have pointed out, "Loans from friends and relatives are generally small and of short duration because they too have low financial base."

5.2.2 Credit Institutions

The first attempt at organised rural credit in Nigeria was undertaken in the Northern Region in the 1930's in connection with the introduction of mixed farming in the Savannah areas. These funds for the purchase of animal drawn ploughs and a pair of oxen were provided by the Native Administration.

The national government created the first nationwide institution for the provision of agricultural credit with the establishment of the Nigerian Local Development Board in 1946. In 1949 this board was replaced by three Regional Development Boards. These were in turn dissolved in 1955. In the West, the Western Region Finance Corporation took over the administration of credit to farmers. From the activities of this corporation it became evident that merely making money available to farmers without adequate supervision and application of proven management techniques does not guarantee its effective use and beneficial results (Ogunfowora et al., 1972). In 1964 the corporation was dissolved and Western Nigeria Credit Corporation was established with the aim of reforming the agricultural credit scheme. Loans were granted on the basis of farm plans and financial budget and prospective repayment capacity was substituted for adequate collateral. Loans were granted to small scale farmers through their cooperative societies (Ijose & Abaelu, 1973).

Ugoh (1973) has given a good account of the operations of the Finance for Agriculture and Industrial Development (FAID) which was established in 1963 to serve as a source of credit for small scale private agricultural and industrial activities

in Eastern Region. Mid Western Agricultural Credit Corporation (1964) served the same purpose in the Midwest. In the North, the programme was administered by the Registrar of Cooperatives, whereby the government guaranteed loans granted by Barclays Bank.

Several attempts have thus been made to set up credit institutions. But generally, only a little measure of success has been recorded as a large proportion of farmers still have no access to institutional credit (see Ijose & Abaelu, Ugoh, Oluwansanmi & Alao, Oshuntogun).

Reasons for non-success are not different from those of similar institutions in other countries. They include:

i) insufficient funds to satisfy the demands of the farmers.
ii) time consuming and high cost loan processing procedure.
iii) inadequate consideration of borrower's repayment ability resulting in high rate of default.
iv) ineffective supervision and follow-up of the use of loans.
v) insufficiency of adequately trained personnel.
vi) political interference.

5.2.2.1 Nigerian Agricultural and Cooperative Bank (NACB) Limited

The Federal Government of Nigeria opened the bank in 1973 under the name 'Nigerian Agricultural Bank'. But the name was changed in 1977 into NACB to reflect the importance of cooperative activities

the bank was supposed to be involved in. It is a limited liability company, which makes it independent of the ministerial strings.

The bank was given a broad mandate to finance agriculture as evidenced by this statement of purposes for which it can grant loans.

1. To grant loans for agricultural production, and for purposes of storage, distribution and marketing connected with such production, to any state, groups of states or any state institution for on-lending to any farmer, group of farmer or body corporate subject to the state or group of states or state institution guaranteeing repayment of the loan.
2. To grant direct loans to individual farmers, cooperative societies or other bodies (corporate or incorporate) in appropriate cases, provided that the bank is satisfied that the schemes for which the loans are requested are viable and there is adequate security to cover such loans.[1]

Following from the above statement, it is apparent that the bank reaches small scale farmers through cooperative societies. Figure 2 (p. 64) shows the categories of customers of the bank.

