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CREDIT FOR SMALL FARMERS: INDONESIA,  
MALAYSIA, THAILAND

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# CREDIT FOR SMALL FARMERS: INDONESIA, MALAYSIA, THAILAND

Millard Long\*

## Introduction

During the summer of 1972 I undertook an investigation of credit programs for small farmers in Indonesia, Malaysia and Thailand. My study was not a comprehensive review but an evaluation of programs utilizing the private sector as a conduit for public loans to small farmers. Using the private sector to administer credit programs is an idea that has gained some popularity among aid-giving agencies desirous of channeling funds into agriculture but discouraged by the high administrative costs and default rates of government programs in this field.

Privately administered credit programs for small farmers can be appraised at two levels: the first assesses the differences between private and public sector administration of credit programs. The second examines the more fundamental issue of whether private or public credit programs are an efficient way of dealing with the problems of the small farmer. Section I considers the costs and comparative efficiency of public and private credit programs for small farmers in three countries--Indonesia, Malaysia and Thailand. Section II and III explore the issue of whether the benefits of any credit program for small farmers will under Southeast Asian conditions justify the costs. Section II presents two alternative views of the expected impact of credit programs on the output and welfare of small farmers. Section III

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\* Though this research was financed by the Agency for International Development (AID), the views and findings are solely those of the author.

considers the available evidence to determine which model is a more accurate description of conditions in Southeast Asia.<sup>1</sup>

#### Section I: Credit Programs in Indonesia, Malaysia and Thailand

There is much that is similar in attitudes, objectives, programs and experience with credit for small farmers in Indonesia, Malaysia and Thailand. Prior to recent reforms, the agricultural credit programs in the three countries were similar. A fraction of small farmers received institutional credit from semi-public cooperatives; larger farmers and agro-businesses could borrow directly from commercial banks. To the extent they borrowed, most small farmers depended for loans on non-institutional sources, such as friends and relatives or merchants-cum-money lenders. (Thisyamongdol, et al. 22) Small merchants, in turn, received credit from larger merchants; for example, wholesalers extended credit to retailers, millers to padi purchase agents, etc. (Geertz 6).

In none of the three countries are the cooperatives considered to be a successful credit program, primarily because of poor repayment records. Lack of success is blamed primarily on inefficient management and failure of farmers to use credit for productive purposes.<sup>2</sup>

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<sup>1</sup>Later in the Fall the data from a worldwide survey of credit programs for small farmers, now being conducted by AID, will become available. I hope to use this data for a more complete test of the two models.

<sup>2</sup>Little consideration has been given to whether cooperatives are culturally an appropriate form of organization in these countries; whether joint liability is a reasonable sanction against non-repayment; and whether low interest rates may not actually discourage repayment. Many of these features have been retained in the new programs.

To overcome these deficiencies new programs have been developed in all three countries to supervise the farmers' use of credit.

The programs are somewhat different, but in each greater emphasis is being placed upon increasing output and securing repayment than upon redistributing income in favor of small farmers. In fact farmers with less than average holdings are underrepresented in the newer programs. To prevent farmers from "misusing" credit for consumption purposes, in Indonesia and Malaysia farmers are given coupons for fertilizer, pesticides, etc., rather than cash, and in Thailand, each borrower's operation is supposed to be supervised by a lending officer.

These new public credit programs are to be the subject of separate papers by other authors and, therefore, will not be described or evaluated here in any detail. However, it is useful to note certain salient features. Except for the emphasis on production and repayment the program in Thailand, which is operated by the Bank for Agriculture and Agricultural Cooperatives (BAAC), differs little in structure from the older credit cooperatives. Farmers are still organized into small groups with joint liability for repaying loans; most loans are for one year and the interest rate is 12 percent. To administer the program and supervise the farmers, the apex bank has set up regional and local offices which roughly duplicate the organization of the Department of Cooperatives, still responsible for the administration of cooperative credit. In addition to public programs in Thailand, three of the commercial banks have voluntarily started credit programs for small farmers. These are very much like government programs--small groups of farmers, joint liability, 12 percent interest, etc. At present

the credit outstanding from the commercial banks amounts to \$7.5 million<sup>1</sup> loaned to 42,000 participants.

