Credit and the Agricultural Sector of Pakistan

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Abstract

Agriculture sector is the single largest contributor to the national income (GDP) contributing nearly 21 percent and provides employment to nearly 43 percent of the workforce and supplies raw material to the industrial sector (notably textile industry) of Pakistan. Credit is an important tool for getting the inputs in time increasing thereby the productivity of the farms particularly those of small ones. There are basically two sources of credit i.e. informal through friends and relatives, village shopkeepers, traders, commission agents etc. and formal through different institutions like Zarai Taraqiati Bank Limited (ZTBL), Commercial Banks, Punjab Provincial Cooperative Bank Ltd (PPCBL) and Domestic Private Banks. Given its importance to the national economy, the Government attaches high priority to raising agricultural productivity and farmer's income. The Government allocated Rs. 160 billion for agriculture credit disbursements for the year 2006- 07 which was 23.1 percent higher than the allocation of the preceding year i.e. Rs. 130 billion. Different studies had been conducted to check the impact of credit on the productivity of the agricultural sector globally. The current study reviewed a few of these studies and found that credit had proved to be an important aid and enhanced the productivity. At the same time it was found that the small farmers faced a lot of problems in getting and returning the loan which must be removed to get better results hence improving the quality and quantity of the agricultural products.

Key words: agriculture, credit, Pakistan.

Introduction

Pakistan is blessed with abundance of natural and human resources, fertile lands, mountains and lakes, variety of seasons, perhaps the best irrigation system of the world and a relatively more productive agriculture sector. Despite the speedy growth in other sectors, agriculture is still the single largest sector contributing nearly 21 percent to Pakistan's national income (GDP) and employing nearly 43 percent of its workforce. It also supplies raw material to Pakistan's Industries, notably

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textile industry, the largest industrial sub-sector of the economy. As much as 66 percent of country's population living in rural areas is directly or indirectly dependent on agriculture for its livelihood (Anonymous, 2007).

Credit is the back bone for any business, more so for agriculture which has traditionally been a non-monetary activity for the rural population in Pakistan. Rural credit, though not a direct tool of production, can help break the vicious circle of 'grow-eat-grow' by removing financial constraints and accelerating the adoption of new technologies. Credit facilities are thus the integral part of the process of commercialization of the rural economy. The introduction of easy and cheap credit is the quickest way to give boost to the agricultural production. Therefore, it was the prime policy of all successive Governments to meet the credit requirements of the farming community of Pakistan.

Credit is necessary for capital formation, diversified agricultural production and efficiency in agricultural resource-use, in the face of excruciating poverty in the rural economy where in farmers are the major players. Agricultural credit has long been identified as a major input in the development of the agricultural sector even in Nigeria. The use of credit facilities would therefore translate to higher resource employment and capacity utilization, increased output and income, and reduce poverty in the rural economy, especially among the farmers and be helpful to increase the food production which would lead to an improvement in the welfare of the farmers and consequently a reduction in their poverty and food insecurity levels (Olagunju, 2007).

For the transformation of subsistence agriculture to commercialized one, credit is a leading factor. Agricultural credit, in reality, is an integral part of the process of modernization of agriculture and commercialization of the rural economy. However, in spite of considerable efforts to streamline, reinforce, expand and institutionalize the agricultural credit system the achievement falls short of proclamations, policies and programs. Unless agriculture credit is systematically institutionalized for small farmers, agricultural development can not be materialized. Due to small holdings, low crop yields and small income there is very little saving among the majority of the farmers of Pakistan. Therefore, it is need of time that credit agencies come up to help them in undertaking the improved farm practices.

Objectives

- To review the agricultural credit system of Pakistan
- To suggest policy measures

Sources of agricultural credit in Pakistan

Agricultural credit provides financial resources to the farming community particularly for purchase of primary inputs like fertilizer, seed, pesticides, machinery, equipment, etc. The rural financial market in Pakistan can be seen as composed of two broad segments, i.e. the informal and formal.

