DOCUMENT RESUME

04302 - [B3474705]

Credit Programs for Small Farmers in Latin America Can Be Improved. ID-77-1; B-159652. December 9, 1977. 33 pp. + 4 appendices (12 pp.).

Report to the Congress; by Elmer B. Staats, Comptroller General.

Issue Area: International Economic and Military Programs: U.S. Development Assistance Overseas (603); Food: Agriculture Productivity and Resource Availability (1702); Food: Alleviating Famine and Malnutrition Abroad (1706).
Contact: International Div.
Budget Function: International Affairs: Foreign Economic and Financial Assistance (151); Agriculture: Farm Income Stabilization (351).
Organization Concerned: Agency for International Development.
Congressional Relevance: House Committee on International Relations; Senate Committee on Foreign Relations; Congress.
Authority: Foreign Assistance Act of 1973.

Providing credit to small farmers is one way the Agency for International Development (AID) has implemented the congressional mandate to improve the lives of the poorest people in developing nations. AID has been successful in providing credit to small farmers in Latin America, but more can be done by better identifying small farmer target groups and by developing consistent and more appropriate criteria for qualifying small farmer recipients of credit assistance. Findings/Conclusions: The United States has provided about $54 million of credit assistance yearly to rural credit programs, about two-thirds of which has gone to Latin America. The objective is to increase the food production and income of small farmers by providing credit to operators of small farms who are considered too high a risk to receive credit from the traditional banking systems. Interest rates charged to farmers on AID-funded loans were generally lower than those of local financial institutions. Economic, social, and other conditions vary so widely from country to country that adopting rigid guidelines for identifying farmer target groups is not practical; thus, some degree of flexibility is needed. However, broadly defined target groups and criteria for direct credit aid to farmers should be refined so that AID can better meet its objective of getting credit aid down to more small farmers and to be more responsive to the overall objective of aiding the poorest majorities. Recommendations: The Administrator of the Agency for International Development should follow up on recent AID initiatives to delineate more clearly small farmer target groups and to see that the definition of target groups in future small farmer credit programs is consistent with the Agency's overall policy and poverty benchmarks. (Author/SC)

4705

043020

REPORT TO THE CONGRESS

BY THE COMPTROLLER GENERAL OF THE UNITED STATES

Credit Programs For Small Farmers In Latin America Can Be Improved

The Agency for International Development has improved its efforts to provide credit assistance to small farmers in Latin America. However, in some countries, target groups to which credit may be made available are too broadly defined.

The Agency can better meet its overall objective of assisting the poorer majorities, and its usual practice of restricting credit to operators of small farms outside the scope of traditional banking systems, by refining target group definitions and criteria.

ID-77-1

DECEMBER 9, 1977

COMPTROLLER GENERAL OF THE UNITED STATES
WASHINGTON, D.C. 20548

B-159652

To the President of the Senate and the
Speaker of the House of Representatives

This report describes the extent to which the Agency for International Development is directing credit assistance to small farmers in Latin America. It also suggests ways in which the Agency can provide more assurance that the truly small farmers are being reached.

We made this review not only to determine how well agricultural credit is reaching the small farmers and is used to improve their productivity but also to find out how well the Agency is following the congressional mandate to improve the lives of the poorest people in developing countries.

Our review was made pursuant to the Budget and Accounting Act, 1921 (31 U.S.C. 53), and the Accounting and Auditing Act of 1950 (31 U.S.C. 67).

We are sending copies of this report to the Acting Director, Office of Management and Budget, and to the Administrator, Agency for International Development.

Elmer B. Staats

Comptroller General
of the United States

COMPTROLLER GENERAL'S
REPORT TO THE CONGRESS

CREDIT PROGRAMS FOR SMALL FARMERS IN LATIN AMERICA CAN BE IMPROVED

D I G E S T

Providing credit to small farmers is one way the Agency for International Development has implemented the congressional mandate to improve the lives of the poorest people in developing nations. The Agency has been successful in providing credit to small farmers, but more can be done by better identifying small farmer target groups and by developing consistent and more appropriate criteria for qualifying small farmer recipients of credit assistance.

The United States has provided about $54 million of credit assistance yearly to rural credit programs, about two-thirds of which has gone to Latin America. The objective, in tandem with other forms of assistance, is to increase the food production and income of small farmers by providing credit to operators of small farms who are considered too high a risk to receive credit from the traditional banking systems.

Most small farmers who use credit obtain it from moneylenders, relatives, and friends. Credit from such informal sources (estimated to be as much as $75 billion) is five times greater than that from formal credit institutions, such as banks and the Agency. Interest rates charged by informal sources are often as much as four times greater than those charged by formal sources. (See pp. 2 and 29.)

Interest rates charged to farmers on Agency-funded loans were generally lower than those of local financial institutions. How well interest rates on Agency loans will cover defaults and administrative expenses is uncertain. Host countries and international financial institutions recognize that lower interest rates and associated loan services are subsidy elements aiding poor farmers. (See pp. 29 and 30.)

Tear Sheet. Upon removal, the report cover date should be noted hereon.

ID-77-1

REACHING POOR MAJORITY SMALL FARMERS

GAO found that credit under the program was being made available to groups defined in broad or general terms in some countries. Better identification of target groups and clearer definitions of qualifying criteria, in GAO's view, would help the Agency better achieve its general objective of providing credit to operators of small farms.

GAO recognizes that identifying farmer target groups and establishing criteria to direct credit aid to small farmers outside normal banking channels, and within the poorer majorities, is very difficult. Economic, social, and other conditions vary so widely from country to country that adopting rigid guidelines is not practical; thus, some degree of flexibility is needed.

GAO believes, however, that broadly defined target groups and criteria should be refined so that the Agency can better meet its objective of getting credit aid down to more small farmers and at the same time be more responsive to the overall objective of assisting the poorest majorities. The agency agrees and is continuing to work in this direction. (See p. 22.)

Defining target groups and poor majorities is difficult, and no single criterion for defining a small farmer may be appropriate, as the Agency points out. GAO recognizes this and does not suggest that the Agency adopt or restrict itself, for example, to the World Bank's landholdings criterion. GAO points out, however, that landholdings has been the criterion most often used by the Agency in defining target groups. (See p. 22.)

In response to a request for comments, the Agency said that they agreed with most of the proposed recommendations and have taken positive action to implement them. (See p. 5.)

The Agency has taken steps to improve its guidelines and procedures for analyzing, identifying, and defining poor farmer target groups before project implementation and to provide more guidance on a continuing basis to the Mission in this process. In GAO's view, the Agency should continue its efforts to improve its small farmer credit programs. (See p. 24.)

The following recommendations are being made to help assure that positive actions already begun are translated into actual improvements in current programs--to the extent possible--and in future small farmer credit programs.

RECOMMENDATIONS

GAO recommends that the Administrator of the Agency for International Development follow up on recent Agency initiatives to (1) more clearly delineate small farmer target groups and (2) see that the definition of target groups in future small farmer credit programs is consistent with the Agency's overall policy and poverty benchmarks. (See p. 24.)

Contents

		Page
DIGEST		i
CHAPTER		
1	AGRICULTURAL CREDIT IN DEVELOPING COUNTRIES	1
	Overall goals of small farmer credit programs	1
	Who is providing credit?	2
	Scope of review	5
	Agency comments	5
2	AID CREDIT EFFORTS--PAST AND PRESENT	7
	What is the congressional mandate and how has AID responded?	7
	AID's overall objectives	8
3	REACHING THE POOR MAJORITY SMALL FARMER	12
	How are AID target groups identified?	14
	Who qualifies as a small farmer?	14
	AID's small farmer credit programs in Latin America	15
	Bolivia	16
	Costa Rica	18
	Dominican Republic	18
	Haiti	19
	Honduras	19
	Panama	21
	Conclusions and observations	22
	Recommendations	24
4	IMPLEMENTING AID CREDIT PROGRAMS	25
	Credit mechanisms	26
	Credit availability and interest rates	28
	Technical assistance	31
	Conclusions and observations	32
APPENDIX		
I	Selected GAO reports on U.S. agricultural programs	34
II	Reaching the poor majority: factors in loans examined	35

APPENDIX | Page

III Letter dated January 17, 1977, from the Auditor General, Agency for International Development 43

IV Principal officials responsible for activities discussed in this report 44

ABBREVIATIONS

AID Agency for International Development

GAO General Accounting Office

CHAPTER 1

AGRICULTURAL CREDIT IN DEVELOPING COUNTRIES

The lack of credit resources for financing modern production and the absence of effective systems for distributing credit to the small farmer has seriously retarded agricultural development in developing countries. Even in countries where agriculture produces the bulk of gross domestic product, 1/ less than 10 percent of institutional credit is available to rural areas, and only a small fraction of that is available to small farmers.

Farmers in developing countries receive most of their credit from loans for one season or for 1 or 2 years. The loans are used mainly to purchase seed, fertilizer, and pesticides; some longer term loans are available to purchase livestock and farm equipment. Credit is critical for small farmers, particularly if they are to produce a marketable surplus and contribute to the development process. Credit is also essential in the long-term process of capital formation on small farms.

OVERALL GOALS OF SMALL FARMER CREDIT PROGRAMS

The objective of agricultural credit programs has been to reduce farmer dependence, especially that of small farmers, on the village moneylenders who, it was thought, exploited them through usurious interest rates.

Today, the World Bank and other international agencies are supporting programs whose primary goals are to increase food production. Many agencies, such as the Agency for International Development (AID), have the added goals of increasing small farmer income and reducing their dependence on usurious moneylenders. Authorities have found that per-acre productivity on small farms is often higher than that of large farms.

1/Gross domestic product is that portion of gross national product which results in an accrual of income for nationals as a result of domestic activity.

WHO IS PROVIDING CREDIT?