The new Indonesian and Malaysian programs are similar in their use of a coupon system rather than cash loans. The credit agency gives the farmer an amount of coupons dependent upon the area farmed. These can be surrendered by the farmer to obtain fertilizer, pesticides, etc. The merchant who receives the coupon then surrenders it for payment to the authorities. The loans are supposed to be repaid at the end of the cropping season.

The two programs differ in interest rates--18 percent per year in Malaysia and 12 percent in Indonesia--and in terms of administration at the local level. In Indonesia under the Improved BIMAS program the government has established village units manned by public officials to select participants and administer the program. In Malaysia those operations are delegated to local credit centers (lcc's) who are chosen from existing cooperatives, farmers associations and private traders. In 1971, the last group consisted of 36 individuals who administered about 35 percent of outstanding loans. It is the lcc's responsibility to select participants and to assure repayment. For this they receive the difference between the 18 percent interest paid by the farmers and the 6 percent interest charged by the apex bank, the Bank Pertanian.

My assignment was to look at credit programs for small farmers in which the private sector served as a conduit for public funds. Only in the case of the Malaysian program is the private sector used

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<sup>1</sup>Except where noted money figures are in U.S. dollars.

directly as a channel for government money. However, in the case of Thailand, the central bank allows the commercial banks to discount loans to small farmers at favorable rates. But because of their very liquid position, the three commercial banks involved in farm credit have made only limited use of this facility,<sup>1</sup> but this channel represents a potential conduit for public credit. In addition, in all three countries there are loans to agro-businesses by government agencies and indirectly by the central bank through discounting of loans by commercial banks. Without these loans there would probably be less private credit for small farmers. However, in the absence of detailed flow of funds data, it is not possible to evaluate these flows; it is quite likely, however, that they constitute an important component of the credit picture for small farmers.

Experience to date in these three countries is too limited to reach any firm conclusion about the relative efficiency of publicly and privately administered credit programs for small farmers. Piecing together what data is available indicates that the commercial bank program in Thailand is the least costly to administer. Of the commercial banks, only the Bangkok Bank could supply figures, but their program is the oldest and accounts for roughly two-thirds of all commercial bank loans to small farmers. They report their administrative costs to be four percent of outstanding loans. At the other extreme

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<sup>1</sup>Presently the World Bank is considering a loan to the central bank, the Bank of Thailand, to establish a fund for discounting loans to farmers of more than two years' duration. Loans by both commercial and public banks would be eligible.

is the Improved BIMAS program in Indonesia. Calculations reported in Turnier (26) and the Fertilizer Study (28) indicate that administrative costs exceed 25 percent of outstanding loans. In 1972 the administrative costs of the Bank Pertanian in Malaysia will be roughly 20 percent of average loan volume, while I estimate that in 1971 the administrative costs of farmers' program of the BAAC in Thailand was roughly 8 percent.

Administrative costs are always high for small loan programs, whether in developed or developing countries. Still there is substantial difference between the commercial bank experience in Thailand and the programs in Indonesia and Malaysia. There are several factors that help explain this difference. In Indonesia and Malaysia the average size of loans is considerably smaller than in Thailand; in Indonesia the average size is \$15, in Malaysia \$70, in Thailand \$160 at both the commercial banks and the BAAC farmers' program. In addition, in both Indonesia and Malaysia they are using a coupon system as against the more traditional cash loans in Thailand. I would expect the former to be more expensive, but in addition the system is new and innovations usually entail additional administrative outlays in their early years. Third in Malaysia, in particular, the program is still small in size compared to its administrative superstructure. While in Malaysia costs will undoubtedly fall with growth, it is not clear that the hoped-for savings from dealing with lcc's rather than directly with farmers will materialize.

