

FINANCING PEASANT AGRICULTURE: THE CASE OF AGRICULTURAL CREDIT GUARANTEE SCHEME IN NIGERIA

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1. Introduction

Development theorists, policy makers and farmers have often identified lack of access to formal credit as a great impediment to agricultural production in developing countries. Schultz rationalised from the point of view of existing traditional system that while peasant farmers are efficient but poor, they will languish in technical and economic equilibrium trap if left unassisted¹. As a way of assisting farmers, governments in developing countries have established institutional credit to provide increased financial resources to the agricultural sector. Formal credit has been argued to provide farmers with opportunities for growth by enabling them to procure inputs and fixed capital required to operate on a superior production function. Unfortunately, however, wrongly perceived credit policies have hampered rather than enhanced the rate of technological and agricultural growth in developing countries.

Provision of preferential credits to farmers has become a national priority in many developing countries. Often supported by international donor agencies, formal agricultural credit is popular in developing countries for two reasons: (1) agriculture provides employment for most of the citizens and (2) subsidised agricultural credit as a development instrument is politically attractive. The cheap credit policies pursued by most developing countries' governments and the high risk of advancing loans to farmers have made agricultural financing highly unattractive to commercial lending institutions.

Generally speaking, public-sector agricultural credit operations in developing countries have typically been plagued by high default and delinquency rates². Even though Vogel (1981) argued that low default and delinquency rates are a necessary but not a sufficient condition for the success of agricultural credit programmes, high delinquency or default rates signal a shoddy programme performance. This is the case with agricultural credit guarantee scheme (ACGS) in Nigeria. For instance, of the total loans of N68.4 million guaranteed in 1986, loans valued at N28.1 million matured between 1986 and 1988, but only N6.1 million or 21.7 percent were fully repaid by 1988. Similarly, out of 16,209 total loans guaranteed in 1987, valued at N102.15 million, 14,571 loans valued

1 Schultz, T.W., *Transforming Traditional Agriculture*, Yale University Press, New Haven, 1964.

2 Vogel, R.C., "Rural Financial Market Performance: Implications for Low Delinquency Rates", *American Journal of Agricultural Economics*, Vol. 63, No. 1, 1981, pp. 58-65.

at N51.5 million were due for payment between 1987 and 1988 but just N18.7 million or 36.3 percent were fully repaid by 1988³.

The objective of this paper is to analyse agricultural credit policies in Nigeria with a particular emphasis on agricultural credit guarantee scheme's operational performance and viability as a lending agency to small-scale farmers. Given that lack of access to credit is a major handicap for farmers, it will be interesting to find out why many farmers participating in the credit guarantee scheme are not responsibly honouring their debt obligations.

This paper is organised into eight sections. Section 2 briefly reviews the literature on agricultural credit in developing countries. Section 3 gives a broad overview of the policies affecting agricultural credit administration in Nigeria. Section 4 analyses some of the contradictions in government policies affecting agricultural credit. Section 5 analyses the agricultural credit guarantee scheme (ACGS) and its activities. Section 6 focuses on how ACGS has fared among small-scale farmers. In section 7, the results of two surveys conducted in north-eastern part of Nigeria with regard to the performance of ACGS are presented. Section 8 ends the paper with policy suggestions which could revamp the scheme for policy effectiveness.

2. Literature Review

The traditional views of rural credit and finance have been identified as the main culprit for lack of progress in agricultural financing in developing countries⁴. The views include (1) cheap credit policy as a compensation for macroeconomic policies which might have depressed farm incomes; (2) making loans available to all farmers as the only means of enhancing technological adoption and profitable farming; (3) informal credit is exploitative and supports consumption rather than investment behaviour, so a cheap, formal credit provides an escape route; and (4) subsidised credit increases the welfare of the poor.

Overwhelmed by the above views, little concern has been shown by policy-makers for

3 Agricultural Credit Guarantee Scheme Fund, 11th Annual Report and Statement of Accounts for the year ending December 1988, p. 5.

4 Von Pischke, J.D., D.W Adams and G. Donald, *Rural Financial Markets in Developing Countries: Their Use and Abuse*, The Johns Hopkins University Press, Baltimore, 1983.

the negative impacts of such views on the efficiency and viability of rural financial agencies. Admittedly, the need for farm credits is copious as indicated by the results of a survey of 40 farmers in three villages of Burkina Faso⁵. Eighty-two percent of the farmers surveyed cited lack of credit facilities as the major constraint to their agricultural production and the same percentage would have liked to borrow had it been possible. About 55 percent of the farmers needed credit to purchase farm equipment, while 23 percent wanted credit for draft animals. Eighty-eight percent of the sample preferred to borrow from semi-government, Rural Development Organisations (ORD) because of their low interest rates and for security purposes. Policy-makers have thus used cheap credit policy to generate superfluous demands for an inelastic supply of funds.

The largest institutional rural lending in Cameroon called the National Fund for Rural Development (FONADER), a government-owned and financed agency, suffered a serious setback in lending to small and medium-scale farmers through its GAM (Groupement d'Agriculteurs Modernes) programme⁶. Under GAM, group credit was channelled through the agricultural extension service to farmers but with disastrous loan repayment records. According to the study, 76 percent of outstanding loans were overdue in 1983. Reporting a similar experience in Jamaica, Graham and Bourne (1983) observed that the fundamental shortcomings in the design and operation of many government-owned credit programmes often undermined the effectiveness, as well as the viability, of rural credit institutions⁷. The observation is corroborated by the interest rate ceilings usually placed on rural credits in developing countries. Such a regulation builds into rural credit schemes an implicit subsidy which is questionable on equity grounds. Commercial lending agencies often focus on proper evaluation and administration of loans. Government-owned credit programmes, on the other hand, are easily transformed into *ad hoc* income transfers, focusing on making out loans to as many people as possible without due considerations for institutional viability.

