Accessibility of Rural Credit Among Small Farmers in the Philippines

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ABSTRACT

Credit plays an important role in agricultural development and it is believed that expansion of credit programmes will have beneficial effects on agricultural production and incomes of small farmers. It is also a key to poverty alleviation, livelihood diversification, and increasing the business skills of small farmers. In the Philippines, small-scale and subsistence agriculture source their loans mostly from informal lenders, thus access to formal credit remains low. There is a need to examine further small farmers' access to credit and investigate their preferences and perceptions regarding credit in order that their access can be improved and their needs through credit can be more effectively met. Determining the problems and the credit needs of small farmers are important considerations in designing appropriate credit systems for them.

Accessibility of rural credit in the Philippines was examined, with the primary objective of exploring the use of and access to rural credit by small farmers. This research attempts to explore and understand the perceptions of small farmers toward rural credit, and to collect information in proposing an appropriate credit system for them.

Two types of respondents were interviewed for the research; 45 individual farmers, and four key informants in New Corella, Davao del Norte. The research focused on how the farmers perceived the rural credit facilities, their preferences, their reasons for borrowing, and their problems in accessing credit. Qualitative data analysis was done for the information gathered.

Access to credit by farmers was limited to the available credit services in the research area, thus farmers' choices and preferences were not well served which led to borrowing from informal lenders. Credit restrictions such as commodity specific credit programmes, credit that requires collateral, and lengthy and complicated procedures restricted the farmers from accessing formal credit. It is recommended that accessibility to credit by small farmers could be improved by providing innovative financing schemes that address problems of farmers who lack collateral, and minimise long processing of documents and other requirements. In this way, farmers may be encouraged to better utilise formal credit and decrease their reliance on informal lenders, thus avoiding higher interest rates and thereby increasing their farm productivity and household incomes.

Keywords: Rural credit, access, small farmers, Philippines

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CHAPTER 1: **INTRODUCTION**

Agriculture is the prime mover of the Philippine economy. Rapid agricultural growth is a key to achieving the country's developmental and social goals but the Philippine agricultural sector has been growing erratically since the early 1980s, and its growth is well below potential and required rates (Balisacan, 2001; Lamberte *et al.*, 1994; WorldBank, 2000). The performance of the agricultural sector is also important in the country's food security and poverty alleviation efforts since a large majority of the poor are located in the rural areas and depend directly on agriculture-related economic activities for their major source of livelihood. About 60% of the country's population is rural and two-thirds of these depend on farming for their livelihood (Balisacan, 2001; Venkataramani, 2005).

The Philippines is characterized by a mixture of small, medium and large farms of which the majority are family smallholdings averaging about 2 hectares. A typical farming system consists of rice, corn and coconut as common base crops, and a few head each of livestock and poultry. The Philippines has a diverse climate where different crops are concentrated in different areas, but productivity tends to be limited more by lack of access of farmers to credit than by agronomy or climatic factors (Venkataramani, 2005).

1.1 Background and Statement of the Problem

Agricultural credit is one of the important interventions to solve rural poverty, and plays an important role in agricultural development (Llanto, 1993; Meyer & Nagarajan, 2000). Expanding the availability of agricultural credit has been widely used as a policy to accelerate agricultural and rural development (ADB, 1998; Binswanger & Khandker, 1995; WorldBank, 2000). It is traditionally employed as a tool for providing the priority sectors with access to production inputs and enabling production to be increased (Llanto, 1993).

Moreover, it is believed that expansion of credit programmes will have beneficial effects on agricultural production of smallholders and rural incomes because credit could facilitate the purchase of costly inputs and the adoption of alternative crops (Zeller *et al.*, 1998). Small farmers[1] need production capital, a scarce resource, to improve their production. The provision of credit can encourage the farmers to use modern technologies, and procure inputs for farm use, thus bringing them to a higher level of productivity and increasing their incomes (Llanto, 1987). As such, increases in household incomes are much needed for improving food security and eventually will come from the gains in agricultural productivity through better technology and more productive crops. Therefore, farm households' access to financial markets is important in influencing farm production and income (Zeller *et al.*, 1998).

Concerns with providing accessible and appropriate credit systems for small farmers in developing countries have been growing for many decades. This is because appropriate credit systems could cater for the financing needs of the small farmers in the rural areas (Yaron, 1992). Most researchers have recognised that increased access by small farmers to production resources like credit is needed for increasing food production and thus deserves particular attention (Zeller *et al.*, 1998). In the Philippines for decades the task of rural credit was primarily seen to be promoting agricultural production by providing credit to farmers, hence it has an important role in the development of the agricultural sector (Llanto, 1993).

Many efforts have been made and a continuous search for sustainable interventions through appropriate credit schemes is being conducted to improve the living conditions and quality of life of small farmers in the rural areas (WorldBank, 2000). However, such efforts and interventions are often hindered by problems, which then contribute to the failures of some rural credit programmes. Some credit programmes are not sustainable because of the failure and collapse of several rural financial institutions, which are due to poor

[1]Natural persons dependent on small-scale subsistence farming as their primary source of income (Agriculture and Fisheries Modernization Act-Implementing Rules and Regulations, 1998).

management and lack of good governance (Yaron *et al.*, 1997). In the Philippines, the demand for funds by intended beneficiaries was neglected in the design and implementation of past agricultural credit programmes, which caused their failure (Clar de Jesus & Cuevas, 1988).

Different rural credit programmes in the Philippines have been implemented under different policy regimes with defined approaches to the problems of rural credit delivery. During the 1970s, the supply-leading approach evolved where the emphasis was on directed credit and interest rate subsidies. This is the supervised credit approach that provided the farmers with a subsidy for risk-taking through production loans below market interest rates. This kind of credit approach was undertaken so that farmer-borrowers could withdraw from private moneylenders' usurious interest rates. However, this approach did not succeed in the long run because the financial institutions were reluctant to continue lending to small farmers due to the high number of borrowers' defaults (Esguerra, 1998). Also, in such approaches to credit, a substantial amount of the loans did not go to the target groups (farmers, small and medium enterprises) but instead went to those who could easily access credit from the formal credit markets (RIDA, 1995).

Following these supervised credit programmes were the market-oriented rural credit programmes where the government implemented a low interest rate policy, but these were still a failure because most of the participating financial institutions discontinued their participation due again to poor loan repayments (Esguerra, 1998).

Credit continues to figure prominently in developing strategies for the agricultural sector in the Philippines. There is a strong demand for agricultural credit and despite the tremendous contribution to agricultural production by small farmers, they are constrained in their access to-and are being disqualified from-formal loan sources due to high transaction costs, high interest rates, and a lack of both collateral and capacity to pay (Yaron *et al.*, 1997). Due to the default problems in borrowing from the formal loan sources, the small farmer-borrowers still go to informal lenders despite usurious interest rates because of their minimum requirements, flexibility and easy procedures, fast processing and timely release of loans, and their acceptance of unconventional forms of security (Llanto, 1993).

It is generally felt that past agricultural credit programmes, though important, still remained ineffective in meeting the needs of the majority of the small farmers. Furthermore, several formal credit programmes are not accessible to small farmers because they are poor and cannot afford to travel to far distant centres, and they do not have collateral or regular incomes (Yaron *et al.*, 1997). Also, in some cases their lack of education makes them afraid to borrow from formal institutions, leaving them instead to borrow from informal lenders for agricultural production use (Chowdhury & Garcia, 1993).

The lack of commercial microfinance institutions, which is common in developing countries, is also a contributing factor that forces small farmers to go to informal lenders, even if it is less expensive to borrow from a commercial microfinance institution (Robinson, 2001). It is true that informal moneylenders provide important financial services to the poor households, but they charge very high interest rates (Robinson, 2001). In some cases, a lack of credit also is a problem in the rural areas because there is no rural bank and the private banks avoid lending due to the risks they are going to face of default payments which will lead to their unprofitability (Yaron *et al.*, 1997). In 1998, about 38% of farm households in the Philippines borrowed, but only 11% borrowed from formal financial institutions (WorldBank, 2000).

Credit plays an important role in agricultural development. It is also a key to poverty alleviation, livelihood diversification and increasing the business skills of small farmers. However, most small farmers in the Philippines depend upon informal sources of credit. Considering the problem of accessibility of credit by small farmers in the rural areas of the Philippines, there is a need to examine further the reasons why they do not access credit from the formal institutions, and to investigate their preferences and perceptions regarding credit in order that their access can be improved and their needs for credit can be more effectively met. This is the focus of this research.

1.2 Research Aim and Objectives

Researchers continue to try to analyse and better understand problems and issues in rural development in general, and the situation of small farmers in particular. It is critical to assess the characteristics of agricultural production strategies among small farmers in order to have a greater understanding of the factors that determine their access to credit. Empirical research has shown that borrowing constraints prevent small farmers in developing countries from adopting high-return innovations such as irrigation systems and modern varieties (Blackman, 2001). In this research an attempt was made to explore and understand the perceptions of small farmers concerning rural credit and to collect information in order to be able to propose an appropriate credit system for them. This allows small farmers to voice their needs and ideas as to the relative role of credit in the context of agricultural production and livelihood strategies.

Specifically, this research was conducted to explore the access to, and use of, rural credit by small farmers, and the reasons for their choices about credit, in the Davao del Norte province of the Philippines. The aims were to:

1. examine the availability and accessibility of credit in the area;

2. determine the credit uses and preferences of small farmers regarding rural credit in the area;

3. determine the factors being considered in choosing their creditors and the problems they encountered in accessing credit services in the area;

4. identify small farmers' perceptions and expectations of rural credit, both now and into the future; and

5. explain policy implications regarding future access to credit.

Knowledge of the socio-economic environment and the perceptions of the small farmers regarding credit will assist policy makers to make better decisions on appropriate credit systems for small farmers. Knowledge of the constraints faced by small farmers should also enable them to avoid costly mistakes and focus their efforts on making constructive policy interventions. This research also will fill part of the void on understanding farmers' perceptions and expectations regarding credit access, given the limited empirical studies that have been done on improvements to credit accessibility for small farmers (WorldBank, 2000).

1.3 Limitations of the Research

This research was undertaken in Davao del Norte province. The primary limitation of the study is the sample size which was limited to only one province given the short time allotted for fieldwork. As such, the research reflects the experiences of farmers in the study area, which may vary from those in other communities within the region and in other parts of the country. Another limitation of this research relates to construct validity and reliability. Because of the subjective nature of the qualitative data, it is difficult to apply conventional standards of reliability and validity (Babbie, 2001). The researcher also has no control over the variables, as they are based on human behaviours and natural influences and applied in the real context of where they are, not like the experiment which is conducted under controllable conditions in a laboratory.

1.4 Thesis Outline

This chapter has provided a brief introduction to the research. The research problem was identified and the objectives were defined. The review of literature follows in the next chapter. The review includes relevant studies of rural credit accessibility by small farmers. It describes the history and origin of the rural credit system, discusses the role of rural credit and some experiences on the provision of credit for small farmers in the developing countries. It also discusses the types and sources of rural credit and describes the situation of rural credit in the Philippines and the credit issues. The methodology used in the research is outlined in Chapter 3. This gives an account of how the research was conducted. The research area is described and the sampling and data collection are discussed. The results of the research are presented and discussed in Chapter 4. The closing chapter summarises the results from the research and conclusions are drawn. Recommendations arising from the research and related areas requiring further research are also presented.

CHAPTER 2: **LITERATURE REVIEW**

In this chapter, studies of rural credit accessibility, particularly those with emphasis on small farmers, are reviewed. The review covers some experiences of developing countries and areas of relevance to the Philippine situation. The chapter includes a description of the history and origin of the rural credit system, roles of rural credit, provision of credit for small farmers in developing countries, and types and sources of rural credit. The rural credit situation in the Philippines is also described.

2.1 History and Origins of Rural Credit

The concept of credit in agriculture has been known since the seventeenth century when peasants in China used rural credit in farm production to increase their cash income, and to improve their standard of living (Ming-te, 1994). Likewise, in Western countries, the German Landschaften was founded by Frederick the Great in 1769, and its principles were used by the Federal Farm Loan System of the United States. The Raiffeisen Agricultural Bank and the Schulze-delitzsch People's Bank were established in 1852, which were believed to be the origin of the establishment of cooperative institutions world-wide (Belshaw, 1931).

According to Heidhues and Schrieder (1999), the origin of the credit concept stems from the necessity to break the vicious circle of low capital formation, as presented in the diagram below.

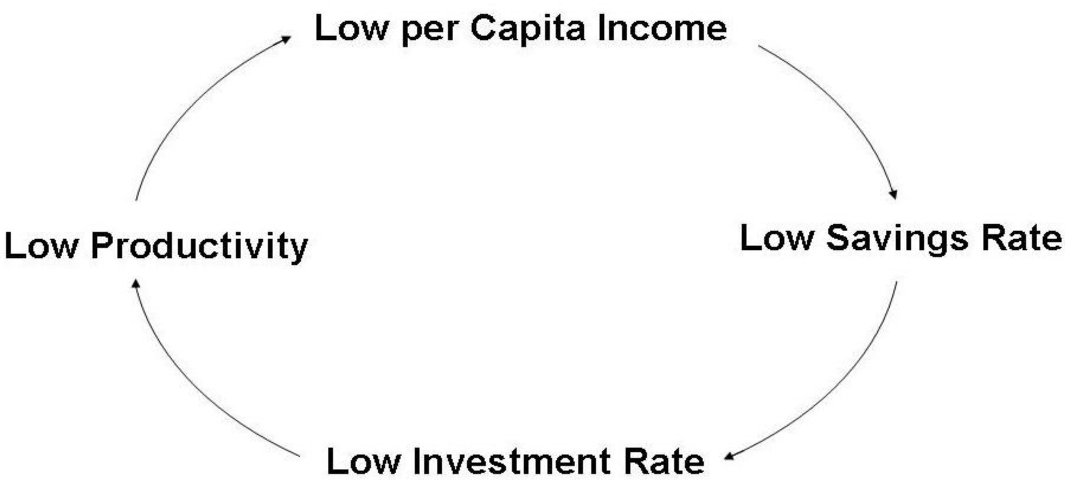

Figure 1.The Vicious Circle of Low Capital Formation (Heidhues & Schrieder, 1999)

The diagram shows that the formation of capital is influenced by per capita income, savings rate, investment rate, and productivity. A low level in any of these factors will impact on capital formation. It is argued that the role of credit programmes is to break this cycle, resulting in an increase in per capita income and thus an increase in savings rate, investment rate and productivity (Heidhues & Schrieder, 1999).

2.2 Role of Rural Credit

Credit is essential for agricultural development and is often a key element of agricultural modernisation. It cannot only remove a financial constraint but it could also increase production and income, and may accelerate the adoption of technologies (Atieno, 1997; Duong & Izumida, 2002; Meyer & Nagarajan, 2000). It can improve income by enabling the undertaking of additional income-generating activities, and the rural households also can finance more consumption and have surplus finance available for further investments (Rosenzweig, 2001; Zeller *et al.*, 1997).

Likewise, credit facilities will help farmers purchase modern inputs such as high-yielding varieties of seeds, fertilisers, and install irrigation to increase production (Chowdhury & Garcia, 1993; Vicente & Vosti, 1995). For decades, rural credit has been primarily seen as promoting agricultural production by farmers and making rural progress possible through growth in farm productivity (Llanto, 1993; Panin *et al.*, 1996).

It is generally an accepted view that agricultural credit programmes can be successful only if they are part of an “integrated approach” to rural development problems (Brake & Lins, 1994; FAO, 1975; Rashid *et al.*, 2004). Granting production loans to small farmers is viewed as a means to augment food production pursued by many donors and governments in developing countries (Irungu *et al.*, 2005; Zeller *et al.*, 1997).

At various points in time farmers rely on external credit because as producers they prefer to hold their savings in physical productive assets on their own farms. It can be noted that farm income and expenditures do not occur at the same time (Desai & Mellor, 1993). A good example of this is a rice farmer who harvests his crops twice or thrice a year whereas his consumption expenditure is continuous. Likewise, for a tree-crop farmer there is a big gap between the times when income is generated and when expenditure is incurred (Desai & Mellor, 1993). Moreover, in the event of unforeseen situations such as bad weather, accidents and illness, rural households usually resort to emergency sales of assets and borrow from family and the informal sector (Chowdhury & Garcia, 1993). The poor have traditionally obtained credit services almost exclusively from informal networks because they have little or no collateral to offer (Pal, 2002; Zeller *et al.*, 1997).

The majority of poor small farmers in developing countries are left out of agricultural extension and credit systems (Lal *et al.*, 2003). These households are characterised by landholdings of less than 1 hectare and very low crop yields. These rural households are unable to grow enough food to feed themselves even though they focus much effort on producing food crops (Lal *et al.*, 2003). It has been noted that most of the farmers are too poor and cashstrapped to be able to benefit from any kind of access to credit (Diagne & Zeller, 2001).

Access to credit is limited in rural areas although a high demand for it exists (Sahu *et al.*, 2004). Thus, establishing formal credit institutions in rural areas for small farmers is considered an adequate financing strategy to help improve their income and livelihood strategies (Heidhues, 1995). Also, the proximity of formal credit institutions in the rural areas encourages financial savings from the small farmers and discourages their borrowing from informal lenders (Rosenzweig, 2001). Designing sustainable rural financial systems could provide an adequate financing strategy for small farmers. A better understanding of existing informal institutions at the household and community levels could provide the key to designing sustainable rural financial systems that serve the poor (Panin *et al.*, 1996; Zeller *et al.*, 1997).

