

IMPACT OF AGRICULTURAL FINANCE IN KENYA.

CASE OF AGRICULTURAL FINANCE

CORPORATION.

BY

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SCIENCES OF KENYATTA UNIVERSITY

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*Impact of
Agricultural finance*



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DECLARATION

This report is my original work and has not been presented for a degree in any other university

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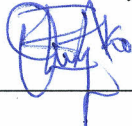
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DEDICATION

To my mother Francisca Amimo whose care, patience and love
opened up the world for me.

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ABSTRACT

The Agricultural Finance Corporation was established in 1963 and reconstructed on 21st March 1969 by an Act of Parliament Cap.323. The main function of the Corporation was to assist in the development of Agriculture and Agricultural Industries. This it would achieve by making loans to farmers, Cooperative Societies, Public bodies, Local Authorities and other Persons engaging in agriculture or agricultural industries. The Corporation was empowered by the act as a body Corporation with perpetual succession and a common seal. It was granted authority and power to acquire, own, possess and dispose of property and to contract and sue and be sued in its own name. The Corporation was exempted from the Companies and Banking Acts. Agricultural Finance Corporation offers different loan products key amongst them are, seasonal crop credit open line, other seasonal crop production loans, mechanization loans, livestock development loans, loans for plantation crops and loans for legal entities. During the year 1998, Kshs 172.98 million was lent to farmers, which was a decline from Kshs 249 million lent in 1997. Due to the reduced lending the principal loan portfolio fell by Kshs 55 million from Kshs 2,253 million in 1997 to Kshs 2,198 million in 1998. The total loan portfolio however increased by Kshs 149 million from Kshs 3,561 million in 1997 to Kshs 3,710 million in 1998. This increase of 4.2% is a result of poor loan repayments. In the same year (1998) Kshs 425.3 million collected in 1997. The story of ever decreasing repayments became a constant feature in the history of Agricultural Finance Corporation. (A.F.C annual report 1998). In the similar manner, Kenya Rural Enterprise Program (KREP) was established as a non Governmental Organization in early eighties. Its main task was to provide financial services to other institutions for on lending to small-scale entrepreneurs. This method did not work satisfactorily. KREP transformed itself into a big institution offering services to entrepreneurs directly. Its main products are Chikola (Group Loans) and Juhudi (targeting individuals). Through continuous researches KREP today have the small holder agriculture credit project. This facility is being implemented in Kibwezi, Taita Taveta and Migori. It is an initiative aimed to access small holder farmers in the rural areas with credit for agricultural development. Its popularity with the farmers is because apart from the group guarantee, no other tangible collateral is required. The research therefore delved in assessing the impact of the loans extended by the Agricultural Finance Corporation both on the recipient farmers and the appropriateness of the disbursement methodology. A comparison ^{will} be made with other institutions mostly Non Governmental Organizations extending credit to Agriculture. It will be of significance and interest to look at a facility like the small holder Agricultural Credit, currently offered by the Kenya Rural Enterprise Programme (KREP).

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ACRONYMS/ABBREVIATION:

AFC – Agricultural Finance Corporation

AID – Agency for International Development

BAT – British American Tobacco

CARIPLO – Cassadi Risparmio Delle Provincie Lombarde

COMESA – common Market for Eastern and Southern Africa

EABL- East African Breweries Limited

FAO – Food and Agricultural Organization

FGD- Focus Group Discussion

GDP – Gross Domestic Product

IRDP – Integrated Rural Development Programme

KIE – Kenya Industrial Estates

KREP – Kenya Rural Enterprise Program

NGO – Non Governmental Organizations

ODI – Overseas Development Institute

PRA – Participatory Rapid Appraisal

UK – United Kingdom

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INTRODUCTION

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1.0 INTRODUCTION

1.1 Background:

This Research is being carried out at a time when the agricultural sector in Kenya is in a crisis. The marketing structures are not performing to expectations. The cost of production is at times higher than the market prices. This has made it difficult for the local products to compete favourably with imports from other COMESA countries, Brazil and the Far East. Goods like sugar and rice from these regions sell much more cheaply than our local products despite have passed long distances.

Part of the above problem is caused by small scale production. Many small scale farmers develop small acreages. This does not make them benefit from economics of scale. Many of them are unable to go beyond two acres because of lack of funds. This makes the provision of credit to this sector very critical to its development.

In order to get solutions on how to treat the issue of credit to the agricultural sector, it is important that the causes of the problems bedeviling this service be unveiled and addressed.

1.2 **Statement of the Problem:**

There is no adequate credit extended to the agricultural sector to spur the required growth in the Gross Domestic Product (GDP).

1.3 **Objectives: (General)**

- a. To find the principal causes of failure by institutions lending to farmers.
- b. To investigate appropriate methods that can support successful agricultural lending.

1.4 **Objectives: (Specific)**

- a. To study different institutions lending to agriculture and identify loopholes and strengths in their lending patterns.
- b. To obtain the opinion of farmers on what they consider appropriate mechanisms for lending to the sector.
- c. Compare different lending methodologies and identify their strengths.
- d. Look at the role of different support institutions i.e. research institutions and see if they play the roles as required.

1.5 **Research Questions:**

1. Study Agricultural Finance Corporation's (AFC) Provision of Financial Services to Farmers and Compare it with KREPs Smallholder Agricultural Project; Identify strengths and loopholes in their lending
2. Obtain farmers opinion on what constitutes good agricultural financing.
3. Establish the link between agricultural production and lending.
4. Establish why agricultural credit is going down in volume and outreach.

1.6 **Hypothesis:**

Lending to the agricultural sector is possible and only wrong approaches lead to failure of the institutions to attain good repayment rates.

1.7 **Justification:**

Kenya today is predominantly supported by an Agrarian economy. The history of nations confirms the theory that all countries start with agriculture as their principal income generating sector. It is on a sound agricultural foundation that industrialization and the service industries

later emerge. This aspect makes it important to nurture the upcoming agricultural production.

Agricultural production on the other hand requires adequate financial input. Indeed you need money to acquire basic inputs in agriculture. The Basic Machinery like tractors have to be bought or hired at a fee to break and tilt the land. The farmers are sometimes overburdened with an increasing domestic budget and responsibilities. They need some form of assistance to participate in meaningful production. Grants are hard to come by. They can never be availed to a whole nation. In Kenya even basic services like medical and education witnessed a decrease in Government support to citizens.

The cost sharing arrangements recommended by the World Bank and International Monetary Fund have had a lot of erosion on the purchasing power of the ordinary citizens. The situation is worsened by the increase in death of the most active family members resulting from Aids pandemic.