5 Singh, R.D. (1988) Economics of the Family and Farming Systems in Sub-Saharan Africa — Development Perspectives, Westview Special Studies in Social, Political, and Economic Development, Westview Press, Inc., Boulder, Colorado, 1988.

6 Schaefer-Kehnert, Hans-Christoph, Institutions and Technical Change in the Development of Smallholder Agriculture: An Economic Analysis of Cooperatives Promoting Coffee and Cocoa Production in Cameroon, Wissenschaftsverlag Vauk, Kiel, 1988.

7 Graham, D.H. and C. Bourne, "Agricultural Credit and Rural Progress in Jamaica", in Von Pischke, J. D., D.W Adams, and G. Donald, eds., Rural Financial Markets in Developing Countries: Their Use and Abuse, The Johns Hopkins University Press, Baltimore, 1983.

While interfering in rural financial markets, policy makers had pursued conflicting goals from those of commercial lending institutions. Policy makers often determine the success of a credit system in terms of programme outreach based on credit needs. Von Pischke (1989) has criticised such criterion for evaluating the success of a credit system. He argued that such evaluation overlooks the risk dimension in credit decisionmaking. The criterion is also analytically flawed because it diverts attention from ability to pay and ignores incentives to lenders. For effectiveness, he suggested that intervention in rural financial markets should recognise the importance of repayment capacity of borrowers as a reflection of the lenders' perspective. Intervention, he said, should be such that will build confidence (between the borrower and the lender) and should create debt capacity.⁸

3. Agricultural Credit Policy in Nigeria

The Central Bank of Nigeria (CBN) has mandatory guidelines on allocation of credit to the various sectors of the economy, to which commercial and merchant banks are required to comply with. Using credit controls, the whole economy is divided into two categories (A and B). Category A is comprised of the high priority sectors, including agriculture and manufacturing. Category B includes other sectors. The credit controls used by the CBN entail portfolio quotas and reserve requirement penalties. Table 1 shows the amounts of loans and advances to agriculture by commercial and merchant banks from 1980-89 and their compliance with the CBN guidelines. Over the 10-year period, commercial banks' credit allocations to the agricultural sector were consistently below the prescribed minimum rates (PMR), except in 1988 and 1989 when loans and advances to agriculture marginally exceeded the cut-off point of 15 percent. In absolute terms, the commercial banks' loans and advances to agriculture increased by more than seven times from 1980-89, yet the amounts fell short of the CBN requirements in 8 of the 10 years.

The merchant banks' compliance with the CBN guidelines with respect to the agricultural sector was better than the commercial banks'. Although the PMR required to be allocated to the agricultural sector by the merchant banks are less, the merchant banks met the

8 Von Pischke, J.D., "Risk: The Neglected Dimension in Rural Credit Projects", *Savings and Development*, Vol. XIII, No. 2, 1989, pp. 133-147.

CBN requirements in 4 of the 10 years considered. In absolute terms, the amounts of loans and advances to agriculture by the merchant banks increased by four times over the period 1980-89. Relative to commercial banks, the merchant banks' loans to agriculture increased from 4 percent in 1980 to 23 percent in 1989.

Table 1

LOANS AND ADVANCES TO AGRICULTURE BY COMMERCIAL AND MERCHANT BANKS AND THEIR COMPLIANCY WITH THE CREDIT REGULATION, 1980-89

| Year | Loans and Advances to Agriculture by | | | | | | | |
|------|--------------------------------------|-------------------------------|-------------------------|------------------------|------------------------------|-------------------------------|-------------------------|------------------------|
| | Commercial banks | | | | Merchant banks | | | |
| | Amount N mil ^a | % Total Loans ^b | PMR (%) ^c | PI (%) ^d | Amount N mil ^a | % Total Loans ^b | PMR (%) ^c | PI (%) ^d |
| 1980 | 462.2 | 7.3 | 8 | 91 | 20.0 | 5.0 | 5 | 100 |
| 1981 | 590.6 | 6.9 | 8 | 86 | 28.6 | 4.0 | 5 | 80 |
| 1982 | 786.6 | 7.7 | 8 | 96 | 40.1 | 3.9 | 5 | 78 |
| 1983 | 940.4 | 8.5 | 10 | 85 | 54.3 | 3.7 | 5 | 74 |
| 1984 | 1,052.1 | 9.1 | 10 | 91 | 79.3 | 4.7 | 5 | 94 |
| 1985 | 1,310.2 | 10.8 | 12 | 90 | 120.2 | 6.7 | 6 | 112 |
| 1986 | 1,830.3 | 11.7 | 15 | 78 | 211.8 | 7.6 | 8 | 95 |
| 1987 | 2,427.1 | 13.8 | 15 | 92 | 327.7 | 7.9 | 10 | 79 |
| 1988 | 3,066.7 | 15.8 | 15 | 105 | 576.5 | 13.4 | 10 | 134 |
| 1989 | 3,470.5 | 15.6 | 15 | 104 | 815.1 | 15.3 | 10 | 153 |

^a Amount of loans and advances by commercial and merchant banks are in millions of Naira.

^b Loans and advances to agriculture as a percentage of total loans to the economy, respectively, by commercial and merchant banks.

^c PMR is the prescribed minimum loan rate or quota of loan portfolio that the Central Bank of Nigeria required respective banks to lend to agriculture.