2.3 Provision of Credit for Small Farmers in Developing Countries

The provision of credit for small farmers in developing countries is centred on two main issues: the establishment of specialised agricultural credit institutions and the outreach of rural credit institutions. Specialised agricultural credit institutions (SACI) have existed for decades and their establishment was based on a political response from the government, which is highly supervised and controlled (Adams, 1980; von Pischke, 1980; Yaron, 1992). The SACIs had many operational problems, such as limited outreach of credit which was available to the wealthy and large farmers only, and a high dependence on subsidies from external donors. Thus, these institutions were unable to be sustained due to capital deficit and poor loan repayment (Yaron, 1992). The failure of several SACIs pushed donors and government agencies to shift the focus of interventions from agricultural credit to rural finance, from farm credit assistance and state-owned agricultural banks to micro-enterprise financing (microfinance) and the promotion of non-government financial institutions (Yaron, 1992).

Moreover, after the collapse of many agricultural development banks, the remaining or recently established financial institutions were not capable of solving the problems of limited outreach and unsustainability (Coffey, 1998; Klein *et al.*, 1999). Thus, a new approach to agricultural finance needed to be formulated to ensure the demands of farmers, especially the small-scale operators, were met and to overcome existing agricultural credit constraints like high transaction costs, specific risks, lack of collateral, and so on (Klein *et al.*, 1999).

It is argued that in order to make microfinance lending efficient, it is better to divide the target beneficiaries into categories, such as lower-middle income, economically active poor, and extremely poor (Robinson, 2001). Commercial microfinance is appropriate for both the lower-middle income and the economically active poor. However, the extremely poor who can not use credit effectively, and who are unable to repay (which tremendously hinders the sustainability of financial institutions), must be funded through direct subsidies or grants (Robinson, 2001).

Microfinance institutions should be client-centred not product-centred, where the design of microfinance products should be based on clients' needs (Wright, 2000). Likewise, Meyer (2002) asserts that client-centred microfinance is important to avoid drop-outs, loan delinquency, and multiple membership of the microfinance customers. Financial institutions' products and services must be designed to meet clients' demands. Failing to consider clients' preferences in some microfinance institutions has caused their operational failures (Blackman, 2001; Meyer & Nagarajan, 2000).

About 90% of the people in developing countries lack access to financial services (Robinson, 2001). A large proportion of the rural population is denied access to formal financial institutions for reasons like incomplete information about rural access and the viability of the credit services. Also, there is a problem of limited influence by poor households who require credit, but who are unable to communicate their demands to the formal credit markets or meet their collateral requirements, so the services are not provided (Robinson, 2001).

The lack of financial institutions in rural areas is also attributed to some problems that jeopardise the sustainability of the credit institutions. In some cases, government financial institutions provided subsidised credit but did not reach the poor households because it was taken by the local elites, thereby causing the unsustainability of the financial institutions in giving the services (Robinson, 2001). Another problem is loan recovery, thus greater attention should be given to the clients' preferences so that there will be a better rate of loan recovery (Meyer & Nagarajan, 2000).

2.4 Types of Rural Credit

Two different types of credit, formal and informal, are accessed by small farmers. Some features of these credit types are discussed below.

2.4.1 Formal Financial Institutions

Formal financial institutions are organisations which are owned, controlled, licensed and registered or regulated by the government. These include the commercial banks, state-owned banks, agricultural development banks and rural banks (Martokoesoemo, 1994). Most of the commercial banks are active in urban centres financing trade business while the agricultural development banks are usually situated in rural areas serving mostly farmers. They provide transfers, savings, and lending services.

Based on the study by Chowdhury and Garcia (1993), the number of loans from the formal financial institutions in the developing countries obtained by rural borrowers is low. The reasons for such low availment include complicated and lengthy loan procedures that often overwhelm the poor and uneducated farmer-borrowers. Also, obtaining loan from formal institutions overburdened the rural borrowers in terms of slow release of the funds and higher transaction costs, which led them to borrow from informal sources instead (Chowdhury & Garcia, 1993). Moreover, some restrictive features of loans also affects them. One is the credit scope which is limited to only a specific commodity, and another is the security requirements as the borrowers do not have the assets to support their credit (Martokoesoemo, 1994). In some cases, many remote rural areas lack banking and other institutional facilities and credit services (Chowdhury & Garcia, 1993).

2.4.2 Informal Financial Institutions

Informal financial institutions operate without physical collateral, involve small loans and short-term transactions, and are characterised by adaptability and flexibility of operations in a certain area (Adams & Fitchett, 1992; Ghate, 1988). The characteristics are the same as for the informal sector and no data on their activities are available through official statistical offices (Martokoesoemo, 1994). Lower transaction costs provide a comparative advantage for informal financial institutions because of their small scale operations and specialisation (ADB, 1989).

The Asian Development Bank (ADB, 1989) identifies four broad categories of informal credit:

- direct lending – characterised by loans extended by friends and relatives, which are sometimes called *community loans* because of their non-commercial character;

- untied credit – lenders enter the market and act as borrowers if direct lending is commercial. These lenders are the professional moneylenders, pawnbrokers, and other types of non-bank financial institutions that operate with self-generating funds or on borrowed money. They do not tie their credit transactions to other market transactions;

- tied credit – credit is linked with simultaneous transactions in other markets where the relationship in other markets serve as a substitute for collateral. The lenders may be landlords, suppliers of raw materials, or collectors of agricultural produce; and

- group or mutual finance – groups of individuals pool their savings and lend exclusively or primarily to one another on a rotating or non-rotating basis (ADB, 1989). This credit type can be found in most Asian countries. They are called *chits* in India, *paluwagans* in the Philippines and *arisans* in Indonesia. In these systems, a few individuals form a group and select a leader who periodically collects a given amount of money from each member. The money collected is then given in rotation to each member of the group so transaction cost is minimal and interest is not charged (Martokoesoemo, 1994).

Informal finance is based on mutual trust because it operates outside state control and legal business regulations. Non-material collateral-such as character, reputation, kinship and family ties-plays an important role in borrowing from informal sources (Tolentino, 1988). Informal credit sources represent a large informal capital market in the rural areas of the Philippines, and rural households continue borrowing and relying on informal finance for their credit requirements, both for personal and business-related financing needs (Castillo & Casuga, 1999). About two-thirds of farmers borrow from informal lenders (Santos & Guce, 2001; Tolentino, 1988). Based on a survey conducted by the Agricultural Credit Policy Council (ACPC) in 1997, about 76% borrowed from informal sources, and this had remained unchanged over the preceding 10 years (Santos & Guce, 2001).

The informal sector re-emerged in the rural areas due to the failure of many formal credit programmes. Informal credit is attractive in the rural areas since these sources are the only way to provide financial services to the rural households located in remote areas, and their loan recovery record is better than for many formal institutions (Kashuliza, 1993; Rajeev & Deb, 1998). Likewise, informal lenders accept payments in kind, rarely demand paperwork, and they lend not only for production but also for consumption purposes (Kashuliza, 1993; Rajeev & Deb, 1998; Tolentino, 1988). Other reasons also for accessing informal finance include easy accessibility, the fact that they are collateral-free, higher loan amounts can be extended and the hesitancy of formal-lending institutions to extend loans to small farmers because of the risk of non-repayment (Corales, 1983). There is still much to be learned about the practices of the informal sector in the Philippines and how they evolved in the different areas.

Furthermore, a study by the ADB in 1989 showed that rural informal credit in Asia remains an important force, accounting for about two-fifths of total rural credit in Bangladesh, India and Thailand and more than two-thirds in the Philippines. The reasons for the strength and attraction of informal finance can be summarised as follows: proximity, anytime access and comfortable atmosphere of the location, quick processing in which collateral is not obligatory, freely implemented, repayment flexibility, and lower transaction costs for borrowers and savers (Kashuliza, 1993; Padmanabhan, 1988; Panin *et al.*, 1996).

2.5 Sources of Rural Credit

Different forms of credit delivery mechanisms are discussed below, such as rural banks, NGO models of credit delivery, cooperatives, provision through development assistance by external agencies or donors, and other forms of financial assistance being undertaken in the selected Asian countries. The different credit facilities are described as to the different kinds of strategies that are generated and to what extent these strategies achieve their intended aims.

2.5.1 Rural Banks

Rural banks are one of governments' efforts for credit delivery in every developing country for facilitating access to credit in rural areas (Puhazhendhi & Jayaraman, 1999). The following describes three successful rural banks, Grameen Bank in Bangladesh, Bank Rakyat Indonesia, and Bank for Agriculture and Agricultural Cooperatives in Thailand.

2.5.1.1 Grameen Bank in Bangladesh

The Grameen Bank was initiated in 1977 as a project to try out a new approach to rural credit in Bangladesh. It was initially rooted in the Central Bank of

Bangladesh, and later become an independent bank (Jain & Moore, 2003). Loans were given without asking borrowers either to provide collateral or to engage in paperwork. The borrowers were provided with financial services at their doorstep. It pioneered what has come to be known as *group lending* and established a system of reliable loan repayment from the borrowers who were below the poverty line (Jain & Moore, 2003). In 1999, more than 2.3 million borrower members were served in Bangladesh and started replication projects in many countries. Grameen become the acknowledged leader of international microcredit programmes and was the first to become large and famous. The bank has access to low-cost capital and a nominal interest rate of around 16-20% on outstanding loans is charged (Jain & Moore, 2003).

The Grameen Bank approach is built on the concept of joint-liability of group members. Membership is limited to people who have similar economic status and live within the same village. The clients are mostly women. Loans are given to borrowing groups so peer pressure for repayment is created (Llanto, 2005).

The Grameen model consists of three key elements. The first is social collateral - the idea that individual borrowers repay because of strong socially-constructed collective responsibility at the level of the small group of about five people to which each borrower belongs. The group will approve loans only to individual members who are likely to repay; and jointly assume repayment responsibility in case of individual default (Jain & Moore, 2003). The concept of effective group responsibility for loan repayment is an important element within an array of norms and practices designed for borrowers to have a sense of affinity with "their" microcredit organisation, and to instil within them a culture of financial responsibility and discipline (Zeller *et al.*, 2001). According to Stiglitz (1990), the group mechanism is a good solution to the problem of high transaction costs in identifying reliable borrowers and ensuring repayment, which is a problem in most credit programmes.

The second key element of the Grameen model is borrower participation – the involvement of borrowers in both operational and policy decisions creates strong participatory elements in the management of microcredit. The third element is absence of subsidy – the belief that the interest rates paid by borrowers are not subsidised (Jain & Moore, 2003). The absence of subsidy will discipline the borrowers not to try to take on more credit than they can afford to repay (Yaron, 1992). This strategy is consistent with the lessons learnt from the experience of earlier cooperative and other government-aided credit programmes for the poor whose failure has been blamed on the subsidised interest rate policy (Adams *et al.*, 1984).

The success of the Grameen model can be determined by managing the three objectives of keeping costs low, offering a set of products, and enabling, encouraging and enforcing a high level of loan repayment (Yaron *et al.*, 1997).

2.5.1.2 Bank Rakyat of Indonesia

The Bank Rakyat Indonesia (BRI) is a good example of a self-sustainable rural financial institution in Indonesia. The BRI started as an official programme organised by the Central Bank of Indonesia to provide credit to the rural poor of the province. The moral commitment of the BRI is embodied in its motto to provide the rural poor with a credit programme which is fast, cheap and productive (Yaron, 1992).

Likewise, the BRI was the implementing bank for Bimas (rice intensification programme). The BRI units were selected to channel subsidised credit to rice farmers (Martokoesoemo, 1994). Bimas started in 1969 and lasted until 1982. The management of the BRI was confronted with a dilemma in 1984 with the phasing out of the Bimas credit programme. However, the government introduced a radical reform of the financial regulatory system in 1983-1990, which created a major impetus for banks to innovate, to create and develop financial markets (Martokoesoemo, 1994).

Following the collapse of Bimas, policy changes were introduced between 1983 and 1984 to reform the unit system. The new unit system began in early 1984 wherein commercial microbanking (primarily loans and savings services) was offered at all units throughout Indonesia (Robinson, 2004). Local village officials are involved in the screening by acting as character referees for the borrowers. As such, the unit system ranks as one of the most effective rural financial institutions in Indonesia and has produced spectacular results in outreach and financial performance as it has done every year since 1984 (Corpuz & Kraft, 2005; Robinson, 2004).

The BRI transformed from a massive, failed subsidised rural credit programme in 1970 to the largest commercial microbanking system in the world now (Robinson, 2004). The transformation to commercial microbanking in 1984 was made possible by the consistent economic development and political stability which prevailed for 20 years. The BRI was the first bank to provide commercial financial services to millions of economically active poor and lower-middle-income households (Robinson, 2004).

There were four factors that made the BRI the largest commercial microbanking system in the world. One was the government's long-serving economics team who provided continuing high-quality leadership characterised by a good vision. Other factors were the number of relevant policies that were introduced, and there were politics where credit subsidies also reach to rural elites being relied by government to deliver rural votes. Then, changing the culture of the bank which includes professionalism and responsibility, change of attitude toward a business focus, training and incentives for staff based on profitability, high priority of transparency and accountability, and knowledge of the microfinance market (Robinson, 2004). Other aspects also of culture change included the extensive research into what kinds of financial products the low-income people preferred, consequently the bank's loan and basic savings products were designed to customise the clients' needs (Robinson, 2004).

2.5.1.3 Bank for Agriculture and Agricultural Cooperatives in Thailand

The Bank for Agriculture and Agricultural Cooperatives (BAAC) in Thailand was founded in 1966 to improve the agricultural sector by extending financial services. The BAAC operates as a state-owned bank under the supervision of the Ministry of Finance and provides loans on activities related to agriculture

(Yaron *et al.*, 1997). It replaced the Bank for Cooperatives, whose funding was limited and whose lending activities were restricted to agricultural cooperatives. Commercial banks, BAAC, and cooperatives are the most important rural financial institutions in Thailand. The number and distribution of banking outlets have a strong influence on access to banking services in rural areas (Corpuz & Kraft, 2005). The BAAC originally lent mostly through large agricultural cooperatives but repayment problems led the bank to increase its direct lending to individual farmers (Yaron *et al.*, 1997).

The BAAC, as a specialised institution, represents the country's most important effort to support small and medium–sized farmers, since one of the problems of farmer borrowers of Thailand is meeting the collateral requirement of banks (Llanto, 2005). It enjoys substantial autonomy in setting its operational and financial policies and has focused mainly on lending to borrowers in the low to medium income range. It has attained impressive performance in outreach, in its lending portfolio, savings mobilisation, efficiency, and profitability (Llanto, 2005). The BAAC provides loans to farm households with no collateral requirement and uses the joint liability group loans to ensure the repayment of loans. It has also mobilised savings among its borrowers. It is highly successful with about 90% outreach of farm households, accounting for half of the total agricultural lending in Thailand, and has high repayment rates and savings mobilisation (Corpuz & Kraft, 2005).

2.5.2 Non-Government Organisations (NGOs)

The exclusionary practices of many government credit interventions for the poor as well as of the banks are compensated for by the Non-Government Organisations (NGOs) (Hoff *et al.*, 1993). There are four broad classifications of credit-based NGO activities: NGOs which act as financial intermediaries between government schemes and the poor; NGOs which lend directly to the poor; NGOs which promote self-help thrift and savings groups; and the non-government cooperative banks for the poor (Hoff *et al.*, 1993).

Direct NGO lending has the advantage of being free of many of the bureaucratic norms and procedures in order to be able to meet the credit needs of the poor (Hoff *et al.*, 1993). Also, greater flexibility can be observed in terms of loan size, range of permissible uses and timing of repayment schedules (Lal *et al.*, 2003). However, flexibility is not always operationalised because the scope for flexibility is limited by the fact that NGOs do not have infinite funds and their lending operations can continue only if they are able to ensure loan recovery (Zeller *et al.*, 2001).

It could also be noted that in practice there is sometimes considerable overlap of NGO activities because different NGOs have various strategies in credit delivery to the poor (Hoff *et al.*, 1993)**.** The NGOs may start out using one strategy and then shift to, or combine it with, another. Sometimes NGOs may collaborate with the government to produce a hybrid of these strategies (Lal *et al.*, 2003). Some NGOs which are handling small-scale production and consumption needs are experiencing the same problems as with the banks. (Lal *et al.*, 2003). NGOs also have played a positive role in the lives of poor women – and poor men – simply by increasing the range of credit options available to them (IFAD, 2003).

NGOs differ from other formal institutions in two fundamental ways. First, financial institutions operated by NGOs lend to groups and make use of joint liability, peer selection, and investments in repeated financial transactions to overcome the informational constraints in financial markets. Second, these institutions do not depend solely on the government for loanable funds, nor have they been subjected to interest rate and other controls imposed by the central bank (Zeller *et al.*, 2001).

Some NGOs lack experience in finance in institutionalising credit delivery. The complexity of the concept of financial sustainability needs to be learned by them, and they must accept its importance in the process (Todd, 1996). On the other hand, most NGOs are cursed with a “grant mentality”, resulting from funding small projects and one-off activities from donor grants (Todd, 1996). The Grameen Bank of Bangladesh is an example of a group-based movement, like an NGO in microfinance that has been transformed into a bank. Another example of an NGO is the Association for Social Advancement (ASA) in Bangladesh that has not registered as a bank, but has collected savings and made loans through their own local branch networks.

2.5.3 Cooperatives

A *cooperative* is *a voluntary, democratically controlled association of people with the specific purpose of conducting some kind of business*. Voluntary associations are established for all kinds of social, political, cultural, recreational or defensive purposes (FAO, 1957). They differ from all other group or mutual finance in being an association especially set up for the purpose of going into business (Caneda, 1996; Puhazhendhi & Jayaraman, 1999). The purpose of establishing a cooperative is to apply principles of voluntary association to business. The essence of a cooperative is that it is owned by its members who are its customers and it is an important element for reaching small farmers (Belshaw, 1959).