2.0 LITERATURE REVIEW

In agricultural credit in African countries the author argues that , Contrary to what many people think, it is not the main purpose of agricultural credit system to supply individual farms on a permanent basis with a more plentiful volume of credit from banks or other sources, with a view to enabling farmers to expand production at least cost to them. In our days we should say that the paramount aim of an agricultural credit system must be to make the best use of capital resources of various origin with a view to maximizing the contribution of agriculture to the general economic development of the country concerned. It follows that there exists no system which is everywhere preferable to others and no system in any one country , either which does not need to be reviewed as time goes on, in the light of social progress and of the economic and financial policy .

To be sure, in countries where agriculture suffers from chronic shortage of funds, every effort must be made to channel to it an abundant flow of credit, but the interests of the individual farmers must not be confused with the social aspects of the problem.

“The interests of the community as a whole require individual farmers economic condition always to be set in the context of the nation bent on achieving continuous, orderly and balanced economic progress”. (Professor Giordano Dell’ Amore)

It must at once be added that in African countries, barring few exceptions, agriculture is so starved of funds that there is every justification for experts trying to devise means of remedying the shortage through a re-orientation of economic and financial policy .

Lack of adequate finance has been one of the main problems confronting the establishment, growth and revival of small units. Commercial banks and other credit institutions had, due to several historical reasons, shown a marked reluctance in the past to finance small-scale enterprises.

After social control and nationalization of major Indian banks, most of the banks both in public and private sectors, evolved a scheme to assist various categories of small enterprises.

Donald Gordon Prioritizes agriculture as a sector that is long neglected .He says, *“in considering why it is necessary to give particular attention to the small farmers of developing countries, we will begin with the reasons for an increased priority for agriculture in general and go on the basis for a special concern with the small producers. Neither agriculture nor the small farmer have been rated very high in the operational thinking of most development theories and practitioners until fairly recently”*.

Rather the small farmer has been seen as the main representation of the backwardness, which developing countries were rejecting in their efforts to emulate the “advanced” industrial countries.

The dominant development approach adopted by newly independent countries in the 1950s and 60s emphasized industrial import substitution. This policy has had negative results for agriculture. The nation’s attention and resources tended to be concentrated on urban activities, to the neglect of farming.

For the success of a credit program more than money is needed. There must be a new technology, markets that can supply additional inputs and absorb additional outputs, institutions willing to lend to small farmers on terms the farmers consider attractive and perhaps more important, farmers willing to borrow, to invest and to repay loans.

Sources of Credit:

In most developing countries informal private lending is a far more important source of funds for farmers than credit from public institutions. In only a few countries does public credit exceed 20 percent of outstanding agricultural loans . (Donald Gordon, Credit for small farmers in developing countries).

In small farmer credit programmes government strategies show a preference for devised complicated schemes based on standardized economic

assumptions, and relying on a transfer of modern institutions from an urban to a rural setting (Sudarshan Lal, Loans to small industries and small borrowers).

A report initiated and carried out as a result of an agreement between Food and Agricultural Organization (FAO) and the Cassadi Risparmio delle Provincie Lombarde (CARIPLO) provides a good insight on agro- credit as follows;

Credit to small farmers:

Potential and limitations

The development model adopted either fully or partially by most of the less developed countries (LDCs) during the decade 1960/70 with the full technical support of foreign advisors and Aid agencies, was based on the fastest possible growth of Growth Domestic Product, and therefore on capital investment in areas of highest financial potential. This approach has increased the vulnerability character of many LDCs by creating new small islands of property and conspicuous consumption in the old ocean of absolute poverty. It is increasingly doubtful whether the effects of the growth in the privileged sectors of the economy will trickle down to reach the lower income groups before it is too late. This is particularly so if one considers that the world population will double in the next thirty years.

A FAO report of 2002 shows a decline on funding to agriculture . According to provisional data, in 1999 the major bilateral and multinational donors committed \$.10,700 million in current prices as external assistance for

agriculture development, compared with \$.12,605 million in 1998. When these figures are converted into constant 1995 prices, this corresponds to a decline of 17 percent after increases of 14.5 and 4.6 percent in 1997 and 1998 respectively. Partial data available for 2,000 suggest that the level of external assistance to agriculture would decline further (FAO , annual report 2000) .

In an economic analysis , credit may be a private good in the sense that it is excludable and subtractable, but these attributes are not necessarily sufficient to make it attractive to private suppliers. This is because the credit market combines the problems of imperfect information and risk. In developing countries this risk drives especially from the poor legal frameworks for loan recovery and securing collateral. Risk aversion in the private sector leads to the provision of credit only to those with better access to collateral or particular ties to the lenders. It also leads to high borrowing costs which reduce the demand for credit.

On the poor, she says, when credit was subsidized, it was usually not the poorest who benefited, whatever the intentions of the Governments. Artificially low, sometimes negative interest rates and little pressure to repay meant that the demand for credit often exceeded supply. In such situations it was the more influential and richer farmers who benefited as opposed to the poor farmers (Diana Carney , ODI) .

While it may be implicit in some development approaches, the need for rural-enterprise promotion has not been developed purely from economic considerations of harnessing the known and latent resources in rural areas. The type of rural enterprise programmes and the manner in which they are being run, especially in developing countries, only confirm their welfare orientation. In India for instance, subsidies of up to 50% are provided on bank loans granted to beneficiaries identified under the massive Integrated Rural Development Programme (IRDP).

“There exist fares for on the spot loan disbursement to the beneficiaries, large budgets for classroom vocational training of rural youths; government subsidies on purchases of farm inputs and on interests “(Shailendra Vvyaharman, when the harvest is in).

3.0 RESEARCH METHODOLOGY

The research employed both qualitative and quantitative data gathering.

3.1 Qualitative Methods:

The study collected data on agricultural credit, looking at the past, the situation prevailing and hopes for the future. The qualitative method captured the general description of the subject and behavioral attitudes. It also defined certain concepts as they emerged in the study.

3.2 Quantitative:

This method involved statistical appearance of data. Data collected was quantified and studied in the aggregate. The results of the data analysis have provided useful indicators to draw conclusions on Agricultural lending, the opinion of farmers on their needs and the view of the lending institutions on agro credit.

Data Collection:

The research relied on two major sources of data, the primary and secondary.

Primary: Applied to facts and assumptions obtained directly from field interviews and questionnaires.

Secondary: This applied to facts and assumptions obtained from documents authored by others (library, journals, surveys and periodicals).

