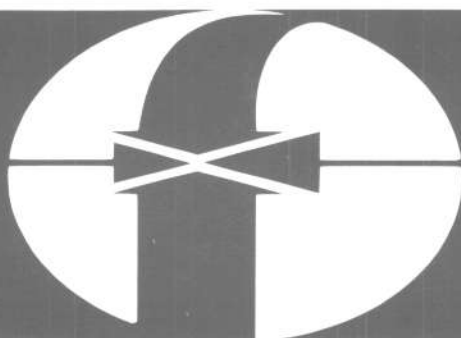


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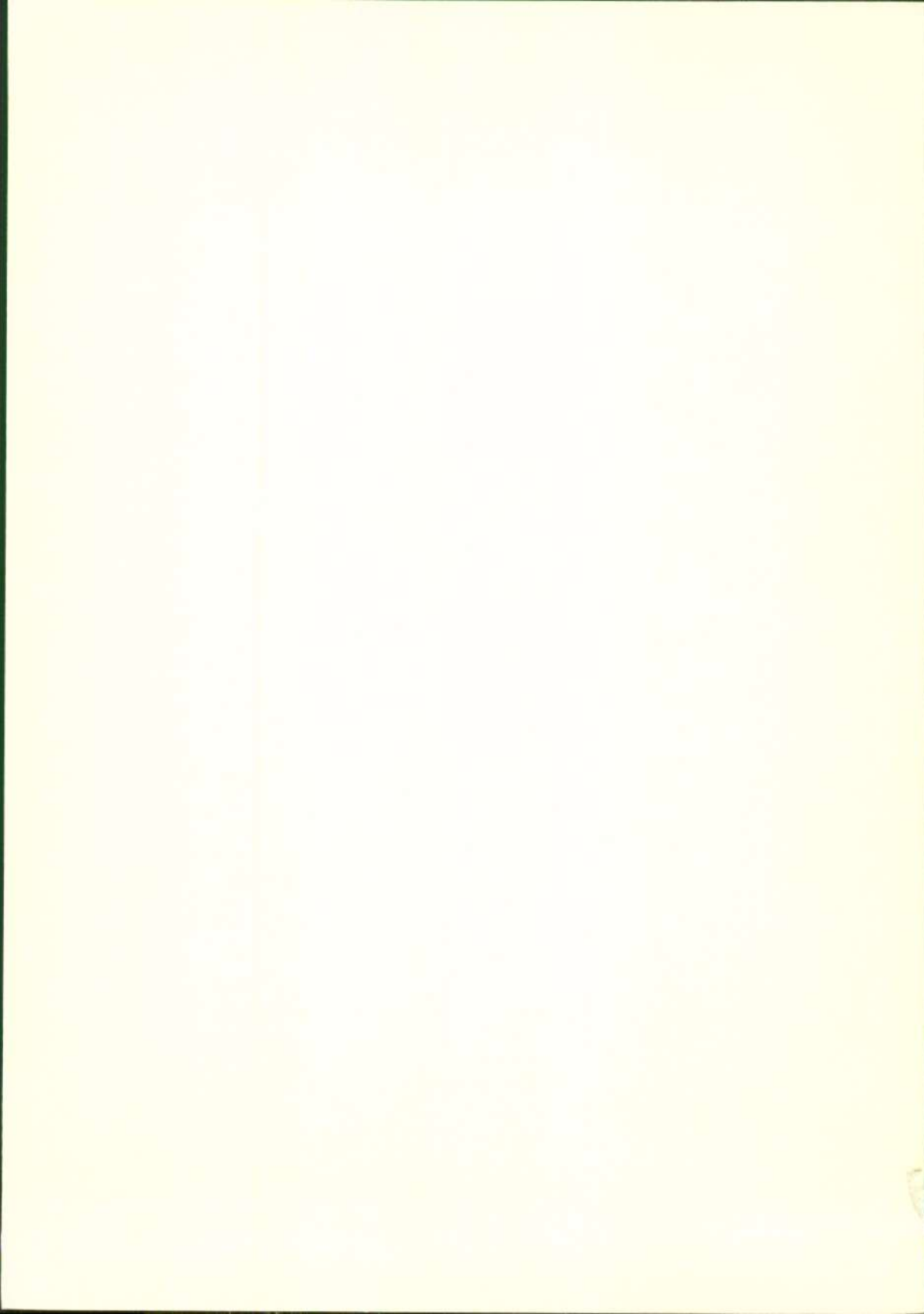


