ADDIS ABABA UNIVERSITY
SCHOOL OF GRADUATE STUDIES
INSTITUTE OF REGIONAL AND LOCAL DEVELOPMENT STUDIES (IRLDS)

ASSESSMENT ON THE MECHANISMS AND CHALLENGES OF SMALL SCALE AGRICULTURAL CREDIT FROM COMMERCIAL BANKS IN ETHIOPIA: THE CASE OF ADA'A LIBEN WOREDA

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A Thesis Submitted to the School of Graduate Studies of Addis Ababa University in Partial Fulfillment of the Requirement for the Degree of Master of Arts in Development Studies from the Institute of Regional and Local Development Studies

July 2009
Addis Ababa

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By: Atikilt Admasu

Approved by Board of Examiners

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Chairman, Graduate Committee **Signature**

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Advisor **Signature**

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Examiner **Signature**

Acknowledgment

First and foremost, I would like to extend my deepest appreciation to my advisor, Isaac Paul (PhD), for his kindness and assistance through out preparing this thesis. Secondly, I like to thank *Erer* Farmers Cooperative Union, *Ada'a Liben Woreda* Cooperative Promotion Commission, Commercial Bank of Ethiopia and Bank of Abyssinia, among others, for their untiring cooperation during data collection. Of course, I can not pass with out thanking Samrawit Tsegaye and Biruke Tekle for their contribution in the editorial works. Finally, all the gratefulness goes to my family, especially for Solomon Mitiku and Yared Mitiku, who have been there in each step of the way till the end of this program.

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LIST OF ACRONYMS AND ABBREVATIONS

ADLI	Agricultural Development Led Industrialization
Agric	Agriculture
BoA	Bank of Abyssinia
CBE	Commercial Bank of Ethiopia
CGAP	Consultative Group to Assist the Poor
DAs	Development Agents
EPRDF	Ethiopian People Revolutionary Front
FDRE	Federal Democratic Republic of Ethiopia
FFTC	Food and Fertilizer Technology Centre
MEDA	Mennonite Economic Development Associates
MFIs	Micro Finance Institutions
MoFED	Ministry of Finance and Economic Development
NBE	National Bank of Ethiopia
NGOs	Non-Governmental Organizations
RFIs	Rural Financial Institutions
SHG	Self Help Group
USAID	United States Assistance for Industrial Development

GLOSSARY OF LOCAL TERMS

Ada'a Liden	Name of a district and the selected study area in East Shewa
Amhara	Ethnic group in Ethiopia
Birr	Ethiopian National currency (1 USD = 11.1081 on March 31, 2009)
Dukem	Name of a town 10 Kms away from Bishoftu
Derg	A regime in Ethiopia that reigned from 1974 to 1991G.C
Fird Shengo	A form of court that is used at the Kebele level
Godino	Name of a town in Ada'a Woreda
Idir	Community association organized mainly for support members in times of grief from death
Iqub	Rotating credit association/ Community based informal saving institutions
Irrecha	A ritual ceremony carried out yearly in Bishoftu
Kebele	The Lowest administrative unit in Ethiopia
Kajima	Name of a village in Bishoftu Town
Oromo	Name of an ethnic group
Wereda	Name of a District
Teff	Type of crop used to produce a staple food
Udee	Name of a village
Ziquala	A Mountain where yearly rituals are held by Orthodox Christians

CHAPTER I

1. INTRODUCTION

1.1. Background of the Study

Agricultural development is the foundation of industrial development and, consequently, of a country's overall economic development. To attain agricultural development, every government must consider agricultural credit as an important policy instrument. Besides, agriculture has been the main stay of the economy for many developing countries which supports the majority of the population for their livelihood at subsistence level. In Africa, agriculture has been the main source of employment, income, foreign exchange, saving and investment. 80% of the total population of sub-Saharan Africa is dependent on agriculture for life sustenance, out of which, 70% are engaged in the production of agricultural products directly from farming and livestock production (Odiahmbo: 2007)

Being one of the sub-Saharan African countries, Ethiopia is not an exception from this reality. The share of the total population engaged in agriculture has been more than 85%. In fact, the government of the Federal Democratic Republic of Ethiopia (FDRE) has formulated an over all economic development strategy that is anchored in the development of the agricultural sector. Agriculture is expected to bring growth in the other sectors as well. In Ethiopia, Agricultural Development Led Industrialization (ADLI) has been believed to transform the subsistence form of production to a commercial oriented one (MoFED: 2002). This shows the level of emphasis that should be given to the sector considering the proportion of the population it supports and the level of income generated from it.