^d PI represents the annual performance index of respective banks with respect to the government credit regulation.

Increased loans and advances to agriculture by commercial and merchant banks were sustained through credit controls, introduction of ACGS and deregulation (in 1987) of interest rate on agricultural lending. Beginning from January 1987, farmers were expected to negotiate lending rates with banks subject to the 15 percent ceiling allowed on all loans. As from August 1987, however, farmers, just like other borrowers, had to pay the market interest rates upon removal of the ceiling on lending rates. This explains why both commercial and merchant banks recently exceeded the PMR.

The Federal Government of Nigeria (FGN) regulates financial markets in order to increase lending to agriculture by various means:⁹

- (1) The government specifies from year to year the minimum percentage of the commercial and merchant banks loan portfolios that must be advanced or lent to agriculture. From 1980-89, the minimum percentage rates increased from 8-15 percent for commercial banks and from 5-10 percent for merchant banks.
- (2) Loans in excess of the minimum percentage rates were exempted from banks' aggregate ceilings.
- (3) A minimum percentage of total deposits generated in rural areas must be lent to borrowers in such areas. For example, the minimum percentage of aggregate commercial bank loans that must be lent to rural borrowers increased from 30 percent in 1984 to 45 percent in 1988.
- (4) Interest rates on bank lending to agriculture had been at concessionary rates, until 1987 when interest rate ceilings were removed as a result of the structural adjustment policies. In 1984, the interest rate on agricultural production loans was 7 percent compared with 13 percent in other sectors.
- (5) One of the CBN credit policies stipulates that a minimum of 16 percent of commercial banks' total loans and advances must be allocated to small-scale, wholly Nigerian-owned enterprises.

The principal sources of formal agricultural credit in Nigeria are the Nigerian Agricultural and Cooperative Bank (NACB), ACGS, Commercial and Merchant Banks, State Credit Corporations, Credit Units of State Ministries, Cooperative Organisations, and World Bank-Assisted Agricultural Development Programmes. NACB is the largest single source of formal credit to agriculture. ACGS is second to NACB in terms of outreach and value of loans granted. For example, in 1987 the number and amount of loans granted by NACB were 28,153 and N320 million, respectively, as against 16,209 loans valued at N102.1 million by ACGS. Similarly in 1988, NACB granted 31,109 loans valued at N430.1 million, while ACGS guaranteed 24,358 loans valued at N118.6 million.¹⁰

9 Central Bank of Nigeria, Annual Report and Statement of Accounts, various issues.

10 *ibid.*, 1989.

4. Paradoxes in Agricultural Credit Policy in Nigeria

The government appears to be sensitive to the vast volume of credit needed for development of the agricultural sector by effecting various institutional designs and policy guidelines. One of the government objectives for intervening in the credit market was to accelerate the volume of capital inflow to the sector from non-farm sources by coercing financial institutions to participate in farm financing with the hope of alleviating income inequality in rural areas.

Table 2 shows the stable increase of agricultural gross domestic product (GDP) as a percent of total GDP in the 1980s. The ratios of aggregate credit to the economy by both commercial and merchant banks in relation to total GDP also increased, which reflect growing rate of inflationary financing, perhaps through substantial increases in money supply. As indicated in the table, agricultural loans as a percent of agricultural GDP steadily increased from 3 percent in 1983 to 14 percent in 1989. The steady increase suggests that outstanding loans to agriculture are either in permanent default or leaked to non-agricultural uses as a result of fungibility of credit or leaked out of the economy as capital flights.¹¹

Despite the massive capital inflow designed to facilitate agricultural development, there are some incoherences in government financial policies towards the sector. The main source of institutional and policy deficiency in the country's rural credit policy results from lack of the right institutional and organisational structure for agricultural credit administration.¹² Manufacturing and agriculture were mandatorily classified as the high priority sectors in terms of preferences for loans from the commercial and merchant banks. But the government has not been consistent in its general policy towards agriculture. One would expect that the government which coerces financial institutions to channel capital resources to the agricultural sector should simultaneously embark on infrastructural development to harness the resources. Unfortunately, budgetary allocations during the 1980s indicated government investment bias (GIB) against agriculture.

Government investment bias (GIB) measures the proportional allocation of government

¹¹ Graham, D. H. and C. Bourne, *op. cit.*

¹² Olomola, A.S., "Dimensions of Institutional and Policy Deficiencies in the Nigerian Agricultural System", *Development Policy Review*, Vol. 7, 1989, pp. 171-183.

capital expenditure to a sector in relation to the sector's contribution to total GDP¹³ A GIB value of one indicates that the sector receives comparable investment resources to the value of its contribution to national output growth. A GIB value of less than one suggests that the sector receives less investment resources than it contributed total GDP and vice versa.

Table 2

CONTRIBUTION TO GROSS DOMESTIC PRODUCT, DEBT STRUCTURE OF AGRICULTURE AND GOVERNMENT INVESTMENT BIAS, NIGERIA, 1981-89*

| Year | 1981 | 1982 | 1983 | 1984 | 1985 | 1986 | 1987 | 1988 | 1989 |
|---|------|------|------|------|------|------|------|------|------|
| Agric GDP as % Total GDP ^b | 25 | 27 | 31 | 35 | 34 | 35 | 35 | 35 | 35 |
| Agg. Credit as % Total GDP ^c | 28 | 35 | 43 | 44 | 41 | 45 | 52 | 68 | 58 |
| Agric Loans as % Total Loans ^d | 7 | 7 | 8 | 9 | 10 | 11 | 13 | 15 | 16 |
| Agric Loans as % of Agric GDP | 4 | 5 | 3 | 4 | 5 | 7 | 10 | 12 | 14 |
| Government Investment Bias (GIB) ^e | 0.72 | 0.29 | 0.36 | 0.15 | 0.04 | 0.12 | 0.20 | 0.23 | 0.33 |

* Agriculture includes crop, livestock, fishing and forestry. Data sources include Annual Abstracts of Statistics, 1988 edition; Central Bank of Nigeria Annual Report, 1989; and Central Bank of Nigeria, Economic and Financial Review, various issues.

