



# ACPC Monitor

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## Revisiting the AFMA Chapter on Credit : How Far Have We Gone?

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To date, Republic Act 8435 or the Agriculture and Fisheries Modernization Act (AFMA) is more than three years old. Enacted into law in early 1997, the law's major contribution is the laying down of several reforms aimed at overhauling outdated protectionist policies that over the years have succeeded only in constraining the agriculture sector rather than uplifting it. The AFMA reforms, in other words, attempt to re-highlight the role of market forces in guiding sector players (including government) towards making optimum investment decisions while also prescribing means by which the global competitiveness of local agriculture and fisheries products could be strengthened. In the law, nowhere else are these policy thrusts more clearly demonstrated than in Sections 20-25 – the chapter on Credit.

Among the important mandates of AFMA as provided in the Credit Chapter is the phase out of all existing commodity-specific directed credit programs or Agri-DCPs. Aimed at rationalizing the government's administration costs and loan-pricing policies with respect to credit delivery, Agri-DCPs are to be consolidated instead into a *demand-driven* global credit program – the Agro-Industry Modernization Credit and Financing Program (AMCFP).

Moreover, by specifically directing the adoption of *market-based interest rates*, the AFMA not only aims to junk the practice of arbitrary loan pricing but also aspires for more program efficiency primarily through the full recovery of all costs associated with lending.

By directly addressing the distortions and inefficiencies currently prevalent in the rural financial market, the AFMA Credit Chapter's bottomline is to enhance small farmers' and fisherfolk's chances of access to credit from formal financial institutions – the finance market's most efficient matchmakers (or intermediaries) between fund supply and demand.

After the passage of three years since the law became effective, a revisit to the AFMA Credit Chapter's status of implementation now provides a good case study of the process of government policy reform.

### Phasing-out Agri-DCPs and Setting Up the AMCFP

The Implementing Rules and Regulations (IRR) of the AFMA directs the Department of Agriculture's (DA) Agricultural Credit Policy Council (ACPC)

<sup>1</sup> The comments and views expressed by the authors do not necessarily represent the position of the Agricultural Credit Policy Council.

and the Department of Finance's (DoF) National Credit Council (NCC) to formulate the program for the rationalization of Agri-DCPs and the transfer of all Agri-DCP loanable funds to the AMCFP. A major consideration was to ensure no or minimal disruption in lending to agricultural borrowers. In December 11, 1998, after a series of consultations and dialogues with various stakeholders in the agriculture and fisheries sector, the Council of NCC approved the ACPC/NCC-crafted Agri-DCP rationalization design. Consequently, the Council of ACPC followed suit in January 7, 1999.

ACPC and NCC later presided over the activities connected to the rationalization process:

a. ***The review of Agri-DCPs' administrative and/or legal arrangements.***

NCC completed in March 1999 the review of executive or legal agreements binding the implementation of the various Agri-DCPs. The review recommends, among others, the hiring of a consultant to draw up the systems and procedures that would facilitate the rationalization and transfer of Agri-DCP funds into the AMCFP.

b. ***The preparation (and submission) of phase-out plans by DCP-implementing agencies.***

By May 3, 1999, all DA DCP-implementing agencies were already asked to submit to ACPC their respective rationalization/phase-out plans (by virtue of DA Department Order No.1), particularly the identification of possible legal and administrative impediment/s to the phase out of each Agri-DCP and their proposed date of cessation of lending operations and/or funds transfer to the AMCFP. As of June 2000, 6 out of the 7 DA agencies that implement Agri-DCPs have already submitted phase-out plans covering 23 out of 24 Agri-DCPs. These are the ACPC, Quedan and Rural Credit Guarantee Corporation (Quedancor), Bureau of Animal Industry (BAI), National Dairy Administration (NDA), National Agriculture and Fisheries Council (NAFC) and the DA-Special Concerns Office (DA-SCO).

c. ***Facilitating the consolidation and transfer of Agri-DCP loanable funds into the AMCFP.***

Meanwhile, the mechanics and timetable for the consolidation and transfer of all Agri-DCP loanable funds to the AMCFP have been finalized by the ACPC taking into consideration the AFMA's target completion date for these activities (i.e., February 2002). ACPC has also taken the lead in accounting and auditing the total loanable funds of Agri-DCPs, including determining recoverable loans that may help initially finance the AMCFP. The first Agri-DCP is expected to be subsumed into the new global program by year-end 2000.

d. ***Laying the groundwork for the establishment of the AMCFP.***

In line with the objective of minimizing possible disruption/s to government credit delivery for agriculture and fisheries during the period of transition to a new policy setting, it is important for the alternative program, i.e., AMCFP, to already be in place even before the actual phase out of Agri-DCPs takes place. In this regard, the ACPC and NCC also immediately conducted consultations and dialogues nationwide for the drafting of the AMCFP design and implementing guidelines. By December 11, 1998, the Council of NCC already approved the AMCFP design, again followed by the Council of ACPC in January 1999. The ACPC Council later also approved the program's implementing guidelines in July 26, 1999. Consequently, upon ACPC's request, the Department of Budget and Management (DBM) issued a fund code to establish a separate account for the AMCFP.

e. ***Rationalization of Non-Agri DCPs.***

To broaden the scope of reforms beyond the AFMA, i.e., to sectors outside of agriculture, President Joseph Estrada signed Executive Order No. 138 in August 10, 1999, directing all government entities involved in the implementation of credit programs to adopt the credit policy guidelines formulated by the NCC. The issuance of the E.O. is consistent with the mandate of the NCC to likewise spearhead the rationalization of non-agri

DCPs (per Administrative Order No. 86, S. 1994).