With this strategy in mind, assuming the achievement of agricultural development with out the support of the financial system does not seem easy. Indeed, the access to credit service for various purposes ranging from production and harvesting to marketing of agricultural products is vital. The egalitarian nature of the Ethiopian land tenure system (i.e. the predominant share of the agrarian society being smallholding) also leads to the

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1.2. Statement of the Problem

Capital has been among the prevailing problems that are frequently raised in relation to the stagnation of agriculture in general and small-holder farming in particular. It is needed to finance various aspects of the production, harvesting, and marketing of agricultural products. According to Assefa (1987), the poverty trap in the sector i.e. the low productivity, low income and again low productivity cycle can only be broken through the availability of credit for the small holders so that farmers will be fortunate to adopt new technologies, improve productivity and increase bargaining power to market their outputs at higher prices.

On the other hand, commercial banks know the sector for its unique set of risks. Among the predominant problems are the lack of physical assets for collateral and absence of predictable source of income for repayment of loans. The problems could arise from different factors such as changing climatic condition and market fragmentation. As a result, banks usually shift their lending business to markets other than agriculture. Besides, other problems such as lack of infrastructure, high loan administration cost and information asymmetry led to the limited operation of commercial banks (Pearce: 2004).

To alleviate these problems, many countries have been pursuing innovative mechanisms. These may include establishing Specialized Agricultural Credit Institutions, forming Rural Microfinance Institutions, and following group lending techniques, each of them having their own merits and demerits. For instance, Yaron (1992) criticized informal lenders and Micro Finance Institutions (MFIs) on the grounds of charging high interest rate, which is socially undesirable and the small nature of the loans. In Ethiopia, there were attempts to link small holders' with the banking sector through cooperative associations. For instance, loans used to be availed from the Bank of Abyssinia (BoA) against United States Agency for Industrial Development (USAID)'s loan guarantee program. It was reported that the bank's loan recovery performance was 100% for two seasons (Tesfaye: 2008). In addition, the Commercial Bank of Ethiopia (CBE) was providing loans to small scale farmers that have been increasing over the years (Grover

and Anteneh: 2004). This reflects the need and possibility of creating innovative approaches to improve smallholdings' access to bank credit.

However, there were no recent research works that studied the linkage between smallholding farmers and commercial banks in the credit market. Therefore, one of the main thrust of this study was to look at the issue closely in terms of its problems and prospects on contextual basis. It intended to give clear picture on the problems from various stakeholders point of view such as commercial banks, cooperatives, farmers and other institutions.

1.3. Objectives of the Study

The general objective of the study was to assess the mechanism of accessing small scale agricultural loans from commercial banks in Ethiopia and closely look at the existing challenges and prospects on contextual basis. The specific objectives targeted:

- To elucidate the existing modes of delivering small scale agricultural loans to farmers from commercial banks.
- To unfold the challenges and their causes in delivering small scale credit to farmers in the case area.
- To reveal the role of other institutions in facilitating the credit delivery process.

1.4. Research Questions

The study attempted to address the following specific questions:

- What are the over all small scale credit lending approaches of commercial banks?
- What efforts have been made to enhance small holders' access to small agricultural credit from commercial banks?
- What challenges do farmers face in a bid to access credit from commercial banks?
- What are the roles of the government in the process of availing small scale credit to poor farmers?
- How can other stakeholders participate in the process of small scale credit provision?

1.5. Significance of the Study

Primarily, the study is a partial fulfillment of the graduate program from the Institute of Regional and Local Development Studies (IRLDS). In addition, the output is sought to give insights to policy makers on the issue and also serve as a base for further advanced research on the area by the academia. In fact, credit for smallholding credit is of paramount importance. Therefore, the study can stimulate the interest of other stakeholders such NGOs and donors to give more focus to the sector. Considering the bulk of financial resources that commercial banks hold in Ethiopia, studies surrounding this linkage enhance the future endeavors to minimize the constraints and develop the positive aspects. The study is also aimed at giving concerned government agencies and non-government organizations clues on the policy gaps so that they focus to find ways to supplement it.