Perhaps most difficult to explain is why the commercial banks in Thailand should have half the administrative costs of the very

similar semi-public program run by the BAAC. I do not have the information to judge whether the private sector is more efficient or whether the BAAC is providing more in the way of services to less accessible farmers.

In addition to having the lowest costs, the commercial banks in Thailand report by far the best repayment record. Again only the Bangkok Bank could provide detailed information; for this program arrears amount to between 3 and 4 percent. In its first two years of operation the BAAC had a similar record - 4 percent arrears; subsequently this increased to 28 percent in 1970 and 49 percent in 1971. Officials at the BAAC blame the decline on poor harvests and low farm prices. But spot checks conducted this summer indicated that in areas in which both the BAAC and Bangkok Bank were operating, the commercial bank had maintained a high level of repayment with the same output and price conditions.

Officials in the commercial banks believe it is the better preparation and incentives to field officers in the form of promotion that has helped them achieve their better repayment record. Very rapid expansion in the BAAC program has undoubtedly led to a decline in the quality of field personnel; regional directors complained of the poor training of new recruits. Secondly, the BAAC's program now includes 250,000 farmers; perhaps expansion has forced the BAAC to accept less creditworthy clients. Third, new loans can be used to repay old. In the early stages of a credit program, that is as long as individual farmers are getting larger amounts of credit each time period, they will make repayments. Their repayments slow however, as soon as expansion stops.

Among the different types of lcc's in the Malaysian program the cooperatives and farmers associations have better repayment records, averaging 10 percent arrears against 20 percent for the private lcc's. However, of the present 36 private lcc's, two are responsible for all the arrears, while among the semi-public lcc's many have overdue loans outstanding. Officials of the Bank Pertanian believe that when the fraudulent operators have been removed, private lcc's will, as expected, prove to be better collection agencies than the semi-public lcc's. Because the program is only in its third year the overall repayment rate, 14 percent arrears, is hard to appraise. The Bank Pertanian is attempting to avoid administrative and repayment problems by expanding slowly. Only experience will show whether it can avoid the high level of arrears of the BAAC in Thailand. In Indonesia, arrears under the Improved BIMAS program amount to 19 percent. This is a vast improvement over earlier credit schemes, but this record refers to only 1½ years of operation and it is too early to judge whether this record can be maintained.

In terms of resources used, defaults are a transfer payment, not an operating cost. In fact they constitute a transfer to some of the small farmers the credit program was designed to help. However, governments in South-east Asia are not so sanguine about defaults, considering them a cost not a benefit of the program. Their behavior suggests that administrators of public credit programs do not consider a dollar of defaults to have the same social cost as a dollar of administrative outlays. In each of the public programs reviewed, additional expenditures on administration would probably

have led to more than an equivalent reduction in defaults. The cost coefficient public administrators implicitly assign defaults appears to be less than one. This should be borne in mind in comparing the efficiency of public and private credit schemes <sup>and</sup> /of credit and possible alternative programs.

Though all of the programs stress their semi-commercial nature, it is clear that only the scheme of the Thai commercial banks comes close to covering costs. The Bangkok Bank has a combined <sup>administrative</sup> /cost and default rate between seven and eight percent against interest charges of 12 percent.<sup>1</sup> To break even in the long run the commercial banks would require a return over costs of seven percent, the rate they pay for time deposits. However, as the banks presently have excess liquidity, they are not too concerned about the immediate return as long as they cover operating costs. Each of the three banks stated their loans to small farmers were not profitable, but that they had entered the program for service reasons and to build a position with the farm community that in the long run might prove profitable. However, given the lack of profitability and the growing doubts (discussed below) that the program is really helping farmers, there is little incentive for the banks to expand. In recent years no additional banks in Thailand have started credit programs for small farmers, and two out of the three banks presently making loans have decided to hold their programs to the present size.

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<sup>1</sup> Banks can now rediscount agricultural loans at the Bank of Thailand at 5 percent. However, they must then limit their interest charges to farmers to 10 percent.