The cooperative movement in developing countries originated in India, and the manner in which it was introduced has set a pattern which has been followed throughout the developing world (Howell, 1980; Suresh, 1991). The Primary Agricultural Cooperative Society (PACS) was the original credit cooperative introduced in India and its sole purpose was to make loans (Howell, 1980). In some countries, primary cooperatives make both short and longer-term loans and the members may contribute minimal amounts of share capital, but they do not use the cooperative societies for savings (Belshaw, 1959; Caneda, 1996). The principle behind establishing such a society is that a group of small farmers which is legally constituted as a cooperative society can borrow on better terms, can shoulder some of the costs of loan administration and can offer better security than can individuals borrowing on their own account (Belshaw, 1959; Caneda, 1996; Grace, 1978).

In most countries, the cooperatives are weak, they cover only a small proportion of the population and provide only a slight fraction of the total credit needs of small farmers (Desai & Mellor, 1993). However, in some other countries, cooperative credit is an effective tool for farmers. Some of the collective farms or previous agricultural financing follows some of the same principles in the formation of such cooperatives (OECD, 1999; Suresh, 1991).

In the formation of cooperatives, the membership is solicited from within an area of daily contact and the members are required to contribute capital. The increases in capitalisation are planned and the lending limits are linked to the amount of the capital and the contribution deposited (OECD, 1999). The rules of membership are prepared where the cooperatives operate, including the selection and retirement of the cooperative head and the democratic rules followed in the daily operations. Lending decisions are based on assembly voting, and the lending rates are positive and dividends are paid according to the capital contributions (OECD, 1999).

Furthermore, agricultural credit cooperatives provide a venue for farmers to save and promote recycling of funds in the farming sector (Mahalingam, 1996; OECD, 1999). The creditworthiness for credit cooperative is judged on the basis of ownership, not on repaying capacity, and consequently sharecroppers and tenants are not allowed to borrow from cooperative credit (Kabeer & Murthy, 1996). Each member of the cooperative can directly monitor the use of his/her funds (regardless of the form of the funds, whether a capital contribution or deposits) and have a say in the use of the funds (OECD, 1999). Thus, activities of credit cooperatives rooted in the autonomy of the farmers can be a powerful tool in the fostering of the economic culture needed to remove the bottlenecks of credit in the rural sector (Desai & Mellor, 1993; Mahalingam, 1996).

2.5.4 Development Assistance

The public sources of credit are usually in the form of development assistance. Development assistance is classified in different ways according to whether the funds concerned are granted on a bilateral or multilateral basis, and through special international organisations (FAO, 1975). The funds are made available as grants, soft loans or loans at market conditions.

Foreign development assistance to agriculture in developing countries has taken many forms and has generated considerable effects on agricultural productivity (Norton *et al.*, 1992). Aid for agricultural development is determined by a complex set of economic, political and bureaucratic factors and developing countries need to enhance their capacity in food and agricultural policy design . Foreign financing is urgently required in a particular country when there is a shortage of capital for lending to farmers. This usually occurs when institutional saving is at a very low volume in the early stages of development, and when existing financial resources are all utilised for more attractive uses (Desai & Mellor, 1993).

Pressure for most of the government intervention to influence the direction and magnitude of rural development has come from external donor agencies like the Asian Development Bank (ADB). The ADB disburses credit and financial services to Asian countries through public sector programmes and projects which are designed to benefit the rural sector (Jain & Moore, 2003). One of the commitments of the ADB is to provide finance for agricultural and rural development projects through provision of credit lines to public development financial institutions for on-lending to agricultural users of inputs. Another is provision of technical assistance for strengthening credit institutions serving the agricultural sector (Jain & Moore, 2003; Schuh, 1988). Development assistance contributes significantly to economic development in the recipient country (Pinstrup-Andersen *et al.*, 1995; Therien & Lloyd, 2000).

2.5.5 Self-Help Groups

Some forms of credit delivery mechanisms have evolved in other Asian countries. One is the self-help groups (SHGs), which emanate from India (Zeller *et al.*, 1997). The SHGs represent a hybrid model with characteristics borrowed from models that link indigenous groups to banks, from models that create self-governed village banks, and from models that create joint-liability borrowing groups (Zeller *et al.*, 1997). The organisational frameworks and the services rendered by this kind of informal financial group vary with location. The SHGs are also defined as *voluntary groups valuing personal interactions and mutual* *aid as means of altering or solving the problems of its members* (Zeller *et al.*, 1997).

The SHGs are an important source of informal loans in many developing countries and play an important role in rural credit as an efficient channel of credit to the rural poor (Rangarajan, 1994). It has been a long tradition in developing countries that groups designed like SHGs are used by members to cope with daily financial problems (Lal *et al.*, 2003). Financial SHGs offer a wide variety of services and play an important role in capital accumulation, consumption credit and insurance (Zeller *et al.*, 2001). Also, the SHGs are viable alternatives to reduce the transaction costs in rural lending since the work relating to borrower identification, loan processing, loan disbursement, and monitoring is done by groups of clients (Girija & Satish, 2001). The peer pressure acts on information needs and has a positive influence on loan repayment (Girija & Satish, 2001). Also, the contractual savings and membership restrictions replace the need for other collateral (Lal *et al.*, 2003).

There are some limitations of such informal group-based microfinance systems, like SHGs, wherein the effectiveness of peer pressure as a contract-enforcement mechanism for group lending may decline after several loan cycles (Zeller *et al.*, 2001). As experienced in India, local elites may eventually dominate the groups and monopolise access to loans at the expense of the weaker members. Also, the women often take on huge additional burdens in order to receive financial services through SHGs, and the potential negative aspects of this do not seem to be as well appreciated as they are in Bangladesh (Kabeer, 1998). Other constraints of SHGs include the financial and geographical limitations of the group’s activities (Zeller *et al.*, 2001). The homogeneity of the membership in terms of occupation and financial scope may endanger the group’s financial stability (Lal *et al.*, 2003). Another weakness of this kind of group-based finance is that the demand for loans and emergency aid by its members happens all at once when natural calamities occur, and such demand cannot be satisfied (Zeller *et al.*, 2001).

2.6 Rural Credit in the Philippines

2.6.1 Country Overview

The Philippines is an archipelago of 7,107 islands located in the heart of Southeast Asia with Luzon, Visayas and Mindanao as its three main island groups (Figure 2. Map of the Philippines). The country is divided into 16 political regions which define their geographical location and cultural identity. Each region is composed of provinces and municipalities. The municipality is further divided into barangays (FAO, 2006). Metropolitan Manila is the national capital of the country and is the seat of government, trade and commerce, located in Luzon (Gerdes & Pehrson, 1998). The Philippines has 87 ethnic languages and dialects with Filipino or Tagalog as the national language, and English is widely used as a medium in government, education, and business (AusAid, 2006).

The country's population in 2000 was 76.5 million and there was an estimated population growth of 2.36% in 2003 (NSCB, 2003). The majority of Filipinos are Roman Catholic (86%), followed by Muslims and Protestants. The Philippines boasted a high literacy rate of 84% in 2003, but communication can still be difficult given the historical, cultural, religious, language and economic diversity in each region (NSCB, 2003).

Figure 2. Map of the Philippines

In 2003, GNP was 5.5% and GDP at 4.5% propelled by a mixture of the agriculture, light industry and services sectors. Electronic products are the main export and chief imports. Other exports include articles of apparel, clothing accessories and coconut oil (NSCB, 2003).

2.6.1.1 Agriculture

Agriculture plays a dominant role in the Philippine economy since 60% of the country's population is rural and two-thirds of these depend on farming for their livelihood (Balisacan, 2001; Venkataramani, 2005). The Philippines has a diverse climate where different crops are produced in different areas. A typical farming system consists of rice, corn and coconut as common base crops, and a few heads each of livestock and poultry. Coconuts have traditionally been a major export earner, and other important export crops are sugarcane, pineapples and bananas (Venkataramani, 2005). Philippine agriculture is characterised by a mixture of small, medium and large farms, but the majority are family smallholdings averaging about 2 hectares (Venkataramani, 2005).

The Philippine agricultural sector experienced a rapid growth rate during the period 1965-1980. This was substantially higher than most developing Asian countries (Lamberte *et al.*, 1994). The increases were due to the expansion of irrigation systems, increased application of fertilisers, adoption of high-yielding varieties, and investments in rural infrastructure (Balisacan, 2001). However, during the 1980s and 1990s, there was a dismal growth of agriculture which paralleled the poor performance of the overall economy (Balisacan, 2001). The decrease in growth of the agriculture sector in the 1980s was caused by drops in world commodity prices affecting the country's traditional export crops, a series of calamities and droughts, and the completion of the green revolution by the early 1980s (Balisacan, 2001). Also, with the continuing growth in population, decreasing food security is of rising concern (Venkataramani, 2005).

2.6.1.2 Poverty and Rural Development

Poverty in the Philippines is largely a rural phenomenon. The rural sector, which comprises approximately 60% of the population of the Philippines, accounts for over 70% of all the poor nationwide (Balisacan, 2001; UPLB, 1991). The overwhelming majority of the rural poor are in agriculture, and had a poverty incidence of 60% in 1997 which is substantially higher than in either industry or services sector (Balisacan, 2001).

The incidence of poverty is higher in rural areas than in urban areas. Among the 60 percent who reside in rural areas, 72.5% of rural families live below the poverty line (Gerdes & Pehrson, 1998). Most of the causes of rural poverty include land ownership, backward agricultural technology, unavailability of credit, lack of basic physical infrastructure and post-harvest facilities, and over-dependence on foreign markets (Gerdes & Pehrson, 1998). In urban areas, 40% of urban families are poor and live in squatter colonies or slums which are constantly threatened by demolitions and relocations. Unemployment, underemployment and low income are among the causes of urban poverty (Gerdes & Pehrson, 1998).

Although poverty in the Philippines is predominantly rural, it differs by region, but is widely spread in the Southern Philippines, particularly Mindanao (AusAid, 2006). The causes of rural poverty include poor productivity growth in agriculture, under-investment in rural infrastructure, unequal land and income distribution, high population growth and the low quality of social services (AusAid, 2006).

Some other factors like natural disasters, the risks associated with variable markets, and the persistence of armed conflict in Mindanao, are disrupting growth and causing severe poverty (AusAid, 2006)

Rural development has been a concern of the Philippine government since its independence in 1946. It was regarded as synonymous with agricultural development in the past (Lamberte *et al.*, 1994). This is because a great majority of the population resides in the rural areas where activities are mainly agriculture in nature. Also, the incidence of poverty is much worse in the rural areas than in urban areas (Lamberte *et al.*, 1994).

The Philippine performance in poverty reduction has been disappointing where it has lagged behind its major East Asian neighbours in achieving economic development. The country has not been able to sustain growth long enough to reduce its incidence of poverty (Balisacan, 2001). The large majority of people in the Philippines depend on agriculture for employment and income, thus poverty alleviation could be sustained through agricultural growth and rural development strategies (Balisacan, 2001). Agricultural growth reduces rural poverty and food insecurity directly by increasing agricultural incomes. Increases in agricultural productivity and farm incomes stimulate the growth of non-farm activities and employment opportunities (Balisacan, 2001).

Rural development in the Philippines needs to be given more attention since an equitable rural development needs faster growth in agricultural production and non-farm rural employment opportunities, as well as policies to channel the benefits of rural growth to the poor (Lamberte *et al.*, 1994).

The Asian Development Bank cites seven priority areas for concerted action to achieve transformation of the rural economy of the country. These are: expansion of irrigation, improving agricultural extension services, expeditious completion of the agrarian reform programme, developing rural infrastructure, improving upland agriculture and natural resource management, strengthening local government units and improving the provision of rural credit (ADB, 1998).

The ADB (1998) noted that inadequate rural credit is a major obstacle to rural employment and income generation. Only 30% of rural credit is provided by banks and savings and loans associations, while the remainder is provided by informal money lenders who charge very high rates of interest.

Since the mid-1980s, the Philippine economy has been undergoing a structural change brought about by important changes in economic policies. Credit programmes have been rationalised and subsidies substantially reduced to make them more effective (Lamberte *et al.*, 1994). To improve the situation, the

ADB (1998) has advocated of improving the formal credit system, reducing the costs of intermediation, allowing other banks and financial institutions to operate in the rural areas, removing credit subsidies, and encouraging NGOs to play a greater role in providing credit.

2.6.2 Rural Credit Situation

In the Philippines, the formal credit system consists of banks, non-bank financial institutions and cooperatives, while the informal sources include friends, relatives, neighbours, private moneylenders, traders, millers, input suppliers, and other informal groups (Tolentino, 1988).

2.6.2.1 Evolution of Credit Policies

Over the years, the Philippine Government has adopted policy measures to enhance the access of small farmers to credit (Corpuz & Kraft, 2005). Prior to the reforms in 1986, the rural credit policy in the Philippines took the supply-led approach with emphasis on directed credit[2] and interest rate subsidies that dominated the 1970s until mid-1980s (Corpuz & Kraft, 2005; Esguerra, 1998). The government's financing approach was supply-led wherein there were mandatory credit allocation, loan targeting, below-market interest rates, and credit subsidies to clients. The intention of such an approach was to provide loans to small farmers, small fisherfolk and generally small-scale borrowers who could not borrow from banks (Llanto, 2003). But various studies showed that many rural banks that participated in the government's subsidised credit programmes collapsed because of high arrearages and poor loan recovery. Also the credit went to unintended beneficiaries, such as rich farmers and those with political affiliation (Castillo & Casuga, 1999; Esguerra, 1981, 1998; Esguerra, 1993; Neri & Llanto, 1985).

Masagana 99 (M99) was a prime example of the implementation of rural credit policy prior to the reforms, which exemplified the government's rice self-

[2] Directed credit is the preferential allocation of credit to specific sectors based on a priority scheme determined by the government.

sufficiency programme through the provision of no-collateral loans at subsidised rates for the purchase of farm inputs (Esguerra, 1981). M99 was the centrepiece of the government's agricultural credit policy in the 1970s and served as a prototype for the succeeding supervised credit programmes (SCPs) in the country. In this programme, small banks were given 65-90% of the credit subsidies from the government that made them dependent on cheap sources of funds and discouraged mobilisation. Loan screening and collection were lax, which led to poor repayment rates (Lim & Esguerra, 1996). Other SCPs for corn, vegetables, fish, cattle, cotton and tobacco were patterned after Masagana 99 (Esguerra, 1981).

Another approach is the supervised credit[3] approach which sought to provide a subsidy for risk-taking through production loans with below-market interest rates. This approach was rationalised as institutional support for farmers opting to change their tenurial status from sharecropping to leasehold or owner-cultivatorship under the Marcos regime (Esguerra, 1981). It arose from the popular perception that farmer-borrowers are exploited by private moneylenders through usurious interest rates. Various assessments concluded that the supervised credit programmes in the Philippines were not successful for reasons such as the lack of effective supervision and control over loan utilisation, reluctance of financial institutions to continue financing because of increasing defaults, reluctance of farmers to borrow because of the fear of prosecution in case of delinquency, and the lack of banks and project management (Esguerra, 1998).

The reform of rural credit policy continued with the eventual change of government in 1986. Executive Order 113 (EO 113) terminated the direct lending programmes of non-financial government agencies and consolidated some 20 agricultural credit programmes into the Comprehensive Agricultural Loan Fund (CALF). There was pooling of funds for agriculture through the CALF wherein separate, commodity-specific lending funds were consolidated and managed by a single entity. The CALF was also used to fund pioneering

[3] A system of lending which combines adequate and timely provision of credit with farm and home management guidance under a trained production or farm management technician.

ventures and experimental credit schemes in the search for cost-effective ways of delivering credit to small farmers (Castillo & Casuga, 1999).

Another reform of government rural credit policy was a change in the approach to rural lending (Corpuz & Kraft, 2005). The new credit programmes provided a comprehensive range of activities instead of being commodity-specific and activity-specific as before (Castillo & Casuga, 1999). An example is the Integrated Rural Financing (IRF) programme which supports multiple and diversified farming systems (Llanto, 2003). There was an emphasis on group lending rather than individual lending, and on the strengthening of the savings mobilisation component of rural credit (Castillo & Casuga, 1999).

Still another reform was the participation of non-bank financial institutions in rural credit, including the cooperatives, credit unions, farmers' associations and Non-Government Organisations (NGOs). The involvement of these organisations aimed at improving small borrowers' access to credit, reducing transaction costs, promoting savings and alleviating poverty (Castillo & Casuga, 1999). The group focus improves the chances of getting a loan and group membership substitutes for collateral, without which an asset-less borrower may not have access to formal credit. Some of the rural credit programmes involving groups include: Grameen Bank Replication Program (GBR), Development Assistance for Cooperatives and People's Organizations (DAPCOCO), Integrated Pump Acquisition Program (IPAP), Livelihood Enhancement for Agricultural Development (LEAD), among others (Llanto, 2003).

2.6.2.2 Current Policies and Programs

The Agriculture and Fisheries Modernization Act (AFMA), or RA 8435, was passed in 1997 to help transform agriculture into a highly productive and competitive sector in order to enable farmers and fisherfolk to meet the challenges of globalisation. The Law covers the many elements critical to agriculture modernisation, such as research and development, infrastructure, training, marketing and credit, among others (1998). It can be noted that one of AFMA's current imperatives is the proper management and utilisation of credit funds. It initiated the Agro-Industry Modernization Credit and Financing Program (AMCFP), which is the current agriculture, fisheries and agrarian reform credit and financing system of the country.

