



ACPC Monitor

A series of policy updates by the Agricultural Credit Policy Council



Department of Agriculture



Issue No. 5 Series of 2001 August 16, 2001

ACPC A Catalyst in Rural Finance Policy Reforms

The creation of the Agricultural Credit Policy Council (ACPC) in 1986 heralded government's commitment to map out serious strategies for addressing the issue of sustaining credit access for small farmers and fisherfolk in connection with the state's mission of rural development and poverty alleviation.

Composed of cabinet-rank policy makers, with the Secretary of the Department of Agriculture (DA) as Chair, the Governor of the Bangko Sentral ng Pilipinas (BSP) as Vice Chair, and the Secretaries of the Department of Finance (DOF), Department of Budget and Management (DBM), and the National Economic Development Authority (NEDA) as members, the Council – through the help of a technical secretariat and the involvement of various visiting experts – has been, and continues to be, instrumental in identifying necessary rural finance policy reforms and programs that would spur increased rural/agricultural investments.

Consequently, the ACPC has pointed to four main factors that influence the lethargic flow of credit to agriculture and fisheries, namely: (a) the much greater demand for credit in the sector vis-à-vis available government resources; (b) the non-bankability of most small farmers and fisherfolk; (c) the inadequacy or even inappropriateness of the existing credit delivery system to small farmers and fisherfolk; and (d) the high cost involved in lending to agricultural projects. The agency's accomplishments over the years, therefore, are all consistent with its overall plan of action and advocacy aimed at addressing these factors:

A. Rationalization of government intervention

- Since the 60s, the involvement of government in rural finance has mainly been characterized by the provision of subsidies and the implementation of directed credit programs (DCPs). However, various investigations/ evaluations conducted by ACPC on these forms of intervention have generally shown them to be ineffective and unsustainable while at the same time discouraging self-sustainability in banks. As a result, sustaining the interventions have only further constrained the availability of credit funds and passed on the burden of maintaining its supply almost entirely to government, which by itself is not capable of producing the total credit needs of the agriculture sector.

- In view of this, the ACPC has been advocating greater private sector participation in rural finance and the rationalization of the state's involvement in the same. For one, the ACPC has spearheaded since 1987 the consolidation of all agriculture and agriculture-related credit programs into the *Comprehensive Agricultural Loan Fund (CALF)* – an activity provided for in Executive Order 113 of 1986. In so doing, the agency has been instrumental in making the handling of government agri-credit funds more manageable. Moreover, by seeing to it that CALF credit funds are channeled mainly through financial institutions (i.e., government, private, or both), ACPC took the lead in efforts to standardize a system where government credit resources are administered more professionally and financing activities for agriculture are made more sustainable.
- Also to encourage participation by private banks in agricultural lending, ACPC introduced the implementation of market-based loan pricing by allowing CALF interest rates to adjust in accordance with market movements, making the interest that can be charged by participating banks more flexible and reflective of the true state of fund availability in the economy.
- Meanwhile, in regularly monitoring both on-going and proposed agri-credit programs, ACPC has in many instances thwarted attempts to revive old credit strategies, such as suggestions to finance rice and other crop production via credit subsidies. However, by also regularly conducting fieldwork and surveys among stakeholders, the agency strives to ensure that alternative strategies and policies being developed are not only consistent with the prevailing policy environment, but are also “needs-sensitive” and practical/doable.
- In 1997, many of the credit policies advocated by ACPC eventually reached legislation with the passing into law of the Agriculture and Fisheries Modernization Act (AFMA) or Republic Act 8435. Together with the National Credit Council (NCC), ACPC again became instrumental in formulating the design and guidelines of the *Agro-Industry Modernization Credit and Financing Program (AMCFP)* – a program provided for under AFMA. The creation of the AMCFP serves as a second round of consolidation of agricultural DCPs, which covers programs

implemented by both DA and non-DA agencies, including the CALF. Through the design of the AMCFP, the ACPC has helped in institutionalizing among others, the use of market-oriented interest rates and the role of government financial institutions (GFIs), like Land Bank, in wholesaling government lending funds.