The United States is not alone in its credit assistance efforts to small farmers. The World Bank 1/ estimates worldwide institutional loans for agriculture in the developing countries at $15 billion; Latin America's share would be about $6 billion. However, the bulk of agricultural credit outstanding in these countries originates from noninstitutional sources and is estimated to be about five times greater than institutional credit, or about $75 billion.

Formal credit institutions

Formal credit institutions lend most of the funds available for agricultural credit to the larger farmers. The small farmers, for reasons of risk and cost of servicing, are generally left out. In recent years, however, new credit institutions have been established and existing ones strengthened so that more small farmers can get credit. In Latin America about 15 percent of the farmers obtain institutional credit. Formal institutions providing credit to small farmers are as follows.

Cooperatives and credit unions

Credit unions, multipurpose cooperatives, and other farm organizations are the more popular institutions in developing countries for providing credit to small farmers. These group-credit institutions are able to expand alternative credit channels and to provide technical, fertilizer, and marketing assistance to farmers. They can provide all services needed and reach many small farmers with relative ease in comparison with other systems. They are generally better able to mobilize local resources and are better placed to operate savings programs.

Local banking systems

The agricultural cooperative and commercial banks, most of which are common to all countries, are characteristic of local banking systems which provide credit to farmers.

1/The International Bank for Reconstruction and Development is often referred to as the World Bank. The World Bank Group consists also of the International Development Association and the International Finance Corporation.

The agricultural banks are the most notable of those providing credit to farmers and have advantages in raising outside funds (government funding). Like cooperatives, the banks are more accessible to the rural poor. For example, the government-owned agricultural bank in Colombia had 685 branches with $870 million in loans outstanding to 442,000 farmers as of June 1975.

Commercial banks have extensive branch networks into rural areas. They are generally more efficient than government agencies and less prone to abuse and political pressure. However, commercial banks tend to concentrate on short-term lending and to avoid small farmers because of high administrative costs.

International financial organizations

Many countries have obtained large loans from the World Bank, the Inter-American Development Bank, and other international financial institutions specifically to expand the funds available for lending to small farmers. These institutions, which in the past have concentrated on large capital projects, are expanding their efforts to help developing countries meet small farmers' credit needs.

World Bank commitments to agriculture were $2.6 billion from 1968 through 1973, $1.4 billion of it in credit. Approximately 25 percent of all credit financed by the World Bank was for small farmers. During this period, agricultural lending to the poorest countries exceeded $1 billion, more than half of it for farm credit.

The Inter-American Development Bank makes concessional loans from its Fund for Special Operations. This fund consists of direct contributions from member countries and about 68 percent represents the U.S. share. Conventional loans are made from ordinary capital, which is basically borrowed in private capital markets, with callable capital of the members as financial backing. All countries in the Americas are members except Guyana.

Agriculture currently accounts for 23 percent of the World Bank's lending activities. It loaned $228 million in 1974, with $36 million allocated for credit programs.

International credit unions

The World Council of Credit Unions is composed of associations from the United States, Canada, Australia, Latin America, Africa, Asia, the Caribbean, and individual credit unions from some countries which have no overall associations. The U.S. Credit Union National Association, Inc., works with AID to develop credit unions as a delivery system for making credit available to small farmers in less developed countries. Local credit unions, in turn, provide small loans to farmers for livestock, seed, insecticides, and farm supplies and equipment, along with technical assistance for improving agricultural practices.

The Confederation of Latin American Credit Cooperatives consists of national credit unions in 15 Latin American countries. Membership includes 124,000 credit unions, which in 1974 had 1,121,000 members. In 1974 credit unions affiliated with the Confederation loaned $180 million and held $165 million in membership savings.

Informal sources of credit

Relatives and neighbors

Small farmers borrow from other farmers--neighbors, friends, and relatives--who charge nominal interest rates and expect comparable financing when they need credit. In some Asian and African countries, friends and relatives provide about 50 percent of the loans; in Latin America, such loans constitute only 10 percent. Small farmers borrow from relatives and friends because they feel at ease with people they know the money is readily available, and little or no documentation is necessary.

Moneylenders

Many small farmers, especially those who borrow regularly, obtain loans from merchants, middlemen, and moneylenders at high interest rates. Some moneylenders have a monopoly and are able to charge rates much higher than competitive market levels. Noninstitutional lenders in certain Latin American countries charge more than 40 percent interest.

Moneylenders in some places compete with each other and charge rates which equate to the cost of institutional lending. Also, an AID-financed study of noninstitutional lenders in Ecuador indicates that this is an excessively maligned group which has a legitimate place in the system, particularly in servicing the small, high-risk, operating credit needs of farmers in the lower strata of the feasible credit range. Interest charges are high by conventional standards but are generally consistent with risk and costs. The study indicated that noninstitutional lenders are better equipped than institutional lenders to service credit needs of small farmers.

Informal credit sources are often convenient and familiar to the poor farmer and may require little or no documentation. The higher cost of credit, however, and general lack of technical aid and advice tend to keep the farmer from improving his economic and financial situation.

We suggest that AID remain alert to opportunities for encouraging host governments to seek greater participation in small farmer credit programs from commercial, international, and other formal lending institutions.

SCOPE OF REVIEW

AID has a mandate from the Congress to help the poor majority in developing countries raise their living standards beyond subsistence levels. AID programs are to concentrate on the major problem areas of food and nutrition, population and health, and education and should be marked by their involvement of the poor in the development process.

We made this review in Latin America to determine how well agricultural credit is reaching the small farmer and how it can be used to improve productivity. Latin America was chosen because it is receiving almost 66 percent of AID's credit program funds. Appendix I lists selected reports we have issued on U.S. agricultural programs.

At AID Headquarters in Washington, D.C., and U.S. Missions in Bolivia, Costa Rica, The Dominican Republic, Haiti, Honduras, and Panama, we examined applicable legislation, program documents, reports, correspondence, and other pertinent documents. We also discussed credit activities with U.S. Missions, host government officials, and representatives of international financial institutions. We visited cooperatives and other farmer organizations and met with small farmers who received credit.

AGENCY COMMENTS

In response to our request for comments, AID stated that they agreed with most of our proposed recommendations and have taken positive action to implement them.

AID also noted problems with some of the findings as presented in the draft report. These have been addressed and are discussed where appropriate in the report. The details were helpful in revising and finalizing our report.

CHAPTER 2

AID CREDIT EFFORTS--PAST AND PRESENT

During a 22-year period, the Agency for International Development and its predecessor agencies invested about $705 million, including counterpart funds (local currency funds generated by commodity import programs), and about 870 technical staff-years in farm credit programs worldwide. The annual flow since 1961 has been approximately $54 million and 55 staff-years, almost 66 percent of it to Latin America. In most countries, the World Bank, the Inter-American Development Bank, and other donors also made contributions and investments.

In addition to providing credit to small farmers, some AID programs provide credit for institution-building, and others are designed to increase production. Some programs feature direct loans to farmers, while others are directed at cooperatives.

WHAT IS THE CONGRESSIONAL MANDATE AND HOW HAS AID RESPONDED?

The Foreign Assistance Act of 1973 directed AID to give highest priority to undertakings which directly improve the lives of the poorest people of the host country. In 1975 this mandate was expanded to require that

"* * * greatest emphasis shall be placed on countries and activities which effectively involve the poor in development, by

"--expanding their access to the economy through services and institutions at the local level,

"--increasing labor-intensive production,

"--spreading productive investment and services out from major cities to small towns and outlying rural areas, and

"--otherwise providing opportunities for the poor to better their lives through their own effort."

The 1973 act mentioned several areas of specific interest, the first being to "increase agricultural productivity per unit of land through small-farm labor-intensive agriculture." The Congress required AID to assist in the development of cooperatives by specifying that not less than $20 million be made available during fiscal years 1974 and 1975.

AID has told the Congress it "enthusiastically supports the emphasis of the new legislation" and will do everything it can to implement the program. It has revised its budget presentations to reflect the three major aspects of the mandate--food, population, and education--and the projects in the presentation are discussed in terms of their impact on the poor. Also, some projects have been left unfunded because AID felt they would be inconsistent with the mandate's emphasis.

In October 1974 the House Committee on International Relations directed AID to report, in detail, on its efforts to implement the mandate. AID's response "Implementation of 'New Directions' in Development Assistance" dated July 22, 1975, discussed how various projects and programs focus on the poor majority and the problems and practical limits of working with the new legislation.

AID views New Directions food and nutrition activities as those that support rural production rather than agriculture in general. This approach envisions

--removal or reduction of the frequently negative effects of less developed country policies;

--provision of adequate physical infrastructure, e.g., improved farm-to-market roads, irrigation, etc.;

--agricultural research coupled with a variety of extension programs; and

--adequate production credit at a fair price.

AID also views credit programs as vehicles to encourage small farmers to save.

AID'S OVERALL OBJECTIVES

If the world is to meet the challenge of hunger, AID estimates that food supplies must double by the year 2000, and to meet this goal, it has the dual objectives of increased food production and increased net income for small farmers.

AID proposes to meet these objectives through a comprehensive program of rural development.

Economic incentives

Farming must be a profitable business if small farmers are to significantly increase food production. The preponderance of unsuccessful credit programs for small farmers has failed because farmers had no feasible way to profitably invest the credit extended them. Either there was no new (i.e., new to that farmer) applicable technology or the farmer was constrained by his aversion to risk; insufficient land; and/or lack of fertilizer, irrigation, or market for the increased production.

Institutional improvements

Farmers must be able to obtain credit, buy fertilizer, learn and apply modern technology, and have the distribution and marketing systems needed to sell their increased production. This requires building and improving such institutions as cooperatives, small business groups, local government agencies, and market information systems.