While intended to be complementary to the AFMA, some inconsistencies with the law were however noted in the E.O. These particularly had to do with crucial implementation details, e.g. the timeframe to be followed for the DCP phase out process and the institutions that would be allowed to perform wholesaling functions, among others. Consequently, amendments suggested by the ACPC in the E.O. guidelines were adopted to make them consistent with those of the AFMA's AMCFP. In March 29, 2000, the E.O. 138 implementing guidelines were finally approved by the NCC.

### **Review of Institutional Mandates**

Rationalizing the role of government and coming up with new policies and measures that would induce more private sector participation in lending to agriculture inevitably requires reviewing the charters and programs of different government institutions that are direct players in the rural finance market. The law therefore calls for the independent review of the Land Bank of the Philippines (LBP), the Philippine Crop Insurance Corporation (PCIC), the Guarantee Fund for Small and Medium Enterprises (GFSME), Quedancor and ACPC. Designated to commission the review, the DoF created a Steering Committee composed of representatives from LBP, PCIC, GFSME, Quedancor, ACPC, the DA and the DoF (as chair) to facilitate the said activity.

The review however became delayed by over a year due to issues of funding (for the review) and in the selection of a consultant. To finally address the funding issue, the DA, through ACPC, volunteered to take over the responsibility of funding (to be charged to the DA-ACPC's Comprehensive Agricultural Loan Fund). Consequently, the Steering Committee was able to select the review consultant. The Inception Report was presented to the Steering Committee in

August 4, 2000, while the review's completion is expected in November 2000.

### **Setting Variable Loan Grace Periods for Long-Gestating Agriculture and Fisheries Projects**

Meanwhile, consistent with its other intention of boosting the competitiveness of the local agriculture and fisheries industry, AFMA also directs the extension of grace periods for loans to agriculture and fisheries projects that take some time before becoming economically productive. R.A. 337, or the General Banking Act of 1949, limited loan grace periods to a maximum of only 3 years.

After a series of consultations jointly conducted by the ACPC and the Bangko Sentral ng Pilipinas (BSP), BSP finally issued a Memorandum Circular in November 1999 extending the maximum allowable grace period on long gestating agriculture and fisheries projects to 7 years, depending on the type of project and its actual gestation period (i.e., BSP Circular No. 217).

But even before the new grace period policy for long gestating agriculture and fisheries projects could take off, the President signed a new law in June 2000 that, among others, advocates anew a policy extending grace periods on loans only up to a maximum of 5 years, i.e., R.A. 8791 or the General Banking Act of 2000. With this more recent development, BSP Circular No. 217 faces a possible major set back. Since the grace period policy prescribed by BSP Circular No. 217 takes more fully into account the welfare and interests of farmers and fisherfolk engaged in long gestating projects, steps are being taken to regain the effectivity of a longer grace period for these types of projects, e.g. the committee jointly chaired by ACPC and BSP that was tasked to formulate the guidelines for the operationalization of longer grace periods for long gestating agriculture and fisheries projects (i.e., by virtue of the AFMA IRR) will be reconvened to take up this issue.

## **Rationalizing Agri-Credit Guarantee Schemes and Funds**

Consistent with the policy on Agri-DCPs, AFMA also stipulates that all the existing credit guarantee schemes and funds applicable to the agriculture and fisheries sector be rationalized and consolidated into an Agriculture and Fisheries Credit Guarantee Fund (AFCGF). Spearheaded by Quedancor, ACPC, and GFSME, a consultant was commissioned for the review of DA credit guarantee programs and for the formulation of a rationalization plan on the same. The consultant submitted the proposed rationalization plan in February 2000.

Meanwhile, to provide a “safety net” for small and ‘less-bankable’ farmers and fisherfolk, the DA created a study team composed of representatives from the different DA line agencies and bureaus as well the private sector to formulate a special credit guarantee arrangement. The aim of this scheme is to cater specifically to small farmer- and fisherfolk-borrowers that do not have collateral (i.e., DA Special Order No. 438, S. 1999). Co-chaired by the LBP and ACPC, the study team completed the implementing guidelines of this special scheme in mid-2000.

### **Final Remarks**

Despite several hitches and delays, the groundwork for the implementation of the AFMA’s Credit Chapter is largely already in place. This is mainly due to the determination and coordinated efforts (and resources) of several government agencies (principal of which are the ACPC, NCC, DA and the BSP) as well as the active involvement of representatives from the private sector to finally bring about necessary reforms in rural finance.

Notwithstanding this seemingly upbeat assessment, it nevertheless cannot be said that the reform process is already out of the woods. The consummation of the Credit Chapter reforms still depends a lot on the completion of several unfinished

or unsettled business including, among others, the results of the review on institutional mandates, the finalization of the Agri-DCP phase out plans, the resolution to the inconsistency between the General Banking Act of 2000 and BSP Circular No. 217 on the policy on loan grace periods, and the immediate allocation of funding out of the annual AFMA budget to support the operationalization of the AMCFP (note: while the law provides that 10% of the total AFMA budget should be allocated for the AMCFP, nothing over the last 3 years has been done to even partially comply with this).

But above the procedural delays, perhaps the more glaring testimony to the difficulty of carrying out changes is the proneness even of already ‘finished’ business to resurface. The fundamental debates on the merits and demerits of phasing out DCPs and shifting to market-oriented interest rates, for example, continue to rage not only despite the already advanced stage of the reform process, but more importantly, also despite the clear mandate of the law. More recently, calls for the shelving of the new policy direction have continued to invite misguided support and even now pose a serious threat to the implementation of the reforms. With barely one and a half years remaining for the final consolidation and transfer of funds to the AMCFP, therefore, the AFMA Credit Chapter reforms are already near and, yet, remain a distant reality.