The AMCFP is designed to make credit more accessible to small farmers by including rural banks, cooperative rural banks, cooperatives, self-help groups, farmers' organisations, and non-government organisations as retailers of the AMCFP fund (1998). Its objective is to make credit delivery more efficient and effective through financial institutions that have adequate experience, expertise and resources, and are less costly by removing the lending task from non-financial agencies of the government (Corpuz & Kraft, 2005). Policymakers continue to be concerned as to how farmers can be mainstreamed into the formal credit market (Castillo & Casuga, 1999).

2.6.2.3 Other Policy Initiatives

The Agricultural Credit Policy Council (ACPC) designs innovative financing schemes to address the particular requirements of marginalised farmers and fisherfolk who cannot put up the collateral required by banks. The objective of designing such innovative financing schemes is to give the farmers and fisherfolk the opportunity to be productive and acquire the necessary tools so that they can be mainstreamed into the credit arena (Corpuz & Kraft, 2005). Likewise, the ACPC provides grant funds to farmer organisations for institution capacity building activities in cooperation with both government and private training institutions. The programme enhances the delivery of credit to small farmers by providing funding assistance for relevant institution capacity building projects/activities such as: capital and savings mobilisation; development of management information systems; social preparation for small farmers and fisherfolk; management training; credit risk management; and organisation, establishment and strengthening of cooperative banks and other farmer-owned financial institutions (Corpuz & Kraft, 2005).

2.7 Credit Issues

Based on one evaluation study by the International Fund for Agricultural Development (IFAD), the Philippines was one of the most prosperous countries in South-East Asia in the 1950s, but at present, it lags behind in terms of economic growth with half the rural population living in poverty (IFAD, 2003). Microcredit was tested as an anti-poverty tool in the early 1990s but was not considered economically viable because the outreach to poor people was insignificant and slow (IFAD, 2003).

Agricultural credit is important in the development of the agricultural sector in the Philippines, but access by the rural households to credit from formal institutions remains very low (Llanto, 1993; Yaron *et al.*, 1997). Small-scale and subsistence agriculture source their loans mostly from informal lenders (Llanto, 1993). This can be attributed to the lack of collateral and the lack of available information to rural borrowers (Yaron *et al.*, 1997). Also, other credit problems encountered by small farmers in the rural areas include non-versatility of formal loans, commodity-specific credit, lack of education of farmer-borrowers, lack of farmer participation in planning agricultural credit programmes, lack or inadequacy of financial institutions, and late release of loans (Octavio & Aragon, 1986).

The presence of a good credit service in the rural areas is important to serve the rural people, since credit is an essential part of their routine both for production and consumption (Llanto, 1993). Most rural households have very low-or no-surplus production, thus they frequently borrow, even at very high interest rates, to subsist (Chowdhury & Garcia, 1993). A wide scope of loan purposes covering production, consumption, and for other non-farm activities should be offered by financial institutions (Chowdhury & Garcia, 1993). In order to accommodate the needs of rural households, different institutional set-ups of rural banking should be effectively conducted in the rural areas (Desai & Mellor, 1993).

Success of the credit services in rural areas has been due to factors such as: the credit programmes having been designed to be simple and transparent with easy credit approval; fast disbursement of loans, with sufficient cash for disbursements to its clients; and locally experienced, well-trained, and highly motivated people working in the credit institutions (Yaron *et al.*, 1997).

2.8 Summary

Credit is essential for agricultural development and is often a key element of agricultural modernisation. It has been primarily been seen as promoting agricultural production and increasing income to farmers. However, access to credit is limited in rural areas and the majority of poor small farmers are excluded from credit systems.

The rate of obtaining loans from the formal financial institutions in the developing countries by rural borrowers is low due to the complicated and lengthy procedures that overwhelm the poor and uneducated farmer-borrowers. In other cases, credit problems which have restricted them from borrowing include commodity-specific credit, lack of participation in planning agricultural credit programmes, lack of, or inadequate, financial institutions in the rural areas, and late releases of loans which led them to borrow from the informal sources.

Determining the problems and the credit needs of small farmers are important considerations in designing appropriate credit systems for them. The design of credit products should be based on clients' demands and needs. Designing appropriate rural financial systems for small farmers is an adequate financing strategy.

A thorough understanding of the small farmers' credit perceptions and preferences will assist policy makers to make better decisions in designing appropriate credit systems for them. There is, however, limited information to enable understanding of the farmers' perceptions and preferences regarding access to credit. This gap in the literature prompted this research.

CHAPTER 3: METHODOLOGY

In this chapter is an account of how the research was conducted. The research method is described, followed by a description of the research location. The sampling procedure and the choice of samples are discussed as also are the processes used for data collection and data analysis.

3.1 Research Method

An interview questionnaire was developed for the research. The questionnaire (Appendix I) was designed to collect the data needed to meet the objectives of the research. Two levels of respondents were used in this research: the individual farmers and key informants. The interview for individual farmers has two components; a survey interview for the 45 farmers using the developed questionnaire (Appendix I), and in-depth interviews for the 15 farmers chosen from the 45 farmers previously interviewed.

The questions for the interview with 45 farmers were divided into two sections: respondent profile or characteristics, and access to credit. The data from the first section describe the social and economic characteristics of small farmers. The second section sought data regarding access to credit. The questions are open-ended and face-to-face interviews were conducted. The aim of the survey interviews from 45 respondents was to obtain detailed information on farmers' profile and characteristics. It gave the general characteristics of small farmers in the research area based on landholdings, types of crops, off-farm and on-farm activities, education attainment, and so on. The information from the second section was also considered in the in-depth interviews.

The in-depth interviews with 15 respondents focused on how they perceived the rural credit facilities in their areas, their choices or preferences of credit sources, the factors they consider in choosing their creditor and how they come to know the credit providers, what problems or difficulties they encounter in accessing the credit facilities, and their expectations and suggestions as to how to improve the credit accessibility in their area. The data collected from the in-depth interviews will answer most of the research objectives. An interview guideline was prepared prior to the interviews (Appendix II). The conversations were open-ended.

The key informants' interviews were conducted to obtain the necessary data on the availability of credit services in the research area and the processes involved in obtaining credit. The key informant interviews were used to validate the results obtained from the farmers' interviews. To address the objectives of the key informant interviews, a guideline was prepared prior to the interviews (Appendix III).

The interviews were conducted in the local dialect.

3.2 Location of the Research

The research was conducted in Davao del Norte province of the Philippines which is strategically located at the south eastern part of Region XI, Southern Mindanao. (Figure 3. Map of Davao del Norte). It is positioned as a "food basket" and "agri-industrial hub" in Mindanao, given its abundant agricultural resources (PPDO, 2000). Davao del Norte is predominantly an agricultural province, and where the people earn their income mostly from agriculture. It is the region's most important rice-producing province and the second ranking corn producer (PPDO, 2000). Davao del Norte was selected as a study area because it produces a variety of agricultural crops, thus varied characteristics of farm households are found in the province. The province was also chosen because of the researcher's knowledge of the local language of the people.

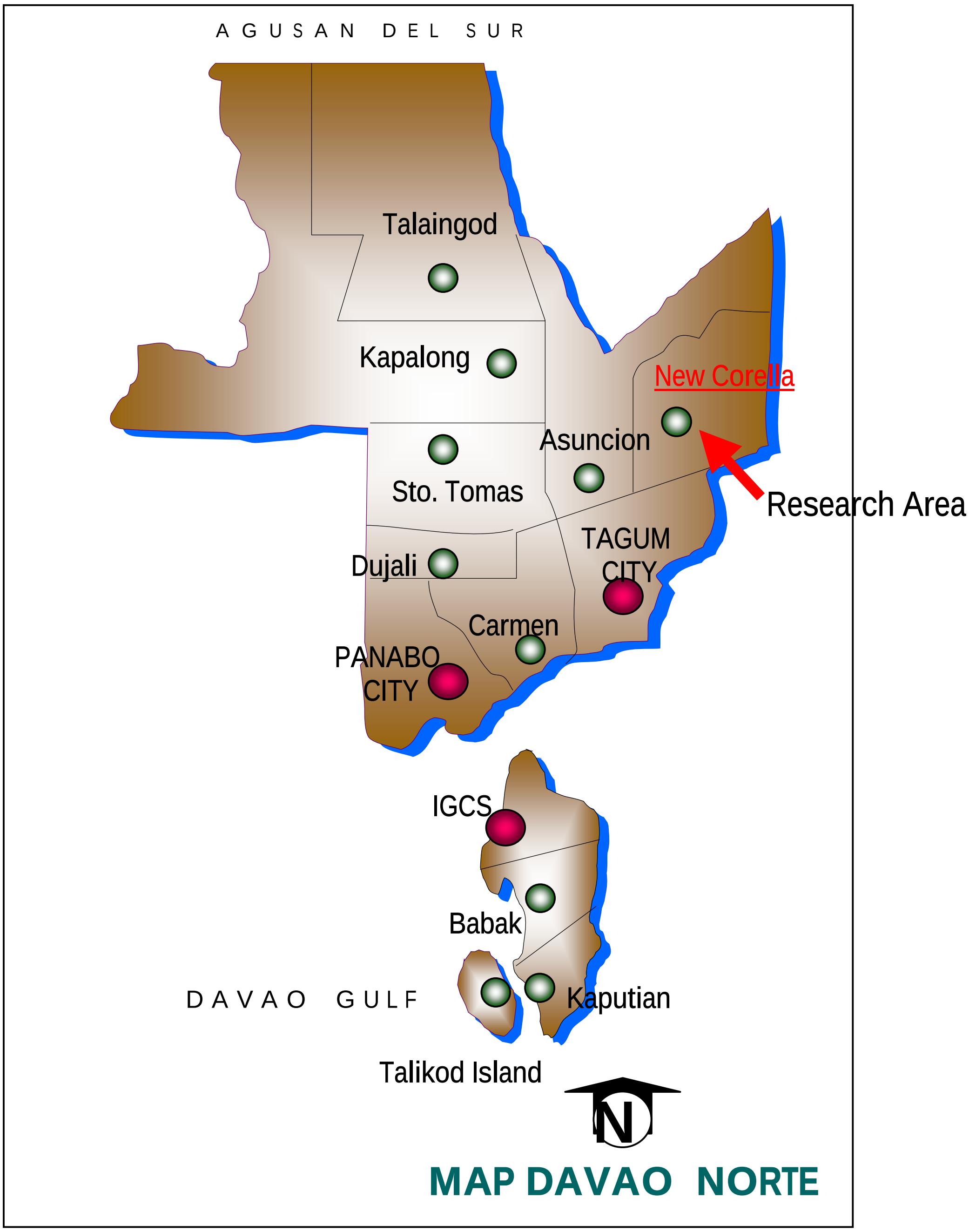

Figure 3. Map of Davao Del Norte showing the research area, New Corella.

Generally, Davao del Norte is characterised by rugged mountains and moderately to steeply sloping areas on the western part and wide alluvial plains on the central lowland area. However, some areas have gently undulating and rolling topography. It is characterised by unpronounced dry and wet seasons and is naturally protected by mountain ranges that act as barriers from the onslaught of typhoons (PPDO, 2000). The province has a total land area of 364,056 hectares and had a population of 500,000 in 2000.

Davao del Norte is endowed with rich and abundant agriculture products as a result of its fertile soil and favourable climate (PPDO, 2000). About 131,827 hectares are devoted to agriculture. Crops commonly grown in the province are rice, banana, coconut and in some areas mixed crops like coconut combined with banana, corn, coffee, fruit trees, vegetables and other crops. For rice, the farmers usually double crop each year with the exception of a few who have three (3) croppings in a year. The province has eight municipalities and two cities (PPDO, 2000)

Figure 4. The motorcycle is the mode of transportation especially in the upland barangays of the New Corella municipality.

The research was conducted in the municipality of New Corella which is located in the central portion of the province of Davao del Norte. It has a total land area of 32,148 hectares, constituting about 8.83% of the total land area of Davao del Norte province. Of the total land area of the municipality, about 9,600 hectares are classified as nearly flat lands and more than 20,000 hectares are hilly to mountainous areas. It is composed of twenty (20) barangays[4] and had a population in 2000 of 44,590 of which 37,048 (83%) live in rural areas. Specifically, the study was conducted in the three barangays of New Corella, Mesaoy, Del Pilar, and New Cortez (MPDO, 2004).

3.3 Sampling

Upon reaching the proposed study region which is Mindanao, a courtesy call was paid to the regional director of the Department of Agriculture, Region XI. Assistance in the selection of the specific province to conduct the research was requested from the regional office based on accessibility and presence of farm households with varied characteristics of the research area. As suggested by the regional office, the province of Davao del Norte was chosen as the study area.

Likewise, assistance was requested from the provincial agricultural office in choosing the municipality. Among the eight municipalities of the province, only one municipality was selected in order to achieve an in-depth understanding of small farmers' perceptions and attitudes toward rural credit and for efficiency reasons given the limited time available for the study. New Corella municipality was selected because it represents a variety of farm characteristics.

The assistance of the municipal government in New Corella was sought in choosing the barangays or villages in the municipality for the research. With advice from the municipal agricultural officer, the barangays were selected based on the types of crops planted by the small farmers and on the criterion that both upland and lowland systems were present. The first consideration on crop type was that as rice is the main crop, it must be planted by the selected farmers. Also, the barangays that were selected for the study were those with constituents who are predominantly engaged in farming activities as their

[4] Smallest political unit of the country.

means of livelihood. The selected barangays were Mesaoy, Del Pilar and New Cortez, as they are big and most of the farmers live in far apart sitios[5].

A list of farmers was secured from the master list of the municipal agricultural office. For every barangay visited, a courtesy call was paid to the barangay captain. A barangay map was requested in order to have a picture of how far one sitio was from the other to get the farmer-respondents. In each barangay, 15 small farmer respondents were selected from the list and interviewed using the semi-structured interview questionnaires[6]. The questionnaire was designed to elicit the data needed to meet the objectives of the research. A total of 45 respondents were interviewed from the three barangays.

In gathering the qualitative data which is dominant in this research, purposive sampling was used. It was used in choosing the samples because prior assessments of the typical characteristics of the farmer-respondents were done, and when the researcher makes a judgement of the samples to include in the research, purposive sampling is used (Scheyvens & Storey, 2003). Out of the 15 respondents interviewed in each barangay, 5 respondents were chosen for the in-depth interviews.

3.4 Data Collection

The field work for the research was conducted between August and October 2005. In this research, both primary and secondary data were collected. The primary data were derived from the interview responses with individual farmers. Other primary data were also collected from in-depth interviews with 15 respondents and four key informants. Secondary data were derived from the Provincial Agriculture Office, Municipal Agriculture Office, Department of Agriculture, and other documents. The questionnaire served as a guide for the interview but to some extent, the conversation tracked to other things that the farmer-respondents wanted to talk about, which sometimes contributed to the

[5] A sub-division of the barangays composed of several families.
[6] Copy attached as Appendix I. The questionnaire is in English but was translated to the local dialect during the interview.

difficulty in refocusing and exploring information related to the objectives of the research. In some instances, the farmer-respondents discussed other personal problems not relevant to the problem of credit accessibility.

A village woman was hired to assist the researcher with the interviews, facilitating entry into the farmers' houses to key local knowledge since the researcher was not familiar with the area, and for safety reasons since the area is infested with insurgents. The distance between farm households and the climatic condition limited the number of interviews which could be completed in a day. The village woman was a great help in locating farmer-respondents because of her familiarity with the area.

Figure 5. An interview with a woman farmer in barangay Del Pilar who obtained credit from the Rural Bank of New Corella.

3.4.1 Interviews with 45 Farmers

Face-to-face semi-structured interviews were conducted with 45 farm households from the three barangays to collect the information necessary for the research. Permission was requested from the farm household prior to the interview. The interview was done only if given a positive reply by the farmer-respondent. Since the respondents are small farmers who usually have little education, the face-to-face interview is considered more efficient than other methods because the researcher can explain directly the contents of the questionnaire (Babbie, 2001; Neuman, 1997). A face-to-face interview was utilised in this research also because this method of interview has the highest response rate when compared to other interview methods, such as mail-out surveys or telephone interviews, and the interviewer can observe the surroundings and observe non-verbal communication (Neuman, 1997; Scheyvens & Storey, 2003).

A pilot test of the interview guide or survey questionnaire was conducted in the first barangay that was surveyed. The initial interviews with farmers posed a few difficulties in some cases because the farmers were hesitant at first to answer some questions, but they became more cooperative as rapport was established. Also, the local language of the study area was used during the interview to increase the level of participation among respondents and to create a comfortable atmosphere for both the respondents and the researcher. With the verbal permission of the respondent, a photograph was taken while the researcher was interviewing for documentation purposes as further evidence of informed consent by which the respondent agreed.

3.4.2 In-Depth Interviews with 15 Farmers

In-depth interviews were conducted with selected small farmers in the study area, five from each of the three barangays. They were selected based on educational attainment, awareness of credit services and programmes in their barangay, the type of land ownership, if they applied for credit, credit use and its purpose, and willingness to be interviewed. This in-depth interview with the farmer-respondents was more relaxed, and they expressed their opinions without hesitation because this was already the second visit to them and rapport with the researcher was already established. The reason for conducting in-depth interviews is to ascertain people’s views, knowledge, experiences, interpretations, perceptions, behaviours, practices, and a good way of generating this information is to talk with people, listen to, and interact with them (Mason, 1996).

The interviews were done as informally as possible based in the most favourable situation for the farmer-respondents. It was usually conducted before their lunch and after their farm work in the morning because it would have been more difficult to interview them if they had been working on the farm, since then their answers would have been too brief and further questions could not have been asked.