1.6. Scope of the Study

Geographically, the study is confined to *Ada'aLiben Wereda* and around the town of *Bishoftu*. Any conclusion drawn based on the study is contextually limited to the study area. In Addition, the study looks at selected sources of credit from commercial banks. It does not include credit services provided from other sources such as micro finance and inputs suppliers.

1.7. Limitation of the Study

The study was constrained by lack of adequate time and budget which, in turn, limited the size of sample selected for analysis. Moreover, the issues in question and the collected data required advanced analytical techniques and models to produce in-depth view about the general population. However, simple statistical tools and techniques were used to compromise with time. Thus, future researches can build up on the outputs of this study.

1.8. Organization of the Paper

The final report of this study is composed of the following parts. The first chapter is the introduction that includes the background, statement of the problem, objectives of the study, research questions, research methodology, and significance of the study, scope and limitations. The second chapter presents the theoretical framework and empirical literature review. Data description and analysis are dealt in the third chapter. Finally, chapter fourth entails the conclusion and recommendation.

2.1.2 Need for Agricultural Finance

Pearce (2004) noted the fact that studies in 150 different countries revealed the positive link between a well-functioning financial system and long-term growth, and national savings and economic growth. Especially, development of the rural sector that accompanies the improvement of living standard of the majority who are dependent on agriculture is a prime concern in developing countries. Rural finance in general and that of rural credit in particular is critical to reduce rural household vulnerability. The availability of agricultural credit helps the poor to smoothen consumption patterns as agricultural income is affected by various factors such as market prices, weather conditions and timely availability of technological inputs. The small holding farmer can also build up assets greater than the value of the liability. Hence, there is strong need to provide adequate credit facilities for sustainable operation and growth of the agricultural sector and farmers living conditions.

Golait (2007) also discussed the contribution of credit for agriculture, as a non- land input. In order to ensure adequacy, the study considered two dimensions of agricultural credit i.e. availability of credit that implies the volume of supply and distribution that shows the fairness in allocation. Nonetheless, Kahlom and Singh (1984) emphasized seeking for agricultural credit facility should not be for the mere question of money-lending or replacing individual lenders with institutional lenders. Rather, it should be development oriented by contributing to the betterment of the society in terms of productivity of land, labor and capital. Thus, agricultural credit involves various intricacies of credit delivery such as *"...how much to borrow, what for to borrow, what would be paid-off, what should be the repayment schedule, ...etc. of the institutions that provide finance to farmers , their organization and operation, coordination, management and controls ...Etc; and of the societies interest in credit for agriculture..."*.

Related to the contributions is the form of credits through which capital is channeled. Similar to other credit products, agricultural credit can be categorized in to various time bands of short term, medium term and long term credit. Short terms credit is usually meant for working capital and ensures adequate liquidity exists in the business. It is

usually repaid at the end of a production season in anticipation of source of income usually from a certain product (Mukwereza and Manzungu: 2003).

As the core of this study revolves around assessing the issues that affect agricultural credit delivery from commercial banks, basic understanding of banking business and the associated risks is deemed important.

2.1.3. Banking

2.1.3.1. Nature of Banking

Gup and Kolar (2005) defined a bank as"... *a financial institution that is owned by stockholders, operated for profit and engages in lending activities.*" Understanding the nature of banks arises from knowledge of their underlying thrust and activities. It is important to understand the specific role of banks as other types of financial institutions such as micro finance institutions, and saving and credit associations can also give the same types of services that banks provide. Quite often, the legal frame establishes the financial playing field for activities of commercial banks set by the central banks of countries (Paul:1996). The legal definition of banks by central banks, as regulator and supervisor of their safe operations, appears important. Therefore, the legal definition can be used to make proper distinction between financial services provided by commercial banks and other financial establishment. Accordingly, the following definition by the National Bank of Ethiopia, the regulatory body of the Ethiopian financial system, is believed to express banks in Ethiopia:"... *a company licensed by the National Bank to undertake banking business or a bank owned by the government" (Negaret Gazeta:2008)*

As indicated by the Proclamation to Provide for Banking Business number 592/2008, banking business has been expressed as a business that delivers the following operations:

- *receiving funds from the public through means that the National Bank has declared to be an authorized manner of receiving funds;*
- *using the funds [received from the public]....., in whole or in part, for the account and at the risk of the person undertaking banking business, for loans or investments in a manner acceptable by the National Bank;*

- *The buying and selling of gold and silver bullion and foreign exchange;*
- *The transfer of funds to other local and foreign persons on behalf of the banks themselves to their customers;*
- *The discounting and negotiation of promissory notes, drafts, bills of exchange and other evidence of debt;*
- *Any other activity recognized as customary banking business, which a bank engaged in the activities ... authorized by the National Bank;*

2.1.3.2. Types of Banks

All banks do not have the same nature and may not provide all sorts of financial services. According to Paul (1996), banks can be classified based mainly on their functions, ownership and domicile. For the purpose of this study, the author's six classifications of banks based on function are considered:

Commercial Banks: These banks perform all kinds of banking business and generally finance trade and commerce. As their deposits are normally short-term, they advance short term loans to businessmen and traders. They avoid medium term and long term lending.

Industrial Banks: These banks are also known as Investment Banks and mainly meet the medium term and long term financial needs of industries. Such long term needs can not be met by commercial banks which generally deal with short term lending. The main features of Industrial Banks is that they accept long term deposits and make long term lending to industrialists.

Agricultural Banks: Agricultural credits are different from those of industry and trade. These types of banks deal with the financial needs of agriculturalists that require short term loans to buy seeds, fertilizers and other inputs, and long term credit to make permanent investments on land, and purchase agricultural machinery and equipment.

Exchange Banks: They deal with foreign exchange and specialize in financing foreign trade. They facilitate international payments through the sale and purchase of bills of exchange and thus play an important role in promoting foreign trade.

Saving Banks: These banks are established to promote the saving habits of a particular community and mobilize the deposits.

Central Banks: It is the "Apex" institution that controls, regulates, and supervises the monitory and credit system in the country. The functions of the central bank include: issuance of domestic currency notes, acts as banker, agent and financial advisor of the state, custodian of the country's reserves in international currency, serves as lender of last resort, and acts as controller of credit.

2.1.3.3. Inherent Risks and their Management in Banking Business

Sanatamero (1996) presented six types of risks that banks face in banking service delivery. These are: *Systemic market risk, credit risk, liquidity risk, operational risk and legal risk.* The paper explains systemic/ market risk as the risk that affects the bank's profitability due to the asset value change associated with systemic factors. The two main concerns in banking business related with market risk are changes in the general level of *interest rates* and the relative value of currencies or *foreign exchange* risk. Where as, *Credit risk* arises from the non-performance of a borrower from the inability or unwillingness to perform according to contractual repayments or the failure of the borrower to meet repayment obligations as per the contractual agreements concluded with a bank. This will affect the financial position of the lender and other creditors to the lender such as depositors. *Liquidity risk,* on the other hand, is the risk of a funding crisis. For instance, when the bank is planning for growth and unexpected expansion of credit, it triggers the potential for unexpected funding crisis. Non-repayment of loans also exposes the bank to liquidity crisis as it affects the cash flow plan of the bank. *Operational risk* arises from the failures in "*...record keeping, processing system failures and compliance with various regulations.*" *Legal risk* arises from two dimensions. First, changes in the existing statue, laws and legislations that put previously concluded transactions into