Precautions taken to avoid failure

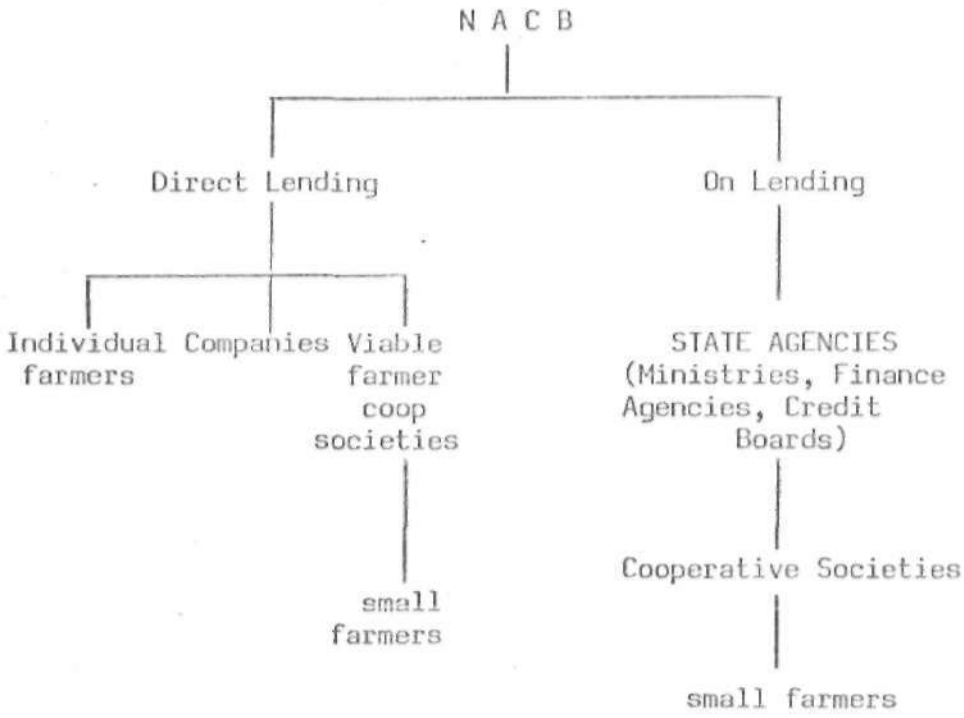
To avoid some of the mistakes of its predecessors the bank adopts certain measures likely to lead to its success.

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[1] NAB Guide to Applicants, 1973.

Figure 2

Operational structure of NACB



1. Clients - Though there are very many small operators needing credit in Nigeria, the bank deals directly only with large farmers, state government agencies, and viable cooperative societies. These are bodies who can provide adequate security and whose projects can be reasonably viable. However, small operators are not left out of the scheme as they are reached via organisations. As shown in Table 8 on-lending schemes account for about 50 percent of the total bank approved loans.
2. Costs - By the above approach, the number of direct clients is limited hence administrative and supervisory costs are reduced reasonably.
3. As much as possible, disbursements are made in kind to

minimize the opportunities for clients to divert NACB loan funds into activites other than those for which the loans are meant.

4. On-lending scheme - By granting credit facilities to state government agencies, the NACB is able to:

   a) give a wider spread of funds by reaching a large number of small farmers.

   b) combine credit with rural education, extension services and input supplies which are provided by the state agencies.

NACB lays emphasis on such matters as:

1. Easy access to input and output markets.
2. Adequacy of management.
3. Soundness of the project.
4. Availability of adequate security or guarantee.

Thus before the approval of loans, particularly direct ones, the bank takes the following factors into careful consideration.

1. Statutory ownership of land - Land disputes crop up frequently in many parts of the country and this can cripple the development of projects. It is therefore necessary that proper title deeds accompany applications where land is a major factor in establishment of the project.
2. Technical, managerial and commercial expertise for the execution of the project.
3. Size of holding:- This has two aspects - to ensure

viability and to avoid high lending costs. Small holders are therefore encouraged to benefit from on-lending schemes.

4. Nature of business: The bank does not lend to applicants who simply trade in agricultural products since this is regarded as exploitative and would normally reject applications for pure industrial projects. Other banks have responsibility for such projects (Nigerian Industrial Development Bank and Nigerian Bank for Commerce and Industry).

Interest Rate

The funds for the programme are provided by the Federal Government on loan to the Bank at two percent interest. NACB is given a period of grace of five years ending in 1980 when it is expected to start repayment of the loan funds at the interest rate. The bank's lending rates of five percent per annum for production loans and seven percent on marketing loans are less than that of commercial banks of 11 percent. The effects of these low and inflexible interest rates have been discussed in detail (Section 4.1.1.1). In Nigeria one can argue that if other constraints were removed most bankable projects can pay interest rates in excess of seven percent. Hence low interest rates may not be as important as ensuring the integration of other agro-services with credit schemes.