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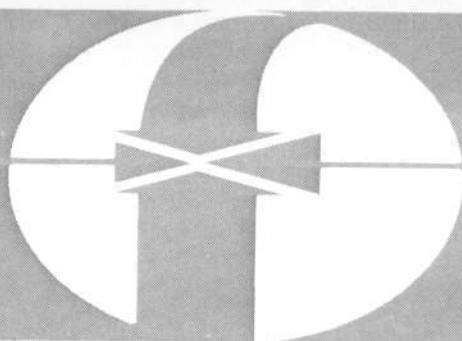
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SAVINGS MOBILIZATION IN RURAL AREAS AND THE PROCESS OF ECONOMIC DEVELOPMENT *

Sandro Sideri

Institute of Social Studies - The Hague

1. Introduction

The special role of savings mobilization for the development process and its actual realization is barely treated in most of the relevant development literature. Although the latter stresses the rate of capital formation, rarely goes into the technical or practical aspects of its actual generation, especially for what concerns savings mobilization in rural areas. One could be tempted to suggest that this omission is the effect of our having identified development with industrialization for too long and, therefore, of having developed a kind of « urban bias » with respect to the topic. In other words, unlike Chaucer's character who « *knew the taverns wel in every town* », development economists do not seem to know this one tavern, possibly because not in town. By default, then, the topic has been left to the financial experts, who often have a strong monetarist bias.

Fortunately, the importance of savings mobilization as a determinant of the rate and direction, or type, of economic growth is gradually gaining recognition. Moreover, since agriculture, or the rural sector, still constitutes the largest economic sector of most countries in the Third World and certainly in Africa, savings mobilization in rural areas must necessarily have top priority regardless of the development strategy that is pursued or the type of government that is in power. Savings mobilization in rural areas is relevant not only for the development of the agricultural sector but also for that of other sectors, and it is with regard to this second aspect that the topic has surfaced in the development literature.

2. Intersectoral Resource Flows

The intersectoral transfer of resources in a closed economy involves flows of goods, labour and finance, and although we seem to concentrate on the latter, the other two constitute the real side of the transfer. All three flows must be considered, however, if we are to obtain a more complete picture of this phenomenon, and to quantify it ¹.

* This article is a slightly revised version of the opening address delivered at the Finafrica Workshop on « Savings Mobilization in Rural Areas and Bankers' Training », Lagos, Nigeria, February 1984.

1 A separate problem results from the fact that « the system of national accounts does not contain separate accounts for farmers or for non-corporate business: these sectors are combined with households into one "personal account". This account therefore exhibits under "personal" saving the savings of farmers and of non-corporate business in addition to those of households ». J. Steindl, « The Role of Household Saving in the Modern Economy », *Banca Nazionale del Lavoro Quarterly Review*, March 1982, p. 74.

The net resource, or « savings surplus », usually assumed to be transferred from agriculture to non-agricultural sectors can be viewed in three ways which, in national accounting terms, are equivalent.

(i) The difference between exports and imports of goods and services, which can be affected by volume or by changes in terms of trade. This also involves labour services provided outside the agricultural sector which — apart from migration — contribute to total farm income.

(ii) The difference between investment and savings, affected by (a) expected rates of return to investment in agriculture, (b) existence of financial institutions, (c) difference between government investment in the sector and the taxes paid by it, and (d) investment by other sectors which in turn depend on the land tenure system.

Finally, (iii) net financial transfers on current account, i.e. current government services minus taxes, subsidies and interest payments, and/or capital account, i.e. government capital expenditures, subsidies and borrowing by farmers from other sectors minus investment by farmers in other sectors and loan repayments ².

In a deeper sense, the transfer from agriculture equals the amount by which the value of its exports exceeds that of its imports. This is the « trade surplus » which underlines the « savings surplus », and brings us back to the creation and mobilization of savings in the rural areas in order to finance the economic growth of other sectors.

