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A.I.D.
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USAID / KENYA

NON-CAPITAL PROJECT PAPER

(PROP)

AGRICULTURE CREDIT

615-11-140-148

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January 26, 1971

January 22, 1971

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Reference Center
Room 1656 NS

NON-CAPITAL PROJECT PAPER (PROP)

Country: Kenya

Project Number: 615-11-140-148

Submission Date: January 22, 1971

Project Title: Agriculture Credit

U.S. Obligation Span: FY 1971 through FY 1979

Physical Implementation Span: FY 1971 through FY 1980

Gross Life-of-Project

Financial Requirements: U.S. Dollars	650,000
U.S. owned local currency:	-
Cooperating Country cash contribution	\$300,000
Other donors	-
Total	<hr/> \$950,000

I SUMMARY DESCRIPTION

A. General

This PROP covers the initial phase of the project and is designed assist the major agricultural lending agency of the Government of Kenya, the Agricultural Finance Corporation (AFC), in its efforts to develop a supervised credit system for both small-scale and large-scale farmers.

B. Necessity and for Project

The major sponsored farm credit programs in Kenya since independence have had numerous problems involving administration, general management, personnel, equipment, funding and long-term objectives in the field of agricultural credit. At the request of the Government of Kenya a study on the state of agricultural credit in the country was carried out by a three-man, AID-financed survey team headed by Robert B. Tootell, during the period January 19 to April 3, 1970.

In its analysis of the agricultural credit programs in Kenya the Tootell Mission found that:

- (1) The greatest deficiency in Kenya is seasonal operating credit which has contributed to arrears on land loans and development loans.
- (2) The poor organizational structure of AFC arising from (a) the centralization of most loan decisions in the Head Office; and (b) the "compartmentalization" of the Nairobi office, limits its ability to properly serve Kenya farmers. There has been much inefficiency in making and servicing loans and long delays in getting loan funds to borrowers.
- (3) There is a tremendous need for an effective educational program for farmers so that they will come to understand the meaning of credit and how to use it effectively.
- (4) The AFC makes many small loans to less experienced farmers who require more loan supervision with greater servicing cost. Without further government subsidy the corporation will be unable to serve more of these small commercial farmers.
- (5) The present office equipment is unsuitable for dealing with the accumulation of cost information and statistical data.
- (6) The Corporation depends heavily upon expatriates because of the acute shortage of trained Kenyan personnel who understand farm business analysis and the gearing of agricultural lending to the needs of each individual farmer and to his ability to repay.

The Tootell Report clearly shows that a critical bottleneck hampering more rapid progress by Kenyan farmers and ranchers is the development of a viable agricultural credit organization capable of meeting the credit needs of both large and small scale Kenyan farmers.

The Government of Kenya recognizes that in order to accelerate agricultural development in the country an institutional pattern for constructive credit service must be devised and a course of action determined. This requires expertise in the highest levels of the major public organization providing credit to farmers

The lack of qualified agricultural credit manpower has led the Government of Kenya to seek external assistance. AID has been asked to provide operational personnel to man several of the top managerial positions in the AFC during an eight-year period, in which Kenyans can be properly trained for these jobs.

C. Project Goals and Targets

- (1) To provide assistance to the AFC in establishing areas of priority for agricultural credit.
- (2) To provide in-service training and counterpart training for staff.
- (3) To identify and propose improved procedures in the operation of a rural credit program for small farmers.
- (4) To reorganize the present structure of AFC in order to improve the administration and management of agricultural credit.
- (5) To provide assistance to the AFC in continuing and improving a rural credit program for newly established Kenyan ranchers.
- (6) To recruit technical staff and establish a cost data accounting system, preferably in cooperation with the Agricultural Development Corporation and other financial organizations.
- (7) To develop and recommend uniform methods of funding, conducive to a sound fiscal policy.