Improved and adapted technology

In developing countries, 80 percent of the farms are 12 acres or less and most are family farms. The technology needed for these tiny enterprises must be appropriate to their size, cheap enough to be afforded by the farmers, and simple enough to be useful at low levels of skill and education.

Producer and consumer links

Rural and urban populations, agriculture, and industry must become mutually supporting. Farmers must be linked to market towns. Effective demand must come from consumers in urban areas; this requires jobs and incomes to buy the farmer's product. Communication systems must be built up so that producer and consumer are aware of needs and opportunities. Distribution and storage systems are required to minimize price fluctuations and avoid "boom and bust" cycles.

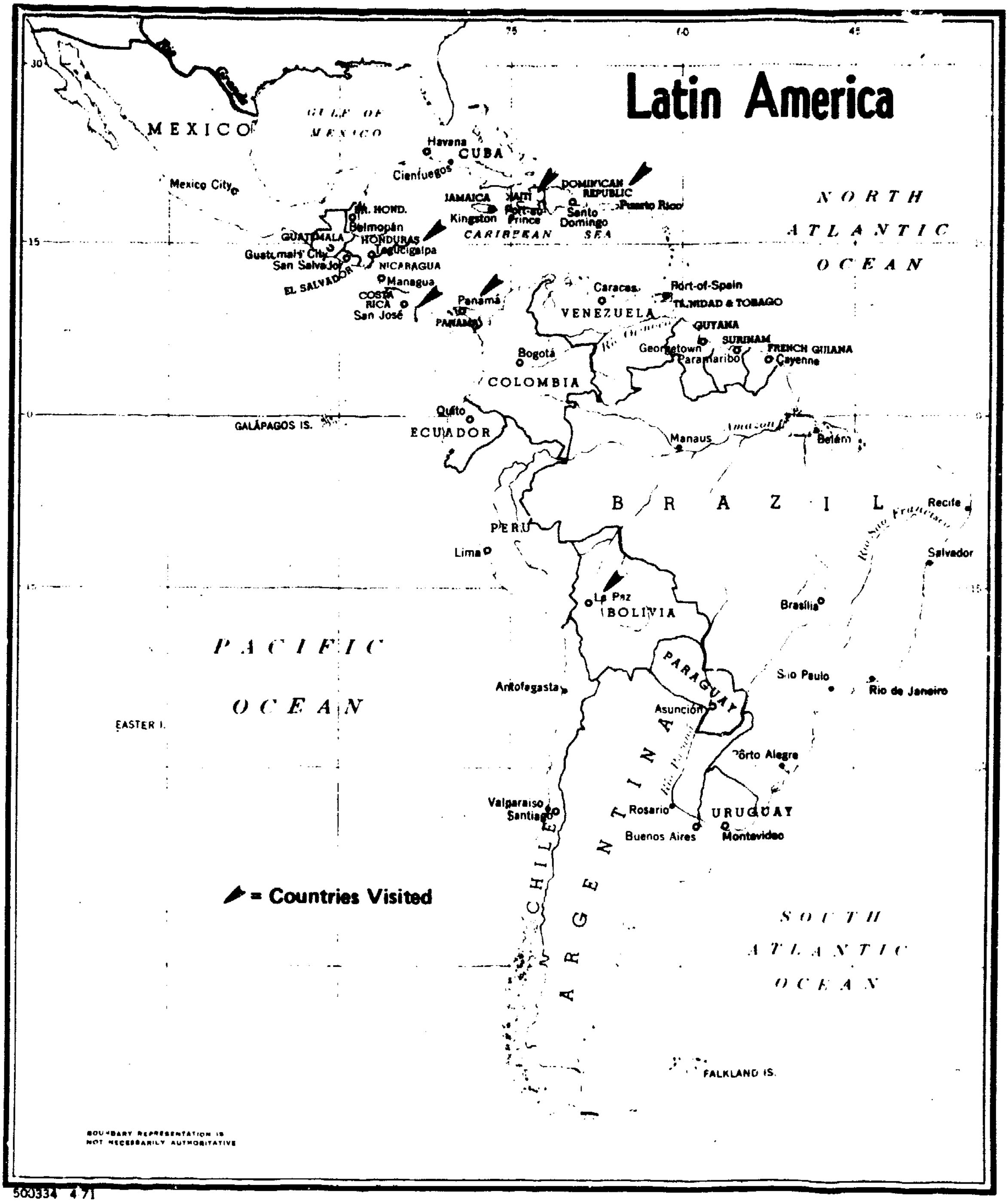
Possibly 10 percent of a country's harvest is lost to rodents, insects, and fungi. Proper storage, combined with effective use of pesticides, could substantially reduce these losses. 1/

Training of host country personnel

For many years AID and the Department of Agriculture have provided training in agriculture and related sciences as part of the overall U.S. foreign assistance program. During fiscal year 1975, more than 2,000 agricultural scientists, administrators, and technicians from AID-assisted countries received training--from short-term, on-the-job training to academic degree programs. To accomplish this, AID and Agriculture use varied resources, including the staffs of 72 U.S. land grant universities, other Federal agencies, State departments of agriculture, agriculture cooperatives, and private agri-business firms.

Courses are given in 36 major subjects, including agricultural cooperatives and agricultural credit. During fiscal year 1975, 232 persons from Latin America received agricultural training, but agency records do not show how many of them took these two courses.

1/For more information on this subject see our report to the Congress "Hungry Nations Need to Reduce Food Losses Caused by Storage, Spillage, and Spoilage" (ID-76-65, Nov. 1, 1976).


Latin America
MEXICO
GULF OF MEXICO
Havana
CUBA
Cienfuegos
Mexico City
DOMINICAN REPUBLIC
Puerto Rico
JAMAICA
HAITI
Kingston
Port-au-Prince
Santo Domingo
CARIBBEAN SEA
NORTH ATLANTIC OCEAN
BR. HOND.
Belmopán
GUATEMALA
HONDURAS
Tegucigalpa
San Salvador
NICARAGUA
EL SALVADOR
Managua
COSTA RICA
San José
Panamá
PANAMA
Caracas
Port-of-Spain
TRINIDAD & TOBAGO
VENEZUELA
GUYANA
SURINAM
FRENCH GUIANA
Georgetown
Paramaribo
Cayenne
Bogotá
COLOMBIA
GALÁPAGOS IS.
Quito
ECUADOR
Manaus
Belém
BRAZIL
Recife
PERU
Lima
Salvador
La Paz
BOLIVIA
Brasília
PACIFIC OCEAN
PARAGUAY
São Paulo
Rio de Janeiro
Antofagasta
Asunción
EASTER I.
Pôrto Alegre
Valparaiso
Santiago
Rosario
URUGUAY
Buenos Aires
Montevideo
ARGENTINA
CHILE
= Countries Visited
SOUTH ATLANTIC OCEAN
FALKLAND IS.
BOUNDARY REPRESENTATION IS NOT NECESSARILY AUTHORITATIVE
500334 4-71

CHAPTER 3

REACHING THE POOR MAJORITY SMALL FARMER

The Congress, in the Foreign Assistance Act of 1973, directed that future U.S. economic assistance focus on critical problems which affect the lives of most of the people in developing countries: (1) food and nutrition, (2) population planning and health, and (3) education and human resources development. The Congress also directed AID to give the highest priority to undertakings submitted by host governments which directly improve the lives of the poorest of their people and their capacity to participate in the development of their countries.

By the time the 1973 legislation (which AID helped develop) was well along in the Congress (it passed the House in July 1973), AID had begun to move in the directions contemplated by the new legislation, which was enacted in December 1973 and stimulated further movement in the New Direction. AID's detailed report on its efforts to implement the New Directions of development assistance was submitted to the House International Relations Committee in July 1975. It discussed the policy and procedural issues associated with implementing the reforms and pointed out certain factors affecting AID's capacity to produce dramatic results in the shortrun. AID reported that, although it must focus its attention on the broad poor majority, it must also be flexible in programing within that group. AID's July 1975 report stated that it uses the following benchmarks or standards of poverty to determine who comprises the poor majority:

1. Per capita income below $150 a year.

2. Daily diet of less than 2,160 to 2,670 calories (depending on the country).

3. Birthrates over 25 per 1,000 population, life expectancy of less than 55 years, infant mortality over 33 per 1,000, or access to broadly defined health services for under 40 percent of the population.

Under the per capita income criteria, the poor majority totals about 800 million people, or around 75 percent of the total population of AID-assisted countries. In some countries, more than 90 percent of the population is in this group; while in others, the proportion is far lower.

The World Bank defines poor majority small farmers as (1) families farming less than 13 acres or (2) farmers from the poorer half of a country's rural population where all farms are small in absolute size.

AID relies heavily on income levels to identify the poor where greater precision is impractical but notes that using income levels alone presents problems. For example, inflation and artificial exchange rates affect comparability; national per capita averages are often inappropriate, actual income can be difficult to measure, and data on persons with annual incomes of less than $150 is scarce.

In July 1975 AID defined the poor majority as including anyone in recipient countries whose annual income falls below $150 in 1969 prices. 1/ The following table, from AID data, shows the poor majority populations of four countries included in our review (Bolivia and Haiti were not included because income distribution data was not available).

Country	Total population	Poor majority population	Percent of total population
Costa Rica	1,700,000	200,000	14
Dominican Republic	4,300,000	1,600,000	38
Honduras	2,600,000	1,500,000	58
Panama	1,500,000	200,000	16

AID feels that such a uniform poverty standard should prove useful in considering intercountry economic assistance allocations, although final decisions will naturally reflect foreign policy concerns as well as the developing country's resources and general absorptive capacity. AID's policy is that every effort should be made to insure that its funds benefit a recipient country's poor population as defined by AID's poverty benchmarks.