- The AFMA also formally incorporated in the implementation of AMCFP the conduct of regular consultations with stakeholders. ACPC is tasked with spearheading these consultations.

B. Reduction of banks' and borrowers' risks

- The studies conducted by ACPC have advocated not only greater agricultural lending among private financial institutions, but also increased loan sourcing by marginal farmers and fisherfolk from formal lenders such as banks and cooperatives to help bridge the information gaps that prevent them from linking with each other. In this regard, ACPC has been a major proponent of government support to incentives for both suppliers and demanders of agri-credit, particularly through the development and/or strengthening of risk-reducing mechanisms.
- ACPC has conducted and/or supported several research works that reviewed government's risk-mitigation schemes for borrowers and lenders, particularly the agri-insurance and credit guarantee programs. In 1999, ACPC collaborated with the Quedan and Rural Credit Guarantee Corporation (Quedancor) and the Guarantee Fund for Small and Medium Enterprises (GFSME) in sponsoring the AFMA-mandated *Review of Agriculture Guarantee Programs and the Design of the Agriculture and Fisheries Credit Guarantee (AFCG) Program*. As in the case of credit funds, the AFCG Program involves the consolidation of all agri-guarantee funds (with which ACPC has already begun to comply as far as the consolidation of CALF's guarantee component is concerned).
- Presently, ACPC is actively campaigning for the implementation of the Review's recommendations, which are aimed at strengthening the agri-credit guarantee system. Among others, these include re-focusing government's role on wholesale instead of retail guarantee.
- The ACPC is also advocating reforms for Quedancor itself and is currently involved in efforts to have the Corporation supervised by the BSP. Moreover, to help the Secretary of Agriculture have more informed policy positions as Chairman of the said Corporation, the ACPC was recently appointed to be a member of the Quedancor Board of Directors.
- One of the biggest factors that enhance the risk of lending to small farmers, though, is the still unfinished implementation of the Comprehensive Agrarian Reform Program (CARP) and the lack of collateral value of agrarian reform lands. ACPC has therefore also supported strategies that would facilitate the implementation of the Program. Among these was the issuance of *Agri-Agra Bonds* to generate funds for CARP.
- Also to lessen agricultural borrowers' risks and encourage them to venture even to longer-term but more profitable commodities,

the ACPC collaborated with the BSP in 1999 on the issuance of *BSP Circular 217*. The Circular serves as the implementing rules for extending the grace period on repaying long-gestating agriculture and fisheries loans. The extension of agricultural loan grace periods is likewise mandated by AFMA. With the issuance of the Circular, the grace period for agriculture loans may now reach a maximum of 7 years in lieu of the previous 3 years.

C. Promote the bankability of farmers/fishermen and agricultural projects

- Aside from reducing risk, making small farmers and fisherfolk more bankable also means making them more profitable. Towards this end, ACPC has consistently argued that government can help make agriculture more profitable and attractive to financial institutions primarily by increasing its expenditures for rural infrastructure, marketing facilities and technical assistance. Among other things, greater access to transport and markets lessen input costs and harvest losses.
- ACPC has also advocated stopping the implementation of commodity-specific programs which only constrain both banks and borrowers to support even unprofitable commodities, and instead to channel more financing support towards non-farm enterprises that generate higher rates of return, contribute to household liquidity and improve creditworthiness of the household. ACPC itself is set to test this approach through one of its action research projects programmed for CY 2001 – *the Rural Household Business Financing (RHBF) Program*.
- Moreover, through the Magna Carta for Small Farmers, ACPC was given the mandate to help build the capacity and viability of both rural financial institutions and farmer/fisherfolk organizations. In line with this, the agency has already implemented, among others, a *Rehabilitation Program for Cooperative Rural Banks (CRBs) and Cooperatives*, which helped strengthen the assisted institutions in managing financial services and products. More recently, ACPC has embarked on the implementation of an *Institution-Building (IB) Program* that also caters to farmers and fisherfolk organizations. Assistance to be provided shall be in terms of training, organizational development and consultancy services to ensure meaningful and effective handling/utilization of credit.