D. Minimum Levels of Output or Achievement.

The minimum levels of output for this project are:

- (1) Reorganization of the Agricultural Finance Corporation.
- (2) Staffing and personnel training at all levels.
- (3) Updating and modernizing the accounting system.
- (4) Adequate GOK financing for the Corporation.
- (5) Adequate coordination of AFC programs with the Ministry of Agriculture and other allied departments.

E. General Approach and Plan of Action

(1) General Approach

To provide technical expertise in the field of agricultural credit through a PASA with the U.S. Department of Agriculture to secure the services of two qualified agricultural credit personnel - one to take over the position of General Manager of the AFC and the other to be Manager of the Loans Department.

The General Manager will be responsible for developing programs, to improve and expand his staff, and for improving the general capabilities of the AFC in all aspects of agricultural finance. The Loans Manager will serve as Head of the Loans Department and will be responsible for overseeing the operation of this department, the implementation of loans, loan collections and the analysis of loan applications.

(2) Plan of Action

1. AID Input

AID will provide two operational technicians to serve as General Manager and Loans Manager of the AFC. These technicians will operate at the highest levels, not only in the AFC, but in the Ministry of Agriculture - to help re-shape the AFC so that within approximately eight years it will be able to effectively manage the credit requirements of a greatly expanded number of Kenya's farmers and ranchers, large and small.

A possible second phase of the project, dependent upon the findings of the two U.S. technicians in consultation with top GOK agriculture and finance officials, may call for the inclusion of additional U.S. technician support to help re-design and expand the branch offices of the AFC. As this aspect is developed early in the project it will be the subject of a revision to the present PROP.

2. GOK Input

The GOK will nominate and select personnel to receive formal training at the degree level in the U.S.A. and counterparts for practical training courses conducted by the agricultural credit advisers, technicians from the extension activities under the Crop and Livestock Project (615-11-130-101) and personnel from Egerton College. The GOK will also provide housing and support for the General Manager; payment into a special USAID account of an amount in Kenya shillings equivalent to the local base salaries of the two technicians, and the housing allowance and local support costs of the Loans Manager.

Other Donors

Other donor contributions to various aspects and activities of the AFC:

<u>Donor:</u>	<u>Assistance</u>
I.D.A. (KF)	\$3,500,000 loaned to AFC for re-lending to small-scale farmers.
West Germany	\$560,000 for small-scale farmer loans \$350,000 for large-scale farmer loans

TABLE 1 - AMOUNT OF CREDIT AFC HAS MADE AVAILABLE ANNUALLY & LONG-TERM

<u>Loans</u>	<u>Amount (U.S.\$)</u>
1. G.M.R. (Guaranteed Minimum Return)	\$11,000,000*
2. I.D.A. #105	3,500,000*
3. I.D.A. #129	7,500,000**
4. British Transfer	3,500,000**
5. K.F.W. Large-scale (Kreditanstalt Fur Wiederaufbau)	400,000 (5-7 years)
6. K.F.W. Small-scale	400,000 (5-7 years)
7. Old Land Bank Loan	10,000**

* Annually

** Long-Term (extends over a period of 20 years)

TABLE II - NUMBER OF LOANS MADE AVAILABLE SINCE AFC CAME INTO EXISTENCE

<u>Loan</u>	<u>Number</u>
1. G. M. R. (Guaranteed Minimum Return)	4,000
2. I. D. A. 105	6,000*
3. Land Loans	4,000

* There are 8,000 loans of which 6,000 have been processed.

NOTE: AFC is servicing 15,000 old accounts.

SETTING OR ENVIRONMENT

A. Description of the AFC

The Agricultural Finance Corporation plays an important part in the agricultural development of Kenya. It is the government's only instrument for dispensing farm credit. In 1963 the Corporation was established to provide credit for the development of agriculture and agricultural industries. It is an amalgamation of two institutions created before the country's independence: the Land and Agricultural Bank of Kenya and the Agricultural Finance Corporation. Both of these institutions were founded originally to serve large-scale European farmers.

As the major public body administering agricultural credit, AFC has taken over outstanding loans previously made by District Loan Boards and a number of other loans made under special schemes. It has the responsibility of carrying out new farm credit programs, either from its own resources, or as the agent of the government. In attempting to carry out its primary function, the AFC has not been as effective as the agricultural situation in Kenya requires.