^b Gross Domestic Products (GDP) are evaluated at market prices.

^c Aggregate credit to the economy from all sources as a percent of total GDP.

^d Agricultural loans are loans and advances to agriculture by commercial and merchant banks, while total loans are loans and advances to the economy by commercial and merchant banks.

^e Government Investment Bias (GIB) = $[CIa/CI] / [GDPa/GDP]$, where

CI = Total Government Capital expenditure

CIa = Government Capital expenditure on Agricultural sector

GDP = Total Gross Domestic Product

GDPa = Agric GDP without Government intervention

For more details on GIB, see Moon (1988)

Table 2 shows the paradox in government's capital resource allocation to the sector. The GIB coefficient for agriculture incredibly fell from 0.72 in 1981 to its lowest value

13 Moon, Pal-Yong, "Agricultural Policy Reforms in South Korea: Motivations, Features and Effects", in Allen Maunders and Alberto Valdes, eds., Agriculture and Governments in an Interdependent World. Proceedings of the 20th International Conference of Agricultural Economists, held at Buenos Aires, Argentina, 24-31 August, 1988. Darmouth Publishing Company, England, 1988, pp. 430-441.

of 0.04 in the 1980s. The average GIB coefficient for the sector during 1981-89 period was 0.27. These coefficients indicate that the agricultural sector received substantially lower investment or capital expenditure from the government relative to its contribution to national output growth. Inconsistent patterns of budgetary allocation to the sector is symptomatic to the policy makers' subordination of agriculture to the manufacturing sector. Resources thus generated from agriculture are appropriated to the industrial and manufacturing sectors, thought to be synonymous with modernity. Instead of maintaining continuity in government capital projects and infrastructural development, capital expenditures on agriculture had been based on haphazard allocations or responses to crises situations.

Farmers' debt capacity could only be enhanced when resources are harnessed to develop infrastructure, storage system, marketing channels and to synchronise the development with access to loans. It has been estimated that about 50 percent of yam tubers and about 30 percent of the 12 million metric tonnes of grains annually produced in Nigeria were lost to lack of proper storage facilities. It is, therefore, only through an organised, institutional framework that the sector would realise the type of structural transformation which could lead to food self-sufficiency, self-sustained growth, and effective management of the financial resources accruing to the sector.

5. Agricultural Credit Guarantee Scheme (ACGS)

The ACGS, established in March 1977 by the Federal Government of Nigeria (FGN), started operation in April 1978. The scheme was established under the management of the CBN to counter the commercial and merchant banks' reluctance to advance loans to agriculture on account of high default risk.

The scheme guarantees bank loans to farmers up to 75 percent of the amount in default. For instance, in case of a default, the CBN pays to the lending bank 75 percent of the amount in default, net of the collateral pledged to the lending bank by the farmer. A fund (with authorised capital of N100 million) was set up by the FGN and CBN and subscribed to in the proportion of 60 percent and 40 percent, respectively, for settling default claims as guaranteed. As is typical of public-sector agricultural loans in many developing countries, loans guaranteed by the scheme had been at concessionary interest rates until 1987.

Loans are guaranteed for production of the following agricultural activities:¹⁴

- (1) rubber, oil palm, coffee, cocoa, tea and similar crops;
- (2) cereal crops, tubers, fruits, cotton, beans, groundnuts, sheanuts, benniseed, vegetables, pineapples, bananas and plantains;
- (3) animal husbandry, that is, poultry, piggery, cattle rearing and the like, and fish farming;
- (4) In 1988, the provisions of the scheme were amended to include fish captures, storage, farm machinery and hire services and integrated agricultural projects, incorporating production and processing, provided the primary production element accounts for no less than 50 percent of the raw materials required by the factory. Table 3 gives a summary of the scheme's loan distribution by enterprise classification from 1978 to 1988.

Table 3

CUMULATIVE LOANS GUARANTEED BY AGRICULTURAL CREDIT GUARANTEE SCHEME (ACGS) BY PURPOSE, 1978-1988.

| Activity | Cumulative number of loans | % of total number of loans | Cumulative value of loans (N 000) | % of total value of loans |
|------------------|----------------------------|----------------------------|-----------------------------------|---------------------------|
| LIVESTOCK | 5,973 | 10.4 | 230,834.9 | 43.0 |
| Poultry | 3,035 | 5.3 | 180,966.5 | 33.7 |
| Cattle | 2,013 | 3.5 | 19,092.5 | 3.5 |
| Fisheries | 410 | 0.7 | 14,690.3 | 2.7 |
| Others | 515 | 0.9 | 16,085.6 | 3.0 |
| FOOD CROPS | 45,697 | 80.2 | 244,822.6 | 45.5 |
| Grains | 35,337 | 62.0 | 180,009.5 | 33.5 |
| Roots and Tubers | 9,759 | 17.1 | 45,009.2 | 8.3 |
| Mixed Farming | 601 | 1.1 | 19,803.9 | 3.7 |
| CASH CROPS | 5,354 | 9.4 | 61,961.8 | 11.5 |
| GRAND TOTAL | 57,024 | 100.0 | 537,619.3 | 100.0 |

Source: Agricultural Credit Guarantee Scheme Fund, Annual Report and Statement of Accounts, various issues.