3. Savings Mobilization in the Development Literature

Schumpeter ³ stressed that the entrepreneur, i.e. the spearhead of the development process, can only become so « by previously becoming a debtor » but, like many others since then, he gave no regard to the establishment of the conditions and institutions that are necessary for financing such debt.

One of the first UN seminal Report states that « the major source of increased domestic capital formation must be increased savings » and then selects the establishment of savings institutions as the first of three policy options chosen for such

2 Shigem Ishikawa, *Economic Development in Asian Perspective* (Tokyo, 1967), ch. 4, and L.G. Reynolds, *Image and Reality in Economic Development* (New Haven, 1972), pp. 143-145.

3 J. Schumpeter, *The Theory of Economic Development* (New York, 1911), first English translation 1934.

a task. Yet, only six paragraphs are dedicated to these institutions (out of a total of 284) plus one of the 16 final recommendations⁴. Furthermore, while the Report recognizes that « people with low incomes ... might save more if those institutions were more widespread, and if more persons were employed by governments to organize them, and to urge people to save more »⁵, not a single word is dedicated to the specific nature of, and the adjustment needed for, savings mobilization in rural areas.

In 1955, Arthur Lewis stressed that « it is particularly important to stimulate savings among the peasants, because of the role which agriculture has to play in economic development »⁶, but did not consider it necessary to explore the problems related to its mobilization and its transformation into capital.

The problem seemed to attract the attention of Hirschman who, in 1958, pointed out that « development is held back primarily by the difficulties of channelling existing or potentially existing savings into available productive investment opportunities »⁷. However, he emphasized less the ability to mobilize savings — they are there — than the « ability to invest », as indicated in the very title of the concerned chapter.

Rostow simply assumed that « during the take-off, the rate of effective investment and savings may rise from, say, 5% of the national income to 10% or more »⁸, without attempting to explain how those rates could be achieved, except « that institutions be developed which provide cheap and adequate working capital »⁹. A « precondition » this, which clearly does not deserve elaboration.

In 1966 Lewis returned to the problem of savings, stressing that « measures to increase the rate of private saving ... deserve high priority », and that « the amount saved is a function of the effort put into promoting saving »¹⁰. The desirability of

4 *Measures for the Economic Development of Underdeveloped Countries* (New York, N.Y., 1951), p. 36. The final recommendation reads as follows: « Prepare programmes to stimulate domestic savings, including the extension of saving institutions and measures involving taxation; and, in order to ensure that capital moves into the most productive uses, establish a development bank and an agricultural credit system, and if necessary, take other measures for influencing the direction of investment, such as credit controls, foreign exchange controls, or licensing of buildings or capital extensions ».

5 *Ibid.*

6 W.A. Lewis, *Theory of Economic Growth* (London, 1955), p. 230.

7 A. Hirschman, *The Strategy of Economic Development* (New Haven, 1958), p. 36.

8 W. Rostow, *The Stages of Economic Growth* (Cambridge, U.K., 1960), p. 8.

9 *Ibid.*, p. 49.

10 W.A. Lewis, *Development Planning* (London, 1966), pp. 117-118.

creating « a countrywide network of savings institutions of various kinds » and that « some public agency should concern itself specifically with making saving easy »¹¹ were the only suggestions he could make on the issue. What he did emphasize, however, was that « the main source of private savings is the profits of business enterprises » as « it must be recognized that the net contribution of the farmers ... will be small »¹².

A Third World scholar, Celso Furtado, did not even find it necessary to mention the problem of savings mobilization in his *Obstacles to Development in Latin America* published in 1970.

It is not surprising, then, that Shaw, at the beginning of his important contribution, quite correctly remarks that « some development theory seems to be designed for a barter world. In other models finance is passively adaptive, and its deepening is a by-product of accelerated growth in "real" things », while « that guiding beacon of development practice, the Plan, gives scant head to finance in the usual case »¹³.