Security:

Much emphasis is laid on security. Understandably this is due to 1) risky nature of tropical agriculture and 2) the

fact that most farmers lack technical agricultural training and experience. The bank however expects that production loans for bankable agricultural projects should not be denied bona fide farmers merely because of lack of sufficient tangible securities for the loans. One would therefore expect that as agricultural technology improves in Nigeria, the bank would rely more on performance guarantee.

Operations

Tables 8 and 9 (below and overleaf, respectively) show the operational figures of the bank as at February 1979. In six years of operation one would have expected more approved projects. Oyinlola (1979) agrees that "the success of this programme in terms of number of farmers reached had been below expectation."

Table 8

Approved projects

Project type	Number 1979	Number 1976	Value of loans (1976) (₦'000)
Crops (arable/trees)	51	35	38,971
Poultry	50	29	3,204
Mixed farming	9	7	2,662
Cattle	12	2	717
Piggery	3	4	717
Fishery	6	4	3,259
On lending	58	19	50,146
Others	2	3	3,298
Total	191	103	102,975

NB: By 1979, 10 of the 1976 projects have been closed.

Sources: Oyinlola (1979) and Miller (1977).

Table 9

Volume of loans approved and disbursements 1973 - 1979

Amount in ₦'000

Year	Number of projects	Amount approved	Cumulative amount	Disbursement	Cumulative disbursement
1973/74	1	3,752	3,752	3,752	3,752
1974/74	47	46,831	50,583	7,713	11,456
1975/76	55	52,392	102,975	19,982	31,447
1976/77	67	162,805	265,780	40,527	71,974
1977/78	7	20,523	286,303	52,452	124,426
1978/79	24	28,935	315,238	40,144	146,570
Total	201	315,238	-	164,570	-

Most of the funds committed for one vegetative season remained unused for months and in some cases for years. The main reasons for this are lack of adequately equipped personnel and full understanding of the programme packages." The bank has only six branch offices to serve millions of Nigerian farmers. It would mean that some farmers have to travel hundreds of miles to the bank offices. This could rather be a deterrent particularly as loan decisions are still taken at the Head Office.

Repayment of loans due is not particularly attractive except for short term loans (Table 10). However with 35 percent of the total loan disbursed so far, repaid in advance, one would expect a good repayment record.

Table 10

Loan repayments as at 28/2/79

Amounts in ₦'000

Type of loan	Repayment due	Actual repayment	% payment of payment due	Repayment in advance	Total repayment
Short term	5,478	4,078	74	44,449	48,527
Medium term	8,876	2,752	31	11,160	13,912
Long term	4,702	2,119	45	1,691	3,810
Total	19,056	8,949	47	57,300	66,249

5.2.2.2 Agricultural Credit Guarantee Scheme

The Federal Government has realised the unwillingness of the commercial banks to extend their credit facilities to farmers because of the unduly high risk and uncertainty in farming. In 1977 it established the Agricultural Credit Guarantee Scheme Fund whose purpose is "to provide guarantee in respect of loans granted by any bank for agricultural purposes with the aim of increasing the level of bank credit to the agricultural sector"[1]. The limit of the guarantee is 75 percent of the amount in default, subject to a maximum of ₦50,000 in the case of an individual and ₦1 million in the case of a cooperative society or a corporate body.

As would be expected, commercial banks would insist on adequate security to cover the unguaranteed portion (25 percent) of the loan. The scheme clearly stipulates that "the security which may be offered to a bank for the purpose of any loan under the scheme may be one or more of the following:-

a) a charge on land in which the borrower holds a legal interest or a right to farm, or a charge on assets on the land including fixed assets, crops or live-stock.
b) a charge on the movable property of the borrower.
c) a life assurance policy, a promisory note or other negotiable security.