The Tootell Report, among other things, found that the AFC had developed the habit of establishing a separate section to handle each new function, as it was added to the AFC. The organization of the head office, for example, reports directly to the General Manager. The administrative and supporting services report to the Deputy General Manager. The General Manager, Deputy General Manager, and the Financial Comptroller serve as an informal loan committee for large-scale loans whereas all other loans are approved by the Division handling related functions. These weaknesses arise primarily from the centralization of most loan decisions in the Head Office and the "compartmentalized" set up in the Head Office. This has resulted in:

- (1) delays in making and servicing loans;
- (2) similar operations being performed in several places in the Head Office;
- (3) branch offices consulting several departments and different individuals for instructions in carrying out comparable functions;
- (4) major functions of authority and responsibility not clearly defined, creating confusion and delay in carrying out daily tasks.

B. Problem Areas

(1) The most serious limitation to expanding credit services to Kenya farmers is the acute shortage of personnel in the AFC and other agencies able to analyze a farm business and determine the optimum level of credit it requires. Borrowers who have successfully obtained credit from the AFC in the past have not received the required supervision and/or instruction on how to utilize the credit properly.

(2) Collections of loans have been made primarily through threat of foreclosure rather than from the desire of the borrower to repay from the increments of production and his desire to maintain a good credit rating as a basis for future production financing.

(3) A lack of seasonal operating credit has been a related major problem. Not only must credit be ample, it must be timely - available when the farmer needs it. This will require improved management and planning, as well as a trustworthy flow of information from the AFC field staff. To date all of these are inadequate and as a result the farmer suffers.

(4) Teaching and research in farm business and credit have been inadequate in providing workers in these fields with instruction in farm business analysis and in the nature of and practical use of credit.

C. Description of the Overall Situation Confronting Agriculture in Kenya

The Government of Kenya has, naturally, placed a very high priority on rapid agricultural development. The preponderant majority of Kenyans depend on agriculture for their livelihood. Likewise, because agriculture is such an important component of the economy, rapid development of the agricultural sector has a major role to play in contributing to the growth of the whole economy.

Much of the government's effort in the agricultural sector before and after independence was devoted to the land transfer and resettlement programs. Subsequently, it was decided to give much greater emphasis to the development of the small-scale farm areas. Such areas have not been expanding agricultural output. A contributing factor to this lack of expansion has been the unavailability of public credit to smallholder agriculture. In 1966 it was estimated that there were about 35,000 small farmers in the Scheduled Areas, formerly restricted to European farmers. In addition, there were about 150,000 small-scale farmers in the former African areas who required credit programs fitted to their needs.

The number of small scale farmers has increased, but has not substantially contributed to increase agricultural output in helping to finance the economic development of the country. The standard of living of the small holder farmers has remained stagnant.

The problems encountered in administering loans for small-scale farmers are serious, but must be faced and solved if the majority of Kenyan farmers are to be a part of the country's economic development.

The machinery necessary for identifying qualified borrowers, processing applications and monitoring repayments has simply not functioned effectively. The agricultural credit institutions are generally burdened with heavy arrears and potential losses as a result of a poorly conceived and administered program.

An increase in the availability of properly managed agricultural credit will improve the economic condition of a substantial number of farmers and ranchers which will help increase the economic stability of the country. It will also improve the effective utilization of loan funds; and provide a more systematic collection and follow up mechanism.

D. Relationship of Project to Goals of Kenya's Development Plan, 1970-74.

(1) Purpose of Project

The overall objective is to improve the ability of AFC to function effectively in making credit available to larger numbers of agricultural producers in Kenya..

(2) Relevant Goals of the Plan

- (a) To increase agricultural incomes of rural farmers.
- (b) To help improve the standard of living of the rural population.
- (c) To provide a well administered credit system for small-scale as well as large-scale farmers.

An improved agricultural credit institution and a well administered program would assist in increasing the agricultural productivity of rural farmers in the country.