3.3 Data Collection

3.3.1 Questionnaire:

Questionnaires were administered by myself and research assistants. It enabled the research to benefit from a big sample (population). I also received information within a short time using the questionnaires. Three types of questionnaires were used, one to the farmers, another to the lending institutions while a third went to institutions supporting agricultural research and other services.

3.3.2 Interviews:

This involved discussions with the target group. It was more useful in providing qualitative information that went along way in building the accuracy of the research.

3.3.2.1 Focus Group Discussions:

This method was used to collect information from the farmers . It allowed the collection of detailed information using a question guide with key areas of supply and demand for financial services by farmers in Kenya .The tool facilitated an in depth examination of issues through the dynamics of peer group discussions.

Such issues included their perception of services offered, needs for other services, and the short comings of the available services. FGDs were used with PRA techniques including seasonality analysis , simple wealth ranking , financial sector trend analysis , and cash mobility mapping.

3.3.2.2 Seasonality analysis.

Was used to obtain information on seasonal flows of Income and Expenditure and the potential demand for credit and savings services. This analysis provided insights into some of the pressures faced by clients and how they would use financial institutions Services to respond to these. This tool also provided insights into the financial intermediation needs of the community and what products can be designed in response to them.

3.3.2.3 Simple Wealth Ranking.

This tool was a rapid way of segregating a community into categories in terms of poor, not so poor, and rich. This helped to identify different needs as shown across the social strata.

3.3.2.4 Financial services matrix.

Was useful in determining which financial services are used by which socio-economic or socio-cultural strata of society and why. This is useful in designing or refining appropriate financial products.

3.3.2.5 Cash Mobility mapping.

Provided an understanding of where the community goes to acquire or spend cash (markets, waged labor, co-operatives, informal financial organizations etc.) and to lead into discussions of which financial service institutions they trust and value and why.

FGD TOOLS

1. a) Seasonality Analysis;

	JAN	FEB	MAR	APR	MAY	JUN	JUL	AUG	SEP	OCT	NOV	DEC
INCOME												
EXPENDITURE												
SAVINGS												
CREDIT												

Table 3.1, Source: Author 2004

b)

PARAMETER	HIGH SEASON	LOW SEASON	REASONS	OPPORTUNITIES FOR INTERVENTION
INCOME				
EXPENDITURE				
SAVINGS				
CREDIT				

Table 3.2, Source: Author 2004

2. Financial Services Matrix;

	Rich	Not so Rich	Poor
Money Lender			
Bank			
Sacco			
MFI			
AFC			
Savings Club			

Table 3.3, Source: Author 2004

3.3.3 Sampling:

The research focused on 5 branches of Agricultural Finance Corporation randomly selected out of the 30 branches

The study covered 47 farmers who have received loans from AFC interviewed individually and another 4 groups using PRA tools

For comparison, KREP's small holder farmer credit project was studied

3.3.4 Data Analysis and Presentation:

Measures of Central tendency were used while analyzing data. These included; the mean, mode, and the standard deviation. Computer packages such as the SPSS and Excel have been used.

For data presentation pie charts, Graphs and bars have been used.

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4.0 RESULTS AND DISCUSSION

- (a) **Study Agricultural Finance Corporation's (AFC) Provisional of Financial Services to Farmers and Compare it with KREP's Smallholder Agricultural Project; Identify strengths and loopholes in their lending.**

A.F.C.		KREP SMALL HOLDER PROJECT
Repayment rate	Less than 60%	Above 95%
Savings	None	A must
M/s	Very poor	Good
Non performing portfolio	Over 2 billion	Less than 3 percent of portfolio
Loan sizes	Over 55,000	Lowest is 10,000
Linkage to markets	Not involved	Not involved
Outreach	Relies on Government Officers	Has credit officers attending farmers meetings
Security	Land Bank guarantees	Group Solidarity

Table 4.1, Source: Author 2004

4.1 Issues

4.1.1 Repayment

Agricultural Finance Corporation has a big default rate. In the four branches visited, Kisumu, Kakamega, Turbo and Eldoret, the Managers were very reluctant to give information on their repayment rates. Most of them indicated that it was only the Public Relations Officer at the Head Office (Development House) Nairobi who had the power to do so. In the headquarters, no print outs, could be released. The answer I was given was that repayment rate was about 60%. I was also told that loans worth 400 million were treated as bad debts in the year 2003.

KREP small holder agricultural project which just started five years ago has a good repayment record. The information in their Wundanyi Office (Taita/Taveta), is freely available. Their repayment rate stands at over 95%.

a) **Performance of AFC Over a Ten (10) Year Period**

Year	No. of Staff	Loans Given (Millions)	Repayment (Millions)	Bad debts (Millions)	Arrears (Millions)
1988	1161	249	703	1.1	46
1989	1201	337	573	2.5	57
1990	1176	342	552	5.6	60
1991	1171	375	499	8	65
1992	1212	516	479	176	72
1997	1101	249	708	468	2,400
1998	1087	172	425	529	2,600

Table 4.2, Source: AFC 2004

AFC's repayment is clearly decreasing and the value of bad debts have sky rocketed by more than 500% in 10 years.

b) i. Repayment Statistics of KREP Small Holder Agricultural Project

K-REP DEVELOPMENT AGENCY			
SMALLHOLDER CREDIT PROJECT	Wundanyi		
Monthly Operation Statistics	Month		
		July	
	Last Month	This Month	Year to Date
MEMBERSHIP			
Number of Groups	14	1	15
Number of Members	342	24	366
i) Men	163	13	176
ii) Women	179	11	190
Number of New Groups		1	1
Number of New Members	172	24	196
i) Men	97	13	110
ii) Women	75	11	86
Number of Inquiries	23	8	31
SAVINGS STATISTICS			
No. of Active Savers	338	362	362
i) Men	159	172	331
ii) Women	179	190	369
Total Amount of Savings	943,500.00	144,662.00	1,088,162.00
i) Men	471,519.00	74,336.00	545,855.00
ii) Women	471,981.00	70,326.00	542,307.00
No. of Forfeitures			
Amount of Forfeitures			
No. of Savings Refunds			

Amount of Savings Refunds			
Net Savings	943,500.00	144,662.00	1,088,162.00
PORTFOLIO STATUS			
No. of Loans Disbursed	284	39	323
i) Men	142	19	161
ii) Women	142	20	162
Amount of Loans Disbursed	4,682,000.00	820,000.00	5,502,000.00
i) Men	2,469,000.00	405,000.00	2,874,000.00
ii) Women	2,213,000.00	415,000.00	2,628,000.00
No. of Loans Outstanding	228	235	235
i) Men	121	109	109
ii) Women	107	126	126
Amount of Loans Outstanding	2,801,237.00	2,953,600.00	2,953,600.00
i) Men	1,499,513.50	1,566,591.00	1,566,591.00
ii) Women	1,301,723.50	1,387,009.00	1,387,009.00
No. of Loans Due for Repayment	692	226	918
i) Men	323	119	442
ii) Women	309	107	476