3.4.3 Key Informant Interviews

A total of four key informants were interviewed. The municipal mayor and the municipal agricultural officer of New Corella were interviewed regarding the implementation of the LGU Financing Programme. The Rural Bank of New Corella is the only lending bank in the municipality and an interview with the loans officer of the bank was undertaken to gather information about the credit mechanisms of the agricultural loans offered by the bank. The Quedancor is an attached corporation of the Department of Agriculture, which is tasked under the Republic Act 8435 as the fund administrator of all existing agriculture and fishery credit guarantee schemes. The district supervisor of Quedancor in Davao del Norte province was interviewed about the credit schemes they offer to small farmers in the province. The key informant interviews were used to validate the results obtained from the farmer interviews. The interviews were informal and conversational, but carefully facilitated to meet the objectives of the research. The interviews lasted for 60 to 80 minutes.

3.5 Data Analysis

The questionnaire data were edited and some responses in the local dialect were translated to English. The information from key informant interviews was organised and narrated. An EXCEL spreadsheet was used for socio-economic data entry. The socio-economic data from the questionnaires were tabulated and categorised. Responses to the questions on the socio-economic characteristics of farmers were first categorised. The following variables such as gender, age, educational attainment, farm size, tenurial status, and the incidence of borrowing were tabulated. The frequencies and corresponding percentages for the different socio-economic characteristics were described and compared.

The characteristics of small farmers in the study area were described (quantitatively, when possible) based on landholdings, types of crops/commodities, off-farm and on-farm activities, household size and income, education level, and the years of farming.

The responses to the questions regarding access to credit were categorised. Similar responses were classified, grouped and connected to other responses. Responses from the key informant interviews were described and connected to the responses of the farmer-respondents in the analysis.

The open-ended responses from the in-depth interviews were coded and categorised. There were some unique responses from the open-ended questions which posed some difficulties in coding. These unique responses were connected to the other responses in the analysis. In analysing the qualitative data, repeated iterations were done before moving toward a final analysis. After several iterations, comprehensive analysis with generalisations was gathered after those vague ideas and concrete details. According to Neuman (1997) the analysis of qualitative data can be modified over and over to become successively more accurate.

The secondary data cover the profile of the study area such as the geographical characteristics, availability of rural financial institutions and rural credit programmes, and the credit status of the small farmers in the research area.

3.6 Summary

In this chapter the methodology used in the research of exploring the use and access of rural credit by small farmers in Davao del Norte Province of the Philippines has been discussed. A combination of qualitative and quantitative methods was used in gathering data from the field. Semi-structured interviews were undertaken for the 45 farmers from the three barangays selected. In-depth interviews were undertaken for the 15 farmers to gather information on their preferences, level of awareness concerning credit availability, reasons for borrowing, problems encountered in obtaining credit, and their suggestions to improve access to credit. In addition to the semi-structured interviews administered to the farmers, the researcher also conducted key informant interviews with the municipal government official, bank loans officer, and government credit programme implementers in the research area. The results of the research are presented in the next chapter.

CHAPTER 4: **RESULTS AND DISCUSSIONS**

In this chapter the results of research conducted within three *barangays* in Southern Mindanao, the Philippines, are presented.

The chapter includes a brief background of the research area, the characteristics of the farmer-respondents, and available credit services in New Corella, both formal and informal. The different processes of obtaining loans with the existing formal credit services are also presented. Then the credit preferences of small farmers as well as the factors they considered in choosing their lenders are provided. The problems/difficulties encountered by the farmers in obtaining credit and some of their suggestions to improve their credit accessibility are also presented and discussed in this chapter.

4.1 The Research Area

The research was conducted in three barangays, Mesaoy, Del Pilar, and New Cortez, in the municipality of New Corella, province of Davao del Norte, which is located in the Southern Mindanao region of the Philippines. Davao del Norte was created under the Republic Act 4867 together with the provinces of Davao del Sur and Davao Oriental on May 8, 1967 (PPDO, 2000). The province has eight municipalities, two cities, and 223 barangays. Tagum City is the centre of business and trade in Davao del Norte.

The province is characterised by relatively evenly distributed rainfall throughout the year with no pronounced rainy season or dry season. Davao del Norte is basically rural and the provincial economy is agriculturally based, with 36.2 percent of the land area or 131,827 hectares, devoted to agriculture (PPDO, 2000). This includes approximately 29,390 hectares of rice, 21, 347 hectares of coconut, and about 41,404 hectares of mixed cropping of coconut combined with banana, corn, coffee, fruit trees, vegetables and other crops (PPDO, 2000).

Figure 6. A Diversified Farm in the municipality of New Corella.

New Corella is located in the central portion of the province of Davao del Norte. It is bounded on the west by the municipality of Asuncion, on the northeast by the municipalities of Montevista and Nabunturan, and on the south by the municipalities of Tagum and Mawab. New Corella has a total land area of 32,148 hectares constituting about 8.83% of the total land area of the province of Davao del Norte. It is composed of twenty (20) barangays and had a population of 44,590 in 2000, which was an increase of 7.15% from 1990 (MPDO, 2004).

4.2 Characteristics of the Farmer-Respondents

4.2.1 Sources of Income of Farmer-Respondents

A total of 45 farmers were interviewed, 15 from each barangay. Rice farming is the main source of income in the municipality, with bananas and coconuts as the second and third crops respectively, produced by the farmers. Other cash crops include corn, vegetables, and fruit trees. However, only a very few farmers produce livestock and poultry for income purposes – these are mostly for their own consumption.

Figure 7. A rice farm of a farmer-borrower from LGU Financing Programme in Barangay Mesaoy in New Corella

Most of the farmer-respondents have been farming for 10 to 25 years. Among the 45 respondents, two years is the shortest time farming while 30 years is the longest. Carpentry, motorcycle driving, teaching, fish vending, rice trading, small *sari-sari* (variety) stores, and government employment were among the non-farm and off-farm sources of income of the farmers in the research area. A few respondents have sources of income from remittances abroad.

4.2.2 Gender and Age Distribution of Farmer Respondents

The age of the farmers in the three barangays ranged from 30 to 69 years, with the ages relatively evenly distributed across this range. Women accounted for almost one-third of the total respondents (Table 1).

Table 1. *Distribution of Farmer-Respondents according to Gender and Age*

Characteristics	Mesaoy	Del Pilar	New Cortez	**Total**
Gender				
Male	10	11	10	**31**
Female	5	4	5	**14**
Total	15	15	15	**45**
Age				
30 – 40	5	4	2	**11**
41 – 50	5	4	8	**17**
51 – 60	4	4	2	**10**
> 60 years	1	3	3	**7**
Total	15	15	15	**45**

4.2.3 Educational Attainment of Farmer-Respondents

Significant variation among the three barangays was observed with respect to the educational attainment of the respondents. In general, the New Cortez respondents were relatively less educated and the Del Pilar farmers had a higher level of formal education. Among the fifteen respondents in Del Pilar, five had attended college level and six had graduated from high school (Table 2). It can be observed that accessibility to educational institutions has affected the educational attainment of the people in the barangays. New Cortez is located in an upland area which is far from the schools, while Del Pilar is in the lowland area which is nearer to the schools in the municipality.

Table 2. *Educational Attainment of Farmer-Respondents*

Educational Attainment	Mesaoy	Del Pilar	New Cortez	**Total**
Primary level	3	3	11	**17**
Some High School	4	-	2	**6**
High School graduate	3	6	1	**10**
College level	4	5	1	**10**
Vocational	-	1	-	**1**
Others	1	-	-	**1**
Total	**15**	**15**	**15**	**45**

4.2.4 Farm Size of Farmer-Respondents

About two-thirds of the respondents farm more than one hectare of land (Table 3). The farm size of the respondents in the study area ranges from 0.5 hectares to 8 hectares.

Table 3. *Farm Size of Farmer-Respondents*

Farm Size	Mesaoy	Del Pilar	New Cortez	**Total**
0.5 – 1.0 ha.	4	5	5	**14**
> 1.0 ha.	11	10	10	**31**
Total	15	15	15	**45**

4.2.5 Farm Tenure of Farmer-Respondents

About 58 percent of the farmer-respondents are owner-cultivators and 24 percent are share tenants. Some 18 percent of farmer-respondents are both owners and share tenants of the farms they work (Table 4). From the interviews, most of the share tenants' farms are owned by parents or close relatives.

Table 4. *Farm Tenurial Status of Farmer-Respondents*

Tenure	Mesaoy	Del Pilar	New Cortez	**Total**
Owner	6	9	11	**26**
Share Tenant	6	3	2	**11**
Both Owner & Share Tenant	3	3	2	**8**
Total	15	15	15	**45**

4.3 Availability of Credit Services in the Municipality of New Corella

The available credit services in the research area from where farmers obtain credit were determined. Information on the availability of agricultural credit in New Corella comes from interviews with key informants as well as from interviews with 45 farmers in three barangays. Farmers were questioned on how they financed their farming and how they have accessed credit over the past five years.

Formal credit sources currently available (in 2005) in the municipality include the Rural Bank of New Corella, the Local Government Unit (LGU) Financing Programme, and Quedancor's Unlad-Ani (improved harvest) for Income Augmentation and Livelihood for the Self-Reliant Farmers participating in the Hybrid Rice Cultivation Project (UNLAD-ANI-IAL-SRF-HRCP). Others available in the recent past include the National Irrigators Association (NIA) credit group, and the now dissolved New Corella Federation of Agrarian Reform Beneficiaries (NECOFARBIA). Informal credit sources include rice traders, copra buyers, private moneylenders, landowners, neighbours, friends, and relatives.

4.3.1 The New Corella Rural Bank Credit Service

The following features of this credit provider were collected through an interview with the Loans Officer of the Rural Bank. To describe better the process and requirements for obtaining loans, the mechanism is diagrammed and described below.

Figure 8. The New Corella Rural Bank in Davao del Norte.

The New Corella Rural Bank offers agricultural loans to the farmers in the municipality with 14% per annum interest rates. Two schemes of agricultural loans are available for the farmers, *with collateral* and *without collateral* credit schemes.

4.3.1.1 With Collateral Credit Scheme

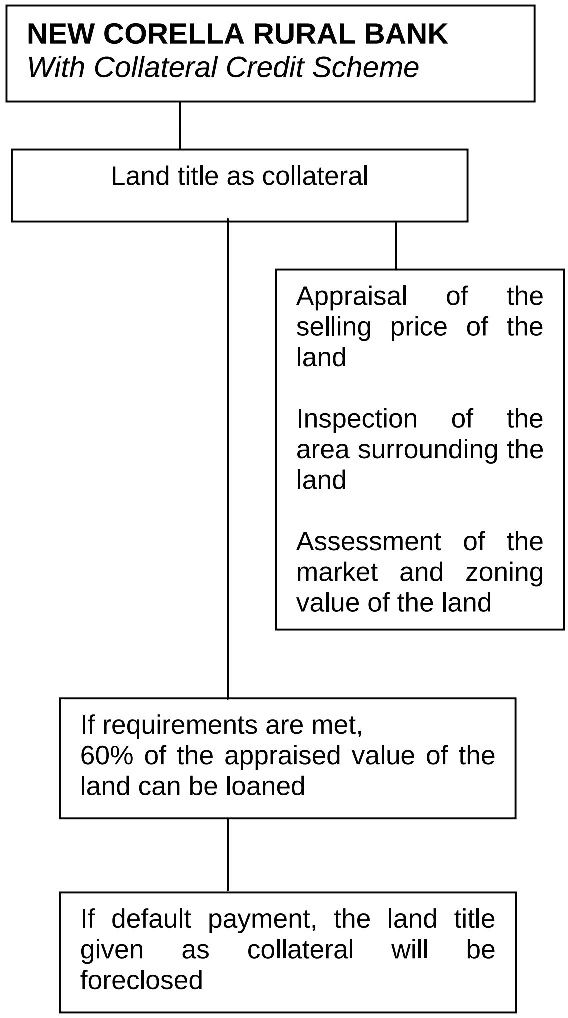

Figure 9. Mechanism of Agricultural Loan Applications with Collateral Credit Scheme in New Corella Rural Bank

As shown in Figure 9, *with collateral* agricultural loan requires collateral such as land title. The following will be undertaken by the bank for the land title as collateral: appraisal considering the selling price of the land; inspection of the surroundings of the area where the land is located; and assessment of the market value of the land in the tax declaration and the zoning value. About 60% of the appraised value of the land will be the amount that can be loaned to the borrower. If the borrower can not repay the loan, the bank will foreclose the property given as collateral (e.g. land title). The borrower will be given three (3) consecutive foreclosure notices and a one-year redemption period. If not redeemed in this period, a lawyer's notice will be given. Finally, the title of the land will be transferred to the bank's name.

4.3.1.2 Without Collateral Credit Scheme

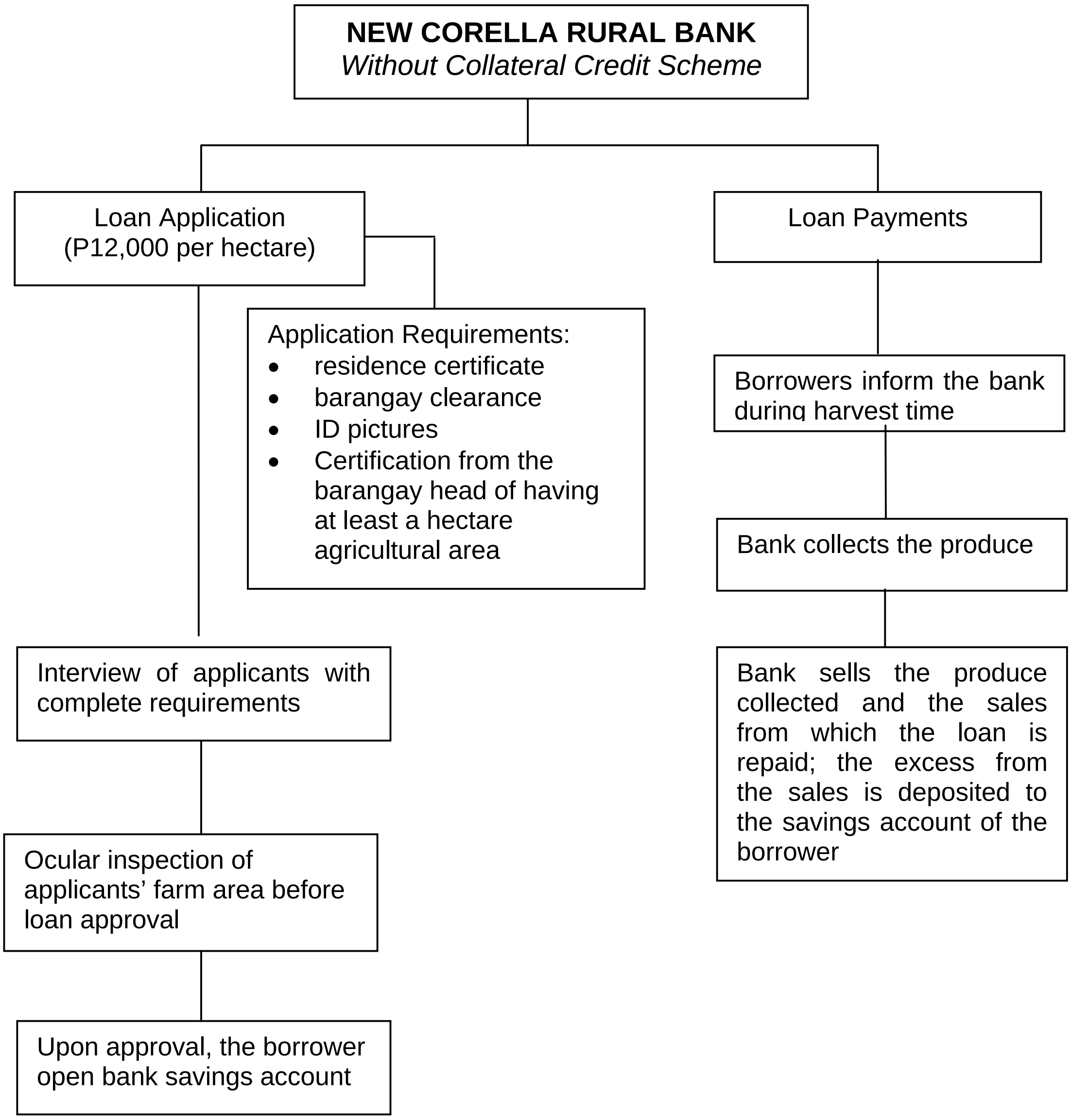

Figure 10. Mechanism of Agricultural Loan Applications Without Collateral Credit Scheme in New Corella Rural Bank

As diagrammed in Figure 10, the *without collateral* mechanism requires from the applicants the following: residence certificate, barangay clearance, ID pictures, and certification from the barangay head that the farmer has an agricultural area of at least one hectare. Once these requirements are met, an interview is conducted with the applicant. The farm area of the applicant is inspected before the application will be approved. The amount that can be loaned is P12,000 per hectare.

Upon approval and prior to the release of the loan, the borrowers are required to open a savings account with the bank. The borrowers are allowed up to three consecutive loans once they are approved as borrowers based on the above mentioned requirements. However, if the borrowers want to borrow again from the bank, they need to have three good credit records with no overdue payments during the three consecutive loans they had. For those who are not repaying on time, the overdue payments incur 3% interest per month. The Loans Officer said that they have close supervision of the borrowers as one of their loan monitoring systems in the bank. The bank's process of collecting the payment from the loan is that the borrowers need to inform the bank during harvest time so that the bank will collect the payment from the produce. The bank is the agent who sells the produce and the income from the sales of the produce will be paid to offset the loan of the borrowers. The excess from the sales will be deposited to the savings account of the borrowers wherein the borrowers withdraw the money from their savings account.

The Rural Bank offers loans for both individuals and groups, like cooperatives. The maximum amount that can be loaned to a cooperative is P100,000. The agricultural loans for different crops have different loan maturities. For rice and corn, the maximum loan maturity is six months, but for coconut and mango, the maximum loan maturity period is two years.