Characteristically, short-term loans (maturing within 3 years) formed the bulk of the loans

¹⁴ Agricultural Credit Guarantee Scheme Fund, 13th Annual Report and Statement of Accounts for the year ending December 1990.

guaranteed to farmers by the scheme. Between 1984 and 1988, the number of short-term loans guaranteed ranged between 94.6 percent and 99.2 percent. Over the same period, medium-term loans (maturing within 3-5 years) ranged between 0.7 percent and 5.3 percent of total loans guaranteed, while long-term loans (maturing over 5 years) were between 0.1 percent and 0.5 percent.

The maximum amount that can be guaranteed to an individual farmer was N50,000 but increased to N100,000 in 1988, while the approved maximum value to a cooperative society or a company remained at N1.0 million. As from 1988, security requirement for loans of N5,000 and below was formally waived (Decree no. 18 of 14th June, 1988).

The largest number of borrowers were individual farmers, who constituted between 93.6 percent and 99.2 percent of the total number of loans guaranteed from 1983 to 1988. In terms of loan values, individual farmers borrowed between 39.1 percent and 67.5 percent of the total value of loans guaranteed by the scheme from 1983-88. Agricultural companies had been the main beneficiaries of the loans on a per capita basis. Between 1983 and 1988, companies represented 0.4-5.5 percent of number of loans but represented 29.0-60.9 percent in terms of value. Individual farmers recently started to play increasing roles of importance. In 1988, loans of N5,000 and below were granted to 23,225 small-scale farmers, valued at N63.35 million, i.e., 55.1 percent of the total value of loans guaranteed. Of the total loans of 34,518 granted in 1989, valued at N129.3 million, 96 percent (valued at N88.1 million) went to small-scale farmers borrowing N5,000 or below. Unfortunately however, just 10,057 small-scale borrowers fully repaid their loans, valued at N21.3 million in 1989.

The major problem is that as many farmers continue to borrow from the scheme, the average value of loans to individual farmers considerably declined from N11,377 in 1983 to N3,288 in 1988. Given the rising inflation rates, per capita loans advanced to small-scale farmers had further declined in real terms. On the other hand, per capita loans guaranteed to companies increased from N294,518 in 1983 to N357,977 in 1988. While production costs have increased by more than 100 percent over the same period, and concessionary interest rates and other forms of farm subsidies have been partially or completely eliminated, the typical amount of loans approved for small-scale farmers are not sufficient for productive activities. This might be a good explanation for the high default rates among this category of borrowers.

Concessionary interest rates probably have hurt the ones it intended to protect. Because of the non-price rationing of agricultural loans, demand for credit is highly elastic but the supply is inelastic. Mass involvement of borrowers made available credit to be spread

thin, which probably had resulted in under-financing of investments. Under-financing of investment could have resulted in a search for high-cost, supplementary loans from informal sources thereby pre-empting the payment of formal loans. In the alternative, underfinanced investments may remain incomplete for lack of finance.

6. ACGS and the Small-scale Farmers

For expositional purpose, small-scale farmers are described in this section as small-holder farmers borrowing N5,000 or below. Although farmers borrowing up to N10,000 fit well into this category of small-scale farmers, the analysis that follows is limited to farmers borrowing not more than N5,000.

An analysis of loans guaranteed to small-scale farmers shows a substantial increase in the number of beneficiaries. From 885 in 1983 to 33,133 in 1989, the number of small-scale farmers or borrowers increased from 66 percent to 96 percent of total loans guaranteed. In nominal value terms, however, the increases over the same period were from N2.17 million to N88.1 million, representing 6 to 68 percent of the total value of loans guaranteed.

Between 1985 and 1988, 75-95 percent of total number of loans guaranteed by the ACGS fund went to small-scale farmers. However, they only received 13-55 percent of the total value of loans guaranteed. The repayment records of this category of borrowers are quite disappointing, unlike the great performance (in terms of low delinquency rates) of small farmers in Costa Rica.¹⁵ During the period 1985-88, the number of loans fully repaid on time ranged from 10-25 percent of the total number of loans guaranteed, representing 8-25 percent of total loans granted to this category of borrowers. In other words, 75-92 percent of the loans guaranteed to the small-scale farmers were either delinquent or defaulted.

Reasons adduced for the good performance of small-scale farmers in Costa Rica were efficient information gathering process about potential borrowers and the promise of concessionary interest rates only if prompt payments were made. Both reasons are inapplicable to the case of ACGS. The government's focus is on credit needs as against ability to repay or creating a debt capacity for the small-scale borrowers. The emphasis

¹⁵ Vogel, R.C., *op. cit.*

is on mass involvement of farmers because this is politically attractive. For instance, since 1986 farmers borrowing N5,000 or below have been mandatorily exempted from providing securities or collaterals before loans are granted. For this regulation to carry more weight or be legally binding to the banks, it was enacted by Decree no.18 of 14th June, 1988. High delinquency rates, however, had been related to the political economy of agricultural credit, whereby politicians are reluctant to bear the political consequences of enforcing loan repayments.¹⁶ The fact remains true with non-democratic, military regimes (such as in Nigeria) which also solicit for support by avoiding any action that might lead to social unrest and hence precipitate a counter coup.