Table 4.3, Source: K-REP 2004

Table 4.3, Source: K-REP 2004

Amount of Loan Due for Repayment	2,173,411.50	578,084.00	2,751,495.50
i) Men	1,198,253.50	475,455.00	1,673,708.50
ii) Women	975,158.00	282,629.00	1,257,787.00
No. of Loans Paid	694	233	927
I) Men	323	110	433
ii) Women	371	123	494
Amount of Loans Paid	2,381,628.50	667,690.00	3,049,318.50
I) Men	1,311,291.50	352,047.00	1,663,338.50
ii) Women	1,070,337.00	315,643.00	1,385,980.00
No. of Loans Prepaid	188	64	252
Amount of Loans Prepaid	208,217.00	89,606.00	297,823.00
Quantitative Repayment Rate		115.5%	110.8%
Qualitative Repayment Rate		100%	100%
DELIQUENCY RATES			
Arrears Rate			
I) No. of Late Payments			
ii) Value of Late Payments			
iii) Value of Late Payments as Share of Outstanding Portfolio			
Portfolio At Risk (PAR)			
i) No. of Unpaid Balances of Delinquent Loans			
ii) Value of Unpaid Balances of Delinquent Loans			

iii) PAR as share of Outstanding Portfolio			
SECTORS FUNDED			
No. of Clients from each Sector			
i) Dairy	25	3	28
ii) Crop Production	44	5	49
iii) Farming Inputs			
iv) Agri-Business	166	23	189
v) MSEs	36	8	44
vi) Poultry	13		13
Amounts Disbursed to each Sector			
i) Dairy	408,000.00	700,000.00	478,000.00
ii) Crop Production	585,000.00	950,000.00	680,000.00
iii) Farming Inputs			
iv) Agri-Business	2,814,000.00	485,000.00	3,299,000.00
v) MSEs	640,000.00	170,000.00	810,000.00
vi) Poultry	235,000.00		235,000.00

Table 4.3, Source: K-REP 2004

b) ii. K-Rep Development Agency - Smallholder Agriculture Credit Project

(Terms for Credit Acquisition)

This is an initiative of K-Rep development agency to access smallholder farmers in rural areas with credit for agricultural intensification, hence high productivity. They target beneficiaries as small – scale crop producers, dairy farmers and entrepreneurs with business that have strong backward and forward linkage to Agriculture.

Eligibility

Loans are advanced to smallholder farmers who fall within project areas and have registered and complied with rules and regulations of K-Rep and their respective group.

The group

- The group must meet the following conditions:
- Be in a specified project area where they can be accessed.
- Be registered with relevant government authority.
- Members must be currently engaged in farming or other Micro – Agricultural related activities and of good character.
- Be in a group of 20 to 30 members who are 18 years and above and not close relatives.
- Register with K – Rep small holders’ agriculture credit project.

- Open a group savings bank account for members' savings.
- Be cohesive and well managed with capacities to administer loans funds.
- Be willing to meet as directed by KDA.

Loan Collateral

K-Rep provides loans to small – scale farmers who lack conventional form of securities to borrow from commercial banks. These loans are secured through alternative means:

Cash Collateral: Members must contribute a minimum of 10% of their 1st loan in the group's savings account.

Group Guarantee: group members are collectively liable to K- Rep in event of one member defaulting.

Character: through group participation and general relationship with other group members the character of a member, his/her honest integrity and commitment to the group and farming is known.

4.1.2 Savings

AFC doesn't offer any facilities for savings. It is all about credit. Once you have adequate security, and a plan, you can access the credit.

KREP's small holder facility, advocates for forced savings to reduce the level of risks. The credit given has a ratio to the level of savings e.g. 1 to 5 times.

4.1.3 Management Information Systems

AFC still uses manual systems to tabulate the billions of shillings disbursed over the years. This sounds cumbersome. The records are again kept at the head office.

KREP small holder relies on the Management Information System set up by the KREP Development Agency. Even at the branch level the credit officers keep up-to-date repayment information.

4.1.4 Loan Sizes

In AFC's case this is based on an acreage estimation of Ksh. 11,000. The least number of acres financed are 5. Therefore the lowest loan size is Ksh 55,000. The highest ceiling is however not clear. The main argument put forward by the managers is that it keeps on changing.

KREP small holder credit project gives a minimum of Ksh 10,000 and a maximum of Ksh 200,000

4.1.5 Linkage to Markets/Others Services

The history of AFC is rich with collaboration and Networks with other organizations to help the farmers market their products. The organizations

include, Kenya Farmers Association and Kenya Seed Company. Others were government departments like, Prisons and the armed forces. These guaranteed markets to farmers. These arrangements have since collapsed,, leaving the farmer to fend for himself.

KREP has not ventured into other activities beyond credit provision. They have adopted an approach of, everybody should provide what he/she best understands.

4.1.6 Outreach

AFC relies on government officers mostly from the Ministry of Agriculture and Livestock to reach the farmers. Whereas it has credit officers, their capacities are over stretched. Most districts have only 2 field officers. They cannot cope with the demand and terrain. The farmers then have to go through government officers, for business plans and advice. Sometimes they have to visit private consultants at a fee. This makes the cost of credit to hike substantially.

4.1.7 Security

A.F.C absolutely accepts only hard security. This is in the form of land titles, bank guarantees and shares in reputable institutions. However good your plan reads it can never be funded without tangible security.

KREP relies on group solidarity and forced savings. Members of your group recommend you for a loan. If you default then they remain at risk. This is friendly to the poor segment of the society.

Interest

Rate of interest

Interest

Rate of interest

Table 4-4, Source: Author 2004

(b) Opinion of Farmers on AFC

Waiting time	Too long	42
	Appropriate	5
	Short	0
Interest	Too high	47
	Average	0
	Too low	0
Information on status of credit	Too slow	31
	Appropriate	16
	Too fast	0
Loan sizes	Based on farm needs	6
	Determined by funds available	13
	Appropriate	28
Technical advice	Good	14
	Poor	20
	Average	3
Marketing	Completely involved	3
	No input	12
	Average	22
Process of valuation	Expensive	47
	Average	0
	Cheap	0

Table 4.4, Source: Author 2004

AFC is evidently not the lending institution of choice because you not only wait exceedingly long for your loan advancement, but their interest rates are too high, loan sizes uncertain, information on status of credit, too slow, they offer very little technical advice and their valuation process is too expensive for the average farmer.