Informal / Non-Institutional Credit Sources:

Traditionally, friends and relatives, village shopkeepers, traders, commission agents, etc. have remained a major source of agricultural credit. These sources generally lend for short periods and charge an exorbitant rate of interest. Such loans are given to tide over bad periods and as such are meant for consumption purposes. Loans are also made available for buying seasonal inputs where cash is essentially required. These sources are both inadequate and non dependable. No comprehensive data are available on the amount of credit advanced by informal credit sources. As such it is difficult to find solid evidence regarding the relative share of these sources in the total credit supply. However, few reports and some other rough estimates show that the formal credit sources have been able to meet only 50 percent of the total credit requirements of the farm sector and it may be assumed that the rest are met by informal sources of credit. These sources play a vital role in our rural economy, especially for meeting the consumption requirements of thousands of small farmers along with fulfilling the need for irrigation water, hiring of farm power, cost of fuel etc. Mark-up tends to vary from product to product and also by type of borrower as well as lender. On the average, the mark-up is estimated to be 25 percent. In the case of fertilizer it is 29 percent while for the pesticides it comes around 35 percent. High mark-up charged on pesticides sold on credit is mostly due to rather unholy alliance between the manufacturers and traders/dealers. The case studies suggest that pure money lending is on the rise with quite exploitative interest rates ranging from 48 percent to 120 percent per year (Irfan M. *et al,* 1999).

The informal credit sources however are still popular particularly among the small farmers, because of easy access, no documentation, no collaterals and availability of credit in time.

Formal / Institutional Credit Sources

Government considers it an important instrument for achieving higher production and attaches high priority to ensure its timely availability to the farmers. Credit requirements of the farming community have shown an increasing trend over the years. Credit requirements of the farming sector have been increasing over the years mainly due to the rise in the use of fertilizer, pesticides and mechanization. In order to cope with the increasing demand for agricultural credit, institutional credit to farmers is being provided through Zarai Taraqiati Bank Limited (ZTBL), Commercial Banks, Punjab Provincial

Cooperative Bank Ltd (PPCBL) and Domestic Private Banks. The Government allocated Rs 160 billion for agriculture credit disbursements for the year 2006- 07 which was 23.1 percent higher than the allocation of the preceding year i.e. Rs 130 billion. The allocations, however, are totally voluntary and indicative in nature as the mandatory allocations policy has been totally phased out and the allocations for commercial banks have also been made indicative. The elimination of mandatory credit allocations coupled with active involvement of commercial banks in agri-finance is a major milestone achieved towards mainstreaming of agri-finance in the country’s financial system. The flow of necessary funding to the sector will now be ensured through conducive policy and regulatory environment, policy advocacy and promotional initiatives and monitoring of agri-disbursements and portfolio build-up plans. Out of the total credit target of Rs. 160 billion, Rs. 80 billion were allocated to commercial banks, Rs. 48 billion to ZTBL, Rs. 9 billion to Punjab Provincial Cooperative Bank Ltd. (PPCBL), and Rs. 23 billion to Domestic Private Commercial Banks (DPCBs) (Anonymous, 2007). Table 1 shows the credit disbursement by the different institutions from 1990-91 to 2006-07.

Table:1 Credit Disbursed by Institutions

						(Rs. Million)
Fiscal Year	**ZTBL**	**Taccavi***	**DPCBs**	**PPCBL**	**Commercial Banks**	***Total***
1990-91	8,323.95	56.30	--	3,017.45	3,517.69	*14,915.29*
1991-92	6,996.44	56.80	--	3,247.01	4,179.56	*14,479.31*
1992-93	8,645.40	50.80	--	2,978.00	4,525.91	*16,198.11*
1993-94	8,989.26	--	--	2,621.49	4,063.30	*15,674.05*
1994-95	14,525.74	--	--	3,756.74	4,040.79	*22,373.27*
1995-96	10,339.27	--	--	3,803.38	5,044.66	*19,187.31*
1996-97	11,687.11	--	--	3,431.13	4,429.43	*19,547.67*
1997-98	22,353.60	--	--	4,928.93	6,109.70	*33,392.30*
1998-99	30,175.96	--	--	5,439.97	7,236.00	*42,852.00*
1999-00	24,423.89	--	--	5,951.23	9,312.50	*39,687.60*
2000-01	27,610.20	--	--	5,124.20	12,056.00	*44,790.40*
2001-02	29,108.01	--	592.82	5,127.54	17,486.12	*52,314.49*
2002-03	29,270.17	--	1,421.11	5,485.39	22,738.60	*58,915.27*
2003-04	29,933.07	--	2,701.80	7,563.54	33,247.45	*73,445.86*
2004-05	37,408.84	--	12,406.82	7,607.47	51,319.78	*108,732.91*
2005-06	47,594.14	--	16,023.38	5,889.40	67,967.40	*137,474.32*
2006-07P	*34,529.86*	--	*16,081.99*	*5,269.56*	*48,962.19*	*104,843.60*