In the other programs costs plus defaults greatly exceed earnings. Only in the case of the BAAC in Thailand do interest earnings at 12 percent cover administrative costs. At 12 and 18 percent in Indonesia and Malaysia respectively, interest rates do not cover administrative costs of between 20 and 30 percent, let alone provide an allowance for bad debts/ or a return on capital. I have argued earlier that governments do not and probably should not consider a dollar of bad debts on agricultural loans as equivalent to a dollar of administrative costs. But even if a zero cost is assigned to bad debts in Indonesia and Malaysia, the programs still do not cover/ administrative costs. In commercial terms, with the full costs of defaults considered, none of the three government programs come close to breaking even.

Sections II and III explore the question of whether the benefits from a credit program for small farmers is likely to cover the costs discussed in this section. But for governments that decide in favor of a credit program, channeling funds through the private sector is an administrative technique worth considering. There are many alternative procedures which range from loans to agro-business as presently done by the Bank Rakyat and Bank Bumidaya in Indonesia and the commercial banks in Malaysia and Thailand, to programs for central bank rediscounting of loans to farmers as in Thailand, to employing private traders to screen and insure repayment on loans as in Malaysia.

Thus far the evidence from Malaysia and Thailand on the supposed advantages of using the private sector is mixed. In Malaysia the administrative costs remain high and the private lcc's repayment record

is spotty. From the standpoint of budgetary efficiency, the agricultural credit program of the commercial banks in Thailand has proved more efficient than any of the other programs reviewed. But the reasons for its success are not fully understood and might disappear were the program to expand. Only further experimentation with private sector credit programs tailored to the specific needs and institutions in each country will test their efficacy against publicly administered alternatives.

## Section II. Benefits of Credit Programs--Alternative Views

The objectives of credit schemes for small farmers are to increase agricultural output and to raise the welfare level of small farmers. But such objectives are common to many programs, and given the high costs of credit mentioned in Section I, are there not perhaps more efficient ways for accomplishing these objectives? Without information on the administrative costs and problems of alternative approaches no decision can be reached, but the advantages of a credit program depend in large part upon the workings of the credit market about which we have little direct information. This section describes two polar views of that market and the next explores the available bits and pieces of information which may help us distinguish between the two models.

Those in Asia who advocate credit programs for small farmers seem to hold the following picture of the credit market: small farmers are poor because they lack sufficient capital. To take advantage of existing opportunities, they need loans, which often they cannot obtain from the private sector at a reasonable rate of

interest. Private rates are considered unreasonable for one or more of the following reasons: the interest rate charged exceeds the rate of return on agricultural investment; credit does not flow easily and quickly between sectors causing higher rates in agriculture than elsewhere in the economy; the credit market is monopolized. In Southeast Asia those who hold the last view often add that the monopolistic lender is Chinese, while the disadvantaged borrower is of the indigenous stock. Supporters of credit often add that small farmers are unaware of their opportunities and tend to use credit for consumption purposes. If allowed to do this, farmers find themselves with added debts and no more income and, therefore, unable to repay their loans. For this reason the farmer's use of credit must be supervised to insure the money is spent for productive purposes.

The alternative view starts from the proposition that net investment in traditional agriculture is small not because farmers cannot obtain credit, but because the rate of return on capital in traditional agriculture is low (Schultz 20). When the rate of return rises, as with the green revolution, new investment takes place. Farmers find the funds to meet these expenditures by increased savings, by sale of lower yielding assets or by borrowing. Government credit programs can probably speed the rate of adoption of new technology, especially among small farmers, but to the extent the new technology is advantageous and divisible, it will be adopted by small farmers whether or not they have access to institutional credit.

In this model capital, albeit not instantaneously, gets allocated to those uses in which it has the highest yield. As long as yields are higher elsewhere than in agriculture, capital will be gravitating toward other uses. When the yield increases in agriculture, the direction of flow is reversed. To attempt through a loan program to move resources into agriculture when yields favor the use of capital in other sectors is to move against a very strong current.