There would be expanded credit services to the farmers which include:

- (1) a better repayment scheme to the lender;
- (2) increased farmer income resulting from greater output;
- (3) improved farming methods such as the use of improved livestock, fertilizers, better seeds and pesticides, yielding greater agriculture outputs.

E. Economic, Social and Administrative Obstacles

(1) Economic

There are two major economic obstacles which affect the achievement of project goals:

- (a) the small size of the vast majority of Kenyan farms, and
- (b) the need for a relatively small but, nevertheless, difficult to obtain initial slug of capital to raise the economic level of many cultivators to a point where they can take advantage of a credit system. This may require a fair amount of subsidization of loan money for farm production purposes and the completion of the on-going program of land surveys upon which title to land is recognized.

(2) Social

The social obstacles involve educating the farming public to understand the need for proper utilization and repayment of loans; also, alleviating superstitions of indebtedness (for example: that a curse will be placed on the rest of the family upon the death of the individual who has incurred an unpaid debt).

(3) Administrative

- (a) Poor management techniques.
- (b) Current structure not properly aligned to perform required functions.
- (c) Lack of trained personnel at all levels.

F. Strategy and Method Proposed to Achieve Project Purpose

(1) Inputs

AID will provide two credit technicians to serve as General Manager and Loans Manager of the AFC.

The General Manager will:

- A. 1. Advise the Ministry of Agriculture, the Treasury and the Central Bank of the Government's short and long term policies, regarding agricultural credit and related financial matters.

2. Recruit technical staff and establish a cost data system accounting, preferably in cooperation with the ADC and other financial organizations.
3. Develop and recommend uniform methods of funding, conducive to a sound fiscal policy.
4. Recruit such staff members and technical assistants as seem necessary to overhaul and improve the house-keeping and general management in the major problem areas.
5. Study and determine, in cooperation with government officials, the long term objectives of the Agricultural Finance Corporation, in the field of agricultural credit and initiate comprehensive technical and development programs to carry these out.

The Loans Manager will:

1. Serve as head of the Loans Department and oversee the operations of that department.
2. Manage the loan implementation processes of the AFC.
3. Be responsible for continuing the improvement of the loans collections.
4. Improve the system of analysis and review of loan applications.

b. Participants

AID will provide financing for participant training at the university level in the U.S.A. for Kenyans identified by the U.S. technicians as showing a high degree of promise for rapid advancement within the AFC. The total number of participants to be sent will be approximately six. If the General Manager, in consultation with GOK authorities and USAID/ Kenya determines that the need for training in U.S. universities is greater than this figure, he will prepare a justification which will serve as an amendment to this PROP.

c. Commodities

No U.S. commodity input is being considered at this time.

d. Other Costs

The Other Costs element will be limited to housing for the Loans Manager (for which the GOK will provide partial reimbursement to AID in the form of payments equal to the standard GOK housing allowance for technicians at an equivalent grade), plus small miscellaneous support costs for the two technicians

2. GOK Inputs

a. Personnel-

The GOK would continue providing all costs for the on-going personnel establishment of the AFC. The government has agreed to pay to the Mission an amount in Kenyan shillings, equivalent to the local base salaries of the two U.S. technicians.

b. Participants

The GOK would assist in the selection of participants, would agree to release them from present assignments for training in the U.S.A., would continue to pay base salary and allowances, and would pay one-half of the round trip air fare from Kenya to port of entry in the U.S.A.

c. Commodities

The GOK has already shown willingness to replace the current inadequate loan processing and budgeting office equipment with more modern and efficient equipment, capable of keeping up with the paper work load. This will vastly improve the system of maintenance of accounting records and in accordance with one of the important recommendations of the Tootell Survey Mission.

d. Other Costs

The GOK provides housing for the General Manager and a housing allowance (paid to the Mission) for the Loans Manager.