4. Rural Savings and Overall Economic Growth

Development models tend to incorporate the assumption that agriculture must make a net transfer of resources to other sectors in order to accelerate the country's rate of economic growth. The assumption has not gone unchallenged (see M. Dobb, A.K. Sen, V.W. Ruttan, T.W. Schultz and E. Mason), giving rise to a controversy that is closely related to the level and intensity of technological change in the sector. In fact, « the magnitude and direction of resource flows between agriculture and other sectors depend on ... a complex of factors including (a) the rates of return on capital, (b) the capital-output ratios, (c) the saving rates, and (d) the demand for agricultural output »¹⁴. The best-researched case studies regarding the direction of resource flows are those of Taiwan, India, Japan and Kenya and, of course, the « classical » case of Soviet Russia.

11 *Ibid.*

12 *Ibid.*, p. 120.

13 E.S. Shaw, *Financial Deepening in Economic Development* (London, 1973), p. 4.

14 J.W. Mellor, « Accelerated Growth in Agricultural Production and the Intersectoral Transfer of Resources », *Economic Development and Cultural Change*, 1973, p. 2.

In Taiwan between 1895 and 1960, the outflow from agriculture remained quite high, often representing one-half of the value of agricultural sales until it started to decline in 1959-60 ¹⁵.

Data for Kenya indicate that between 1964 and 1972 « there was a large net capital outflow from the agricultural sector », an outflow that persistently increased during the period and which represented an average of 79% of the country's gross capital formation ¹⁶.

A recent, unpublished, comparative analysis of the Japanese and Indian experiences shows that « while savings flow from agriculture made a significant contribution to the industrialization process of Japan (particularly in the earlier decades of the 20th century), there is no evidence of such outflows in India in the period broadly corresponding to it (i.e. in the 1950s and the 1960s) » ¹⁷, « Institutional factors such as the relatively even size-distribution of operation holdings in Japan », but not in India, « have contributed significantly to differences in bias in the technology adopted for increasing agricultural output during this period and thereby to differences in resources requirements. Such differences ... must also be expected to have considerable effects on the balance of social and political power in the countryside. While it was possible to maintain a fairly high land tax in Japan for at least two to three decades after the Meiji Restoration, there were limits to the rates of land revenue that could be imposed in India even during the British period and, since Independence, taxation of land has had to be almost abandoned for political reasons. At the same time, while the wealthier owners of land in Japan developed strong commercial and industrial interests and got associated rapidly with the industrialization process, there has been only limited evidence of such movements in India since Independence » ¹⁸.

In the case of the USSR for the First Five-Year Plan (1928-1932) Ellman indicates that although « agriculture made an essential contribution to the development of the Soviet economy » during that period ¹⁹, « there is no basis whatsoever for the view that the

15 T.H. Lee, *Intersectoral Capital Flows in the Economic Development of Taiwan, 1895-1960* (Ithaca, N.Y., 1961).

16 J. Sharpley, « Intersectoral Capital Flows, Evidence from Kenya », *Journal of Development Economics*, 1979, pp. 560, 562.

17 A. Mody, S. Mundle and K.N. Raj, « Resources Flows from Agriculture and Industrialization » (mimeographed, 1981), p. 66.

18 *Ibid.*, pp. 67-68.

19 M. Ellman, « Did the Agricultural Surplus Provide the Resources for the Increase in Investment in the USSR during the First Five-Year Plan? », *Economic Journal*, 1975, p. 858.

increase in investment during the First Five-Year Plan was financed by an increase in the agricultural surplus ». Furthermore, « collectivisation did *not* increase the net agricultural surplus ..., nor did it turn the terms of trade between agriculture and industry in favour of industry, nor did it increase agricultural output »²⁰.

While demonstrating the relevance of agricultural surplus to a country's economic growth, these cases also illustrate that institutional factors may seriously limit such a contribution, with the result of a slower rate of growth and/or a more painful process of transformation.

5. The Political Economy of the Extraction Mechanism

In addition to a net capital outflow, and to the transfer of human capital through migration, the agricultural sector can contribute to a country's economic growth by the deterioration of its terms of trade with the rest of the economy, principally with the industrial sector. Shifts of the domestic terms of trade affect capital accumulation and the growth path of a country, while simultaneously reflecting the development strategy enforced.