At the time when production costs have considerably increased because of the structural adjustment policy (SAP), the amount of loans advanced to small-scale farmers was inadequate for any meaningful or productive operation. For example between 1985 and 1988, labour costs had increased by more than four times. The costs of hiring tractor, fertilizers, interest and inflation had also increased substantially. These factors are catalysts for problem loans. The following section examines the causes of high default and delinquency rates which now threaten the viability of the scheme.

7. A Case Study of the Agricultural Credit Guarantee Scheme

An empirical analysis of the causes of loan repayment problems among small-scale farmers is undertaken in this section. Low repayment rates constitute a potential threat to ACGS's viability. Two surveys were conducted in two north-eastern states of Nigeria in 1988 and 1989. In 1988, 45 small-scale farmers were surveyed in Gombi local government area of Gongola state¹⁷ and 60 small-scale farmers in Maiduguri local government area of Borno state in 1989¹⁸.

A purposive random sampling approach was used to select names and addresses of

16 Ladman, J. R. and R. L. Tinnermeier, "The Political Economy of Agricultural Credit: The Case of Bolivia", *American Journal of Agricultural Economics*, Vol. 63, No. 1, 1981, pp. 66-72.

17 Bashir, A. B., "An Analysis of the Factors Affecting Loan Repayment Under the Commercial Banks' Small-Scale Farmers Loan Scheme", Unpublished final year project, Department of Agricultural Economics and Extension, University of Maiduguri, Nigeria, 1988.

18 Nyako, M. A., "Agricultural Credit Guarantee Scheme Loan Repayment Problems: An Analysis of Selected Banks in Maiduguri Metropolitan Council", Unpublished final year project, Department of Agricultural Economics and Extension, University of Maiduguri, Nigeria, 1989.

small-scale farmers who benefited from the scheme through selected banks. Fifteen farmers each were selected from the First Bank of Nigeria (FBN), United Bank for Africa (UBA) and Union Bank of Nigeria (UBN) in 1988. In 1989, 20 farmers each were chosen from FBN, UBA and Nigerian Agricultural and Cooperative Bank (NACB). All the banks mandatorily participated in the scheme. Samples were chosen from different banks because of the differences in the policy requirements for loan advances to farmers by each bank. However, the same CBN guidelines regarding the scheme apply to all banks. For example, FBN has the most stringent policy, Table 4. FBN requires that each borrower must open an account with a minimum balance of N200.00, and loan disbursement is arranged by instalments. Thus, samples from different banks are expected to reflect how inter-bank policy variations influenced loan recovery.

Table 4

POLICY REQUIREMENTS OF SELECTED BANKS FOR AGRICULTURAL CREDIT GUARANTEE SCHEME LENDING TO SMALL-SCALE FARMERS IN NIGERIA.

| POLICY | FBN ^a | UBA ^b | UBN ^c | NACB ^d |
|-----------------------------------|---|-----------------------------|-----------------------------|--------------------------|
| Loan Disbursement | By cash only | By cash only | By cash only | By cash only |
| Mode of Loan Disbursement | By instalment | Payment at once | Payment at once | Payment at once |
| Term Structure of Loans | One year | One year | One year | One year |
| Maximum Loan Without Collateral | N5,000.00 | N5,000.00 | N5,000.00 | N10,000.00 |
| Bank Requirement for Transactions | Savings Account Required with N200.00 minimum balance | Savings Account Recommended | Savings Account Recommended | Savings Account Optional |

NOTE: All loans granted under the scheme are guaranteed up to 75 percent by the Central Bank of Nigeria.

^a FBN is First Bank of Nigeria Limited.

^b UBA is United Bank for Africa.

^c UBN is United Bank of Nigeria Limited.

^d NACB is Nigerian Agricultural and Cooperative Bank.

7.1. Major Causes of Delinquent Loans

Table 5 shows the reasons given as the root causes of delinquent loans in the two surveys. When the reasons adduced were ranked in terms of the number of times mentioned by respondents, crop and animal diseases and pests ranked first as the main

cause of problem loans in the two areas, Table 5. Disease and pest infestation indicates that the farmers concerned lacked proper management skills. Had these farmers been assisted by the government by providing adequate extension services whereby the state-of-the-art cultural practices, such as crop rotation, spraying, immunisation, etc., had been the rule rather than exception, incidence of diseases and pests could have been drastically minimised.

Table 5

REASONS FOR DEFAULT AND THEIR RANKING — SURVEY RESULTS FROM GONGOLA AND BORNO STATES OF NIGERIA, 1988 AND 1989

| Causes of Default | Number of Times Mentioned | | | |
|---|---------------------------|------|--------------------------|------|
| | 1988 Survey ^a | Rank | 1989 Survey ^b | Rank |
| Drought | 17 | 2 | 11 | 3 |
| Too Small Proceeds | 10 | 4 | 8 | 4 |
| Animal and Crop Diseases | 21 | 1 | 21 | 1 |
| Untimely Loan Disbursement | 16 | 3 | 12 | 2 |
| Spearman's Rank-Order Correlation between 1988 and 1989 surveys = 0.80 | | | | |

^a Bashir (1988).

^b Nyako (1989).

Drought came second in importance as a real cause of delinquent loans in Gombi local government area, while it was cited as number three problem in Maiduguri local government area. Drought is a recurrent problem in the northern part of Nigeria. Thus, mere provision of loans to the farmers does not properly address their felt needs. A complementary solution should be devised, such as large-scale irrigation projects whereby plots will be allotted to farmers at full cost of providing the services. This measure will certainly ensure that farmers have something to harvest and therefore be able to repay their loans.