For those who hold this view, existing interest rates in agriculture are high, but the rates can be explained by the scarcity of capital, the default rate and the costs of administering small loans. The observed rates are believed compatible with competition and the relatively free flow of capital between the rural and urban sectors. In this view, an increase in institutional loans may through a change in the interest rate structure cause a reallocation of private funds to non-agricultural uses which may frustrate an attempt to increase total credit to agriculture.

The models outlined above are polar alternatives; most would admit that reality falls somewhere between. Capital markets are not perfect and adjustments to changes less than instantaneous. Yet the question is which model best describes the situation in Southeast Asia. If credit is fairly fungible then the rate of return, not the initial placement of loans, will determine in the long run the sectoral allocation of capital. The channels by which credit can be shifted to other uses are many, from increased consumption or relending by farmers, to reduced lending by private sources of credit. From a

policy viewpoint, the issue is not that every dollar of institutional loans slips away if the rate of return on agricultural expenditures is less than in other uses, but that too many slip away too quickly to justify the high administrative costs outlined in Section I. In the later model the only way to attract and to keep more resources in agriculture is to raise the rate of return on farm outlays.

### Section III. Evidence

To date there is very little direct information on the influence of credit programs on the allocation of resources. Some authors have attempted to make inferences from macro data; for example, a credit program may be called successful because agricultural output expands or national fertilizer sales increase following a program of credit for fertilizer purchases (Adams, et al., 1) Given the dynamic nature of agriculture in many developing countries today, such inferences may be of a post hoc, propter hoc nature. Below I have attempted to piece together available information on the following questions: 1) What effect does the availability of institutional credit have on the operations of small farmers practicing traditional agriculture? 2) In a dynamic agriculture what practices are used by small farmers not receiving institutional

credit? 3) What do market studies suggest about the nature of the agricultural credit market? 4) Given the objective of improving small holders' welfare, what information do we have on the distribution of benefits from credit programs?

Looking now at the evidence on question one, in 1971 the Bangkok Bank (27) reviewed the position of the 32,000 small farmers to which it was then making loans. As a result of this survey, the Bank decided that only 25 percent of the farmers had used the borrowed funds to expand production and were now prepared to use and service additional credit; 56 percent had changed their operations but little and, though capable of handling the present level of loans, the Bank felt they should not be given increased credit; 18 percent were judged to be worse off than at the time of their initial bank loan and were no longer considered to be good credit risks. On average, then, the Bank judged credit, even with a modicum of supervision, had had little impact on farmer income.

Penny (16) examines the failure of many government credit programs for small farmers to expand production. He cites several reasons why they have not succeeded, but his major point is that the attitudes of peasants in traditional agriculture militates against their using credit for productive investment, a view he backs with evidence from North Sumatra. Indeed "they (peasants) also feel that debt is something to be avoided, but if the government wants to provide cheap credit they are usually willing to take the handout." (Penny, 16, p. 44) Penny cites evidence from India that peasants have a considerable potential to save, but that in

traditional situations this is channelled into unproductive uses. However, he argues, they have the potential to finance productive investment and do so once their objective becomes increased production.

The findings from Latin America are similar; Nesbit (13) in analyzing the credit program in Chile and Miller (10) and Timmermeir (23) in separate reports on the Peruvian scheme, all conclude that the availability of institutional credit, even when supervised, has had little impact on output. On the first question most researches appear to agree; it is not the absence of credit, but an unproductive technology that has retarded growth in traditional agriculture.