The responses recorded were obtained from 47 farmers in four branches. All of them have received credit from Agricultural Finance Corporation. Opinion of farmers on the various aspects of the organizational performance can be summarized as

4.1.8 Waiting Time

Whereas the policy talks of an average of one month for loan processing, this is not the practice. The farmer needs to fill the forms, consult government officers and eventually see his/her properly valued. Then the loan committee must sit and forward their recommendations to the head office. The process sometimes takes six months or even longer. For seasonal credit, it defeats the purpose as crops depend on weather.

4.1.9 Interest

The branch managers were not clear on this. A figure of 30% per annum was quoted by some of them and even the farmers. It was however, not authoritatively declared.

4.1.10 Information

Most of the farmers feel that they need regular statements on the status of their loans. What they receive at present takes a little longer than necessary.

4.1.11 Loan Sizes

The majority felt that the loan sizes are appropriate. This could be attributed to the fact that most of those loaned have other incomes to supplement their operations.

4.1.12 Technical Advice

Farmers indicated that more extension staff needs to be deployed to assist them do better crop/animal husbandry. This would enable them get better yields to improve their living standards and repay credit.

4.1.13 Marketing

In the past the farmers appreciated linkages to markets. Today, the story is miserable. They are calling for a concerted intervention to help them sell at competitive prices.

4.1.14 Process or Valuation

All the Farmers felt that this process is so expensive. It makes the cost of credit shoot tremendously. It also delays the disbursement process quite a lot.

A measure needs to be devised to make it less expensive and short.

4.2 Lending Methodologies

AFC uses individual lending approach. Other organizations use Group Solidarity.

4.2.1 Individual Lending Methodology

Strengths

- (i) The farmer stands for himself and has a drive to repay the loan. Failure would mean loss of his/her security.
- (ii) The institution is adequately cushioned incase of default. There is ready security (properly) to sell to recover the loan.
- (iii) The farmer determines the period to obtain credit and can effectively plan his/her repayment calendar.

Weaknesses

- (i) It alienates the poor farmers who have no substantial security to pledge.
- (ii) A study of KREP small holder project and AFC shows that security is not the only determinant of good repayment. KREP has over 95% repayment rate compared to AFC's under 60% repayment rate.
- (iii) The farmer doesn't enjoy the group support (peer pressure) and advice as in the group solidarity lending.

4.2.2 Group Solidarity Lending

How Farmers Across Societies Use Group Solidarity Lending

Strengths

- (i) Makes credit accessible to poor farmers without tangible collateral.
- (ii) Team work enables farmers to copy the successful ones.
- (iii) A lot of information and support is provided during group meetings.
- (iv) Problems are shared amongst the group members.
- (v) Defaulters are tracked by their own group members who know them well. Loan appraisal is also done by the group members who understand their neighbours better than a lending institution.

Weaknesses

- (i) Puts all members at risk when a few default.
- (ii) The institution can easily loose when the group integrates. It is difficult to follow members into their homesteads when they are no longer meeting.

4.3 Financial Services Matrix

This FGD tool was applied in a group, Njukini Nyayo in Taveta division of Taita/Taveta District. It shows how different social strata of people use services from various institutions. Stones were used to plot the scores. They were based on a scale of 0 – 5.

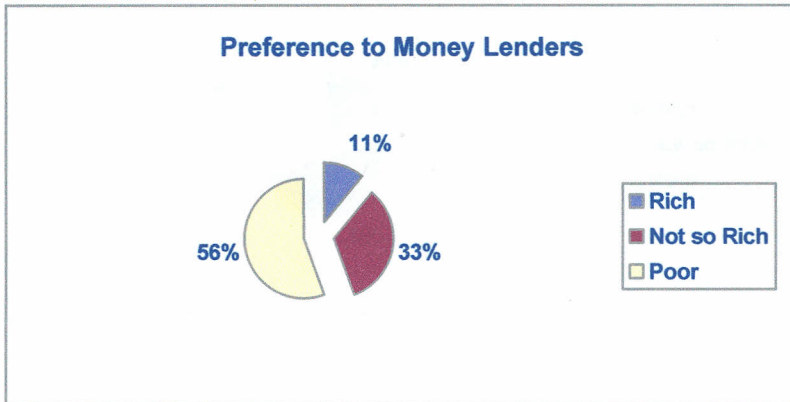
5 is the best score

How Farmers Across Social Strata Use different Institutions to Access Financial Services

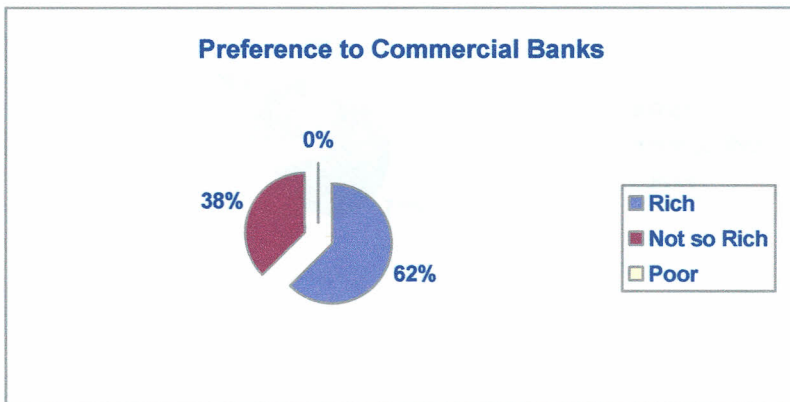
	Rich	Not so Rich	Poor
Money lender	1	3	5
Commercial Bank	5	3	0
Sacco	3	5	2
MFI	2	5	3
AFC	5	2	0
Savings club	0	3	5