Untimely disbursement of loans featured prominently among the problems cited. Farmers cited cases whereby loans were received after harvest. Such late disbursements of loans are subject to diversions which could ultimately precipitate loan default. Lack of storage facilities and too small proceeds from farming were among the problems causing delinquent loans. Farmers who generally complained about low proceeds from farming were

observed to have large family sizes compared to their farm sizes. Integration of marketing and storage facilities with the credit scheme could facilitate an effective use of loans and at the same time increase the welfare of the small-scale farmers.

7.2. Characteristics of Loan Defaults by Farm Category and by Bank

Sampled farmers were categorised into three on the basis of their farming characteristics, viz: monocropping, mixed cropping and livestock husbandry. When loan repayment ability was analysed under these three categories, the frequency of defaults was highest among farmers practising monocropping in the two surveys. Because this category of farmers did not diversify their production risk, not only was it difficult for them to repay their debts, it was excruciatingly difficult for them to feed their families. Livestock farmers had the lowest rate of loan default and therefore the highest record of loan recovery.

In the 1989 survey, 13 livestock farmers borrowed from the three banks a total sum of N83,500 and repaid 61.2 percent of the loans. Twenty-three farmers practising mixed cropping received total loans of N143,000 and repaid 58.3 percent. Twenty-four monocroppers received N145,000 but repaid barely 50 percent of the loans. The results for the 1988 survey were also very similar.

In the 1988 survey, 45 farmers were interviewed. Of the 45, 14 fully repaid their loans; 23 partially defaulted and 8 were completely delinquent. In other words, roughly one-half of the number of loans disbursed were delinquent. Of the 60 farmers interviewed in 1989, 26 loans were fully repaid; 20 were partially delinquent, while the remaining 14 did not pay back at all. That is, 57 percent of the sample did not meet up their repayment obligations.

Considering interbank policy variations, the survey results showed that the more liberal the bank was in extending loans to the farmers, the greater was the rate of defaults. NACB has the most liberal loan policy of all the banks included in this study and recorded the lowest recovery rate of 51 percent. FBN, with the most stringent requirements (see Table 4), had a fairer recovery rate than UBN and NACB. In the 1988 and 1989 surveys, FBN recovered 63 percent and 61 percent of the loans disbursed, respectively. In respective years, UBA similarly recovered 60 percent and 69 percent of the loans disbursed to the sampled farmers. UBN, on the other hand, neither fared well as FBN nor UBA but did slightly better than NACB by recovering 53 percent of the loans disbursed over the study period.

8. Policy Suggestions for Rural Credit Effectiveness

It is not just enough to make credit available to farmers and expect remarkable improvements in their productivity and general welfare without first addressing some underlining policy deficiencies. Certain institutional and organisational policy structure has to be developed before credit can be used as an effective development instrument. Factors that are crucial to agricultural credit policy effectiveness centre around development and coordination of institutional and organisational structure for agricultural credit administration. For one thing, the agricultural policy environment in Nigeria has been beclouded by lack of programme continuity or lack of policy cohesiveness, due probably to frequent political instability. Rather than building on an existing programme, each successive government starts a new programme which does not necessarily complement the previous one.

For ACGS to be effective in achieving its primary objectives and to ensure its viability, the following suggestions are paramount.

8.1. *Provision of the Right Institutional Framework for Rural Credit Administration*

The rural credit market in Nigeria needs to be restructured and strengthened so that the new focus will be more on credit capacity rather on credit needs in order for the system to be self-perpetuating. Credit should be conceived of just like a marketable product that has to be well organised, packaged, and merchandised.

The design of ACGS did not give a careful consideration to contract law and enforcement. Such situation has encouraged wilful default, which has eroded away confidence in the system and thus increased lending and borrowing costs. The government should therefore see to enforcement of contract law in order to restore confidence into the system. Confidence is a fundamental requirement for lasting relationships to exist between the lender and the borrower, without which the survival of the rural financial market will be threatened.

A relevant observation with regard to the ACGS loans is that the loan structure is characterised by short-term loans, which are indicative of shaky confidence and lack of commitments of lenders to longer-term relationships.

The government should create a competitive environment in the rural financial market, which is characterised by minimal intervention in order to enhance efficient functioning. More effort should also be geared to institutional building, such as proper training of managers, supervisors and loan officers, so as to facilitate efficient management and viability of the credit system. Institutional viability is a prerequisite for any credit system

to succeed. The institutional framework should be such that will coordinate provision of credit with research and extension, infrastructural development and marketing services.

8.2. Establishment of Interlinked Relationships Between Lenders and Borrowers

The rural credit policy environment in Nigeria is such that mandatory lending requirements create a state of conflicting goals between financial institutions and the government. Lending at subsidised interest rates and without collaterals ignore the risk involved in lending and give no incentives to financial institutions to avow their support for the policy to succeed. The design of rural credit system has, therefore, not ensured banks' participation but has otherwise created a state of conflict.

A realistic rural credit scheme will encourage interlinked transactions between lenders and borrowers. Systematic and mutual links between lenders and borrowers will facilitate screening and therefore reduce the costs of asymmetric information associated with lending to agriculture. Moreover, disbursement lags will be reduced once a rapport has been established and designing more flexible lending and repayment arrangements will be enhanced.

8.3. Coordination of Loan Disbursement and Repayment with Marketing of Products

Lack of organised marketing arrangements for agricultural commodities has been a serious problem for Nigerian farmers. Coupled with absence of adequate on-farm storage facilities or proper preservative techniques, farmers are forced to sell at low prices during harvest, and cases of wastages due to lack of access to market outlets are even rampant. This problem does not augur well for production activities supported with borrowed money.