Of course, even if not a constraint on output in traditional situations, absence of institutional credit may retard expansion in a growing agriculture. The new technology requires increased inputs; can small farmers finance these inputs without institutional credit? On this question the evidence is less conclusive. Adoption of new technologies by farmers of different size has been extensively studied in India and Pakistan. Malone (9) found in his study of the Intensive Agricultural Development Program (IADP) in India that as many very small and small farmers had adopted the new technology and had the same level of success as the larger farmers. This was true of small farmers on average despite a much lower participation rate of the smaller farmers in the government's special program (IADP). For all inputs except tubewell water, Gotsch (7) reports similar findings for Pakistan--small farmers as well as large are using the new inputs regardless of credit conditions. With tubewells, unlike

fertilizer, pesticides, etc., there is a lumpiness in the use of the factor which creates difficulties for small farmers. Markets have not yet developed to overcome the indivisibility of tubewells. In the case of both India and Pakistan, small farmers without access to institutional credit have adopted the new technologies, though perhaps at a slightly less rapid pace than larger farmers (Gotsch 7). Unfortunately, it is not known whether those without access to institutional credit paid for the increased outlays from additional saving, sale of other assets, or borrowing from non-institutional sources.<sup>1</sup>

Researchers working on Latin America report, however, that on that continent access to credit does affect agricultural practices. Rask's study (17) of a sample of farms in Southern Brazil shows the larger farms used more credit and more modern inputs. Colyer and Jimenez (5) examined use of credit by farmers in Colombia. They attempted to match a sample of farmers in and outside an institutional credit program. Those involved in the program, they found, used more fertilizer, pesticides, etc. than those who were not.

The evidence on the second question is too scanty to be conclusive. In Asia small farmers without access to institutional credit appear to be able to finance the inputs necessary to take advantage of the green revolution. In Latin America institutional credit appears to be of greater importance in increasing the output of small farmers. Still attention must be paid to the efficiency of the programs. In a

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<sup>1</sup>Evidence from the Indonesian Agricultural Survey (29) also supports the view that there is little difference in agricultural practices between those who do and do not have access to institutional credit.

separate paper on the same program in Southern Brazil mentioned above, Rask and Sorenson (18) concluded that while the credit scheme did increase output the benefits did not cover the program's social costs.

The third question posed dealt with the workings of the credit market. In an earlier paper (Long, 8), I attempted to show that observed high interest rates on agricultural loans in India and Thailand were consistent with competition in the credit market and a relatively free flow of capital among sectors. Very likely there are isolated individuals or whole villages in which the credit market is monopolized but that is not a primary cause of high interest rates. Rather rates on agricultural loans are high because capital is scarce, because farm loans are costly to administer; because the rate of default is high, and because the demand for credit is seasonal, causing loanable funds to be employed only part of the year. Penny (16) supports this view of Asian credit markets. Sansom in his study (19) of Vietnam also concluded that the interest rates on agricultural loans in that country were consistent with a competitive market and mobility of capital.<sup>1</sup>

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<sup>1</sup> During my stay in Indonesia this summer I was on several occasions told of men who were financing investments in service industries in Djakarta from the profits on agro-business undertakings in other areas of the country, which suggests both sectoral and regional mobility of capital.

Still this view is less than universally accepted. Wharton (26) sees control over the credit market as the key to middlemen's monopsonistic power in rural Malaya. Bottomley argues that much of the difference in interest rates between commercial and agricultural loans can be explained by higher administrative costs (2) and loss through default (3) but still believes there is an element of monopoly rent (4). In an analysis similar to that of Wharton's, Nesbit (12) describes the agricultural credit market in Chile as being monopolized. Neither absolutely high rates on agricultural loans nor disparity in rates is in itself proof of monopoly. The more sophisticated analysis which will enable us to distinguish cost differences from monopoly rents is only just beginning. On the question of the organization of the market<sup>1</sup> and the mobility of capital, the evidence is too sketchy to be conclusive.

As to the distribution of benefits, many of the older cooperative credit programs in Asia were designed to enable smaller farmers to pay off existing debts to prevent the loss of their land. But the present emphasis of government credit programs is on loan repayment and output increases. Thus in the three countries the author visited institutional loans no longer go to the smallest quartile of farmers. Nesbit (14) cites figures indicating a substantial bias in favor of larger farmers in Chile; Adams et al. (1) reports similar findings for Brazil, as does Montero (11) for Colombia. The cost of supplying

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<sup>1</sup>In addition to the credit market studies, there are a growing number of reports (see for example Tongpan, 24) revising the view that agricultural markets in Asia are monopolized. More researchers are concluding that exit and entry into these markets is easy, and that prices charged and paid farmers are on the whole competitive.

institutional credit to the smallest farmers has simply proved too great.

