THE PRESENT SITUATION AND OUTLOOK OF SHORT-TERM CREDIT FACILITIES WITH EMPHASIS ON THEIR IMPLICATIONS ON THE RICE PROBLEM OF THE COUNTRY

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In the face of a rapidly growing population, and with agriculture occupying a strategic position in our national economy, the attainment of a high level of productivity and increased production becomes a vital issue. The problem assumes particular significance in the case of rice production, since rice is the mainstay in the diet of a large proportion of our population and a large number of families is dependent on the rice industry for their livelihood.

Over the years, numerous and varied programs have been evolved and directed towards the attainment of basic sufficiency in rice production to meet the expanding requirements of an increasing number of consumers. However, there are strong indications in the existing situation which show that we have not altogether made much headway in solving the problem. Thus, we find that the increase in total rice output has hardly kept pace with the population growth and we continue to import rice from our neighboring countries in the region.

Undoubtedly, the persistence of low production and low productivity on Philippine rice farms is the result of the interplay of closely related factors, among the most important of which are small size farms, poor and inefficient organization of the farm business, unfair tenancy practices, lack of efficient and dependable irrigation systems, use of primitive methods of

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production, and lack of economic incentives to increase production. One of the major causes of the problem is the lack of capital to finance the acquisition of input factors needed for improving production. The farmer needs adequate funds to finance the maintenance, replacement and development of capital goods and equipment in farming, to meet the day-to-day costs of agricultural operations, to enhance the adoption of technological improvements in farm production, and to maintain basic consumption levels of his family. As farming becomes more and more market-oriented, the need for greater amounts of capital will also expand.

But this increasing need for capital cannot be fully met by the farmer out of his own savings. Operating at a low level of technology, the farmer gets a low income from his farm operations. Having a low income, he will tend to have little or no savings to augment his operating capital or even to meet family living expenditures from one harvest to the next. Therefore, he will have to rely on credit for his capital requirements.

It is the purpose of this paper to examine the present situation and outlook of short-term credit facilities for agriculture, particularly in relation to rice production. Another paper in today's session will discuss the situation and outlook of long-term agricultural credit.

A SURVEY OF THE PRESENT SITUATION

Farmers' Need for Credit

As stated earlier, because the small farmers derive only a small margin from the low returns in their farm business operations, they have little or no savings to use as capital and perforce they have to depend on credit for their financial requirements. Dalisay[2] observed that it is customary in our

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2 Dalisay, Amando M. "Credit and Marketing as Aids to the Enlarging of Farm Size." Proceedings of the Fifth FAO Development Center on Farm Management for Asia and the Far East. 1960, pp. 251-261.

rural areas for farmers and their families to avail themselves of some form of credit, be it store credit for essential consumption supplies or a small production loan from rural money lenders. These forms of credit are short-term and generally characterized by high interest rates.

In a study of 5,144 farmers conducted by the U.P. College of Agriculture in 1955,[3] it was reported that only 26 per cent of the farmers did not use any form of credit; in other words, seven out of every ten farmers incurred debts. About 57 per cent of these farmers used store credit for their food supplies, school supplies, fiesta supplies, clothing and miscellaneous household and farm items. In another study conducted in 1959[4] it was revealed that practically all the farmers surveyed obtained short-term loans. All of the part-owners, 94 per cent of the owner-operators and 98 per cent of the tenant farmers included in the study obtained short-term loans, while more than four-fifths of all farmers used store credit in addition to short-term loans.

Sources of Short-Term Credit

Studies made by the U.P. College of Agriculture[5] points out that non-institutionalized private lenders, including merchants and landlords, are still the major sources of short-term agricultural credit in this country. Of the 2,411 short-term loans studied in 1957, about 88 per cent came from private individuals, landlord's, merchants, and friends or re-

3 Guzman, Leopoldo P. de. "An Economic Analysis of the Methods of Farm Financing Used on 5,144 Farms, 1955." The Philippine Agriculturist, Vol. 41 (1958), pp. 460-480.