1/The World Bank includes those whose per capita income falls below $50 in 1969 prices and those with incomes above $50 but below one-third of the nation's average per capita income. AID considers this definition too restrictive because it excludes many poor people that it feels should be eligible for U.S. assistance.

AID expressed concern that credit projects, developed and negotiated with host governments in 1973 and 1974, were being evaluated using AID poverty benchmarks that were not published until July 1975. AID poverty benchmarks are introduced and discussed only as additional data available, at least since July 1975, for use in defining poor majorities and developing target group definitions.

AID stated that, during the early years of the New Directions legislation (1973-75), sufficiently detailed information was not available in many countries to present a detailed profile of the poor majority target group. Accordingly, AID Missions used their best judgment in determining the nature of the AID target group.

HOW ARE AID TARGET GROUPS IDENTIFIED?

Although AID says its economic assistance programs must attempt to reach large numbers of poor people, its primary target group will often be a limited portion of the poor majority in each country. However, the programs are also designed to yield secondary benefits to as many of the poor as possible and to avoid worsening the plight of the poorest.

AID believes it is possible to identify primary beneficiaries of its assistance programs consistent with the mandate without needlessly limiting who may benefit. It emphasizes that major beneficiaries of an AID-assisted program or project should not be a country's prosperous elite--major merchants, bankers, industrialists, or farmers--even if they should happen to qualify because of some health or diet idiosyncracy under some benchmark, as this would contradict AID's policy and the spirit of the congressional mandate.

AID believes, that it must focus its attention on the broad poor majority, but preserve the flexibility needed to program effectively within that group in each individual case.

WHO QUALIFIES AS A SMALL FARMER?

AID has acknowledged that it has not developed, and probably will not attempt to develop, the precise definition of a small farmer. Accurate figures on the minimal economic farm size differ widely within countries, let alone across national boundaries and continents. Differing climates, soils, cropping patterns, and so forth, all serve to make rigid definitions difficult to sustain.

AID's project proposals usually describe the nature of the target group and its relationship to the total population. While an occasional better-off farmer may benefit from improvements made in the total system, the prime focus is on improving the quality of life of the poor farmer.

AID'S SMALL FARMER CREDIT PROGRAMS IN LATIN AMERICA

In response to the congressional mandate in the Foreign Assistance Act of 1973, AID is providing credit assistance to small farmers. However, in some countries the loan target groups are so broadly defined that they include farmers whose resources would keep them from being considered small, relative to the size and income of other farmers, or from being included in the poor majority.

In six countries we visited, approximately $47.6 million in credit had been committed to small farmer credit programs during fiscal years 1973-75, as shown below.

Country	Number of loans	Total value	Credit element	Credit extended as of January 1977
		(millions)		
Bolivia	3	$26.9	a/$10.5	$ 2.52
Costa Rica	1	7.9	b/ 0.5	-
Dominican Republic	1	12.0	9.0	5.08
Haiti	1	6.0	5.0	.12
Honduras	2	24.5	15.8	9.29
Panama	1	8.1	6.8	.78
Total	9	$85.4	$47.6	$17.79

a/An additional $2 million is to go to small farmer cooperatives for processing/marketing credit and capital goods credit for importation of equipment for agricultural production.

b/An additional $2.2 million is to go to small farmer cooperatives for processing and marketing credit.

Bilateral agricultural programs are targeted to farmers whose resources make them economically viable to participate in credit programs. In some countries, missions and host governments have jointly analyzed the farm population to determine who can be classified as small farmers. Within this category, the limits of eligibility are established and then various factors, e.g., on-farm annual income, acreage owned, and total assets, are used to establish who can be considered economically viable. Nevertheless some of the poorest farmers and landless farm workers have been helped.

The condition of some of these groups has been addressed by AID's agricultural credit programs (for example, the landless or land-poor target groups in segments of one agricultural loan to Bolivia and one to Honduras).

The Bolivian loan seeks to aid many small farm families in overcrowded highland regions to resettle in underpopulated and underused fertile lowland areas. The Honduran loan offers assistance to the government's ongoing agrarian reform effort, whose goal is to settle landless families on government and underused private lands. The major constraint to extending credit under this loan had been the lack of government regulations establishing the legal status of farmers and farm settlements that were to receive funds.

- - - -

Criteria to be met by potential farmer recipients may be specified in various loan documents, such as the AID capital assistance papers, the loan agreements, agreements between host country implementing agencies, lists of cooperative restrictions, and lists of individual host country requirements.

Criteria used to select small farmers who are among the poor majority include size of landholdings, either total acres or acres under cultivation; income, from either farming or other sources; and asset limits.

Our analysis and comparison of target group criteria used against the poor majority universe in several Latin American countries suggested that many medium and large size farmers are within the target groups qualifying for credit. The results of our country analyses follow. (See app. II for more detail.)

BOLIVIA

The three active AID loans in Bolivia include $10.5 million in direct farmer credit.

GAO photos

MEMBERS OF DAIRY AND RICE COOPS TALKING TO GAO REPRESENTATIVES IN BOLIVIA

The target group for lending to farmers for one of the loans had not been established. Our analysis of the other two loans showed that the target groups generally consisted of poor farmers but those in the upper spectrum of farm income and landholdings. (See p. 35.) Although the poor Bolivian farmers were not explicitly precluded from obtaining loans, Mission officials felt that the majority of these farmers would not have sufficient assets or credit worthiness to carry the available credit. AID/Washington said that the loan was directed to farmers in the upper farm income levels because this target group could most effectively use the production credit.

COSTA RICA

Disbursements to small farmers from the Costa Rican rural development loan, signed in November 1974, had not begun as of January 1977. During our fieldwork, Mission officials had not been able to determine the size of the loan's target group nor a quantitative definition of a Costa Rican small farmer. Annual income limits on this loan are expected to average $500 a family but may go as high as $3,000 or more a family.

AID stated that the $3,000 was an outside figure and the norm is expected to be significantly below the limit. Again, our concern is that the target group is so broadly defined that it lessens the prospects of restricting the available credit to small farmers--those among the poorest majority.

We agree with AID that the loan's main focus was not production credit. Selected aspects of the program, such as cooperative development and rural municipal development, also benefit the small farmer. Our analysis of the program, however, indicated that neither a specific target group nor reasonable limitations as to the level of the small farmer to be addressed had been developed.

DOMINICAN REPUBLIC

In October 1974 AID and the Dominican Republic signed an agricultural sector loan which contained a $9 million credit element. By January 1977 over half of this amount had been disbursed.

Loans have been extended to farmers having an average landholding of 6 acres and the major portion of the credit is being extended to farmers in the original target group.

In our view, the project is providing credit to the small Dominican Republic farmers.

AID stated that loan results as of June 30, 1976, indicate that 22,517 subloans had been approved with an average crop acreage of 5.79 per subloan. Serving farmers with this acreage is commendable and should be the thrust of the credit program in other countries.

HAITI

Haiti, the poorest country in the Western Hemisphere, has an annual per capita income of $135, $65 in rural areas. It seems that the target group for the loan to assist the small farm coffee production program is well focused on the small farmer in the rural poor majority.

Moreover, AID stated that since our review work in Haiti, the AID project brought about an important policy change by which the small farmer is to receive 50 percent of the export price of coffee. According to AID, interviews with coffee farmers indicate that the percentage they now receive has improved over past years. These additional benefits accruing to the small farmer from the AID loan are encouraging and demonstrate that AID credit programs can assist small farmers at very low income levels.

HONDURAS

AID has two loans in Honduras which include agricultural credit. The hurricane recovery loan was for emergencies and, thus, not limited to small farmers since restoring food production for the country was the main concern. The agricultural sector loan consists of a model agrarian fund and a cooperative window.

The agrarian fund has established a minimum farm size of about 7 acres but not an upper limit. A Mission official said that an upper limit was not necessary since the agrarian reform policy would preclude large landholdings. There are no other subloan restrictions except that such crops as tobacco, bananas, and cotton cannot be grown.

The cooperative window has established income and wealth limits for members of participating cooperatives. The cooperatives restrict large farmers from membership.

MEMBERS OF SMALL COFFEE FARMER GROUPS IN HAITI

GAO photos

MEMBERS OF SMALL FARMER SETTLEMENTS IN HONDURAS.

During our review, however, the Mission was not able to provide documentation which quantified the small farmer target group in terms of landholdings or income levels.

AID questioned our rationale for wanting AID to establish landholding limits since information that the Mission has indicates that average per family holdings are about 12 acres. AID also felt that we were suggesting the establishment of a single criteria. We agree that landholding limits should not necessarily be the sole criteria but feel that if this landholding figure is accurate then it could be reflected as a farmer qualification constraint in the loan agreement.

In the cooperative window segment of the loan, AID feels that our suggestions of improved monitoring of loan usage and specific qualifying criteria for small farmers were unnecessary because it felt that host country organizations could do this best. We agree that monitoring loan usage should be the prime responsibility of the host country agency but because of their general lack of experience and inadequate staffing it is essential that AID make spot checks to make certain that the program functions properly. Regarding the development of qualifying criteria for small farmers, we feel that the host country and AID should establish subloan restrictions to help assure that small farmers will be the principal beneficiaries.

PANAMA

In June 1974 AID authorized a loan to Panama designed to develop, strengthen, and expand rural cooperatives. The target group is to consist of (1) small producers with total assets of less than $15,000, 80 percent of total income from farming and landholdings of approximately 50 acres or less and (2) medium-sized producers with assets between $15,000 and $35,000, 50 percent of total income from farming and landholdings of approximately 1,250 acres or less. The executing agency is also to limit the size of individual loans to $7,500, which AID officials believe will preclude larger farmers from participating because they would not want to be inconvenienced by applying for such small loans.

We did not determine how AID arrived at this amount; however, this loan ceiling was the highest we encountered.