Table 4.5, Source: Author 2004

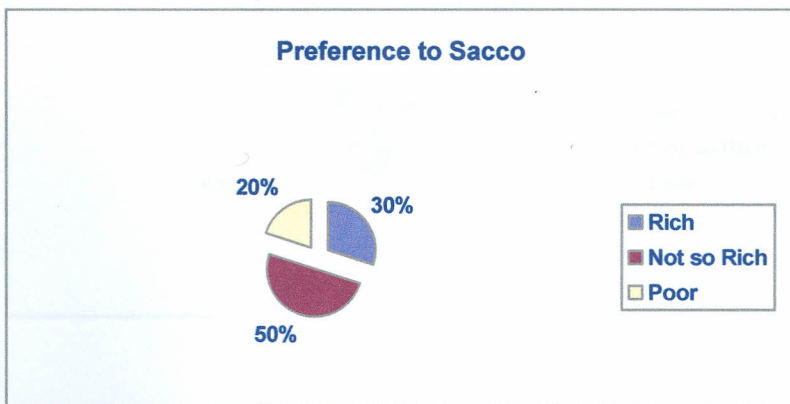
Figure 4.5, Source: Author 2004



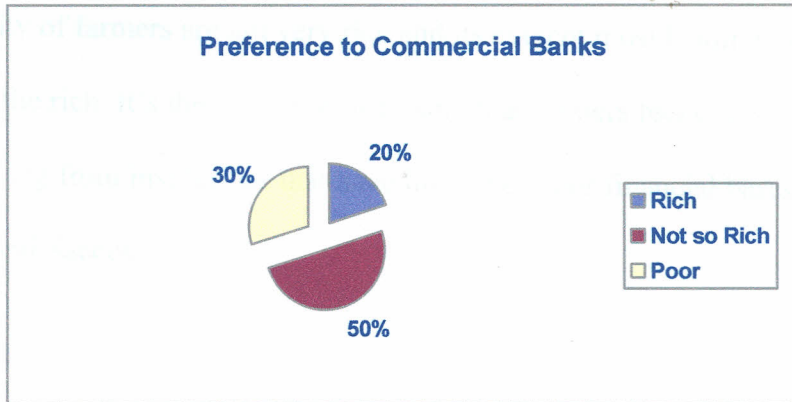
(a)



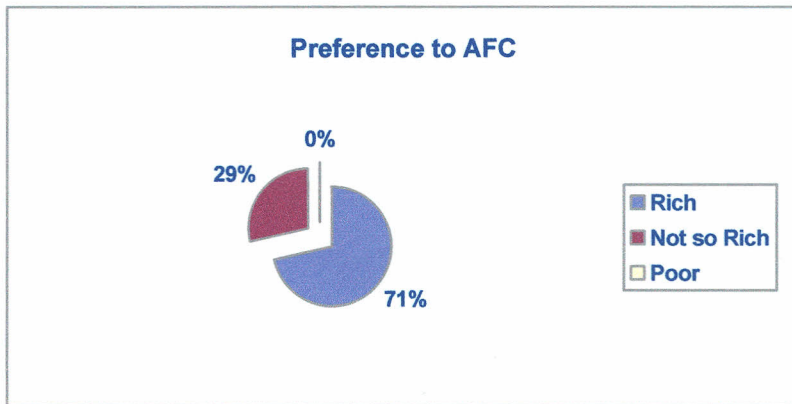
(b)



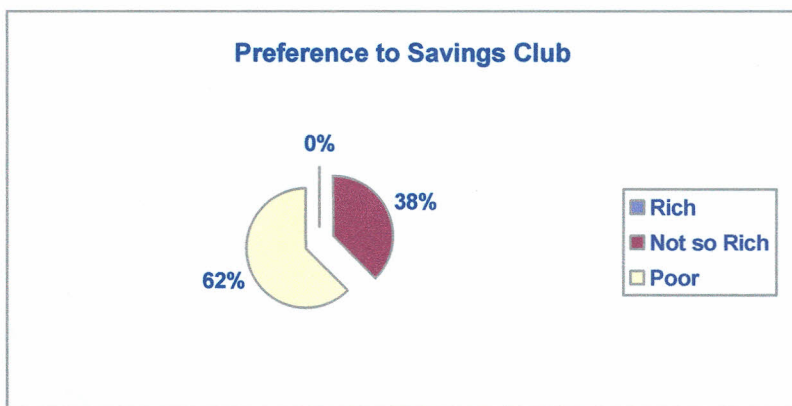
(c)



(d)



(e)



(f)

Figure 4.5, Source: Author 2004

Majority of farmers are not very rich and its evident most lending institutions prefer the rich. It's therefore not surprising that farmers feel comfortable borrowing from institutions that have limited or poor financial bases as savings clubs and Saccos.

Credit Institutions

Table 3.3, Source: AFC

If this trend (in the personality analysis) is to be assumed throughout the country then it's clear that AFC has had timing for loan disbursement

4.6 Seasonality Analysis

Parameter	High Season	Low Season	Reasons	Opportunities for intervention
Income	July – October	January to May	-	-
Expenditure	November to April	July to November	-	-
Savings	August to October	December to April	-	-
Credit	January to April		-	-

Table 4.6, Source: Author 2004

If this trend (in the seasonality analysis) is to be assumed throughout the country then it's clear that AFC has bad timing for loan disbursement

Effect of credit on Production per Acre

Production in Bags	Number of Farmers	
	Before Credit	After Credit
0-2	3	0
3-5	7	3
6-8	11	9
9-11	13	19
12-14	10	11
15-17	2	4
18-20	1	1

Table 4.7, Source: Author 2004

After interviewing 47 farmers who have taken credit from AFC, the following results were found. The table above shows the effect of credit on production per acre per farmer before and after credit was given.

Major Problems Affecting Agricultural Production in Nigeria

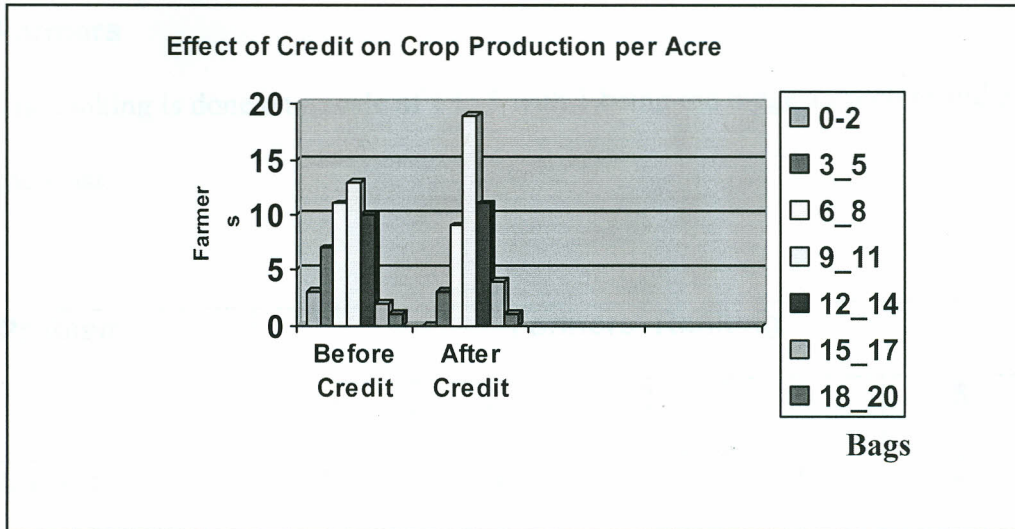


Figure 4.7, representing Table 4.7 Source: Author 2004

Conclusion

It's evident that with credit crop production increased remarkably with farmers within the average highest production of 10 bags increasing from 13 to 19.