[1] Guidelines for the Agricultural Credit Guarantee Scheme, 1977.

d) stocks and shares.

e) a personal guarantee.

f) any other security acceptable to the bank.

Most small farmers cannot provide any of the above securities and therefore are eliminated from direct lending by the banks. Even if they would, the bank may not wish to lend to such farmers because of the high costs involved. However, the government has made provision for on-lending scheme in this instance.

An interest rate of four percent per annum is chargeable on loans to institutions which are to onlend to others, and six percent in all other cases. In a perfect financial market, the amount of money available for farm loans would be zero under the stipulated interest rates. But because of the regulation that at least six percent of the total annual loan made by any bank should go to the farming sector some credit must be provided.

As the banks do not receive 100 percent guarantee on the loans, and they are already placed at a disadvantage by lending at four or six percent interest rate, it means they have to be careful in granting any farm loan. Detailed project appraisal will become necessary, and this might lead to additional costs. The provision in the guidelines that "if a bank rejects any request for a loan under the scheme, the bank should give reasons for the rejection to the person making the request. It should also specify the steps the person should take to enable him to comply with the requirements" calls not only for an appraisal but for an agricultural manager who will carry out such an appraisal.

No reports have been published yet that will enable an assessment of the viability of this programme. The success of the scheme can be judged in the long run by the degree of effort it has had on the country's agricultural sector. In the short run, banks' profits may be adversely affected because of the low interest rates. To avoid any further losses in agricultural lending, one would expect a greater percentage of the loans to be made to large scale farmers.