AID said that the project's purpose is to strengthen the capacity of the cooperative movement and that the small farmer will be an indirect beneficiary. AID also said that a Mission survey indicates that loans go to farmers having gross assets smaller than the established maximums. For example, loans have gone to farmers with average gross assets of $10,800 and farm sizes of up to 395 acres. In our view, AID could do more to assure that credit is targeted to smaller farmers in Panama, 50 percent of whom have farms of 12 acres or less.

CONCLUSIONS AND OBSERVATIONS

It is AID's objective and usual practice to restrict credit to operators of small farms who are considered too great a risk to receive credit from the traditional banking systems. AID agricultural loans are being made available to small farmers. In some countries credit is being made available to groups defined only in broad, general terms.

We recognize that the identification of farmer target groups and the establishment of criteria to direct credit aid to small farmers outside normal banking channels, and within the poorer majorities, is very difficult. Economic, social, and other conditions vary so widely from country to country that adopting rigid guidelines is not always practical; thus, some degree of flexibility is needed.

We believe, however, that broadly defined target groups and criteria indicate a need for AID to refine them so that AID can better meet its objective of getting credit aid down to more small farmers and, at the same time, be more responsive to the overall objective of assisting the poorest majorities. In this regard, AID has recognized the need for better identification of target groups and definition of criteria.

AID said it appreciates our efforts to reinforce its adherence to the New Directions to concentrate assistance on the poor majority. We agree that no one criterion is completely satisfactory for defining the poor majority. Moreover, no single criterion for defining a small farmer may be appropriate.

In our analysis we considered World Bank data which indicated that over 58 percent of the landholdings in the world were less than 5 acres; we also consider the World Bank definition of a small farmer which includes families farming less than 13 acres or, in countries where all farms are small in absolute size, farmers in the poorer half of the country's rural population.

In our examination of AID's agricultural credit programs, we found that a number of potential or actual loan recipients did not fit these measures of poverty. For example, in one country 47 percent of the farmers had farms of 13 acres or more and were in AID's target groups along with the 52 percent of farmers with less acreage.

We do not suggest that AID adopt or restrict itself to World Bank landholdings or other criteria, although it is the criteria most often used by AID missions. We do suggest that target groups need to be more specifically identified by using less broadly stated criteria so that small farm credit programs can become more responsive to AID's usual practice of restricting credit to small farmers not having access to bank credit. This also would provide more assurance that the congressional mandate aimed at improving the lives of the poorest people is being followed.

Economic viability is an important consideration, as AID points out, if credit programs are to be successful. The problem often centers on identifying farmers viable enough to profit from credit along with other necessary inputs, yet not viable enough to qualify for credit and other needed inputs from the traditional banking and supply systems. AID pointed out that its efforts to carry out the New Directions included noncredit-type projects such as rural community development, rural education, and agro-industrial and infrastructure development to assist the landless rural poor, agricultural laborers, and subsistence (nonviable) small farmers. Indeed, previously landless farmers and laborers are among the direct beneficiaries of AID loans we reviewed in Honduras and Bolivia. (See p. 16.) We recognize that credit is not the only appropriate instrument for dealing with these groups who are often among the poorest elements of a target group.

Consistent with the above, we proposed in our draft report that the AID Administrator (1) more specifically identify poor farmer target groups before approving loan agreements, (2) be sure that criteria for identifying small farmer groups in future programs would be consistent with AID's poverty benchmarks, (3) provide more timely direction and guidance to Missions regarding AID policy and target group identification procedures, and (4) improve monitoring, evaluation, and coordination of farm credit programs.

AID stated that it recognized the need to continually improve its guidelines and procedures for analyzing, identifying, and defining poor farmer target groups before project implementation. AID has taken steps to identify small farmer target groups early in the design of loans, and to provide more guidance on a continuing basis to the Missions. We encourage AID to continue efforts to improve its small farmer credit programs.

The following recommendations are being made to help assure that positive actions already begun are translated into actual improvements in current programs--to the extent possible--and in future small farmer credit programs.

RECOMMENDATIONS

We recommend that the Administrator of AID follow up on recent initiatives to (1) more clearly delineate small farmer target groups and (2) see that the definition of target groups in future small farmer credit programs is consistent with AID's overall policy and poverty benchmarks.

CHAPTER 4

IMPLEMENTING AID CREDIT PROGRAMS

To successfully implement a small farmer credit program, the credit mechanism or delivery system, interest rate, and technical assistance to the small farmer must be properly designed.

In determining a credit mechanism, the host country generally designates a bank, an executing agency, and/or an implementing agency, and identifies the small farmer groups to be aided. It is essential that the implementing agencies provide credit and technical assistance at the farm level in a manner convenient to the small farmer. Host government institutions also must be strong enough to properly support the program, otherwise its chances for succeeding and continuing are not good.

If the interest rate charged to the small farmer is based on actual or anticipated costs, then, to keep the loan program solvent, the factors involved would include the costs of (1) the overall loan to the host country, (2) processing, delivering, and administering subloans, (3) collections and defaults, and (4) providing technical and other assistance. Generally, the more carefully subloans are examined and supervised and delinquents pursued, the lower the default rate but the higher the administrative costs.

Since AID grant or loan assistance is concessional by nature, AID credit programs are designed to help small farmers improve their economic status to the extent that they "graduate" from the need to rely on subsidized credit and other inputs. Charging reasonable interest rates and providing training and other technical assistance we feel are efforts to accomplish this. In our review some of the realities and problems encountered include (1) most small farmers in the poorest majorities have virtually no access to institutional credit, (2) the farmers whom AID is attempting to identify and reach have few assets and probably could not afford interest rates that would be necessary to cover all operational and administrative credit costs involved, and (3) categorizing, identifying, and reaching small farmers in the poorest majorities is difficult.

Credit is important to small farmers in developing countries, but it alone cannot increase food production and income. Borrowed funds must be spent by the small farmer on seed, fertilizer, pesticides, and labor, whose effective use depends on the quality of technical assistance and training the farmer receives.

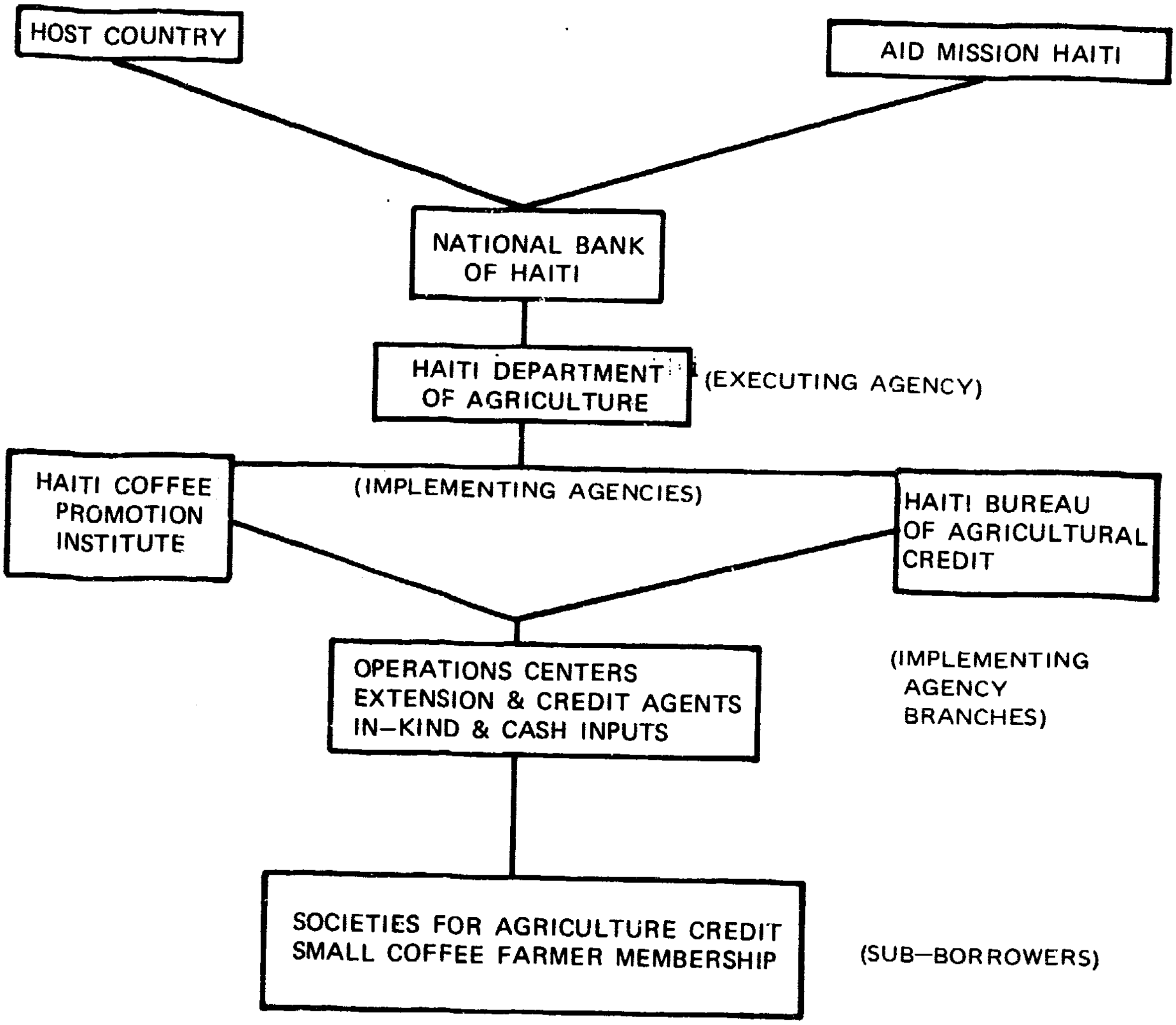
Technical assistance to the small farmer usually takes the form of supervision, marketing assistance, or provision of direct inputs. Supervision is the most extensive form of technical assistance and includes (1) providing information on farming techniques and new production technology, (2) specifying and instructing on the use of inputs to maximize the use of loan funds, and (3) helping to insure repayment of subloans. Assistance in procuring inputs, utilizing large-scale buying power where possible, can help insure that the small farmer has the proper inputs at the appropriate time and at lowest possible prices.