References

Books

Table 4.3, Source: Author 2004

Major Problems Affecting Agricultural Lending as Ranked by Farmers

The ranking is done on a scale of 1 to 5 with 1 being the biggest problem and 5 the least.

Problem	Farmers' Ranking				
	1	2	3	4	5
Lack of Finances	13	17	7	8	2
Poor Access to Markets	20	10	6	6	5
Weather	7	13	7	10	10
Infrastructure	2	4	16	13	12
Pests	2	3	10	12	20

Table 4.8, Source: Author 2004

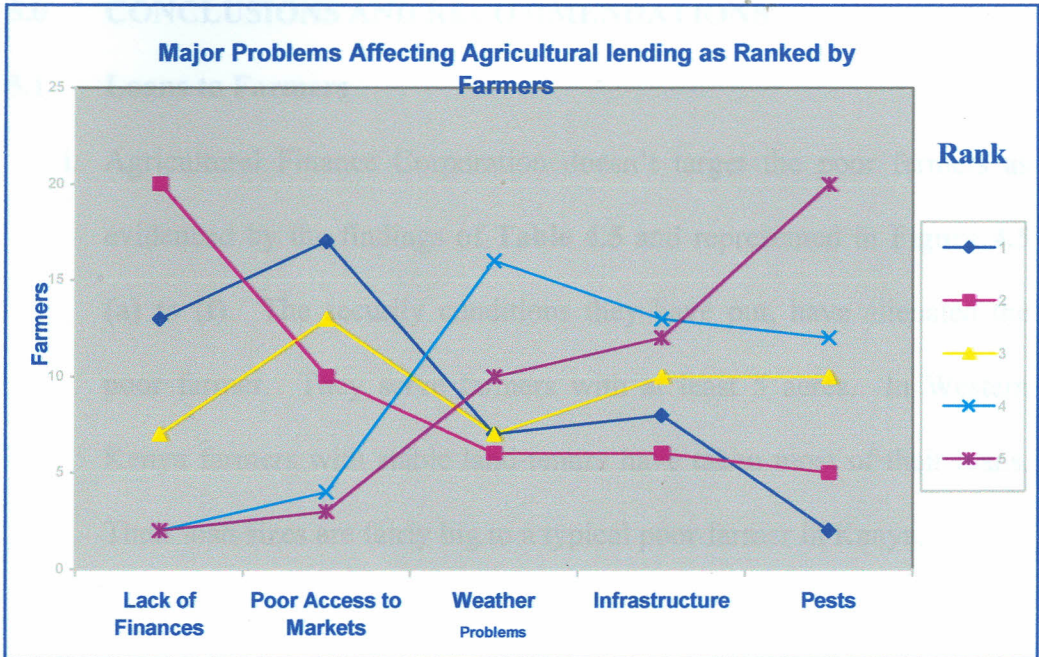


Figure 4.8, representing Table 4.8 Source: Author 2004

There is an important knowledge which brought about by separation of credit.

It's recommended to be funded by the lowest level of the below Rs 50,000 to allow small scale farmers pay for this can be achieved through networks. The rest of credit recovery can be done to groups collecting on behalf of the cooperative and bankers.

iii. No proper linkage of the farmer to Market available. This is an arrangement that A.P. used to be in handment.

5.0 CONCLUSIONS AND RECOMMENDATIONS

5.1 Loans to Farmers

- i. Agricultural Finance Corporation doesn't target the poor farmers as evidenced by the findings of **Table 4.5** and represented in **Figure 4.5 (a) to (f)**. The security conditions they have put, have alienated the poor farmer. They serve farmers with at least 5 acres. In Western Kenya farmers with stable land tenure have taken most of their loans. Their loan sizes are fairly big to a typical poor farmer in Kenya.

It's recommended that the timing of credit (as shown in **Table 4.6**) should be pegged to the aspects like weather especially for seasonal credit.

- ii. There is an improvement in yields brought about by acquisition of credit.

It's recommended that AFC reduces the lowest loan size to below Kshs. 50,000 to allow small scale framers benefit. This can be achieved through networks. The cost of credit recovery can be taken to groups collecting on behalf of the corporation and banking.

- iii. No proper linkages of the farmer to Market are done. This is an arrangement that AFC used to do but abandoned.

It's recommended that working relationships with marketing organizations like co-operatives be established. This would even ensure better repayments. Some money can also be invested in market surveys and researches.

5.2 Repayment

The repayment rate of Agricultural Finance Corporation is worrying. It is a subject that they don't want discussions on. Findings in **Table 4.2** reveal that bad debts and arrears are steadily increasing. Between 1992 and 1997 the value of arrears increased by 3300% and stood at 2.6 billion by 1998. No subsequent reports could be accessed after 1998. Perhaps nobody feels the loss directly since the money is from the state.

Good repayment rates can be achieved even without tangible securities like land titles.

It's recommended that all loans in arrears must be repaid immediately. Political goodwill is required; information from the branches show that politics was used to shield defaulters. Even some defaulters who were able to pay, didn't see the need as AFC officers felt intimidated by the prevailing forces.

A decision also needs to be taken on what can not be recovered. AFC can then start afresh and build a clean portfolio and a balance sheet.

5.3 Facilities for Savings

Farmers need a facility for savings. Credit extension is good but there are farmers who just need an opportunity to save. They can later invest their savings in Agriculture.

It's recommended that saving facilities need to be established immediately. It may mean change of registration. At one point there was an idea of turning Agricultural Finance Corporation into a Bank. Whereas it may have a few shortcomings like, a change of focus, it would create a facility for savings for the farmer. In the meantime other registrations can be explored to enable the farmer keep at least part of the proceeds.

5.4 Information Management

The management information system is very poor. It takes too long to know the portfolio that is threatened.

It's recommended that a comprehensive data base (MIS) needs to be put in place in AFC. At present management has little information to base their judgments on. Modern institutions involved with finance receive information on repayments on a weekly and sometimes even daily basis. One month in a credit world is too long. The defaulter may have room to interfere even with the security. Again through information, the loanee can be advised in good time.

Even on employee performance a sound MIS enables the management to evaluate the performance of its staff.

The loan approval/disbursement process is slow and expensive. The various stages, from the branch and later forwarded to the head office makes it long. Property valuation is very costly to the farmer.