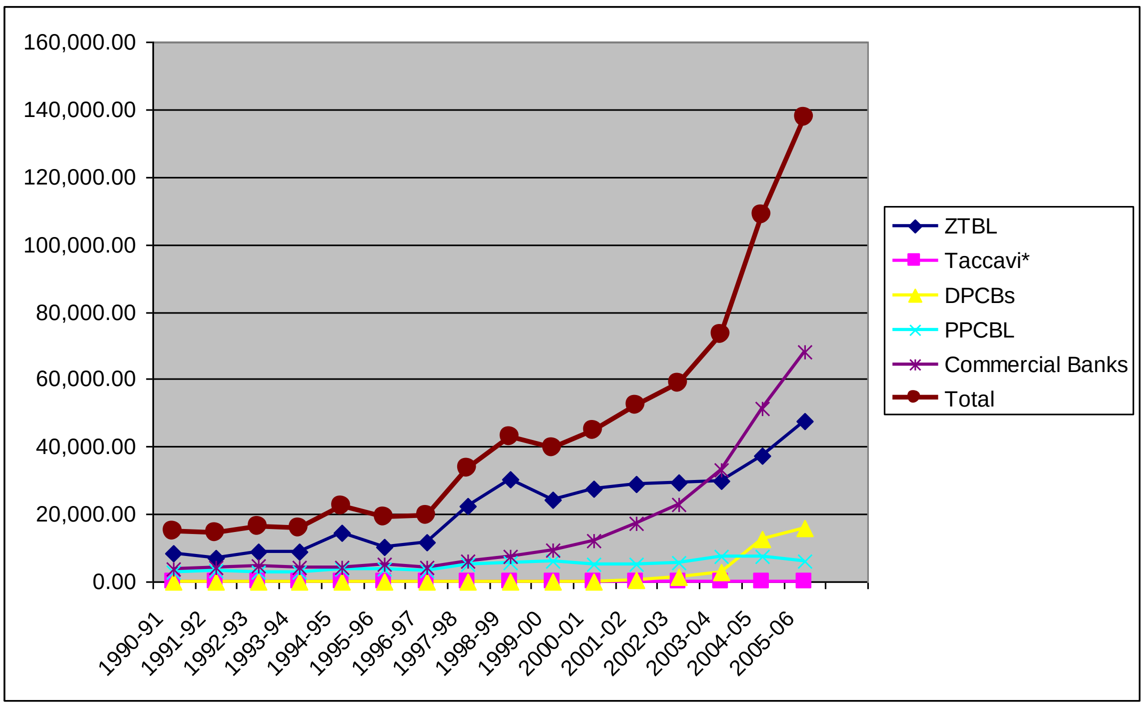
Source: Economic Survey of Pakistan, 2006-07
*: Taccavi Loans are no more in existence

P: Provisional (Jul-Mar)

Table and figure 1 show an increasing trend in the credit disbursements by the different institutions except for Taccavi which are no more advanced now a days.

These figures show the importance which Government attaches to the Agricultural sector. As the prices of farm inputs are on a steady increase it is imperative that the allocation and disbursement of credit have a matching trend with demand.

Fig:1 Credit Disbursed by Institutions



Credit has contributed very positively in the increase of agricultural productivity. To check its impact, different studies having been conducted from time to time a few of which are reviewed hereunder indicating issues, opportunities and a deep look into the system;

Waheed (2001) concluded that micro credit program was a vital intervention in poverty alleviation policy. The refinement in the program was required to be introduced in targeting the poor only. It was analyzed that in 2001, 21 percent of the loans went to 'well-to-do' and 'better-off' and the remaining to poor and very poor.