The issue relative to the terms of trade effect goes far back into the history of economic thought: Ricardo, Malthus and Marx all contributed to the generation of a strong antagonism against peasants, who were considered to be an obstacle to that capital formation which largely rested with the bourgeoisie. Thus, the « town » and « country » dichotomy and the need to extract a sizeable surplus from agriculture so as to enable that capital accumulation which is at the core of economic growth. In a closed economy in particular, accumulation is determined largely by a mutual price relationship between agriculture and industry. While this relationship is affected in turn by developments in the overall economy, the role of the State is paramount through its commercial and fiscal policies which decide the modalities and the rate of accumulation; in other words, who pays what for whom.

Savings mobilization in rural areas concerns only that part of the agricultural surplus that is left over by deteriorating terms of trade, or is augmented by their improvements. The question of whether or not the « country » saves sufficiently therefore cannot be answered without adding to the financial savings, channelled through official or

²⁰ *Ibid.*, p. 859.

unofficial institutions, the surplus generated by the terms of trade effect. And as the « country » is in any case the most important source of surplus, only the modalities of the extraction will vary according to the socio-political context and to the role the State is able, and willing, to play.

The terms of trade effect stresses the danger that the landlords, fearing an « immiserizing growth »²¹ — i.e. in order to avoid any worsening of the terms of trade, and therefore the erosion of their income — may resist any relevant expansion of agricultural production. Therefore, whether or not agriculture can expand without fear of adverse shifts of the terms of trade will depend on (i) social and institutional arrangements; (ii) extent or degree of dependence of agriculture on industrial inputs — the more traditional the technology utilized, including organic fertilizers, the more likely are the terms of trade to worsen; and (iii) income distribution — the more egalitarian the latter, the weaker the demand for industrial goods relative to agricultural ones²².

A movement of the terms of trade in favour of an agricultural sector that is characterized by large land-ownership will most likely worsen income distribution but will not necessarily increase savings. With a different land tenure and land distribution system, the incomes of small cultivators, sharecroppers and agricultural workers will increase and so probably will their savings. The latter can either be reinvested in the sector and so further increase its production, or be channelled into savings institutions for extrasectoral use. Landless labourers and other fixed-income groups, however, are bound to suffer declining incomes as agricultural terms of trade improve.

Available data indicate that « intersectoral terms of trade turned against the agricultural sector in Taiwan between 1923-1930 and 1956-1960 »²³, so that they generated 40 per cent of the transfer from the latter sector during the first half of the 50s²⁴. Also in Kenya domestic terms of trade turned against agriculture during the period analyzed by Sharply, namely 1964-1972. In India instead « the terms of trade clearly moved toward the agricultural sector » between 1952-1953 and 1964-1965²⁵ and possibly even to the middle of the 70s²⁶.

21 J.N. Bhagwati, « Immiserizing Growth: A Geometrical Note », *Review of Economic Studies*, 1958.

22 A. Mitra, *Terms of Trade and Class Relations* (London, 1977).

23 Sharply, *op. cit.*, p. 567.

24 Mellor, *op. cit.*, p. 5.

25 *Ibid.*, p. 8.

26 Mody, Mundle and Raj, *op. cit.*, p. 39, Table 2.4.

6. Savings Mobilization, Agricultural Development and Overall Development

Another aspect of savings mobilization which is not often considered is its dependence on agricultural development and, consequently, on the structural reforms that the latter requires²⁷. Personal income has to rise if more savings are to be produced. Not even the most ingenious mobilization scheme can therefore succeed if income stagnates. Agrarian reforms, land redistribution, rural extension, infrastructure, selective technology, all help to increase agricultural incomes, i.e. farmer's product per head, but they also represent the necessary conditions for agriculture to provide a growing surplus per head from which to feed the non-farmers. Since agriculture contributes the largest share of national income of most LDCs, an increase of farmers' savings is highly relevant. Naturally, the rate of savings will vary according to the situation, but it does not necessarily tend to be higher, as expected by the 1951 UN Report quoted above, in societies where the distribution of income is more unequal.

In fact, continuous technological change in agriculture enables expansion in the demand for agricultural products without causing relative prices to rise, thereby pushing resources back into that sector. Studies on the recent Indian and Taiwanese experiences seem to indicate that « a very high proportion of the increments to income from new technology are saved »²⁸.