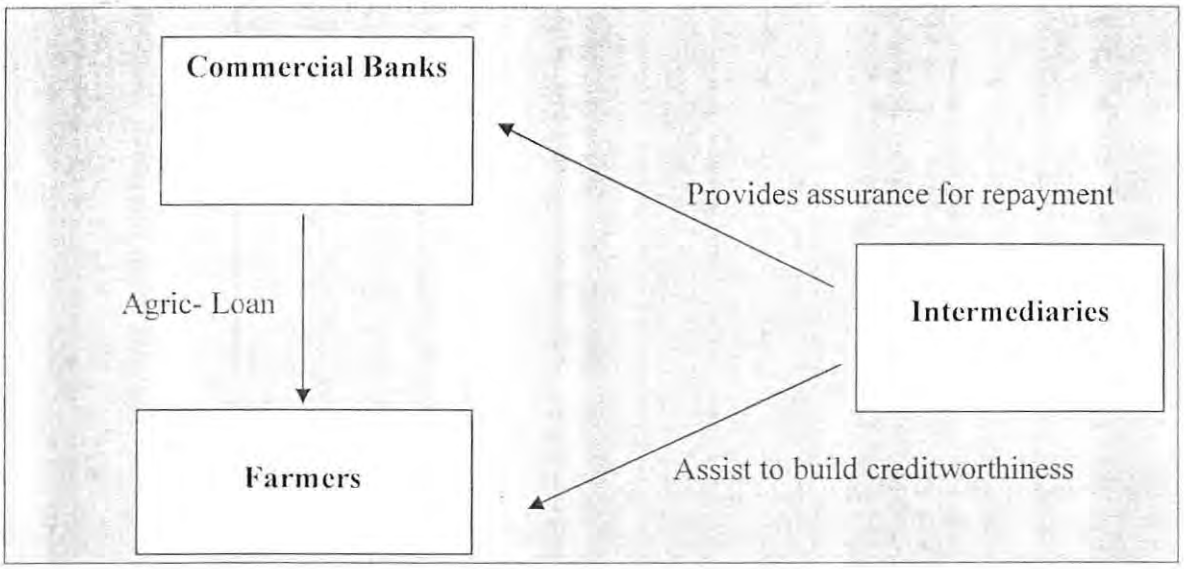
jeopardy even if counterparties are performing adequately and will do so in the future. Secondly, legal risk can arise from deeds of management and employees that may include fraud, violations of regulations and laws. All financial institutions are with all types of risks despite the difference in the level of exposure.

Primarily, very relevant to agricultural credit is the threat of credit risk arising from non-repayment of borrowed funds by farmers, which is also referred as 'default', which could instigate other risks such as liquidity and legal risks. According to Sy (2007:6), credit default was defined from two perspectives, delinquency and insolvency. Credit default from delinquency is "*... a failure to meet a loan repayment by a due date.*" On the other hand, insolvency was defined as "*...a situation where [borrower's] assets are less than liabilities.*" However, most definitions of credit default are a 90 days delinquency in repayment of loans.

In order to minimize the potentials that can instigate the risk of loan default, the role of other institutions appears crucial. Gupta and Shroff (2003) noted the role of membership organizations that can facilitate services. Odiahmbo (2007) discussed the role of the government in building infrastructural capabilities localities so that lenders and borrowers have a platform to establish relationship.

Figure 2.2 depicts the conceptual framework of agricultural credit delivery for the smallholding farmers. The loans originate from the commercial banks and end up for use in the hands of farmers. Intermediaries such as the government and membership organizations may need to facilitate the communication between the transacting entities and give assurance as required.

Figure 2.2: Conceptual Framework of Agricultural Credit from Commercial Banks



2.2. EMPIRICAL LITERATURE REVIEW

2.2.1. The Financial System Approach to Small Scale Agric-Credit

Adams et al (1987) attributed past failures to expand financial services in the rural areas and the agricultural sector in particular to the numerous failures in political, social and economic endeavors. According to the author, political interference by the government was a cause for many of the failures in expanding financial markets in rural areas. Governments, in both developed and developing countries have been emphasizing the need for income transfers and extending subsidies to meet social objectives. In most developing countries, governments attempted to bring income transfer to the rural poor through loans. However, past endeavor ended up by negatively affecting the credit culture and discipline of the rural population. As a result, financing agriculture through formal institutions becomes difficult. The past experience of various institutions created myth leading to the conclusion that the rural financial market is unfavorable to institutional operators. In addition to the obvious external factors that affect both the borrowers and lenders such as natural disasters, poor markets and unsuitable land tenure system have enormous contributions to the thinning of the rural credit market.

As a remedial solution to the problem, there is need to establish specialized banking and credit institutions dedicated for agriculture only that fits the specific and unique nature of the sector (FFTC:2007). However, the idea has also been refuted on the grounds of inefficiency problems. Rather, the need to create innovative financial products and delivery mechanism to promote agricultural finance within the financial systems approach has been emphasized (Pearce: 2004). For instance, introducing flexible and more accessible saving facilities reduces risk of seasonal income loss. By the same fashion, credit culture and discipline can also be promoted through client education, use of group collateral, and close and regular monitoring of clients by loan officers.