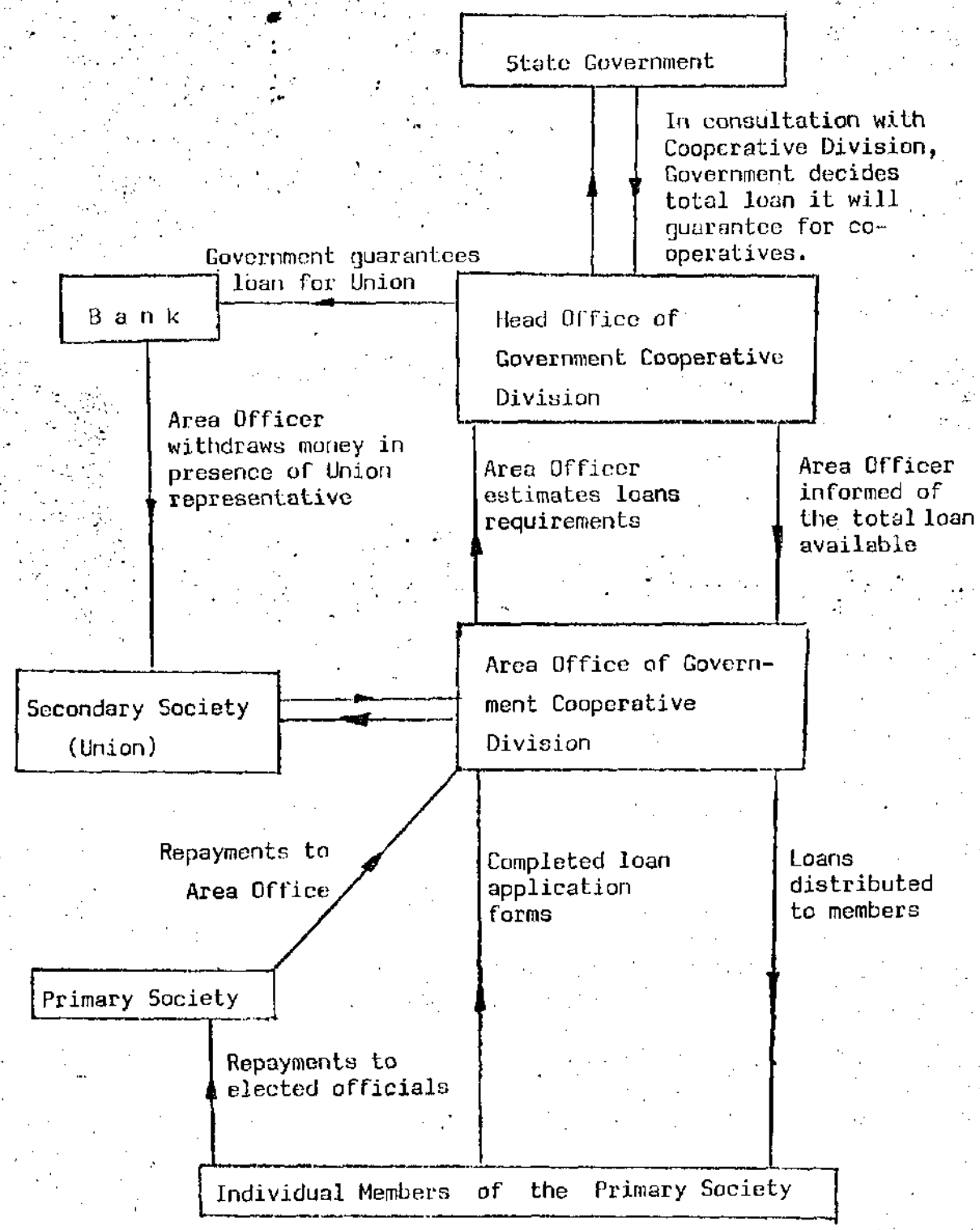
5.2.2.3 Cooperative Societies

NACB and the Agricultural Credit Guarantee Scheme have emphasized on some form of farmer organisation as a means of reaching the small farmers. Faced with a very large number of small farmers spread over a wide area, governments in Nigeria look for farmer organisation to facilitate their efforts in encouraging rural development. There is therefore no doubt that cooperative societies have an important role to play in Nigeria.

In the early stages of the societies government guidance and help would be sought but sight should not be lost of the aim of building an independent, self-financing society. A member of a cooperative should be able to deposit savings, receive loans, sell his produce to the cooperative which should resell it at the best possible price. The profits realised should be utilised in the upkeep of the society and to the benefit of its members.