Among the 45 farmer-respondents in the research area, only six farmers have borrowed from the New Corella Rural Bank in the last five years. These farmer-borrowers are all owner-cultivators and own more than one hectare of land. The farm size of the farmer-borrowers ranges from 1.5 hectares to 7 hectares. Rice is the main crop they are farming. Other crops such as bananas, coconuts, and fruit trees are also produced by them. Two of the farmer-borrowers who obtained loans from New Corella Rural Bank have achieved college level education, and the other four graduated from high school. Their age ranged from 42 to 69 years old. They all have been farming for quite some time as their means of livelihood, ranging from 15 to 30 years. Two have farmed for 15 years; two for 25 years; one for 26 years; and one for 30 years. Only one of these respondents has a sari-sari (variety) store as another source of income. The loans obtained from the New Corella Rural Bank by these farmer-borrowers were used for land preparation of their farms, purchase of production inputs such as fertilisers and pesticides, purchase of tractor, and as initial capital for the *sari-sari* store. One farmer-respondent borrowed from the bank because he said that he knows somebody from the bank who facilitated his application.

4.3.2 The Local Government Unit (LGU) Financing Programme

The Local Government Unit (LGU) Financing Programme was implemented as an initiative of the municipal government to help the small rice farmers in the community who lack capital in their farms. Likewise, the municipal government wants to protect the small rice farmers from usurious lending and unfair market prices. This is also one of their poverty alleviation programmes. Twenty percent of the municipality's development fund every year was allocated for the financing programme in order to help the farmers in food production and to give them low interest loan financing through a technology package. The financing programme provides a production loan amounting to P7,000 per hectare with a 2.5% service fee. The production loan is repayable over six months. The process of obtaining the production loan is diagrammed in Figure 11.

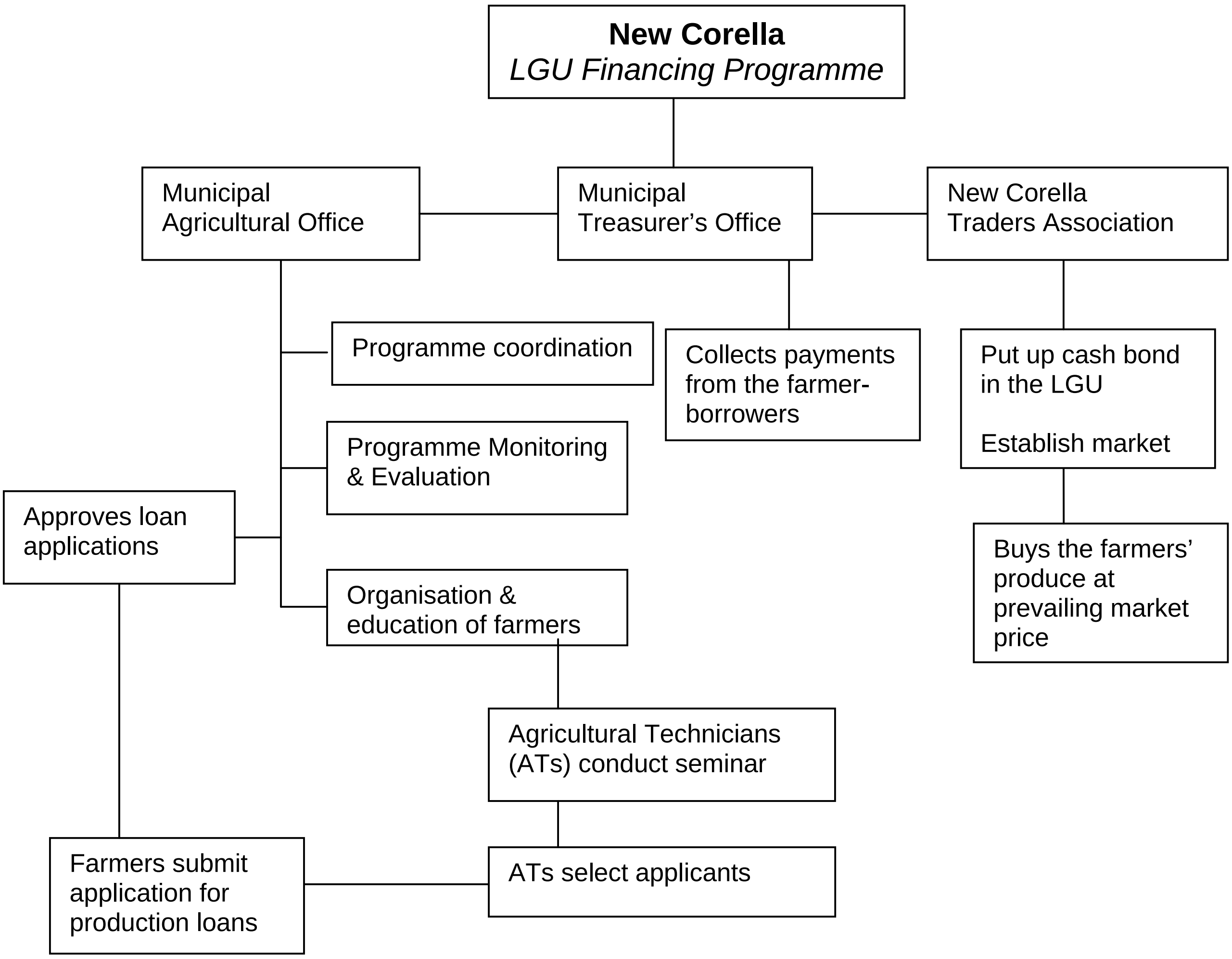

Figure 11. Mechanism of Production Loan Applications for LGU Financing Programme

The Municipal Agricultural Officer explained that the local traders' association in the municipality also supports the municipal food production financing programme by taking part in the establishment of a just marketing system. They put a cash bond in the municipal government office of not less than the total amount released for loans to farmers during each cropping season. The Municipal Agricultural Office (MAO) is responsible for the coordination, monitoring and evaluation of the programme. The MAO also leads in organising and educating the farmers and traders. The farmer-recipients are selected by the agricultural technicians in the programme areas after attending a seminar.

The recipients submit application forms for the production loans for approval by the municipal agricultural office. For the approved applicants, a memorandum of agreement is instituted between the contracting parties. The farmer-recipients must provide the labour counterpart for land preparation and crop maintenance, and adopt the appropriate package of technologies recommended by the supervising agricultural technicians. They are also responsible for providing security and protection of their own crops against stray animals and pilferage. There is no collateral required for the loan. The municipal treasurer’s office is responsible for the collection of payments from the farmer-borrowers.

The municipal agricultural officer said that it is a common attitude among the farmers in New Corella that the farmer-borrowers (rice farmers) prefer to pay with their produce during harvesting time rather than in cash. He stressed that the LGU Financing Programme has been in operation for seven years and the repayment performance is 88%.

From the 45 farmer-respondents, 14 farmers have borrowed from the LGU Financing Programme. The farmer-borrowers are all rice farmers. The ages of the farmer-borrowers range from 33 to 62 years old, and they attained various educational levels. Four of the respondents attained primary level, five are high school level or graduate and five attended college level. Most of the farmer-borrowers of the LGU Financing Programme are owner cultivators, only five respondents are share tenants. The farm sizes of these borrowers range from 0.5 to 5 hectares and they had been farming for 2 to 30 years. The main reason for borrowing among these farmer-respondents is for the purchase of production inputs.

4.3.3 Quedancor's Unlad Ani (Improved Harvest) for Income Augmentation and Livelihood for the Self-Reliant Farmers

Figure 12. Quedan and Rural Credit Guarantee Corporation (Quedancor) District Office in Tagum City, Davao del Norte.

The Quedan and Rural Credit Guarantee Corporation (Quedancor), an attached government corporation of the Department of Agriculture, also provides a credit service in New Corella. According to the District Supervisor of Quedancor in Davao del Norte, it is an innovative financing scheme referred to as the Self-Reliant Team (SRT) Model for the marginalised group of the community. The Quedancor is also promoting the significance and usefulness of credit as a tool for augmenting incomes and improving the economic well-being of the people in the community. One of the credit schemes being implemented is the Unlad-Ani (improved harvest) for Income Augmentation and Livelihood for the Self-Reliant Farmers participating in the Hybrid Rice Cultivation Project (UNLAD-ANI-IAL-SRF-HRCP). This is a package of a collateral-free loan for *palay* (rice) farmers who want to utilise hybrid seeds and modern technologies in undertaking farm activities to increase yields and income. The mechanism of the credit scheme is illustrated in Figure 13.

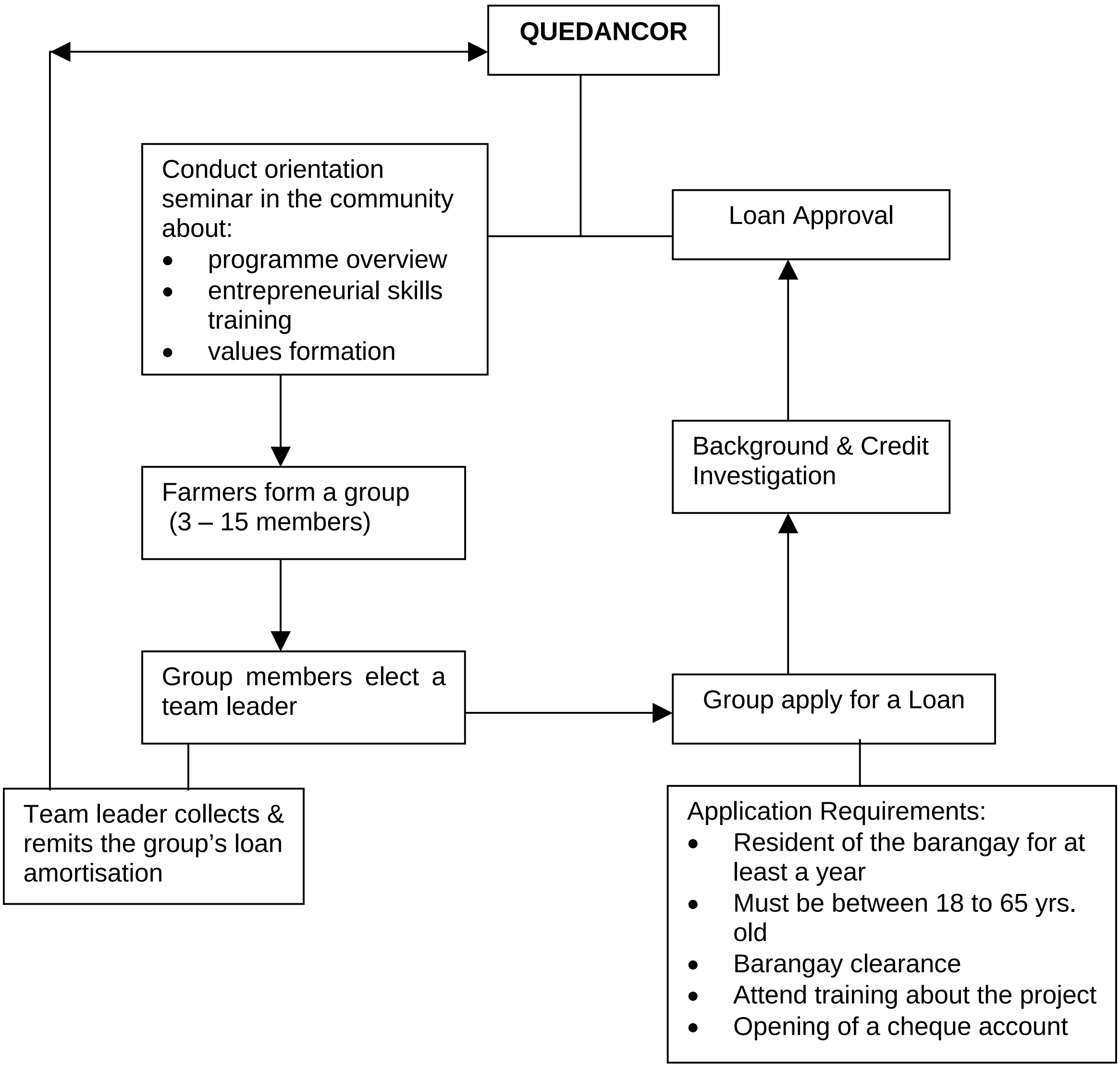

Figure 13. Mechanism of Loan Applications for Quedancor Financing Scheme

According to the District Supervisor, the Quedancor provides finance for the working capital or production requirements of Self-Reliant Hybrid Seed Farmers (SRHSF) who are engaged-or will engage-in production activities involving the use of hybrid seeds and modern technologies and other livelihood projects. The loan covers production inputs such as hybrid seeds, agro-chemicals and fertilisers, integrated farm production activities and/or livelihood projects (at least 25% agri-related) of self-reliant hybrid seed farmers. The maximum loanable amount is up to 80% of the total project cost but not to exceed

P50,000 per borrower. The interest rate is 14 percent per annum based on the principal amount of the loan plus a service fee of three percent.

As explained by the District Supervisor, the Quedancor promotes the programme through actual visitation, the conducting of orientation seminars, and distribution of information materials in the community. The orientation seminar covers the programme overview, entrepreneurial skills training, and values formation. The farmers will be encouraged to form a group as SRHSF. The SRHSF is a group of three to fifteen accredited *palay* farmers living in the same barangay for at least one year and voluntarily forming themselves into a group primarily to participate in the financing programme. They will elect a team leader from among themselves who will collect and remit the group's loan amortisation to Quedancor.

The loan application is made through the group. The requirements of the borrowers are as follows: they must have resided in the barangay for at least one year; be between 18 to 65 years old; have barangay clearance; have experience/knowledge and be willing to undergo training on the project; and open a cheque account. The loan is payable either monthly, quarterly, semi-annually or annually depending on the cash-flow of the project as determined by the Credit Assessment Group of Quedancor.

A background and credit investigation is conducted by Quedancor before loan approval to ascertain the character of prospective borrowers and assess their capacity to repay the loans. According also to the District Supervisor, it was apparent that only very few constituents in New Corella attend the seminars about the programme; thus actual visits were undertaken to promote the programme.

From the interviews with the 45 farmer-respondents in the research area, not one had borrowed from the programme of Quedancor. Likewise, based on the interview with the District Supervisor of Quedancor in Davao del Norte, it was confirmed that no borrowers were from the barangays chosen as research areas. On the other hand, for those barangays in New Corella with farmer-borrowers in their financing programme, they said that only about 10 percent are repaying because the borrowers perceive that if it is a government programme, the financing programme is considered a dole out. The district supervisor also said that it is a common attitude of the farmer-borrowers to not repay loans from government credit programmes, which really caused the problems of the sustainability of the government credit programmes.

Only three different providers of formal credit exist at present in New Corella, as confirmed from interviews with the key informants from the respective credit providers. Other credit providers mentioned by the farmers no longer exist but evolved from the responses of the farmer-respondents to the question about where they have obtained credit for the past five years. The intention in discussing the various processes in obtaining loans from the existing credit providers in the research area was to determine how these can be accessed by the farmers and how these processes affect their credit preferences and choices in the research area. In addition to the above three credit providers, farmer-respondents also indicated that they have borrowed from the National Irrigators Association (NIA) credit group and New Corella Federation of Agrarian Reform Beneficiaries (NECOFARBIA) credit cooperative in the last five years. However, these providers no longer offer credit services in the municipality.

4.3.4 Informal Credit Sources

According to the farmer-respondents, their informal sources of credit include rice traders, copra buyers, private moneylenders, landowners, neighbours, friends, and relatives.

Among the 45 farmer-respondents, 19 farmers obtained credit mainly from informal sources: 13 from rice traders, two from private moneylenders, two from neighbours, friends and relatives, one from the landowner, and one from the copra buyer. A further nine farmers borrowed from both formal and informal sources. For borrowers who obtained credit from both formal and informal sources, the informal source is mainly the rice traders. Thus, the rice traders seem to be the most accessed informal source for credit by the farmer-borrowers in the research area.

A majority of the farmer-respondents who obtain credit from informal sources are share tenants. About half of the 28 farmer-borrowers who access informal sources of credit, including those who use both formal and informal sources, are share tenants solely, eight are owner-cultivators, and six are both owner-cultivators and share tenants. The interest rates charged by the informal lenders vary, ranging from 2% to 10% per month. The rice traders charge interest rates ranging from 5% to 10% per month. The copra buyer charges the lowest interest rate of 2% per month. Only one respondent, with coconut as the main crop borrowed from a copra buyer. He said that his reason for borrowing from the copra buyer is that it is easy to get cash, and he provides a sure market for his produce. Two farmer-respondents said that they borrowed from neighbours, friends, and relatives who can easily give loans with an agreement of that, for every 1,000 pesos borrowed, one sack of *palay* will be given as interest during harvesting time.

4.3.5 Discussion of Credit Availability in New Corella

From what has been described previously concerning the mechanisms of loan application from the three available formal credit services in the research area, it can be noted that one reason for not getting the loan from the formal credit services is the collateral requirement. About 58% of the farmer-respondents are owner-cultivators but still most of the farmers do not borrow from the bank even if they have land titles that can be used as collateral, as the results revealed that only 6 farmer-respondents borrowed from the Rural Bank of New Corella, approximately 13% of the respondents. This can be explained by the fact that they do not access credit that requires collateral.

Also, the farmer-borrowers do not borrow even if there is no collateral required because of the many requirements in the loan application that the farmers have difficulty in meeting and the amount which can be lent is limited. This has been reflected in the result that only 6 farmer-respondents borrowed from the New

Corella Rural Bank even though the bank has offered a *without collateral* credit scheme because there are lots of requirements to fulfil such as residence certificate, barangay clearance, ID pictures, and certification from the barangay head of having at least a hectare agricultural area. Fulfilling the application requirements of the bank is a tedious process and time consuming for the farmer-borrowers who find themselves always busy on the farm.