Ansari (2001) stated that crop productivity could be increased through the introduction and promotion of innovative agricultural technology. Agriculture as the backbone of Pakistan's economy, in the current drought conditions, needed more attention so as to resolve this problem and increase the productivity. Farmers were looking towards financial sources for taking loans on easy terms in order to increase their agricultural productivity.

Sheikh (2001) stated that almost 49 million poor lived in Pakistan consisting of 34 % of its total population. Inadequate resource allocation to education, health and rural development had deprived the poor unprivileged and poverty stricken population in rural areas of Pakistan. He also showed that commercial banks' perception of low rate of recovery of loans obtained by the landless poor and small farmers was not correct. He suggested that loaning agencies should arrange training for the borrowers and supervise the utilization of credit.

Iqbal *et al* (2003) suggested that the commercial banks and other financial institutions be encouraged to expand agricultural credit and extend the net of institutional credit to a larger proportion of the farming community especially, the small farmers. He further emphasized that the institutions should extend consumption loans to the needy farmers in case of a large-scale crop failure especially to farmers with good loan records and these loans be granted in addition to the credit required for their farm operations. Moreover a crop insurance scheme might be launched to provide cover to farmers against losses from drought, pest attacks, hailstorm, thunderstorm, heavy rains and other natural hazards on payment of small premium in addition to credit markup.

Acharya (2006) looked into the Indian Agricultural Credit system and pointed out that there was considerable unmet demand for rural credit. Local money-lenders continued to provide credit to the rural families, as the reach of institutional agencies to weaker sections has remained poor. Meeting the credit needs of 25 million non-farm informal sector enterprises continued to be a challenge to the rural financial institutions (RFIs). Though the coverage of micro-finance scheme had expanded, still around 70% of the poor were out of this network. The micro-finance sub-sector of institutional credit had not explicitly targeted the agricultural sector. RFIs had bypassed tenants and sharecroppers. More than 60% of the farm families were yet to receive the Kisan Credit Cards. The rate of interest charged by RFIs from farmers was considerably higher than that charged by financial institutions from urban consumers. That was beyond the means of owners of small or marginal farms, which were nonviable or viable at the margin, and the self-employed in the informal sector.

Bashir *et al.* (2007) found a positive impact of credit on the productivity in their study of impact of credit disbursed by the commercial banks on the productivity of sugarcane in Faisalabad District.

On the basis of above mentioned studies the major constraints faced by the farmers included eligibility and security problems, transactional costs / high interest rates, procedural difficulties, lack of technical know how and modes of repayment and too lengthy and cumbersome procedures.

A recent study by Bashir and Azeem (2008) confirms the above mentioned constraints in the district Faisalabad According to them "61.4 percent of loanees pointed out that banks' procedure was lengthy and cumbersome. About 77.2 percent of the loanee respondents reported that the interest rate was too high. As for as the cooperation of banks' staff is concerned, 45.6 percent of the loanee farmers were not satisfied with the behavior of concerned officials. About 72 percent of loanees complained that they did not get the loan in time. Security and surety problems were faced by 54.4 percent of the loanees whereas about 28 percent respondents said that the repayment procedures were rigid while according to about 35 percent of loanees it was too rigid".

They also observed that the loan taken for the production purposes was misused by a number of sample farmers either for the sake of consumption, marriages, repayment of the loan taken from the informal sources or even to cover up the legal costs of family or other disputes.

The credit system may be improved to get much better results in the form of improved qualities and quantities of the agricultural products. For the purpose below are some of the suggestions for the policy making process;

1. An appropriate amount of loan may be provided at the time when it is needed otherwise the loan may be misused and recovery would become difficult.
2. In case of any natural calamity the bank should revise the repayment schedule at the convenience of the borrowers.
3. It is essential that supply of inputs and know-how should be ensured along with the loan which is a missing link at present specially in the study area.
4. To avoid the misuse of loan supervised credit schemes must be revived and restructured.
5. Interest free lending on the basis of partnership must be strengthened.

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