4 Gapud, Jose P. "Financing the Farm Business of 100 Lowland Rice Farms in Muñoz, Nueva Ecija." *Farm Finance in the Philippines* (A compilation of research results prepared by the Department of Agricultural Economics, U.P. College of Agriculture, for the FAO Development Center on Farm Management, 1960), p. 34.

5 Farm Finance in the Philippines. *Op. cit.*

latives of the farmers; 42 per cent were granted by private money-lenders; 39 per cent by landlords, 6 per cent by relatives, and 1 per cent by merchants. Loans granted by FaCoMas represented 11 per cent, while those from banks and other registered lenders only about 1 per cent.

Of the total agricultural loans of ₱5.7 billion granted by banking and financial institutions in 1962, about 87 per cent came from commercial banks and only 13 per cent came from rural banks, Development Bank of the Philippines, and non-bank financial institutions.[6] In the fiscal year 1963-1964, the Agricultural Credit Administration (formerly the ACCFA) granted a total of ₱2.9 million of production loans to finance expenses in farm operations, and ₱2.1 million of commodity loans to tide over the farmers in their cash requirements while waiting for their crops to be marketed.[7] As of December 31, 1964, the Agricultural Credit Administration released ₱5.7 million loans in cash and in kind as well as fertilizers in connection with the rice production crash program. In the fiscal year 1963-64, the Development Bank of the Philippines granted the amount of ₱17.8 million to 3,783 food crop producers, of which ₱11.7 million went to 3,465 palay farmers.[8] Agricultural loans in the aggregate amount of ₱411.4 representing 30.6 per cent of the total loans were granted by the Philippine National Bank in 1964. In 1963, the rural banks granted some ₱143 million of agricultural loans, representing about 80 per cent of total loans granted.

The existing credit institutions are still inadequate to cope with the credit needs of a large segment of the farming population. The banking facilities are generally concentrated

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6 Dalisay, Amando M. "Agricultural Credit Structure in the Philippines," Economic Research Journal, Vol. XI, No. 1 (June, 1964), pp. 39-49.

7 Agricultural Credit Administration. "Transition," Annual Report FY 1963-1964.

8 Development Bank of the Philippines. Annual Report 1963-1964.

in cities and provincial capitals; farmers lack knowledge and experience on the proper and wise use of institutionalized sources of credit; there are the unnecessary delays and untimely releases of loans, the imposition of impractical loan requirements based on commercial banking; the nature of agricultural operations are not adapted to orthodox banking practices — these and many other factors and conditions render the credit institutions inadequate to become a major source of agricultural credit. Furthermore, the modern credit institutions are not quite suitable to the kind of socio-economic organization under which the small farmers operate in the rural areas "where relationships are personal and traditional rather than businesslike, where written records are rarely kept, where transactions are generally sealed by oral promises based on trust and honor rather than by sophisticated or elaborate legal documentation, and where the hard shell of custom and attitudes makes farmers resistant to change, new ideas, new techniques and new institutions."[9] For this reason, the private lender remains as the principal source of credit for farmers.

Size of Loans

The size of loans obtained by farmers serves as an indication of the small-scale farming they are pursuing. In the study conducted by Gapud,[10] it was reported that the average amount borrowed by owners was ₱395; by part-owners, ₱270; and by tenants, ₱295. A study of lending operatons of farmers cooperative marketing associations (FaCoMas) and rural banks conducted by Hakim[11] in 1959 revealed that the average amount of loan obtained from rural banks was ₱421 per

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9 "Institutions Mostly Postwar" (Country Report of the Philippines). *Using Credit for Agricultural Development in the Far East.* Report of the Fourth Far East Agricultural Credit Workshop, Taipei, Taiwan, Nov. 12-24, 1962, pp. 85-94.

10 Gapud, Jose P. *Op. Cit.*

11 Hakim, Rusli. "A Comparison of the Agricultural Lending Policies of 2 Rural Banks and 2 FaCoMas in Polo and Baliwag, Bulacan." (Undergraduate thesis presented for graduation at the U.P. College of Agriculture, March, 1959).

farmer, while that obtained from the FaCoMas was ₱129. About 90 per cent of the FaCoMa borrowers studied obtained loans of ₱200 or less, while about 40 per cent of the rural bank borrowers got loans of ₱200 or more.