D. Encourage innovations in the financing of projects

- In the interim period of adjustment to market-oriented interventions, strategies also have to be designed to ensure a continuous flow of credit to the countryside. ACPC has been involved in the design and testing of innovative financing schemes that can circumvent inadequacies in market structures and some asymmetric information that characterize the rural sector. Some of the innovative schemes that were already piloted by ACPC are the following:

1. *The Development Assistance Program for Cooperatives and People's Organizations (DAPCOPO)* – A wholesale lending program that catered to mature and viable cooperatives, which in turn re-lent borrowed funds to their farmer/fisherfolk

members. The program also had a savings mobilization component that required forced deposits among cooperative members.

2. *The Integrated Rural Financing (IRF) Program* – A lending-cum-IB assistance approach for rural banks and cooperatives.

3. *The Grameen Bank Replication (GBR) Project* - Patterned after the successful Grameen Bank in Bangladesh, this replication project targeted non-government organizations (NGOs) and CRBs as project implementors and included credit, training, guarantee cover and savings mobilization components, among others.

- Consequently, some government and private lending institutions have successfully adopted, either in part or in whole, technologies that the agency has piloted. The government-controlled People's Credit and Finance Corporation (PFCF) and the private sector-based Center for Agriculture and Rural Development (CARD) Bank, for instance, now utilize the GBR approach, among others.

- Meanwhile, additional schemes programmed for testing in 2001 promote the role of the informal financial markets as well as that of rural non-farm enterprises. These are:

1. *The Rediscounting-cum-Guarantee Program for Uncollateralized Borrowers* – This scheme involves the channeling of loan funds through informal lending agents such as moneylenders, traders, and millers.

2. *The Rural Household Business Financing (RHBF) Program* – Assistance is for other viable small home or rural industries linked to the main livelihood of the community or farm household.

E. Reduction of intermediation costs

- To lower the cost of lending and bring down lending rates, ACPC has been a chief proponent of the abolition of Presidential Decree 717 or the Agri-Agra Loan Quota Law. This position is based on the agency's own observation that instead of being beneficial to agricultural borrowers, the requirement of a quota (i.e., 25% of total loanable funds) for agriculture and agrarian lending has only

pushed up banks' opportunity costs. Eventually, these increased costs are added on to the interest charge and are accordingly passed on to the intended borrowers. Abolishing the loan quota would, therefore, significantly help reduce the burden imposed on borrowers, to benefit especially the smaller clients. Consequently, although the law has not been repealed, additional alternative forms of compliance have nonetheless been allowed by BSP.

- Also aimed at bringing down costs is ACPC's continuing advocacy for increased government spending for the improvement of rural infrastructure and technical assistance. In the same manner that they are helpful to agricultural producers, the continuous development and maintenance of infrastructure and sustained technical assistance to farmers and fisherfolk makes it easier/less costly for lenders to transact with these clientele.

- ACPC's campaign on IB and group organizing, likewise, has a bearing on lowering transaction costs. In particular, because of the principle of economies of scale, a lender's costs are essentially lessened when it caters to a group instead of dealing with several separate individuals.

- Meanwhile, to lessen the cost of funds for financial intermediaries based in the countryside, ACPC continues to endorse the implementation by government of a *National Savings Mobilization Program* through an institution that will be responsible for promoting savings mobilization nationwide. The role of the institution would be to promote savings mobilization among banks and instill savings awareness among rural households. This Program momentarily found support during the Ramos administration. The ACPC is now set to revive its advocacy for a similar program/campaign.

Over the years, therefore, ACPC has seen to the successful implementation of several vital policies and programs that have not only helped small farmers and fisherfolk gain more access to credit, but have also helped make such access more sustainable. Therefore, to the extent that financing remains an essential ingredient in government's long-term goals of agricultural modernization, rural development, food security and poverty alleviation, ACPC continues to play a crucial role in uplifting the country's economy.