Figure 3

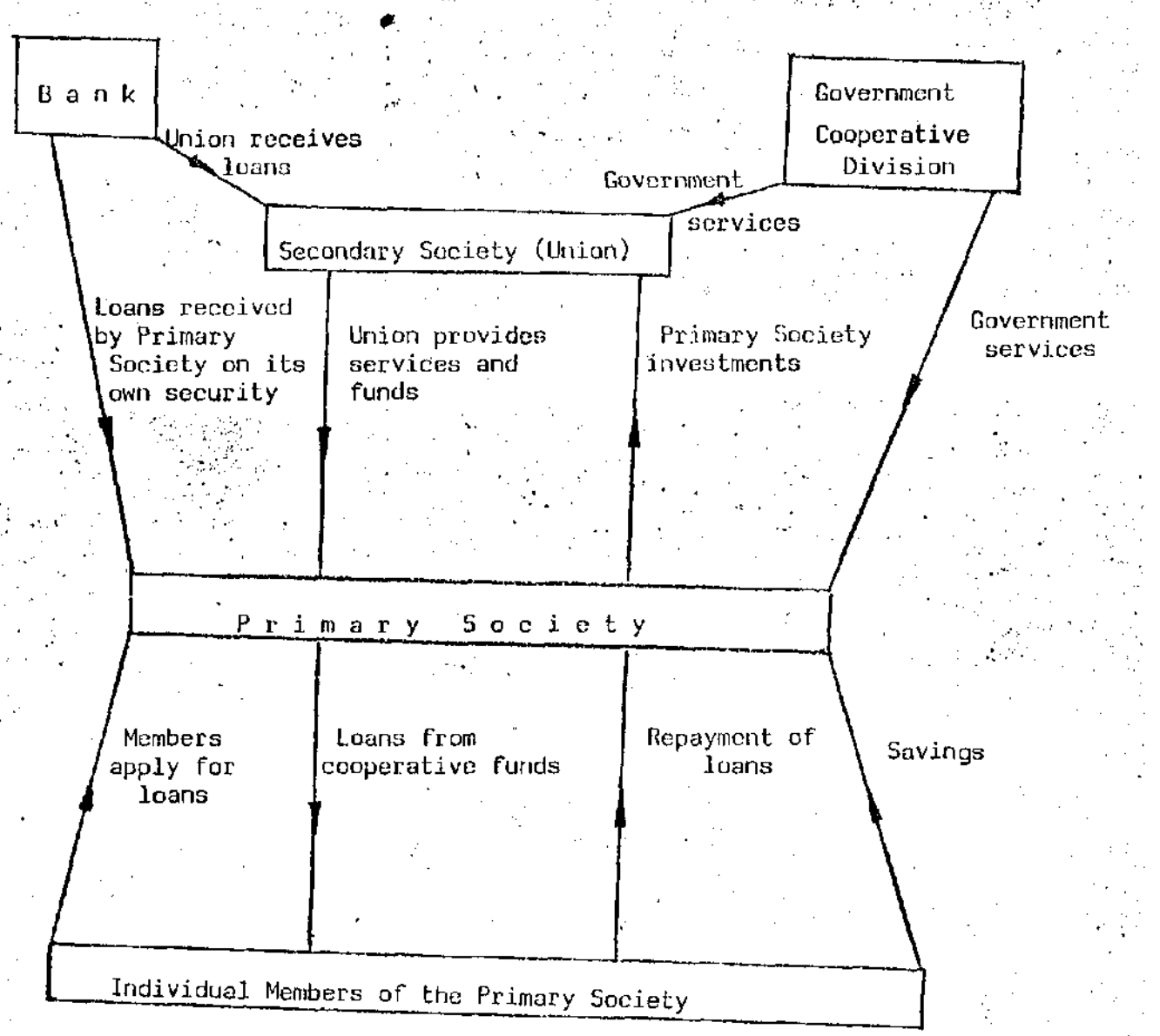
Cooperative Credit Policy in Northern Nigeria



Adapted from King (1976)

Figure 4

The Institutional Blueprint for Cooperative Credit



Modification of Figure 3

However, King (1976) discusses the type of cooperatives existing in Northern Nigeria. The credit policy and procedure are shown in Figure 3. The kind of cooperative to be aimed at should reveal itself as an essentially business operation. It should accumulate savings, make profits and become creditworthy in its own right so that it should be able to negotiate loans against its own security. It should rely on government for education of its members, dissemination of new technology and perhaps guarantees for bank loans at the initial stages (see Figure 4).

If the government continues to administer the affairs of the societies, they will never stand on their own and the national credit schemes which rely on cooperative movements for reaching the small farmers will be unable to do so.

5.3 SUMMARY

Small farmers contribute by far a greater percentage of agricultural production in Nigeria. But they operate under serious constraints including that of credit. Informal Credit System now serving them is performing a useful service but it provides little inducement for the adoption of new technologies to expand food production. Thus there is need for the credit agencies to develop means for effectively extending production credit to small farmers.

The early regional financial institutions had failed for a number of reasons. The current national schemes - NACB and the Agricultural Credit Guarantee Schemes - are supposed to avoid the

mistakes of their predecessors. Current approach of on-lending schemes is in the right direction. But the need for efficient operation of cooperative societies. State financial institutions and, of course, the supporting extension services cannot be over-emphasized if the system must succeed.

The state governments should insist on:

1. Adequate advisory machinery.
2. Timely supply of inputs.
3. Timely supply of loans.
4. Establishment of self-supporting cooperative societies.

Work done by Miller (1975) in Nigeria, revealed that farmers would apply for institutional loans if credit was available and that most of them would use it for the purposes of improved technology and hiring of labour. It would be appropriate if cooperative large farms could be developed so that introduction of mechanization would be possible to enable most of the loans to be used for expansion purposes.