As reported by De Guzman,[12] the short-term loans ranged from ₱79 per loan from private money lenders to ₱590 from banks, or an average of ₱105 per borrower. By type of farms, short-term loans averaged ₱140 for sugar cane farmers, ₱139 for rice farmers growing two crops a year, ₱127 for rice farmers dependent on only one crop, ₱51 for vegetable farmers, and ₱21 for corn growers.

In the study of ten years of rural banking in the Philippines, Muere[13] reported that the average agricultural loan per rural bank was ₱599 in the case of banks in operation for five years or more and ₱507 in the case of banks with less than five years in operation.

Interest Rates

One of the major problems of agricultural credit is the high rate of interest charged by private lenders. In the study reported by De Guzman,[14] the interest charged for short-term loans was about 55 per cent per annum. Including those loans with no interest, the average was about 28 per cent, or more than twice the legal rate. About 53 per cent of the loans granted by landlords to tenants had no interest but 25 per cent had interest rates ranging from 20 to more than 300 per cent a year. One-fourth of the loans had interest rates higher than 20 per cent. The average computed interest rate for 224

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12 Guzman, Leopoldo P. *Op. cit.*

13 Muere, Romeo A. "An Economic Evaluation of a Decade of Rural Banking in the Philippines in Relation to the Development of Agriculture." (Master's thesis presented for graduation, U.P. College of Agriculture, May, 1965).

14 De Guzman, Leopoldo P. *Ibid.*

fully repaid loans was 98 per cent. One-third of these loans had 14 per cent interest; the rest were charged rates varying from 15 to 300 per cent, with a large portion falling between 100 and 300 per cent per annum. On the average, owner-operators paid 46 per cent; part-owners, 40 per cent; and tenants, 61 per cent per annum for their loans. Compare these with the 7-8 per cent and the 12 per cent per annum interest rates charged by the ACA and the rural banks, respectively.

It should be pointed out here that the high interest rates paid by farmers are not actually stated as such in the loan agreement but are based on computed rates of the payments made in kind. The credit practices known as **takipan** (for every cavan of palay borrowed, the debtor pays back two cavans), **talindua** (three cavans paid for every two cavans borrowed), **takalanan** and others like paying three cavans of palay as interest for every ₱100 in cash borrowed, have been reported to be still in existence. If we consider the fact that these loans are for a short period of time only, say three to six months, we will realize that translated on an annual basis, the interest rate would be exorbitant indeed. What makes matters worse is the fact that the farmer usually borrows during the period between planting and harvesting of his crops, when the supply of his commodity is low and, therefore, the price tends to be high. He pays back the loan in kind at harvest time when the supply is plentiful and the price is low.

Dissipation of Productive Credit

Many of our farmers tend to use borrowed funds for consumption purposes rather than for financing production. Gapud,[15] in his study cited earlier, found that only 29 per cent of the money borrowed by farmers was used for farm operations, while 71 per cent was spent for family living and household expenses. In other studies on farm credit,[16] it was re-

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15 Gapud, Jose P. *Op. Cit.*

16 See Farm Finance in the Philippines, *Op. Cit.*

ported that 95 per cent of all farmers included in one survey used their short-term loans for subsistence. Tenants and part-owners tended to use a bigger portion of the amount borrowed for family expenses, particularly subsistence and social expenditures (weddings, fiestas, baptismal parties, etc.), while the owner-operators used a higher percentage for farm expenses. Of loans incurred by FaCoMa members, about 68 per cent was used for living expenses. In a study conducted by Muere[17] of 1,757 rural bank loans, it was found that 30 per cent was used for family living expenses and 10 per cent for non-farming expenses.