The development of agriculture is closely connected to that of other sectors. To neglect this relationship « can lead to a parasitical attempt to "extract a surplus" as opposed to a policy aimed at raising output and productivity in both sectors »²⁹.

7. Conclusions

Savings mobilization in rural areas requires not only the development of an extensive and diversified network of institutions but also an optimum combination of economic growth and income distribution, in that savings capacity is heavily dependent on the last two phenomena. A stagnant agricultural sector will ultimately reduce the country's overall rate of development.

27 See A. Mauri, « A Policy to Mobilize Rural Savings in Less Developed Countries », *Savings and Development*, 1977, 1.

28 Mellor, *op. cit.*, p. 12.

29 Ellman, *op. cit.*, p. 860.

In addition to the development of savings institutions, therefore, policy measures to increase savings in rural areas should aim at

- (i) improving farm productivity;
- (ii) utilizing part of the existing disguised unemployment;
- (iii) reducing conspicuous consumption, i.e. curtailing its domestic production and/or its import; and more importantly,
- (iv) minimizing the demonstration effect by (a) lowering the country's exposure to foreign patterns of consumption, and (b) lowering rural people's exposure to urban consumption;
- (v) maintaining a « moderate » level of inflation;
- (vi) taxing the various sectors and social groups in a more discriminatory manner; and finally,
- (vii) some *à la* Shaw « liberalizing » of the financial system in order to reduce « financial repression ».

The last point is also closely related to the long debated question of whether or not « the financial sector of an economy does matter in economic development ». This question is answered positively by Shaw and others, but it should by now be clear that savings mobilization is influenced by more forces and shaped by more mechanisms than the mere expansion of the financial system. Therefore, in addition to promoting the allocation of savings, the financial system should engage actively in creating conditions for better utilization of the rural surplus and/or for its transfer to other priority sectors so as to maximize production and income. In fact, to enable the difference between income and consumption to widen, i.e. to increase the marginal propensity to save and the volume of savings, incomes must rise.

LA MOBILISATION DE L'ÉPARGNE DANS LES ZONES RURALES ET LE PROCESSUS DE DÉVELOPPEMENT ÉCONOMIQUE

SOMMAIRE

Un bref examen de la littérature économique sur le développement nous confirme que l'importance de la mobilisation de l'épargne dans les zones rurales n'a pas été

suffisamment considérée: on a négligé les effets de l'épargne quant à la croissance du secteur agricole et des autres secteurs dans lesquels elle a été transférée.

Et pourtant de récentes analyses quantitatives nous ont démontré l'importante contribution apportée au développement économique par le surplus de secteur agricole. Ces analyses d'autre part ont mis aussi en lumière les facteurs d'ordre institutionnel qui peuvent limiter de façon remarquable la contribution de l'épargne ayant pour résultat un taux plus faible de croissance et/ou un processus plus difficile de transformation.

Il faut se rappeler que la mobilisation de l'épargne dans les zones rurales concerne seulement la partie des surplus agricoles non absorbée par la dégradation des termes de l'échange (ou qui est augmentée par l'amélioration des termes de l'échange). Ces mêmes études recherchent de déterminer soit l'importance quantitative soit la direction de ces mouvements. Le mécanisme des termes de l'échange représente un instrument très utile pour soustraire des ressources du secteur agricole mais en même temps peut réduire la production du même secteur en causant de graves difficultés dans le processus de développement économique. En tout cas les résultats de ce mécanisme dépendent des paramètres économiques de base les plus importants et des changements d'ordre social et institutionnel.

Enfin, une agriculture en état de stagnation nécessairement réduit le taux global de croissance d'un pays et de cette façon on peut établir clairement une étroite relation entre le développement de l'agriculture et des autres secteurs. On peut donc en déduire que la mobilisation de l'épargne dans les zones rurales joue un rôle capital dans le processus de développement. En même temps on a démontré que la mobilisation de l'épargne est influencée par des forces et façonnée par des mécanismes qui ne peuvent pas se rattacher seulement à l'expansion du système financier: ce qu'on demande c'est une combinaison optimale de croissance économique et de distribution du revenu national.