CREDIT MECHANISMS

In all loans, the principal borrowers of U.S. funds are the host governments who sign the loan agreements. (Loan agreements identify the organizational structures for administering the credit programs.) The organizations are usually composed of executing agencies, implementing agencies, and branches of implementing agencies which serve as focal points for making subloans (cash and in-kind) to small farmers. The executing agencies generally establish noninterest-bearing accounts in banks to serve as depositories for funds received from host governments and AID. Funds flow from the banks through the implementing agencies and their branches to organized farmer groups and/or individual farmers. Repayments flow in reverse, but interest collected is reduced at each level to cover the administrative costs of handling loans.

The organizational structure of the Haitian loan to small coffee farmers shown on the next page is fairly representative of other countries' structures and credit delivery systems.

Of the nine loans we reviewed in six countries, eight had organizations structured so that the ministries of agriculture and/or national agriculture development banks served as executing or implementing agencies. Bolivia, however, used the Ministry of Agriculture or its agencies as principal agents for two of its three loans; for the third loan the Bolivian Central Bank was used as the executing agency and point of origin for funding the implementing agencies.



It has been generally accepted that the most feasible way to administer small farmer credit programs is on the group basis. Dealing with each small farmer individually would not be practical. The history of formal, cooperative organizational performance has been mixed. Members sometimes felt little responsibility to repay their subloans because of the political nature of some programs and because of the large size and consequent impersonal nature of many cooperative organizations. In the larger cooperatives, small and large farmers were mixed and the large farmer often is in control, usually to the detriment of the small farmer.

In Haiti, the small farmer organizations, called Societies for Agriculture Credit, consist of 8 to 15 members. All new members must be approved by the group. This is significant, because all members are jointly responsible for defaulted subloans of other members, which would cause peer pressure to repay loans. Encouraging the formation of such smaller, less formalized groups would appear to offer a greater chance for success in reaching the truly poorer small farmer than, for example, the cooperatives of Costa Rica and Panama.

CREDIT AVAILABILITY AND INTEREST RATES

It is well known that small farmers have limited access to credit sources; they lack the necessary collateral demanded from private financial institutions to qualify for loans. Also, private financial institutions tend to extend credit to larger borrowers, medium and large farmers, because it costs less to administer these loan portfolios and the risks are lower.

The private banking system has very strict requisites that discourage small farmer loans, such as asset levels, proven creditworthiness, and land titles. In addition, the inconveniences that a small farmer can experience, such as multiple personal visits to the bank to fill out forms, costs incurred for transportation, and apathetic treatment by the banking staff, frustrate his attempts to obtain loans.

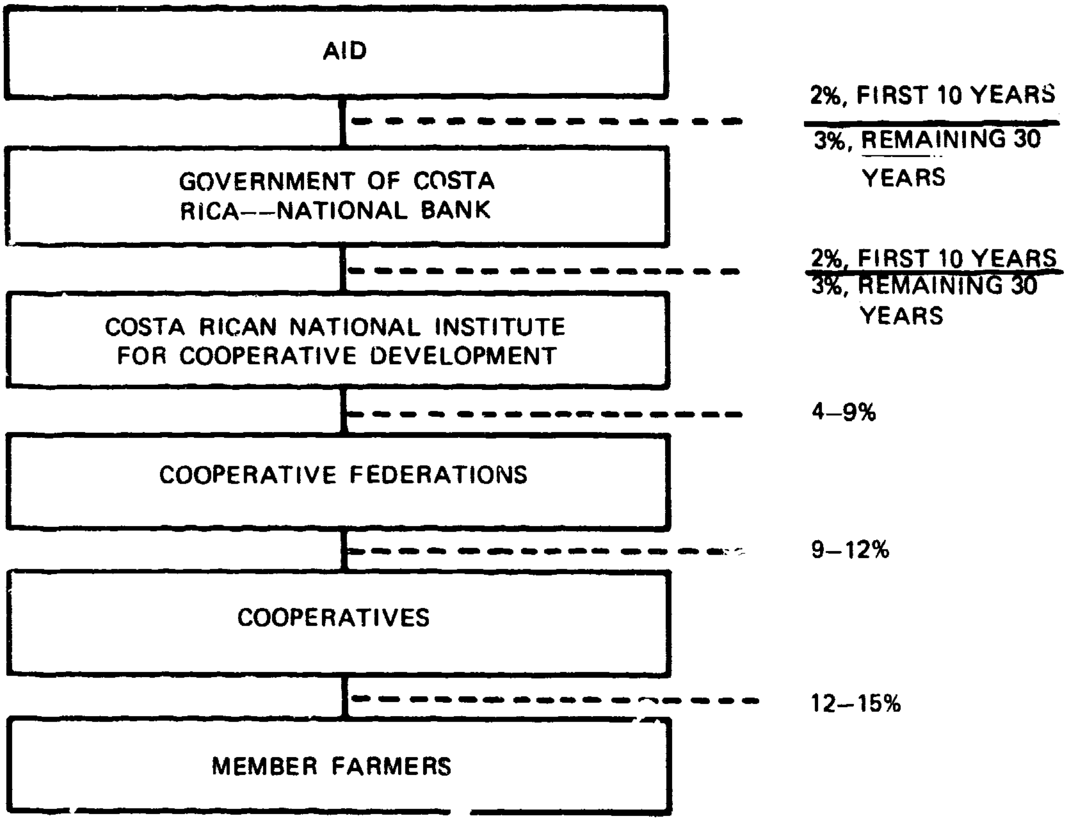
With the private and public financial institutions having limited funds to lend to small farmers, where do they get credit? Mostly from moneylenders, who charge usurious interest rates. In Bolivia, for example, it is estimated that about 60 percent of the money in circulation is outside the banking system. This situation tends to place the small farmer in a state of perpetual bondage, because he is not likely to realize a profit from the sale of his crops if his credit costs are exorbitant.

Estimates of interest rates from commercial and moneylending sources compared to rates paid by small farmers on AID-funded loans are illustrated in the following schedule. Data on financial institutions, merchants, and moneylenders is derived from the World Bank Agricultural Credit sector policy paper dated May 1975. Although interest rates for agricultural credit vary considerably among countries and institutions, the nominal rates range from 6 to 30 percent and average about 10 percent.

	AID loans	Financial institutions	Merchants and moneylenders (note a)
		(percent a year)	
Bolivia	13	23	40
Costa Rica	13	12 to 24	60
Dominican Republic	8	12	25
Haiti	12	15	-
Honduras	11	12 to 14	40
Panama	12	13	40

a/Rates are approximations, based on surveys. Merchant lenders could include agricultural suppliers whose rates in many cases are substantially lower than those of the moneylenders. On the other hand, moneylenders' rates, in some cases, have been estimated at over 100 percent.

An example of the flow of interest rates anticipated in Costa Rica is as follows.



In the countries we visited, farmers receiving credit under AID credit assistance programs were paying 11 to 13 percent interest except for the Dominican Republic, where they were paying 8 percent. The World Bank estimates that total costs of an efficient credit institution (not including extension, advisory, and other public services) could range between 15 and 20 percent, depending on the nature of the operation, and size of the loans. Cost of lending to small farmers would be at the upper end of the range and possibly higher.

Prevailing interest rates under current AID loans seem to be well within this estimate. AID loans, however, tend to reflect subsidies not only for interest rates and host government services but also for such other major noncredit segments as technical aid, that are part of AID loans under which credit to small farmers is made available.

There seems to be no simple answer to the question of what an appropriate interest rate should be for agriculture in general and small farmers in particular. Arguments favoring lower interest rates point out that (1) high interest rates can lead to diversion of resources to other sectors of an economy, (2) low rates can help offset unfavorable trade terms between agriculture and the rest of the economy, (3) high rates may discourage farmers from accepting credit, and (4) subsidized rates can be a method for transferring income to the poorest majorities.

Opposition to subsidized and lower interest rates for farmers centers on the general recognition that, due to rapid inflation, real rates of interest in most economies are likely to be well below the true economic costs of lending. Thus, it is argued that interest rates should always be positive ones which reflect the true costs of lending.

Other arguments against low interest rates point out that subsidized credit (1) can lead to excessive capitalization, including the use of labor-displacing machinery, (2) tends to be absorbed by larger farmers, (3) is prone to corruption and political abuse, (4) does not cover lending institution costs, reducing the flow of funds into institutional credit and, thereby, the level of lending, and (5) when deemed desirable, can be most effective when used to subsidize particular inputs, such as fertilizer, or when related to specific technological changes.

We did not make a detailed analysis of interest rate structures or of the adequacy or propriety of interest rates charged by various lenders. As a point of clarification, AID stated that it does not believe that low interest rates are necessary subsidy elements in aiding the poorest farmers.

TECHNICAL ASSISTANCE

In most cases, technical assistance is provided to small farmers by extension agents working for the agricultural ministries or host government executing and implementing agencies. This effort is supplemented by in-country staff and advisors often hired under contract to AID.

Direct, in-kind inputs have been provided to the small farmer thus far only in the Haiti loan, where reasonably priced fertilizer is apparently being made available in a timely manner with proper supervision.