There were also many cases of misapplication of loan proceeds that have been observed. Gapud[18] revealed as one important finding of his study of the small agricultural loans operations of the Development Bank of the Philippines in the Cabanatuan City Branch in 1960, that about 47 per cent of the farmers included in the survey misapplied either completely or partially the loans obtained and used them for unproductive purposes. In a few cases visited by the author, the loan proceeds that were supposed to have been used for the purchase of breeding stock of pigs were used instead for renovating the farm dwelling or for buying some household items.

Late releases of loans and lack of supervision are major factors which cause misapplication and poor repayments. Of the 400 farmers who borrowed from FaCoMas, 43 per cent reported delayed releases of their loans. Three-fourths of those experiencing late releases reported borrowing outside. About 38 per cent of the cases of misapplication was directly the result of late releases. Only 31 per cent of the 400 borrowers were visited by a FaCoMa official. Eighty-one per cent of the

17 Muere, Romeo A. *Op. Cit.*

18 Gapud, Jose P. "A Study of the Small Agricultural Loan Operations of DBP Cabanatuan Branch, Nueva Ecija, 1960" (Unpublished research paper, Agricultural Credit and Cooperatives Institute, U.P.).

rural bank borrowers interviewed stated that they were not visited at all by any rural bank personnel for the entire duration of the loan.

Attitude of Borrowers and Credit Institutions

Probably the most important problem-area in the field of agricultural credit is the attitude of the farm population with respect to credit. Katigbak,[19] in a paper read before the First Agricultural Credit Conference held in Los Baños, Laguna on February 27-29, 1964, made the observation that—

> "In their traditional or economic and cultural circumstances and background, the average tenant-farmer has had little opportunity to develop the kind of attitude towards credit or borrowed money that would make it easier for a credit institution, particularly one that is of the government, to administer a credit program such as this conference is considering. The general run of tenant-farmer looks at credit as something to avail of to meet personal family needs, not necessarily to use for productive purposes. This is crucial in an agricultural credit program. For what is not invested in production and does not return itself plus margin, is credit that is hard to repay. This and the wellknown attitude towards credit coming from government institutions pose a problem which we must learn to overcome."

The attitude towards credit coming from governmental institutions cited in the above statement refers to the non-interest of farmers to pay back loans granted by the government. They think of credit granted by government lending

19 Katigbak, Jose R. "Problems Expected in Meeting the Credit Needs of a Changing Agriculture Under Land Reform." Conference Report of the First Agricultural Credit Conference, 1964. The Rural Bankers Association of the Philippines. (Mimeographed.)

institutions as hand-outs or doles instead of an obligation on their part to pay back when due. In other words, the farmer-borrowers generally confuse credit with social welfare work. Studies made by Hakim[20] and Hatta,[21] revealed that delinquent FaCoMa borrowers were just as financially able as those borrowers who paid their loans, indicating that these delinquents may have the capacity to pay but not the willingness or the desire to repay their loans. Unlike the rural bank borrowers who gave some form of security for their loans, the FaCoMa borrower with enough money to pay may not feel the same pressure to settle his loan simply because he is not asked to put up a collateral to back up his loan.

Another wrong attitude of many borrowers pertains to the use they make of the loan proceeds. They believe that just because the value of their collateral is much more than the amount of the loan granted to them, it does not matter at all whether or not they use the loan proceeds for purposes stated in their application. After all, they say, if they can not pay their loan on time, the lending institution can always foreclose their property, so why should they concern themselves about following to the letter the use of credit for productive purposes.

As indicated earlier, the institutional sources of agricultural credit have hardly reached the bulk of the rural population, because their policies, loan terms and conditions, and credit procedures are more attuned to commercial and industrial financing rather than to the peculiar characteristics of agriculture and the socio-economic conditions of the farmers. Katigbak[22] in his observations of the agricultural credit situa-

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20 Hakim, Rusli. *Op. Cit.*

21 Hatta, Warga Dalam. "A Comparison of the Agricultural Lending Policies of 2 Rural Banks and 2 FaCoMas in Manaoag and Malasique, Pangasinan." (Thesis presented for graduation, U.P. College of Agricuture, March, 1959; unpublished.)