For effectiveness of the credit scheme, the government should tie loan disbursement and repayment with produce marketing. The design of the marketing channel should be such that will afford the borrowers the opportunity of alternative marketing sources. In other words, the government should be the buyer of the last resort. Interlinked relationships of the lender with the borrower will allow close supervisions and thereby avail the credit agency of the risk of wilful defaults. In event of any unforeseen circumstances, flexible repayment arrangements could be evolved.

8.4. Creation of Debt Capacity Through Infrastructural Development

Small-scale farmers have limited debt-servicing capacity because they are poor. Despite

their precarious position, inadequate provision of physical infrastructure, such as transportation and communication networks, has compounded their ability to meet debt obligations. For example, how will marketable surpluses get to market centres when the roads are impassable? Lack of motorable roads, inaccessibility to latest technological innovation, absence of on-farm storage facilities — just to mention a few — have all contributed to ineffective credit delivery and high rural loan default rates in Nigeria.

Research has shown that a relationship exists between agricultural development and investment in physical infrastructure.¹⁹ The government can improve small-scale farmers' debt capacity (i.e., loan repayment ability) by embarking on rural road construction in order to facilitate accessibility to the market and thereby reduce transport costs. Improvements of storage techniques and facilities (through research and development) will allow farmers to gain control over the timing and pricing of their marketable surpluses. Thus, development of infrastructure will play a facilitative role in making provision of credit an effective development instrument.

Drought has been a persistent problem in northern parts of Nigeria. Some of the delinquent loans have also been associated with drought-related problems. An effective way of making credit works will be for the government to embark on irrigation development policy alongside with provision of credit. The irrigation services should be provided at full cost, while credit will be provided for purchasing production inputs. By synchronising irrigation facility with credit, a great stride can be made in improving the lives of the rural people.

Comparing the social benefits and costs associated with government investment in irrigation systems versus provision of rice price support in the Philippines, it was found that, despite its large initial capital outlay, irrigation investment imposed less financial burden on government compared to fine-tuning commodity prices.²⁰ In terms of social benefit-cost ratio, irrigation development was more efficient than rice price support. In fact, the government cost required for rice price support was almost ten times the amount required for irrigation development. The above findings thus reinforce the thinking that improving physical and institutional infrastructure can provide a long-run efficiency in enhancing the welfare of the people.

19 Antle, J. M., "Infrastructure and Aggregate Agricultural Productivity: International Evidence". *Economic Development and Cultural Change*, Vol. 31, No. 3, 1983, pp. 609-619.

20 Hayami, Y., E. Binnagen and R. Barker, "Price Incentive Versus Irrigation Investment to Achieve Food Self-Sufficiency in the Philippines", *American Journal of Agricultural Economics*, Vol. 59, No. 4, 1977, pp. 717-721.

8.5. *Encouragement of Group or Cooperative Lending Arrangements*

Geographical dispersions of farmers necessitate that farm lenders must incur high administrative and transaction costs on monitoring and servicing loans. Thus, costs can be reduced by targeting group farmers. While such a team approach to lending not only reduces monitoring cost, the rates of default could also be reduced because each group will like to protect its integrity. Following up on irrigation development policy, it will be more manageable and cost effective to provide services to groups of farmers or cooperative societies. Without a carefully planned institutional and organisational structure for rural credit administration, the objective of using credit as a development tool may not be realised.

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Abstract

Governments of many developing countries often intervene in rural credit markets, hoping to induce technological adoption and to increase agricultural productivity. Lack of well coordinated institutional and organisational structure for agricultural credit administration has caused the good intentions for intervention to yield unintended negative results. A case study of Agricultural Credit Guarantee Scheme in Nigeria examines the viability, problems and measures that could enhance an efficient management of the scheme. One hundred and five small-scale farmers and four banks participating in the scheme were surveyed. The fundamental shortcoming of the scheme, vis-a-vis government regulations affecting it, is that its design and operation undermined the role of risk in credit decisionmaking. The scheme's lending focus on credit needs threatens its viability as evidenced by mounting delinquent debts. Suggestions for an efficient management of the scheme are offered with a view to promoting viability and growth.

LE FINANCEMENT DE L'AGRICULTURE PAYSANNE: LE CAS DU PROJET DE GARANTIE DU CREDIT AGRICOLE DU NIGERIA**RESUME**

Les gouvernements de beaucoup de P.V.D. interviennent souvent dans les marchés de crédit agricole dans le but de favoriser l'adoption de technologies modernes et d'augmenter la productivité agricole. Le plus souvent, toutefois, à cause du manque de structures pour l'administration du crédit agricole bien coordonnées au niveau institutionnel et de l'organisation, ces bonnes intentions d'intervention produisent des résultats négatifs non voulus. L'étude du cas du Projet de Garantie du Crédit Agricole (Agricultural Credit Guarantee Scheme) au Nigéria analyse la viabilité et les problèmes du projet aussi bien que les mesures qui pouvaient en rendre plus efficace l'administration. L'étude a concerné 125 fermiers et quatre banques qui ont participé au projet. Le point faible du projet vis-à-vis les prescriptions du gouvernement qui l'ont affecté est que sa conception et son fonctionnement ont sapé à la base le rôle du risque dans le processus de prise de décision concernant l'octroi du crédit. Si, dans le cadre du projet de crédit, on concentre son attention sur le besoin de crédit on met en danger sa viabilité, comme le démontre l'accumulation des impayés. L'Auteur propose des suggestions pour arriver à une administration plus efficace du projet qui pourrait en stimuler la croissance et la viabilité.