AFC as a matter of urgency must source for a comprehensive package of data information management. It will improve the efficiency of the organization. The situation as its today is pathetic.

Its management can learn from what other Banks and Micro Finance institutions have. It should establish a data dedicated MIS department.

5.5 Funding and Policy vis-à-vis Agricultural Finance Corporation

Agricultural Finance Corporation is so much dependent on the government for its existence. Even the policy decisions emanate from the ministry of Agriculture.

Currently the policy decisions are made from the ministry of Agriculture. This leaves little room for creativity, innovation and adjustments to face actual situations. It's recommended that, where as the Government support is desirable, the organization could operate 2 credit windows. One would strictly be modeled along modern financial institutions, disbursing credit

and charging at market rates. The other window could be friendly to the poor farmers. This can then receive subsidies from the Government.

The financial requirements of AFC can be met through loans from other financial institutions. This would enable it to meet all the credit needs.

The financial market is wide enough to meet all the credit needs of the farmers. If the requests are made as loans to be refunded, then AFC can get enough to meet the loan applications at all times.

The Government's supervisory authority, however, should be maintained. Instead of exercising it through the ministry of Agriculture, this can best be done by the Central Bank. Once AFC's principal goal is to avail credit to farmers, then it should at best be seen as a financial intermediary. It should then be guided and evaluated by the Central Bank that has better specialists than the ministry of agriculture.

5.6 Ownership of AFC

The performance of a private sector organization shows that Agricultural financing is very possible.

It's recommended that ownership of AFC should be re-looked at. It should be a private concern with Government support programmes targeting the vulnerable farmers. The possibility of farmers buying shares into it can be explored. This would make them develop a bigger interest and stake into it.

It should however, maintain its mandate to the farmers. It should not get swallowed up in the Commercial Bank drives like the Cooperative Bank. This condition should be maintained so that the farmer doesn't let go this important institution for agro-financing.

5.7 Cost of Credit

Its interest rates although complained about are not higher than the market. It only needs to streamline areas like, property valuation, which contribute to a hike in the cost of credit. Again if the loan portfolio could be expanded, then it can contribute to more interest income. The possibility of lowering the lending rates can then be explored in future. One concern is to be honest with all the fees charged. The farmer should not see some of them as surprise, it demoralizes him/her. There is also an abundant loss of trust when some conditions appear to have been understated or not said at all.

Interest and other fees also need to be put in a business friendly language. Institutions (financial) charge many fees but gain acceptance because of the language used.

In order to reach poorer farmers AFC should use other lending methodologies. The group lending approach doesn't insist on tangible securities like land titles. At present poor farmers cannot access credit from AFC because of the security demanded. Majority of the Kenyan farmers

have small farms and require just a little credit to enable them increase production.

A working relationship needs to be established between institutions providing credit to Agriculture and marketing associations or organizations. There is no need to increase production through credit provision, only for it to rot in the farms and stores. It is also illogical to sell products at prices less the unit cost of production.

Make all the branches cost centers. The branch managers should be given powers to run their branches profitably. The headquarters should only do evaluations of performance. Funding should be tied to the needs of branches plus repayments. Branch managers should look for sources of finance and be ready to repay. The staffing at the branches should also be based on the level of business. Loss making branches should be analyzed. If they are incapable of attaining profitability then their operations should be stopped.

5.8 Further Research

It's recommended that a more comprehensive study needs to be conducted on Agricultural Finance Corporation. It should be able to look at the organizational structure and see if it is capable of carrying out its mandate. It should evaluate the calibre of staff and their technical capacity. There is also need to establish its liquidity and performance. Is the Government funding an institution that is technically insolvent? This must be established. If it is

not a viable institution, changes should be recommended which could even suggest an overhaul, or instituting a new entity, whichever is less costly and practical.

Continuous research and surveys need to be conducted on new needs and loan products. All these should be market driven. Some packages can also be adapted from successful Micro finance institutions and commercial Banks.

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Work Plan

1. Testing the Tools / Amending 4 Weeks

2. Field Interviews 2 Weeks

3. Data Analysis / Compilation of Report 2 Weeks

BUDGET: STATIONNARY

ITEM	COST	QUANTITY	TOTAL
Stationery	10,000		10,000
Transport	5,000	4 People	20,000
Lunch and Accommodation	5,000	4 People	20,000
Dues (Assistants)	500/ day	3 P/ple * 10 days	15,000
Professional Fees	2,000	12 Institutions	24,000
Secretarial Services	5,000		5,000
<u>TOTAL</u>			<u>94,000</u>

RESPONDENT BACKLOG**Work Plan**

1. Testing the Tools / Amending - 1 Week
2. Field Interviews -2 Weeks
3. Data Analysis / Compilation of Report - 2 Weeks

12. (i) How would you describe
.....

(i) Always available

(ii) Not always available
.....

(iii) Completely difficult

(iii)
.....

9. What would you like changed in the method of credit delivery?

Yes

14. (i) Do you do other business
.....

b) If yes in 14(a) above:

(ii)
.....

(iii)
.....

10. Any comments on Agricultural Credit in Kenya.

(iii)

.....
.....
.....

11. Which are your three (3) main farming activities in order of priority?

(a) Crop Husbandry

(b) Animal

Husbandry

(i)

(i)

(ii)

(ii)

(iii)

(iii)

12. How would you describe your markets?

(i) Always available []

(ii) Not always available []

(iii) Completely difficult to find []

13. Do the prices you sell at give you favourable returns on investment?

Yes

No

14. a) Do you do other business besides agriculture? Yes No

b) If yes in 14(a) above, which ones?

(i)

.....

...

(ii)

.....

(iii)

.....

QUESTIONNAIRE FOR INSTITUTIONS EXTENDING CREDIT

Name of Institution:

.....

Geographical Location:

.....

1. Which loan packages do you have

(i)

(ii)

(iii)

(iv)

2. (i) Do you lend to agriculture? Yes No

[] []

(ii) What are the key terms for this lending?

.....

.....

.....

3. Where do you obtain funds for agricultural lending?

(i)

(ii)

(iii)

4. What major obstacles do you face while lending to agriculture?

(i)

(ii)

(iii)

5. What Methodologies do you use to lend to farmers?

.....

.....

6. What can be done to improve financial services to farmers?

.....

...

7. Any general comments on agricultural lending

.....

...

.....

...

.....

.

8. (a) What is your loan portfolio size?

.....

.....

.....

(b) What is your default rate?

.....

.....

.....

(c) What are the powers of the branch managers?

.....
.....
.....

(d) How do you handle defaulters?

.....
.....
...

10. Which other institutions do you relate with during lending?

.....
.....
.....

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