CHAPTER SIX

DISCUSSION AND CONCLUSION

6.1 THE MAIN PROBLEMS OF THE SMALL FARMER

It has been abundantly demonstrated that additional loans to small farmers will not in and of themselves lead to greater agricultural production and profitability. For a credit programme to be successful in increasing output, there must be an opportunity for small farmers to utilize additional capital profitably, which in itself requires an improvement in technology backed by markets that can supply the necessary inputs and absorb the output.

The small farmer's main problems include:

i) Lack of motivation.
ii) Lack of technical knowledge.
iii) The complicated social system.
iv) Lack of funds.

An integrated agricultural development programme will help solve these problems. A sound educational programme through extension services will adequately deal with the first three problems, while a supervised credit scheme will supply the required funds and, perhaps partly, help in the provision of and ensuring the proper application of adequate technology. A well organised rural savings scheme will help in the accumulation of and rapid circulation of funds in the farming community.

Though some new techniques, like improved seeds, require little additional capital, others like fertilizers, tube wells do require additional investment. Some farmers may be able to

raise this capital from savings but many small ones cannot. Evidence suggests that a shortage of capital is a constraint on the adoption of new techniques by small farmers. In areas where other conditions are met, an expansion in the supply of funds does lead to an increase in production by small farmers.

6.2 PROBLEMS OF CREDIT DELIVERY

Delivering credit to small farmers is fraught with problems. Some of the problems will be summarized and suggestions made.

1. Reaching the small farmer: The small farmers are scattered; in some cases, on isolated small holdings in remote rural areas. They can only be reached at very high administrative costs. For this reason, among others, public credit programmes even with specific objectives of helping the small farmer make few loans to them; a greater percentage of the credit goes to the larger farmers.

Credit institutions are under a variety of pressures; political, economic and administrative. Loans to small farmers are costly and more difficult to administer and supervise and often have higher default rates. Yet public institutions are not permitted to levy interest charges on small loans high enough to cover costs. Such loans thus make credit organization's performance appear inadequate. This combined with political pressure larger farmers can exert at the local level, has meant that larger farmers have been the main beneficiaries of public credit. To rectify this problem it may require changes in the rural structure and in the operations of the credit institutions.

More emphasis therefore needs to be laid on cooperative societies and onlending schemes as has been adopted by the Nigerian Agricultural and Cooperative Bank (NACB).

2. Timeliness: The timing of the release of loans approved affects their usefulness to farmers. Delays, which can be as much as six to twelve months defeat the purpose of loans to farmers. Causes of delays are attributed to government red tape in administrative machinery and the remoteness of the credit agency from the beneficiaries. If therefore the point of decision for approval of loans is brought nearer to the farmers - through field credit officers and cooperatives - this problem may at least be partially solved.

3. Staffing: For any agricultural credit programme to be successfully run, it would require a staff with technical competence in both agriculture and credit. Thus more emphasis must be placed on training a pool of field officers to ensure that a new technology once available accompanies credit in a form which the small farmer can understand and use. Training of high cadre management staff who will carry out the management of the programme is a fact that cannot be overemphasized.

4. Repayment: Loan repayment has not generally been reported as impressive. Some system has to be devised to make credit facilities available to a larger number of small farmers without increasing unreasonably the incidence of defaults. Strict requirement of securities will limit the number of farmers who can benefit from credit facilities in view of the land tenure system prevalent in most LDC's.

It appears this situation could be improved by:

a) Improving the farming conditions to make the enterprises profitable and removal or reduction of the risks involved in tropical farming.
b) Lending for the most profitable enterprises, as determined by adequate appraisals, i.e. viability of enterprises.
c) Promoting the formation of cooperative societies as media for channelling of loans and collection of repayments.
d) Integrating marketing of produce and repayment collection.
e) Education to change attitudes towards repayment.