In Bolivia, the Dominican Republic, and Honduras, extension agents devoted only part of their time to assisting the small farmer. A farm agent in Bolivia had not visited the landholdings of the farmers we interviewed. The agent had visited three farmers only at their homes, which were several miles away from their farms. In the Dominican Republic, the program manager for supervised credit said that extension agents should devote most of their time to problems of the small farmer. At the time of our visit, only about a third of the agents' time was being applied to small farmers' needs. The program manager also stated that his loan collection rate could be increased from about 60 to 80 percent if the agents would devote time to small farmer credit problems. In Honduras, several small farmers told us they rarely saw their extension agents.

The losses suffered by some potato farmers in Bolivia further demonstrate why extension agent visits and presence in the farm area are essential. The farmers suffered losses due to frost but could not get their loans extended until agents had assessed the damage. Since agents had not visited the farm area, the farmers did not know when or if this would take place. They were concerned that it could be after the harvest, at which time the agents might allow less than actual damage because of not having seen it.

Extension agents in Bolivia and the Dominican Republic, in our view, were not adequately trained for small farmer supervised credit programs and often lacked the dedication and sincerity necessary to work effectively in these programs.

The small farmers lack experience with institutional credit, may be ignorant of opportunities and cling to their traditional ways of farming. We believe that extension agents should have a key role in small farmer credit programs because they can instill the desire to adopt modern technology and use credit effectively.

Regarding this overall problem of a lack of qualified host country personnel, an AID/Washington nine-Mission survey conducted in 1975 indicated that the major local programing and implementation constraint for small farmer assistance projects was a lack of capable host country counterparts.

CONCLUSIONS AND OBSERVATIONS

Probably the most important single element in the credit mechanism is the strength and vitality of host country executing and implementing institutions. Historically, weak institutions have been a primary cause of small farmer credit program failures. Many loan agreements required these institutions to maintain adequate staffing to service the loan programs.

AID has an important role in insuring that implementing institutions are selected or established in accordance with loan agreements and receive assistance and counsel necessary to successfully administer current and future programs.

The interest rates for the small farmer in AID programs are generally lower than prevailing local rates. We could not determine the extent to which the interest rates would cover defaults and administrative expenses, but it is generally recognized that all loans do contain subsidy elements provided by both the host country and AID. The host country would provide subsidies through the various support services; AID provides it through concessional interest rates and other loan elements. We believe that small farmer credit programs, particularly those directed to the poorest small farmers in developing countries, may always require some degree of subsidy. One of the overall and worthwhile objectives of these programs is to "graduate" as many small farmers as possible into the money economy at a level where they become eligible and capable of obtaining and using credit from traditional institutional sources.

Credit to small farmers is important in developing countries, but technical assistance in the proper use of credit is essential. To achieve AID's increased food production and income objectives, borrowed funds must be spent by small farmers on fertilizer, seeds, pesticides, and labor in ways that will maximize their efforts. Credit gives them the funds to purchase these productive inputs, but whether they do so effectively depends on the timeliness and quality of technical assistance they receive.

SELECTED GAO REPORTS ON U.S. AGRICULTURAL PROGRAMS

"Restrictions on Using More Fertilizer for Food Crops in Developing Countries," ID-77-6, July 5, 1977.

"Hungry Nations Need to Reduce Food Losses Caused by Storage, Spillage and Spoilage," ID-76-65, Nov. 1, 1976.

"U.S. Participation in International Food Organizations: Problems and Issues," ID-76-66, Aug. 6, 1976.

"Providing Economic Incentives to Farmers Increases Food Production in Developing Countries," ID-76-34, May 13, 1976.

"Impact of U.S. Development and Food Aid in Selected Developing Countries," ID-76-53, Apr. 22, 1976.

"Disincentives to Agricultural Production in Developing Countries," ID-76-2, Nov. 26, 1975.

"Some Problems Impeding Economic Improvement of Small-Farm Operations: What the Department of Agriculture Could Do," RED-76-2, Aug. 15, 1975.

"The Overseas Food Donation Programs--Its Constraints and Problems," ID-75-48, Apr. 21, 1975.

"The Agricultural Attache Role Overseas: What He Does and How He Can Be More Effective for the United States," ID-75-40, Apr. 11, 1975.

"Increasing World Food Supplies--Crisis and Challenge," ID-75-4, Sept. 6, 1974.

REACHING THE POOR MAJORITY: FACTORS IN LOANS EXAMINED

BOLIVIA

The primary planning document for the Basic Foods Production Loan 511-T-052 indicates that the loan will deal specifically with small farmers who are already engaged in commercial as well as subsistence farm production. Farmers included in this group cultivate up to 30 acres and have average gross off-farm incomes of $1,000 to $2,000.

A 1972 Bolivia Ministry of Agriculture survey of rural households in the three most important agricultural regions showed that 86 percent of the farmers cultivate less than 10 acres, 13 percent cultivate between 10 and 25 acres, and only 1 percent cultivate more than 25 acres.

Mission officials told us that farmers cultivating between 10 and 25 acres would probably be the target beneficiaries of this loan although farmers cultivating less than 10 acres would not be precluded from obtaining loans.

The following chart shows the distribution of farm income by percentile range for the Bolivian agricultural sector.

Estimated Average Annual Farm Income in Bolivia

Percentile range	Income	
1 to 10	$ 217	
11 to 20	225	
21 to 30	233	
31 to 40	242	
41 to 50	283	
51 to 60	316	
61 to 70	367	
71 to 80	450	
81 to 90	583	$ 666
91 to 95	833	
96 to 97	1,090	$3,333
98	1,350	
99	3,284	
100	9,852	

Mission officials assume that the target group falls within the 81st to 95th percentile with an annual average per farm income of about $666. They stated that farmers in the lower half of the distribution would not have sufficient assets or creditworthiness to meet the lending criteria of the participating credit institutions that carry the credit risk.

The target group for the Bolivian Agriculture Sector Loan 511-T-053 is similar, regarding economic grouping, to that of the Basic Foods Production Loan 511-T-052. According to project documents and Mission officials, farmers with up to 25 acres of cultivated land and gross off-farm sales up to $2,000 will be eligible for credit under this loan.

At the time of our fieldwork, the lending criteria (farm size and income limitations) for beneficiaries of the Sub-Tropical Lands Development Loan 511-T-050 had not been established.

COSTA RICA

Although documentation for the Rural Development Program Loan 515-T-025 indicates that the loan will focus on farmers whose average annual family incomes are about $500, it further states that the executing agency (the National Institute for Cooperative Development) will try to limit loans to farmers with annual family income of less than $3,000.

During discussions with Mission officials, we learned that the $3,000 income figure could be higher if justified and that the executing agency is under no formal restraint to abide by the $3,000 criteria. Any prospective borrower who appeared to be creditworthy and in need of funds could be considered for a loan.

The following table shows the distribution of annual per capita income in Costa Rica at the time of our review.

Annual per capita income	Number of persons	Percent of population
Less than $58	249,835	13.4
$ 58 to 117	263,933	14.1
117 to 140	87,565	4.7
140 to 163	88,111	4.7
163 to 187	71,502	3.8
187 to 210	58,361	3.1
210 to 234	56,122	3.0
234 to 257	47,057	2.5
257 to 281	32,152	1.7
281 to 304	46,771	2.5
304 to 327	21,478	1.1
327 to 351	21,699	1.2
351 to 374	25,097	1.3
374 to 398	18,939	1.0
398 to 421	15,331	0.8
421 to 444	17,259	0.9
444 to 468	14,289	0.8
More than 468	188,246	10.1
Undefined	547,892	29.3
Total	1,871,639	100.0

Considering that the average rural family has 6.82 members, the $3 000 annual family income lending criterion translates to a per capita annual income of about $440. Accordingly, the vast majority of the defined population could qualify for credit under the established lending criteria.

The Mission had not, at the time of our fieldwork, been able to determine the size of the loan target group nor did it have a quantitative definition of a Costa Rican "small farmer." One AID official told us that the Mission and the Government of Costa Rica "think they know who this person is, but are not really sure."

During our review, an AID-funded study was underway to provide better information about the Costa Rican rural poor and small farmer target group. The May 1975 Mission-prepared study proposal stated that:

> "The target group here in Costa Rica has not yet been precisely defined, nor is there good quantified information about this group available to USAID and GOCR (Government of Costa Rica) in order to measure the impact of development programs."

Although the study had not been completed, Mission officials told us the lack of such information should not cause much delay in implementing the loan.

THE DOMINICAN REPUBLIC

Planning documents for the Agricultural Sector Loan 517-T-027 state that the credit program's objective is to provide substantially more credit to small farmers now outside the institutional credit system. The documents indicate that the target group will be farm units of less than 5 hectares (about 12 acres) which are not associated with formal credit sources and do not qualify for or have not recently used credit under other portions of the Dominican Republic's Agricultural Bank portfolio.

An analysis of small farmer credit in the Dominican Republic, prepared by the AID Mission in February 1976, indicated that the implementing agency for the loan (Dominican Republic Secretariat of Agriculture) and AID agreed on the following criteria for the use of project funds.

1. Loans would be extended to farmers operating farms of 32 hectares (about 78 acres) or less.

2. Subloans would have a $1,500 ceiling; as of February 12, 1976, the ceiling was increased to $2,000.

3. Export crops, such as sugar, cacao, tobacco, or coffee, would not be financed.

The analysis noted that no condition was imposed requiring that project funds be lent only to persons who had never received credit, although the Mission strongly encouraged the Government of the Dominican Republic to extend credit to persons who had "no, or limited access, to institutional credit." It also included the following information about loans from February 19 to December 31, 1975.

--15,087 loans were approved and 12,053 were formalized. 1/

1/Bank experience shows that about 20 percent of loans approved are never formalized.

--8,934, or 74 percent, of formalized loans were to new or rehabilitated borrowers (those whose access to the institutional credit system is denied for reasons other than unavailability of funds.)

--Average value of formalized loans was $538.

--Average number of hectares per loan approved was 2.4 hectares (about 6 acres).