2 Katigbak, Jose R. *Ibid.*

tion in the Philippines, appropriately described this condition as follows:

> "On the part of the creditors, particularly of the institutional type, there is also the attitude, doubtless justified by tradition and the level of socio-economic development of the nation as a whole, that credit, like any other commodity must be sold — or given out — at the highest possible margin or profit. It must also be absolutely secured by tangible collateral usually having a value at least double the amount of a loan given. In this sense, one might say that usury is kinder to the propertyless borrowers; at least the usurer does not require gilt-edge collateral. Obviously, this attitude is not in step with the imperatives of changing agriculture nor with the demands of development in an underdeveloped society that is under pressure to expand production or risk being engulfed and overwhelmed by upsurging forces of social reform and conflict."

The Outlook of Short-Term Agricultural Credit

On the basis of trends and recent developments, we can attempt to make a "forecast" of what the situation will be in the years ahead with respect to short-term credit for agriculture, particularly as it relates to the perennial rice problem of the country.

For a long time yet, we can expect private lenders to be the dominant source of agricultural credit. Despite the abuses and malpractices generally associated with this source of credit, private lenders perform a service which can rarely be obtained from credit and financial institutions. Credit is readily available to the borrowers from this source. The private lender renders prompt service and generallly offers adequate amounts of loans needed by the borrowers. It is easily approachable. In many cases, security is not required.

The debtor and the creditor know each other reasonably well. The loan procedure is simple and the conditions of the loan are generally flexible. Compare this with institutional sources of credit. The time spent unnecessarily in processsing and approving loan applications in many credit institutions is such as to frustrate the very object of the lending assistance to farmers. Although the interest rate charged by lending institutions is relatively lower, the actual cost of the loan to the farmer-borrower is rather high. The procedure is so expensive that the farmer often finds at the time the loan is released that a third or one-half of it is already spent in the process of getting it, and the loan is released at a time when it may no longer be needed.

Expect interest rates charged by private lenders to go down to a level approximating the maximum charged by banking institutions. The increase in number of rural banks and branch banks, as well as the improvement in the efficiency of operations of cooperative credit associations in the rural areas, would be a factor in setting the pace for the lowering of interest rates. The increase in available loanable funds generated by savings deposits of farmers who would have higher incomes would also contribute to the downward adjustment of interest rates.

We can also expect a relaxation of collateral requirements, as more and more loans granted by credit institutions would be based on the character and integrity and productive capacity of the borrowers. This would be engendered by a broad program of credit education and by the adoption of a supervised credit system which bases credit assistance on farm and home planning rather than on stiff security requirements.

The implementation of the Agricultural Land Reform would generate an increasing need for more capital and hence a greater demand for agricultural credit. There would be a tendency to use more mechanical equipment on the farms as the farmers begin to operate more efficiently. As a result of innovations in farm practices recommended by agencies under the Land Reform Council, there would be a greater demand for input factors and, therefore, a tendency on the part of the farmers to think in terms of commercialization of rice production. The farmers would henceforth be thinking of cost-price relationships. In order for the farmers to implement the technological advances on their farms as envisioned under the Agricultural Land Reform Program, there would be need for additional capital. Hence, the average size of loans per borrower would also increase.

With more capital being made available to meet the increasing demand of farmers for more funds to finance their productive farming operations, there can be great hopes that our present monoculture, one-crop system of farming can be transformed into a successful, well-balanced agricultural production. The increase in capital injected into the economy of rice agriculture would break the vicious cycle of low productivity — low income — low savings and investments — poor technology — and back again to low productivity, and the perennial problem of rice shortage may thus be solved.

Agricultural productivity is a means to an end, the end purpose being the improvement of human welfare by providing better living not only for the rice farmers but for all people. Achievement of this goal requires that our programs to increase rice production and enduce economic efficiency in agriculture should be carried out in an environment which respects the dignity and worth of each individual as a human being. There is no moral justification for us to trample upon the rights of individuals to share in economic progress just so we could achieve freedom from want. We cannot afford the expensive luxury of a handful of rice in exchange for our most precious democratic freedoms.