Likewise, for the LGU Financing Programme, even if it does not require collateral and has no interest but only a service fee, some farmer-borrowers are not served by this financing programme in the community because it is limited only to rice farmers and has limited funds. This credit service condition illustrates that accessibility is a problem for the borrowers because the implementation is limited to a specific commodity and only limited funds are available.

The farmer-borrowers also wanted immediately to get cash on hand which they could not get from the formal credit providers, since once the loan is approved the release of money is delayed and it is in the form of a cheque that needs to be changed to cash. It is evident from this finding that prompt loan release is also an important consideration of the farmer-borrowers in getting a loan. This can also be attributed as a reason for their borrowing from the informal lenders.

Replies to questions about access to credit in the research areas revealed that despite the high interest rates of borrowing from informal lenders, the farmer-borrowers still obtain credit to these informal lenders with 42% from the farmer-respondents borrowing from them. The farmer-borrowers using informal sources identified some reasons for not borrowing from the existing formal credit services in the research area. One reason is the status of farm tenure which is affecting their access to credit. The farmer-borrowers who are share tenants do not borrow from the bank because they do not have collateral.

It is evident in the results that 14 respondents are share tenants who replied with the same reason-no collateral. Other reasons for borrowing from informal sources are the easy access to cash of any amount and at any time they need it, and the fact that there are no requirements which must be met before they can obtain loans.

The farmer-borrowers who are owner-cultivators borrowed from informal sources because of not wanting to put up their land titles as collateral. They are afraid that the land title will be taken if they cannot immediately repay the loan, fearing that if payment is in default, the land title given as collateral will be foreclosed (see Figure 4). This finding is reflected by the eight owner-cultivators who borrowed from the informal sources, six of them do not want to give their land titles as collateral.

Another finding is that some farmer-borrowers do not want to lose their land titles because they inherited their lands from their parents. They valued their lands so much because the land is their means of livelihood. This could be reflective of Filipino custom, where inherited lands from parents are treasured possessions of the children who inherited them.

Some farmer-borrowers who opted to borrow from informal sources are afraid to borrow from formal sources because of the many requirements with which they must comply, so that they find the procedure of borrowing difficult to understand because they are less educated. As reflected in the characteristics of the farmer-respondents in the research area regarding educational attainment, about 38 percent of the farmer-respondents attained only primary level which showed that most farmers are less educated.

The access of the farmer-respondents to credit is limited by the available credit services that they have in the area wherein their preferences are not served. The availability of credit plays an important role in allowing rural households to finance the purchase of inputs and adoption of modern technology; this requires that credit be available (Sohail Jehangir & Hina, 1999). Credit is an important element in agricultural production systems which allow the farmers to satisfy their cash needs for farm production activities, such as land preparation, planting, and cultivation. The implications of credit availability allow for both greater consumption and greater purchase of production inputs, thus increasing the welfare of the farmers (Feder *et al.*, 1990; Mishra, 1994). Almost every major programme aimed at poverty alleviation or growth of agriculture relied on availability of credit (Gupta, 1991). For instance in India, the private money lenders continue to occupy a dominant place in the rural credit system due to the non-availability of institutional credit for consumption needs and because of easier accessibility to private money lenders (Partap, 1988).

4.4 Awareness of Credit Services in New Corella

The farmer-respondents were asked if they were aware of the available credit services in their community. Among the 45 farmer-respondents, only two were not aware. They said that they were not aware because they do not attend barangay meetings and they are not interested in knowing about the credit services in the community. One of the respondents further elaborated that he is already old and less educated so he is content to borrow from the rice traders. He is a share tenant and has no collateral to give so he did not explore the possibilities of borrowing from formal sources. For those farmer-respondents who are aware, some of them attended the barangay meetings and heard from neighbours and friends about available credit services.

In the research area, the available credit providers were made known to the farmer respondents through information dissemination and meetings conducted by local government, seminars conducted by credit providers, barangay meetings, neighbours and friends. However, even if these efforts were being undertaken to inform the farmers, but based on the results of the interview, only very few farmers in New Corella attend the credit programmes' seminars and meetings. The key informants who were interviewed said that some of the small farmers are not interested in attending such activities as reflected in the attendance at the seminars and actual visits they conducted.

The awareness of credit services is relatively important for credit accessibility in a certain community. Provision and strengthening of awareness about various credit services influenced the farmers in their credit access (Singh, 2001). This can be attributed to the fact that the farmers can not readily obtain credit if they are not aware of the available credit services in the community. The results revealed that there were two farmer-respondents who are not aware because they do not want to attend-or they are not interested in attending-meetings, so they are just contented borrowing from informal sources. This result is similar to that from a study in India in which lack of awareness (the proportion of households without literate members) significantly influenced the dependency of rural households on informal credit and the extent of tied-up credit (Satyasai & Viswanathan, 2003).

4.5 Uses of Credit

The responses of the farmer-respondents to the question on the reasons for their borrowing include: for planting, purchase of production inputs, land preparation, purchase of tractor, and for personal uses like medical care during illness, and school enrolment.

Most of the farmer-respondents borrow for farm production activities, usually during the planting period. About 30 farmer-respondents borrowed for planting purposes and ten farmer-respondents borrowed for land preparation. They said they usually borrow to pay for the farm labour and for planting purposes. Likewise, the farmers borrow more essentially for the purchase of production inputs such as seeds, fertilisers, and chemicals. Approximately, 17 farmer-respondents borrowed for the purchase of production inputs. However, some borrowers also use their loans or portions of them for personal purposes. There were two respondents who borrowed funds to be used as initial capital for their small *sari-sari* (variety) stores. Payment of children's school fees is the most common reason that loans were obtained for personal purposes; there were five farmer-respondents who borrowed for school enrolment. Only two respondents identified that they borrowed for medical reasons, and only one for the purchase of a tractor, and one for a motorcycle.

Since rice is the main crop in the research area and it is the staple food item for more than 90% of all Philippine households (Tolentino *et al.*, 2001), it can be seen that credit is an important element in agricultural production systems, thus most of the farmer-borrowers in the research area are obtaining credit to finance production activities, specifically rice production. A study confirmed that the implementation of rural credit use enables the households to purchase inputs and adopt modern technology thereby increasing productivity and enhancing the welfare of the households (Sohail Jehangir & Hina, 1999).

4.6 Sources of Credit Preferred by Small Farmers

Most of the farmers in the research area obtained their credit from the informal moneylenders. About 42 percent of the respondents borrow from the informal lenders (Table 5), who consist of rice traders, private moneylenders, landowners, neighbours, relatives, and friends. On the other hand, approximately 27 percent of the farmer-respondents borrow from formal creditors and about 20 percent borrow from both formal and informal creditors. However, a proportion of 11 percent of the 45 respondents do not borrow from either formal or informal lenders and are classified as non-borrowers (Table 5).

Table 5. *Incidence of Borrowing*

Name of Barangay	Formal Borrower	Informal Borrower	Both Formal & Informal	Non-Borrower	Total
Mesaoy	7	4	2	2	15
Del Pilar	3	8	3	1	15
New Cortez	2	7	4	2	15
Total	**12**	**19**	**9**	**5**	**45**

The findings show that the informal creditors are the preferred financing sources of farmers in the research area. As presented in the previous discussion of the informal credit sources, 19 farmers obtained credit mainly from informal sources and rice traders are the most often accessed informal source with 13 respondents having borrowed from rice traders among the 19 informal borrowers.

Some distinct responses from farmer-respondents who preferred to borrow from informal sources are as follows: One respondent said that he wanted to borrow from one creditor only because he said that he is a *suki*[7] (regular customer). Another respondent replied that he does not want to go somewhere far from his place. Five farmer-respondents do not want to obtain credit for various reasons: one sets aside money to finance the next cropping season and one is afraid to borrow because he said that he might be imprisoned once he can not pay back his loan. Others did not apply for credit because they have other sources of income such as remittances from abroad, income from a small business like a sari-sari store, and income from teaching. One respondent has a unique response that he does not want to borrow from formal lenders, especially the bank, because he said that he does not want to spend money for a ride into town to apply for credit. This respondent is from barangay New Cortez, an upland barangay and the mode of transportation in going to the town is by a motorcycle. According to him, the application will just incur costly expenses in going back and forth to comply with the requirements, but the loan application approval is not certain.

However, upon asking them about which available formal loan sources in the community they preferred, most replied they prefer the LGU Financing Programme. As presented in the previous section regarding the features of the different existing formal credit services, the LGU Financing Programme does not require collateral. This showed that the respondents really wanted to borrow from lenders not requiring collateral. On the other hand, one farmer-respondent expressed the view that he borrowed from the bank because of knowing somebody who facilitated the loan.

The findings showed that informal credit still remains an important source of finance for rural households in the research area as in developing countries (Eboh *et al.*, 1991). This can be revealed by the strong points that characterise informal credit which include: easy and quick credit availability, no requirements or collateral which is a common characteristic of informal credit, and personal relationship as a fundamental basis between the borrower and lender. The *suki*

[7] The "suki" system is prevalent among traders in the Philippines. This system evolves from the close relationship between lenders and borrowers (Santos, T. & Guce, G. (2001*). The Best Practices of Informal Lenders in the Philippines*. Department of Agriculture - Agricultural Credit Policy Council, Pasig City, Philippines.

system is prevalent in the Philippines which evolves from the close relationship between lenders and borrowers and enable farmers to establish credibility with the lenders resulting in the facilitation of credit transactions (Santos & Guce, 2001).

4.7 Factors Considered in Choosing Creditors by Small Farmers

The responses from the 15 in-depth interviews with farmer-respondents evolved from the question of which factors in obtaining loans they consider in choosing their creditors. Most of the farmer-respondents choose a creditor based on accessibility. Among the 15 farmer-respondents, 12 respondents replied that they choose preferably based on accessibility. The “access” considerations include that they can easily get cash of any amount, with no collateral requirements, and near to their residence. If there are minimal requirements, fast processing of documents is what they want. Two farmer-respondents considered the distance from their residence in their borrowing decisions.

Also, there were some unique answers from other respondents. Two respondents replied that they wanted to be closely supervised and followed up by their lenders so that they can always be reminded of their loans. Some farmer-respondents also mentioned other factors that were considered by them in choosing their creditors. Two farmer-respondents prefer to borrow from creditors that offer a small portion of the interest from their loans as their saving. One farmer-respondent prefers to borrow from lenders who offer production inputs to be loaned, hence production inputs instead of cash will prevent them from spending the cash for personal uses.

The findings showed that the factors considered by farmer borrowers in choosing their creditors are directly related to their preferences in borrowing as they really wanted to get cash easily and loans with no collateral which led them to borrow from informal sources. Based on the study conducted by the Agricultural Credit Policy Council in 2000, the farmers borrow from the informal lenders because of the fast and timely release of loans, non-requirement of collateral, and accessibility which, to some extent, is consistent with the results of this research (Santos & Guce, 2001).

4.8 Problems/Difficulties Encountered by Small Farmers in Obtaining Credit

Farmers were asked to describe any problems or difficulties they encountered in obtaining loans. Out of the 12 farmer-respondents who borrowed from formal sources, 11 of them said that there are lots of documents to complete during the application. They find the preparation of requirements tedious. All of them also expressed the view that obtaining a loan from the bank is a long process and, further, once the loan is approved, the release of money is delayed and it is in the form of a cheque that needs to be changed to cash. Likewise, about 17 farmer-respondents replied that for the less educated, the tendency is to shy away from applying because they said they can hardly understand the procedure. The credit-related problems reported in this research are consistent with the problems found in the study by Octavio and Aragon (1986) that affect the profitability of small farming operations in the Philippines, which include non-versatility of formal loans, mono-crop specific credit, late release of loans, lack of farmers' participation in planning agricultural credit programmes, and lack of education of small farmers.

For those farmers who are share tenants, which is about half of the 28 farmer-borrowers who obtain credit from informal sources, they said that they cannot obtain a loan if collateral is required because they do not own assets for collateral. The assets for collateral that most farmer-respondents have in the study area are as follows: agricultural land they are tilling; motorcycle used as mode of transportation in the area and as source of income; and tractors and threshers.

The 13 farmer-respondents who obtain credit from the rice traders, said that it is difficult for them to look for better prices for their produce. They said that they are already tied up with the rice traders who usually buy their produce and dictate the buying price, which is lower than the normal market price.

Three farmer-respondents were able to obtain loans but their crops were stricken by natural calamities, so they were not able to obtain credit again because they had failed to repay the previous loans. Others have low production because their farms are not irrigated. Consequently, farms stricken by natural calamities and lack of irrigation have been the experience of the majority of farmers with default on loan payment because of poor harvests, thus affecting their credit accessibility which caused them not to repay the loans and not being able to borrow again (ACPC, 2001).

4.9 Suggestions by Small Farmers to Improve their Credit Accessibility

Various responses were gathered from the in-depth interviews with 15 farmer-respondents who were asked what they could suggest to improve their credit accessibility. Five farmer-respondents suggested that the government should provide more credit programmes in the area. As presented in the previous results, there are only two existing government credit services in the research area, the LGU Financing Programme and the Quedancor's Unlad Ani (Improved Harvest) for Income Augmentation and Livelihood for the Self-Reliant Farmers. The Rural Bank of New Corella is not owned by the government.

One respondent recommended that there should be credit offered for livelihood assistance like livestock and poultry production. This can be attributed to the fact that the government credit programmes being offered in the research area, both from the LGU Financing Programme and Quedancor, are limited to farm production, and there are none for livelihood assistance. The credit offerings of the three existing credit services are for crop production specifically for palay farmers. Two respondents recommended that a farmers' association should be organised in their area so that if there are government credit programmes, information about them can easily be passed through the farmers who are members of the association. Also, the participation of the farmers is encouraged through the association. The farmers' association as suggested by the farmers is relative to the group mechanism, an element of the Grameen Bank of Bangladesh which is a successful credit provider whose loans are given to borrowing groups that assume joint responsibility for repayments (Jain & Moore, 2003; Llanto, 2005). As mentioned also by them, farmers' participation is encouraged by creating an association, this holds true with the success of the Grameen Bank approach as its second element is that involvement of borrowers in both operational and policy decisions constitute strong participatory elements in the management of credit (Stiglitz, 1990).

Another suggestion from four farmer-respondents was to provide training for them in obtaining loans because they said most of the farmers are less educated so the tendency is to shy away from applying since it is difficult for them to understand the procedure. They said that meetings and seminars are conducted by the government credit programmes like the LGU Financing Programme and Quedancor but they did not reach to far *sitios* of the barangay so not everyone can attend. These respondents are from barangay New Cortez which is an upland area. One respondent said that the information dissemination about the programmes should be intensive and not selective. He further elaborated that like the LGU Financing Programme, the agricultural technician is the one who will choose the farmers who will participate in the seminar so the borrowers are chosen only from the attendees.

Likewise, two respondents suggested that it is better to educate them about savings mobilisation because they said that they prefer that kind of credit scheme in the area in which they can save and just borrow from the group the amount of money they have put in. The suggestion of savings mobilisation as a kind of credit scheme is a good solution in improving the accessibility to credit by farmers, this kind of credit has been arranged in India through one of its successful projects, the Maharashtra Rural Credit Project, which improved the economic status of the households by providing an easy and periodic availability of credit due to rotation of savings (Madheswaran & Amita, 2001).

4.10 Summary

In this chapter the characteristics of farmers have been described. The accessibility and use of credit in the municipality of New Corella has been outlined and the reasons for the choices and preferences that the small farmers made have been described. Rice farming is the main source of income in the municipality. At present, only three different providers of formal credit exist in New Corella. The various processes in obtaining loans of the three credit providers and how these processes affect the credit preferences and choices of farmers have been diagrammed and discussed. For the past five years, the farmers have obtained formal credit from the New Corella Rural Bank and the LGU Financing Programme. Most of the farmers borrowed from the informal credit sources, and rice traders are the most accessed informal source for credit. Most of the farmers borrow for farm production activities, usually during the planting period. The majority of the farmers who obtain credit from informal sources are share tenants. Farmers do not necessarily access credit if collateral is required and prompt loan release is an important consideration for them. Awareness of the credit programmes is not given importance by the farmers, therefore they tend not to attend seminars and meetings conducted by credit providers. Organising a farmers' association is suggested by the farmers so information about government credit programmes can easily be passed through the association and generate easy access for the members.

In the next chapter the research is summarised, conclusions are drawn and recommendations for further research are presented.

CHAPTER 5: **SUMMARY, CONCLUSIONS AND RECOMMENDATIONS**

5.1 Summary and Conclusions

The performance of the agricultural sector is important in the Philippine food security and poverty alleviation efforts since 60% of the country's population is rural and two-thirds depend on farming for their livelihood. The Philippines has a diverse climate where different crops are produced in different areas, but productivity is limited by-among other things-lack of access to credit, particularly for small farmers. Agricultural credit plays an important role in agricultural development and it is believed that expansion of credit programmes will have beneficial effects on the agricultural production and incomes of small farmers. It is also a key to poverty alleviation, livelihood diversification, and increasing the business skills of small farmers. There is a need to examine further small farmers' access to credit and investigate their preferences and perceptions regarding credit in order that their access can be improved and their needs for credit can be more effectively met.

In this research an attempt has been made to explore and understand the perceptions of small farmers concerning rural credit, and to collect information in proposing an appropriate credit system for them. Knowledge of the perceptions of the small farmers regarding credit will assist policy makers to make better decisions on appropriate credit programmes for them. Given the limited empirical studies that have been done on understanding farmers' perceptions and expectations regarding credit access, this research will fill part of the void and add to the literature. Because of the limited time allotted for the fieldwork and the small sample size, the research reflects only the experiences of farmers in the study area chosen. This may vary from those of other communities in the region and in other parts of the country.