However, the welfare implications of credit programs for the smallest farmer do not end there. Colyer and Jimenez (5) cite evidence from Colombia that those receiving institutional loans had in three years increased their land holdings by 40 percent, despite a ban on borrowing to buy land. This may be happening in other countries as well. The Government of Thailand, for example, is concerned about the increasing tenancy among small holders; its subsidized credit program for middle sized farmers may be exacerbating the problem.

In both Indonesia and Thailand, the interest rate charged on institutional loans was subsidized. Despite the higher costs of agricultural loans the institutional interest rate was only half that on commercial loans in Indonesia and about 0.8 of the rate in Thailand. In Indonesia, particularly, I was told that not all of the subsidy was passed on to the farmers. Some was diverted to the pockets of officials. In a detailed study of the "true" cost to the farmer of official credit in East Pakistan, Shahjahan (21) concludes that a combination of application fees, travel and entertainment costs, and loss of working days in getting loans made public credit as expensive as private borrowing.<sup>1</sup>

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<sup>1</sup>In Indonesia, it was reported that the "real" rate to farmers on institutional credit was almost as high as on loans from money lenders.

In Malaysia the interest rate on agriculture loans under the new government program is between 1.5 and 2 times that on commercial loans. At that rate there is little subsidy involved and there is correspondingly limited demand. Farmers have not rushed to join the program, and those that have joined, do not utilize all the allowed credits. Of the vouchers issued to farmers only 55 percent have been cashed. Actually the interest subsidy may have been of greater advantage to the lcc's than to the farmers. The rate charged by the Bank Pertanian was 9 percent per season of six months with no surcharge for late repayment. Most of the loans were late being repaid and officials of the Bank Pertanian thought the delay rested with the lcc's not the farmers. All the private lcc's were padi buyers who require credit for working capital at the harvest season, that is, at the time the farmers' loans were due. By delaying the repayment for several months, the lcc's got interest free loans just at the time of year they most needed credit (Long, 8).

Nesbit (15) in a survey of attitudes among farmers in Colombia found that despite the higher interest rates more preferred to borrow from the money lenders than the banks. Their complaints were that institutional programs involved too much red tape, were too slow, too rigid as regards repayment, etc.

The smallest farmers do not benefit from government credit programs because they do participate. By Western standards those receiving loans are small farmers; still within their own countries, they tend to be those with average size farms and larger. But only a fraction of middle sized farmers get institutional loans. The

criteria by which individual participants are actually selected differ with each program but seldom bear any reference to national welfare functions. Because of red tape and the practices of officials, even those getting loans may gain little from a public credit program, which is expressed in many countries by a lack of enthusiasm among farmers to participate.

Even if the benefits go to the participants, the typical government credit scheme of subsidized loans for a fraction of middle-sized farmers is hard to justify on welfare grounds. Therefore, most loan programs must be judged in terms of their impact on production. Institutional credit will only increase output if it leads to more resources being used for agricultural production. But credit is fungible and an increase in institutional loans to agriculture does not automatically lead to the use of more productive inputs. Given farmers' attitudes and the rates of return associated with a static technology, loans to small holders using traditional practices are unlikely to be spent on productive inputs. Following a change in technology that raises the rate of return, farmers will invest. The evidence for Asia suggests this adjustment will take place with or without institutional credit, but a loan program may be able to speed the process, especially among the smaller farmers. On the other hand, government programs may through their impact on the interest rate reduce the flow of private funds into agricultural credit. Institutional credit for small farmers will increase production, but from a policy standpoint, the benefits of a credit program must be judged against the alternative use of the resources.

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