In commenting on the landholdings per loan approved, it was suggested that the average number of hectares approximates the total farm size of the operator or, at least, the total arable land of sampled farms.

The following table shows the total number and sizes of farms in the Dominican Republic as of March 1976.

Farm size	Number of farms	Percent of total	Total acreage	Percent of total acreage
(acres)				
Up to 1.24	49,651	16	30,153	0.5
1.24 to 12.1	185,292	61	838,857	12.4
12.1 to 123.4	62,790	21	2,023,335	29.9
123.4 and over	7,087	2	3,866,158	57.2
Total	304,820	100	6,758,503	100.0

HAITI

Loan 521-T-006, the "Small Farmer Improvement" program, was the only active AID agricultural credit loan in Haiti at the time of our review. This loan is designed to help the Haitian Government carry out a 5-year small farmer coffee production program to increase the small farmer income by improving the quantity and quality of Haitian coffee. Increased production will be promoted by introducing new technology to the small farmer through increased research and extension activities, and introducing chemical fertilizer and pesticides, increasing credit availability, improving rural farm roads in coffee-producing areas, expanding training of agricultural agents and farmers, and establishing an agricultural cooperative system.

APPENDIX II

Anyone who farms 15 acres or less is considered a small farmer and about 89 percent of the farms are this size. There are about 750,000 farms in Haiti. The following table gives some indication of farm sizes.

Farm Sizes in Haiti

Landholding (acres)	Percent	Cumulative percent
Up to 1.5	15.0	-
1.5 to 3.2	19.4	34.4
3.2 to 6.5	30.6	65.0
6.5 to 15	23.9	88.9
Over 15	11.1	100.0

Criteria for this small farmer loan are that landholdings must be between about one-half and 15 acres and only coffee may be produced. If the farmer does not have title to his land, he must have signed a lease that expires at least 2 years after the maturity date of his last obligation to the bank. Subloans are limited to $40 in cash and $100 in fertilizer.

The current per capita income in Haiti is the lowest in the Western Hemisphere, $135 a year, $65 in the rural areas. It would appear that the primary focus of this target group is on people among the rural poor majority. We met with representatives of more than 300 farmers and with individual farmers from four geographical regions, examined landholding and other records, and interviewed host country officials about compliance with target group criteria.

HONDURAS

At the time of our review AID had two loans active in Honduras which include farm credit--loan 522-T-025, an agricultural sector program, and 522-T-026, a hurricane recovery loan.

The agricultural sector program consists of two separate activities--a model agrarian fund and a cooperative window. Through the model agrarian fund, production credit is to be provided to about 50 farmer settlements, out of several hundred formed as a result of a 1972 land reform program.

APPENDIX II

Criteria for selecting the settlements included the productive potential of the occupied land, minimum farm size of about 7 acres per family, proximity to access roads, desire and ability of families to work together, location within a government priority region, and land tenure. The primary purpose of this model agrarian fund is to establish the credibility of the government's settlement program so that it can be replicated throughout the country.

The cooperative window activity is to provide credit and technical assistance to small farmers through cooperative group organizations. Mission officials told us that procedures will stipulate that the membership of participating cooperatives must consist of at least 80 percent small farmers with $500 maximum annual income per member and less than $2,000 capital investment. Also, limits had been established on the income and wealth of member farmers of participating cooperatives and the cooperatives themselves had restricted larger farmers from membership. During our fieldwork, however, the Mission was not able to provide documentation which quantified the small farmer target group in terms of landholdings or income levels.

The hurricane recovery program was designed to counteract the effects of Hurricane Fifi, which occurred in September 1974. The hurricane damaged an area along the north coast, the country's most productive agricultural region, and caused major crop losses. The basic purpose of the credit portion of this loan is to regain the former basic food production level by providing credit to small and medium farmers.

To qualify for a subloan not to exceed $10,000, the farmer's landholdings must be 123 acres or less. For farmer cooperatives and associations, the $10,000 and 123-acre limit could be multiplied by the number of active members, so long as each individual met the requirement. Crop selection restrictions cover export crops, tobacco, bananas, and sugar cane.

Since this loan was of an emergency nature, with restoration of food production to feed the country as the main consideration, it was not limited to small farmers.

PANAMA

Under Cooperative Development Loan 525-T-041, sublending terms and amounts will depend on the executing agency's (Panamanian Agriculture Development Bank) definition of small and medium-sized farmer target groups. Currently, a small producer is characterized as having total assets of less than $15,000, 80 percent of his total income from farming, and landholdings of 50 acres or less. A medium-sized producer is described as one having assets between $15,000 and $35,000, at least 50 percent of his total income from farming, and landholdings of approximately 1,250 acres or less.

The following table, taken from the 1970 agricultural census, presents the land distribution of farms in Panama.

Area (acres)	Number of farms	Percent
Less than 2.47	20,000	19.0
2.47 to 12.35	34,400	33.0
12.35 to 24.70	13,900	13.0
24.70 to 49.40	14,200	14.0
49.40 to 123.50	14,100	13.0
123.50 to 247.00	5,500	5.0
247.00 to 1,235.00	2,800	2.7
1,235.00 and over	300	0.3
Total	105,200	100.0

Comparing the above statistics with landholding criteria to be applied by the executing agency, 99.7 percent of the farms in Panama would be eligible for loan funds. AID/Panama relies on participating cooperatives to identify loan recipients.

During our review, we visited a participating cooperative and examined 61 individual member loan files. Loans approved at that level ranged from $665 to $7,500 and averaged $2,664; borrowers' assets ranged from $400 to $107,500 and averaged about $13,000; titled landholdings ranging from a half hectare to 150 hectares (about 370 acres) and averaging about 27 hectares (66 acres) were claimed by 39 of the 61 borrowers.

Three members, who claimed assets of $52,600, $61,500, and $107,500 would be declared ineligible under AID's lending criteria. AID officials said, however, that the executing agency had not yet submitted documentation on these loans and that, if subsequent documentation submitted to AID included these loans, they would be disallowed.

We mention these ineligible borrowers not primarily because they are statistically significant but rather because they are indicative of improvements needed in Mission managerial control over the administration of the loan.

DEPARTMENT OF STATE
AGENCY FOR INTERNATIONAL DEVELOPMENT
WASHINGTON, D.C. 20523

Auditor General

JAN 17 1977

Mr. J. K. Fasick
Director
International Division
U.S. General Accounting Office
441 G Street, N.W.
Washington, D.C. 20548

Dear Mr. Fasick:

Thank you for providing the GAO draft report "Availability and Use of Small Farmer Credit Assistance in Latin America" for AID comment. While AID's comments note some problems with the findings as presented in the draft report, we appreciate the objectives of the GAO's review and are in agreement with most of the recommended actions.

Development of AID's comments took longer than you requested because of other priorities and the significance we placed on a full analysis of this important report. We believe these comments will be of use in preparing your final report and appreciate the efforts of Mr. Zangla and his team in meeting with AID's staff to fully discuss the draft. If we can be of any further assistance, please let us know.

Sincerely yours,

Harry C. Cromer

Harry C. Cromer

Attachment: AID Comments 1/

1/AID's comments were used in the preparation of this final report and are discussed in the body of the report, where appropriate.

PRINCIPAL OFFICIALS RESPONSIBLE FOR ACTIVITIES DISCUSSED IN THIS REPORT

	Appointed
AGENCY FOR INTERNATIONAL DEVELOPMENT	
ADMINISTRATOR:	
John J. Gilligan	Mar. 1977
John E. Murphy (acting)	Jan. 1977
Daniel S. Parker	Oct. 1973
ASSISTANT ADMINISTRATOR: LATIN AMERICA BUREAU:	
Donor M. Lion (acting)	Apr. 1977
E.N.S. Girard II	Oct. 1976
Donor M. Lion (acting)	Aug. 1976
Herman Kleine	Sept. 1971
U.S. OFFICIALS IN BOLIVIA	
U.S. AMBASSADOR:	
William P. Stedman, Jr.	Sept. 1973
DIRECTOR, AID/BOLIVIA:	
Frank Kimball	Nov. 1976
John R. Oleson	Aug. 1973
U.S. OFFICIALS IN COSTA RICA	
U.S. AMBASSADOR:	
Lowell C. Kilday (acting)	Jan. 1977
Terence A. Todman	Jan. 1975
Viron P. Vaky	Sept. 1972
AID AFFAIRS OFFICER:	
Joe J. Sconce	June 1974
Peter M. Kreis	June 1971
U.S. OFFICIALS IN THE DOMINICAN REPUBLIC	
U.S. AMBASSADOR:	
Robert A. Hurwitch	Aug. 1973
Francis E. Meloy, Jr.	Apr. 1969
DIRECTOR, AID/DOMINICAN REPUBLIC:	
Patrick Morris	Jan. 1974
John B. Robinson	Apr. 1974
John P. Robinson	Nov. 1968

APPENDIX IV

	Appointed
U.S. OFFICIALS IN HAITI	
U.S. AMBASSADOR:	
Heyward Isham	Jan. 1974
DIRECTOR, AID/HAITI	
Scott L. Behoteguy	Jan. 1973
U.S. OFFICIALS IN HONDURAS	
U.S. AMBASSADOR:	
Ralph E. Becker	Sept. 1976
Philip V. Sanchez	May 1973
DIRECTOR, AID/HONDURAS:	
John B. Robinson	Dec. 1976
Frank B. Kimball	Sept. 1974
Edward Marasciulo	Apr. 1971
U.S. OFFICIALS IN PANAMA	
U.S AMBASSADOR:	
William J. Jorden	Mar. 1974
Robert M. Sayre	Oct. 1969
DIRECTOR, AID/PANAMA:	
Irving G. Tragen	Dec. 1975
George Rublee (acting)	Apr. 1975
Alexander Firfer	Oct. 1970

(47119)