Accessibility of rural credit in the Philippines was examined, with the primary objective of exploring the use of, and access to, rural credit by small farmers in

Davao del Norte province. The researcher also wanted to explore and examine the reasons for the choices they made and the preferences they had with regard to credit. The availability of credit in the municipality was also examined. The problems encountered in obtaining loans and the suggestions to improve credit accessibility of small farmers were also determined.

Three barangays or villages from the municipality of New Corella were selected for the research. Semi-structured interviews were undertaken with 45 farmer-respondents from the three barangays to gather information about the socio-economic characteristics of small farmers and their access to credit in the research area. In-depth interviews were undertaken with 15 farmers to elicit additional information on their preferences, awareness of credit schemes, reasons for borrowing, problems encountered in obtaining credit, and their suggestions for improving access to credit. Simultaneously, key informant interviews were conducted with a municipal government official, a municipal agricultural officer, a rural bank loans officer, and a government programme implementer to gather information on the availability-of and the processes involved in-obtaining credit in the research area. The data collected from questionnaires were edited and translated where necessary to English before they were tabulated, coded, and described. Data analysis involved repeated iterations before comprehensive analysis with generalisations was made.

5.1.1 Key Informant Interviews

Four key informants were interviewed regarding the availability of credit services in the research area and the processes involved in obtaining the credit. The formal credit sources currently available include the Rural Bank of New Corella, the Local Government Unit (LGU) Financing Programme, and Quedancor's Unlad-Ani (improved harvest) for Income Augmentation and Livelihood for the Self-Reliant Farmers participating in the Hybrid Rice Cultivation Project (UNLAD-ANI-IAL-SRF-HRCP). The New Corella Rural Bank offers agricultural loans to the farmers in the municipality with 14% per annum interest rates. Two schemes of agricultural loans are available for the farmers, *with collateral* and *without collateral* credit schemes. The amount that can be loaned is P12,000 per hectare under the with-collateral scheme. The Rural Bank offers loans for both individuals and groups, like cooperatives.

The Local Government Unit (LGU) Financing Programme was implemented as an initiative of the municipal government of New Corella to help the small rice farmers in the community who lack capital in their farms and it is one of the poverty alleviation programmes in the municipality. The financing programme is allocated from the 20% of the development fund of the municipality every year. The financing programme provides a production loan for rice farmers amounting to P7,000 per hectare with a 2.5% service fee and is payable for six months. There is no collateral required for the loan. The farmer-recipients were selected by the agricultural technicians after attending a seminar about the financing programme. A memorandum of agreement was instituted between the municipal government and the approved recipients. The recipients provided the labour for land preparation and crop maintenance, and adopted the appropriate package of technologies recommended by the agricultural technicians. The LGU Financing Programme has been in operation for seven years and the repayment performance is 88%.

Another government credit programme is offered in the municipality by Quedan and Rural Credit Guarantee Corporation (Quedancor), an attached government corporation of the Department of Agriculture. It is an innovative financing scheme referred to as the Self-Reliant Team (SRT) Model for the marginalised group of the community. The credit scheme is called Unlad-Ani (improved harvest) for Income Augmentation and Livelihood for the Self-Reliant Farmers participating in the Hybrid Rice Cultivation Project (UNLAD-ANI-IAL-SRF-HRCP). This is a package of collateral free loans for *palay* (rice) farmers who want to utilise hybrid seeds and modern technologies in undertaking farm activities to increase yields and income. The Quedancor provides finance for the working capital or production requirements of Self-Reliant Hybrid Seed Farmers (SRHSF). The SRHSF is a group of three to fifteen accredited *palay* farmers living in the same barangay for at least one year and voluntarily forming themselves into a group primarily to participate in the financing programme, the formation of the group being encouraged by Quedancor. The production loan covers production inputs such as hybrid seeds, agro-chemicals and fertilisers, integrated farm production activities and/or livelihood projects (at least 25% agri-related) and the application is made through a group. The maximum loanable amount is up to 80% of the total project cost but not to exceed P50,000 per borrower with 14% interest per annum plus 3% service fee. The loan is payable either monthly, quarterly, semi-annually or annually. The financing programme is promoted through actual visitation, the conducting of conduct of orientation seminars, and distribution of information materials in the community.

At present, only three different providers of formal credit exist in New Corella. The various processes in obtaining loans from the three credit providers affect the credit preferences and choices of farmers in the research area.

5.1.2 Interviews with Farmers

A total of 45 farmers were interviewed, 15 from each barangay. Rice farming is the main source of income in the municipality, with bananas and coconuts as the second and third crops, respectively, produced by the farmers. Most of the farmers have been farming for 10 to 25 years, but among the 45 respondents, two years is the shortest time of farming while 30 years is the longest. About 58 percent of the farmers are owner-cultivators and 24 percent are share tenants. The farm size of the farmers ranges from 0.5 hectares to 8 hectares. The non-farm and off-farm sources of income for the farmers include carpentry, motorcycle driving, teaching, fish vending, rice trading, small *sari-sari* (variety) stores, and government employment.

For the past five years, the farmers in the research area have obtained credit from two of the three existing formal credit sources in the municipality, the Rural Bank of New Corella and the LGU Financing Programme. No one had borrowed from the Quedancor's credit programme. Among the 45 farmer-respondents, only six farmers have borrowed from the New Corella Rural Bank. These farmer-borrowers are all owner-cultivators and own more than one hectare of land. The farm size ranges from 1.5 hectares to 7 hectares and rice is the main crop they are farming. They all have been farming for quite some time as their means of livelihood, ranging from 15 to 30 years. The loans they obtained were used for land preparation, purchase of production inputs, purchase of tractor, and as initial capital for a *sari-sari* store.

Fourteen farmers have borrowed from the LGU Financing Programme, all rice farmers. Most of them are owner-cultivators, with farm size ranging from 0.5 to 5 hectares, and they had been farming for 2 to 30 years. Their ages range from 33 to 62 years old and they had attained various levels of education. The main reason for borrowing is for the purchase of production inputs.

Most of the farmer-respondents borrowed from informal credit sources, which include rice traders, copra buyers, private moneylenders, landowners, neighbours, friends, and relatives. The rice traders are the most often accessed informal source for credit by the farmer borrowers in the research area. The majority of the farmer-respondents who obtain credit from informal sources are share tenants. The interest rates charged by the informal lenders vary, ranging from 2 to 10% per month. But, for rice traders the interest rates range from 5 to 10% per month. The copra buyer charges the lowest interest rate of 2% per month.

A collateral requirement appeared to restrict farmers' access to credit. About 58% of the farmer-respondents are owner-cultivators, but still they choose not to borrow from the bank even if they have land titles for collateral. Other farmer-respondents who are share tenants choose not borrow from the bank because they do not have assets for collateral. They also often choose not to obtain credit even if collateral is not required because of the number of other requirements they must fulfil. Fulfilling the application requirements is a tedious process and time consuming for the farmers-borrowers who find themselves busy on the farm. Other farmer-respondents who are less educated are afraid to borrow from the bank because they find the procedure of borrowing difficult to understand. Farmer-borrowers also wanted to obtain cash on hand immediately-rather than a cheque-which the informal credit sources can accommodate.

Questions about access to credit in the research area revealed that despite the high interest rates of borrowing from informal lenders, the farmer borrowers still obtain credit from them, with 42 percent from the farmer-respondents having borrowed from informal sources. The findings showed that the informal creditors are the preferred financing sources of farmers in the research area. The reasons for borrowing from them include easy and quick credit availability, no requirements and collateral, and proximity to their residence. One characteristic also that enticed the farmer-borrowers to borrow from informal lenders is the *suki* (regular customer) system, which establishes a close relationship between lenders and borrowers and facilitates credit transactions.

The available government credit programmes in the research area, LGU Financing Programme and Quedancor's financing scheme, were known to the farmer-respondents through information dissemination and meetings conducted by local government, seminars conducted by credit providers, barangay meetings, and through neighbours and friends. However, even with these efforts, very few attended the credit programmes' seminars and meetings. Awareness of the credit programmes was not given a high importance by the farmer-respondents, most of whom were aware but chose not to attend seminars and meetings. Two respondents were completely unaware because they are not interested in attending meetings, being content to borrow from informal sources. This particular attitude of the farmers is difficult to manage for those promoting formal credit schemes.

Most of the respondents borrow for farm production activities, usually during the planting period. Likewise, the farmers borrow more essentially for the purchase of production inputs such as seeds, fertilisers, and chemicals. Some borrowers use their loans, or portions of them, for personal purposes, of which payment of children's school fees is the most common followed by medical purposes and purchase of tractors and motorcycles.

In choosing their creditors, the farmer-respondents valued accessibility. The access considerations include their ability to easily get cash of any amount, with no collateral requirements, and nearby to their residence. If there are minimal requirements, fast processing of documents is what they want.

The farmer-respondents suggested some measures to improve their credit accessibility. One suggestion is that the government should provide more credit programmes in the area which are not commodity specific, and credit programmes with enough funds. Another suggestion is a credit offering for livelihood assistance. The credit offerings of the three existing credit services are for crop production, specifically for rice farmers. Organising a farmers' association in the research area is also suggested by the farmer-respondents so government credit programmes can easily be passed through the association and generate easy access for the members. Through the association, participation of farmers is also encouraged. The farmer-respondents also suggested that training in obtaining loans should be provided to everyone, not selectively, that education about savings mobilisation should be provided because they wanted to have a credit scheme in which they can save and then borrow from the group the amount of money they have put in. This kind of scheme will provide easy and periodic availability of credit due to rotation of savings.

The findings of this research show that the access to credit by farmers was limited to the available credit services in the research area, thus farmers' choices and preferences were not well served. As it was found out from the existing LGU Financing Programme, even if it does not require collateral it is restricted to rice farmers only and has limited funds. Therefore, credit restrictions such as commodity-specific credit programmes, credit that requires collateral, and lengthy and complicated procedures prevent the farmers from accessing formal credit.

Knowledge of the credit preferences of small farmers gives opportunity for the financial institutions to offer a wider scope of loan purposes or multiple credit services to the small farmers in the area. In this case, the farmers will be encouraged to use formal credit and decrease their reliance of borrowing from informal lenders, thus avoiding higher interest rates and thereby increasing their farm productivity and household incomes.

5.2 Recommendations

Given the limited government credit programmes in the area, accessibility to credit by small farmers could be improved by providing innovative credit schemes that address problems of small farmers who lack collateral, and by minimising long processing times and other requirements. Also, farmer access to credit could be improved by eliminating the specific commodity requirements for credit.

Policy measures for improving access to credit should be developed based on farmers' preferences and needs. Institution capacity building for both lenders and borrowers should be an integral part of every credit programme that will be provided in order to increase agricultural productivity and the income of farmers.

The government may need to consider conducting an information drive aimed at promoting credit awareness and the establishment of strong and viable farmer organisations (such as cooperatives or credit associations) which can play a major role in increasing small farmers' access to credit. In line with this, savings mobilisation programmes should be developed and promoted in the area, which will encourage participation and provide incentives for farmers to save and recycle their funds. Each member is able to monitor directly and have a say in the use of the funds. Activities of credit organisations rooted in the autonomy of the farmers can be a powerful tool in the improvement of their credit accessibility.

5.3 Suggestion for Further Research

The study of the socio-economic environment and the credit perceptions and preferences of small farmers will assist policy makers to make better decisions on appropriate credit systems for them. In order to have an effective policy, broader research, understanding of-and action to support-rural development through more effective and affordable financial flows are needed.

The presence of appropriate credit programmes in the rural areas designed based on the farmers' preferences is important since credit is an essential element in increasing their agricultural production and incomes, livelihood diversification, and increasing business skills. Also, access to appropriate credit programmes that are responsive to farmers' preferences will discourage farmers from continuously borrowing through informal credit sources.

The research was limited by time and resource constraints and the researcher would like to suggest that a further detailed study on the exploration of small farmers' credit perceptions and preferences at the regional or possibly national level be undertaken. This research covered only one municipality which may differ from other municipalities in the country. The availability of credit services, credit perceptions and preferences of small farmers may also differ in other municipalities.

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APPENDIX I

INSTITUTE OF NATURAL RESOURCES
MASSEY UNIVERSITY

ACCESSIBILITY OF RURAL CREDIT AMONG SMALL FARMERS IN THE PHILIPPINES

SURVEY QUESTIONNAIRE FOR FARMERS

A. RESPONDENT PROFILE/CHARACTERISTICS

Area or Name of Village: ____________________________________

Sex : Male _____ Female ______________

Age : _____ Civil Status : __________

Highest Educational Attainment:

1) No formal schooling
2) Primary level
3) High School level
4) High School Graduate
5) College Level
6) Vocational
7) Others (specify) _________

Number of Household[8] Members: _____________

Proportions of income from various sources:

1) Farm (specify)

   a. Crops _______________
   b. Livestock ______________
   c. Farm labourer

[8] Includes helpers (*katulong*) or other non-relatives who share a common arrangement in the preparation and consumption of food.

2) Non-Farm

<u>Income from other agricultural activities</u>

a. Rice/corn milling ( )
b. Rental/labor for pre/post harvest facilities ( )
c. Others (please specify)______________

<u>Income from non-agricultural activities</u>

a. Small business (i.e. sari-sari store) ( )
b. Teaching ( )
c. Government employee ( )
d. Private employee ( )
e. Remittances from abroad ( )
f. Others (please specify) ______________

Average Annual Household Income:

a. P 10,000 and below ( )
b. P 10,001 to P25,000 ( )
c. P 25,001 to P50,000 ( )
d. P 50,001 to P100,000 ( )
e. P100,001 and above ( )

Farm Tenurial Status:

a. Owner ( )
b. Share Tenant ( )
c. Lease Holder ( )
d Others (please specify) ____________

Farm Size (in hectares):

a. Less than 0.5 hectare ( )
b. 0.5 ha. – 1.0 ha. ( )
c. More than 1.0 ha. ( )

How many years in farming? ______________________

B. ACCESS TO CREDIT

1. How do you finance your farming? ________________________

2. In what ways have you accessed credit over the past 5 years? (Can be more than one)

   a) friends ( )

   b) relatives ( )

   c) neighbours ( )

   d) banks ( )

   e) moneylenders ( )

   f) others (please specify) _________

3. Why did you prefer these sources? __________________________

4. When did you really need to borrow? ________________________

5. What is the distance of the nearest bank in your area?

   a) 1 – 5 kilometres ( )
   b) 6 – 10 kilometres ( )
   c) 11 – 15 kilometres ( )
   d) 16 – 20 kilometres ( )
   e) More than 20 kilometres ( )
   f) Don’t know ( )

6. What is the name of the bank? ______________________

7. Are you aware of credit programmes/facilities in your place? Do you know how to avail yourself of it?

   a) Yes ____ What are these? _________________________

   How far? _______________________________

   b) No _____

8. Did you apply for credit to finance your farm?

a) Yes ____ What for ________________________________

b) No ____ Why not? ______________________________

a) Had enough savings/earnings from other sources( )
b) Afraid to borrow ( )
c) Interest rates were not affordable ( )
d) Too many required documents to submit ( )
e) Uncertainty about repaying the loan ( )
f) Others (please specify) _________________

9. If you applied for credit, was your application successful?

a) Yes ______ b) No ________

10. What are the reasons that your application was not successful?

a) Insufficient income/assets ( )
b) Incurred previous loan (bad credit) ( )
c) Had no collateral ( )
d) Had difficulty in providing required documents ( )
e) Others (please specify) ____________________

11. Was the amount you got sufficient?

a) Yes ______ b) No _____ Explain _____________________

____

____

12. Do you have collaterable assets?

a) Yes ______ b) No _________

13. If yes, what form of collateral assets do you have?

a) Land (residential and/or agricultural) ( )
b) House ( )
c) Vehicle ( )
d) Agricultural equipment (e.g. tractor, sheller) ( )
e) Furniture and Fixtures ( )
g) Others (please specify) ______________

14. Are there lending organisations in this area other than the one you got the credit from?

a) Yes ______ What are these? ________________________

b) No ______

15. Are you still willing to be visited again if I want to come back to have a further conversation with you? When is a convenient time?

APPENDIX II

INSTITUTE OF NATURAL RESOURCES
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ACCESSIBILITY OF RURAL CREDIT AMONG SMALL FARMERS IN THE PHILIPPINES

GUIDELINE FOR IN-DEPTH INTERVIEWS WITH FARMERS

KEY QUESTIONS:

1. What form of available credit services in your area do you prefer? Why?
____
____
____

2. How did you know about the credit facilities in your area?
____
____
____

3. What are the factors you consider in choosing your creditor?
____
____
____

4. What are the problems or difficulties you encountered when applying for and/or obtaining credit? ____
____
____

5. What are your expectations among those credit programmes in your area? ____
____
____

6. Do you have any suggestions/recommendations in order to improve your accessibility to credit in your area? ____
____
____

APPENDIX III

INSTITUTE OF NATURAL RESOURCES
MASSEY UNIVERSITY

ACCESSIBILITY OF RURAL CREDIT AMONG SMALL FARMERS IN THE PHILIPPINES

GUIDELINE FOR KEY INFORMANTS INTERVIEW

1. What credit services do you offer for small farmers in the municipality? What are the features of the credit services you are offering?
2. Do you promote your credit service to the small farmers? How?
3. What are the requirements for obtaining a loan from the credit you offer small farmers?
4. What is the maximum amount that the farmers can borrow? What rate of interest do you charge? How long do you allow the borrowers to repay the loans?
5. How do you collect the payments from the loans?
6. How long have you been offering credit to farmers?