Outputs

Proper performance of project inputs should result in achieving the following outputs:

- a. Reorganized administrative structure of AFC which would enable it to expand its farm credit capacity and manage its credit programs more effectively.
- b. An increase in the number of trained loan officers in the AFC and its branches.
- c. An expanded, better coordinated system of field offices.
- d. Improved financial management.
- e. An increased number of rural farmers and ranchers who have a better understanding of rural credit and who, as a result, have adopted improved farm methods and have been able to utilize the credit program effectively.

These outputs would contribute to the achievement of the project purpose - a self-perpetuating agricultural credit institution in Kenya, able to lend to farmers, and collect from them a fairly large amount of credit in an efficient and effective manner.

The inputs proposed will, however, only partially achieve the desired outputs since the Tootell Report suggests that the approach for reorganizing the AFC and developing new management techniques will cover a period of eight years. This PROP provides only for the input of two technicians which will largely remedy the administrative deficiencies in the head office with some lesser effects being felt in the numerous branch offices around the country. It is anticipated that a minimum of three additional technicians will be needed to more satisfactorily accomplish project objectives. Their expertise would be directed toward an effective training program and raising the quality of performance of branch operations, a very important aspect of AFC's function. It is expected that this additional input will be forthcoming within eighteen months in the form of an amendment to this PROP.

PLANNED TARGETS, RESULTS & OUTPUTS

These will include the following:

1. Redesign the organizational structure of the AFC.
2. Conduct in-service training for professional improvement of the entire AFC staff.
3. Increase loan disbursement by minimum of 50 per cent by 1975.
4. Increase loan collection by 50 per cent by 1975.
5. Increase number of processed loans in branch offices from 0 to 50 per cent by 1975.
6. Machine processing of loans by 75 per cent by 1973.
7. Train six participants in farm credit administration and management at the degree level by 1978.

APPENDIX A

REPAYMENTS ON LOANS
As of Jan. 1. 1971

<u>Loans</u>	<u>Committed</u>	<u>Disbursed</u>	<u>Collected</u>
I.D.A. 105	85%	60%	80%
I. D. A. 129	25%	10%	Repayment on loans not due (just standing).
K. F. W.*	-	-	-
British Land Transfer	100%	95%	70%
G.M.R.**	-	-	60%

* New program

** Handled on an agency basis.

APPENDIX B

STAFFING PATTERN
Senior staff as of Jan 1, 1971

<u>Divisions</u>	<u>Expatriates</u>	<u>Kenyans</u>
Administration	1	2
Loans Department	4	5
Finance & Accounts Dept.*	2	2
Legal section	-	2
Audit Section	1	1

* Two positions not yet appointed. They will be filled by Kenyans

NOTE: AFC employs not on the basis of authorized position, but in terms of needs. Other positions approved by the Ministry of Agriculture and Ministry of Economic Planning and Finance, are the following:

- a. Two German technicians
- b. Two technicians from the Netherlands
- c. One Canadian technician.

AFC is recruiting seven trainees from Egerton College, presumably agriculture trained, for line positions in Branch Offices. Six Kenyan women are being trained for secretarial positions.

APPENDIX C

HEAD OFFICE STAFFING POSITION

General Manager	American
Deputy General Manager	Kenyan
Personnel & Business Services Department	Kenyan
<u>Loans Department</u>	
Head of Department	German
Farm Credit Advisor	American
Head, Farm Loans Section	Kenyan
Crop Production Officer	Kenyan
Officer i/c Small Scale Loans	Canadian
Farm Management Section	British/Kenyan
Credit Controller	Kenyan
<u>Finance & Accounts Department</u>	
Head of Department	Seychelloise
Chief Accountant	British
Deputy Chief Accountant	Kenyan
Senior Accountant i/c G.M.R. & Agency	Kenyan
Accountant i/c Large Scale Accounts	Not yet appointed
Accountant i.c Small Scale Accounts	Not yet appointed
<u>Legal Section</u>	
Head of section	Not yet appointed
Legal Assistant	Kenyan
Legal Assistant	Kenyan
<u>Audit Section</u>	
Internal Auditor	British
Internal Auditor	Kenyan