6.3 MEANS OF CHANNELLING THE LOANS

There is in principle a general desire to replace informal credit agencies with formal institutions. The operation of informal agencies is marked by comprehensiveness (providing both consumption and productive funds), flexibility and timeliness which are virtually absent in the case of formal institutions. Another advantage of informal lenders is that they operate in credit input and product markets. Formal institutions may have to reorient their policies and procedures if they are to successfully replace informal agencies in financing small farmers.

With excessive costs of credit administration, the banking institutions will definitely find it unprofitable to provide

relatively small loans to the vast numbers of small farmers. Cooperative institutions, being grass-root level organizations, have a distinctive advantage in reorienting their functions and policies in the lines that would suit the farmers and still remain viable. They can link credit with marketing and repayment collection machinery can be built into the system easily. They can provide a package of inputs and services in addition to credit and supply essential items of consumption.

Therefore, whatever the system adopted at the top, it is important that at the grass root level, governments should pay attention to cooperative societies as an important medium of reaching the small farmers. In organising the cooperatives the government should aim at ones that will eventually emerge as self-supporting. Nigeria, with a majority of its farmers in the small-farmer class, belongs to a group of countries that must pay heed to the usefulness of cooperatives.

6.4 ASSESSMENT OF THE PERFORMANCE OF CREDIT INSTITUTIONS

The estimation of success or failure in any given credit programme is a complex matter which involves conflicting issues. It requires not only a knowledge of the facts of the programme's performance but also a set of criteria for success against which these facts can be judged. Indeed one of the principal problems of evaluation of a programme is the assumption of goals to be used as criteria for success in evaluation.

Thus the three broad objectives or goals of small farmer

credit programmes, as outlined by Tendler (1973) can be identified as those of:

i) economic efficiency of the activities financed by the credit.

ii) the ability of the programme to serve a hitherto neglected portion of the rural population (equity).

iii) the financial viability of the institution.

Most of the issues around which the usual programme evaluation revolve - default, interest rate, supervision, profitability, lending criteria, etc. - do not belong exclusively to any of these three categories. Opinions could differ in their consideration and institutions with unequal emphasis on different goals will attach relative degrees of importance on the issues. For example, when emphasis is on institutional viability, substantial default rates are considered highly undesirable, and should be avoided at all costs. However, when emphasis is turned on equity, the institution would de-emphasize the importance of default as it would be regarded as accomplishing a transfer of income to farmers. Similar argument is applicable to high or low interest rates.

The issue of lending criteria also draws conflicting response. With institutional viability in mind, the credit institution is justified in attaching importance to repayment capacity. But in terms of efficiency, the outlook is different. If technology is right, ability to repay will be a function of successful application of profitable technology and not necessarily

of the pre-existing repayment capacity of the borrower. From equity point of view, undue emphasis on repayment capacity would result in exclusion of the less-established small farmers.

Indeed, the disappointing results of many programmes may be caused by this conflict in goals, or rather failure to recognise its existence. Not that the three basic goals are mutually exclusive or highly incompatible but the pursuit of any one of them may require a significant compromise with others. There is therefore a need for any government to spell out the definite goals and methods of achievement for any credit institution. It is, therefore, difficult to recommend specifically a set of rules for achieving success in credit programmes; goals differ just as much as the methods for attaining them; equally socio-economic and political environment vary from country to country.

In conclusion, a credit programme should take the following critical elements into consideration in its organisation.

1. Clear definition of goals.
2. Adequate system or avenues for channelling the credit to small farmers.
3. Integration of production and consumption credit.
4. Consideration of support services - input supply, marketing, technology, research and extension services.
5. Making saving mobilization an integral part of loan programmes.
6. Integration of short-term with long-term loans.

The last point is particularly important in that credit should not be used only to promote the use of modern inputs and technology

to raise land and labour productivity in the short run. There is need to use credit as a tool to build new farm capital, expand acreage, and develop a set of viable farmers who can qualify for commercial bank loans on their own merits.

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