Further more, the need to establish institutions with specific laws and regulations are crucial. Nevertheless, improvement of agricultural productivity, competitiveness and income are the most important focal points that can help ensure eligibility and development of credit market and the overall rural economy. This reflects the possibility of using the traditional banking businesses in the development of credit market in rural areas.

Andrews (2006) discussed the new approach in agricultural credit called "the financial systems approach". The paper clarified the need for commercial and market based approach for financial services that can cover large segments of the rural population on a sustainable basis. It considered financial services as part of an interactive system of financial institutions, financial infrastructure, legal and regulatory frameworks, and social and cultural norms.

Pearce (2004) also noted that commercial credit delivery should follow the financial system approach in to ensure adequate out reach and sustainability of financial services. Removal of distortions that cause financial repression such as withdrawal of the state from direct credit provisioning or subsidies, deregulation of interest rate regime and abolition of credit controls are important measures in the financial markets. It is also necessary to eliminate many of the policy distortions such as interest rate ceilings and credit allocation. The financial system enhances more competition and strengthens prudential requirements through supervisory authorities. The involvement of supervisory

authorities has helped to establish and/or improve tight prudential limits such as capital adequacy, related borrowers lending and setting aside adequate provision for credit risk. In addition, formation of both private and public institutions is essential by creating suitable environment for emergence and growth of regulatory regime and financial discipline. Accordingly, the financial systems paradigm has three strategic priorities:

> "*... Creating a favorable policy environment including macroeconomic stability as well as a reduction in the historical bias against the rural sector, strengthening the legal and regulatory framework so that rural financial institutions which are performing well can provide a variety of financial services to low- income households, and building the capacity of RFIs to deliver demand driven credit, savings, and insurance services in a self sustaining manner.*"

One of the major factors constraining the development of credit market in rural areas has been the lack of proper collateral to be used as lien in case of default by borrowers. Financial institutions are reluctant to venture in rural areas as small holding farmers do not have the capacity to offer collateral eligible in the eyes of such institutions' policies and procedures. Some governments offer financial institutions guarantee to replenish lost funds in cases of default by designing various loss sharing mechanisms in the credit delivery system. FFTC (2002) shared the experience of some developed and developing Asian countries governments' endeavor to assist small holding farmers by establishing farm credit guarantee systems. The government's involvement to guarantee the lending process is essential for the sound operation of agricultural banking system. However, rigorous scrutiny of individual borrowers for their creditworthiness and investment potential should be a matter of higher priority for lending institutions. As part of the endeavor to ensure sustainable agricultural credit regime for the small holding farmers, Yaron (1992) raised the importance of diversifying rural credit apart from agricultural credits. Other non-farm activities are important to reduce the danger of loan repayment failures as the agricultural risk is faced with various *'co-variant risks'*. Financial institutions operating as intermediaries in rural market should finance all segments of the rural economy, indiscriminately, in order to carry diversified, balanced and less risky loan portfolio in their assets.

According to Assefa (2004), countries use innovative ways to facilitate the financial service intermediation in the rural areas. Commercial banks' lending mechanisms can be of one or both of the two types i.e. direct lending (One-Tier) to the beneficiary and/or through other form of agencies (Two-Tier). Under the former approach, the bank directly extends the credit product to the end user. In such a case, the beneficiary concludes the loan contract directly with the bank and the repayment obligation will be limited to the beneficiary. In the latter case, organization or agencies such as cooperatives, governments or other parties make the borrowing from the bank and transfer the fund to the end users who can also be members of the associations.

Despite the many efforts, FFTC (2007) noted that the financial systems approach to delivery loans in the rural market has not been with out challenges. Previous experiences in developing countries in financing agriculture through commercial banks exhibited certain features that hamper credit expansion in the rural market such as strict collateral requirement. As a result, access by small holders to financial institutions has been highly limited. Even though agricultural credit policies rely on commercial banking intermediation, the institutions are not "compatible" with the borrowing capacity of farmers who have smaller credit demand commensurate with their land size. Therefore, the sum effect of the barriers triggers the need to redesign and improve the credit delivery system that may include creating new credit products and adopt innovative lending approaches. A good instance for the new approach, apart from the traditional ways of availing credit, is the adoption of the farm credit guarantees system by governments. In both developed and developing Asian countries, the farm credit guarantee system has been applied to help farmers lacking proper collateral and create sound operation of agricultural banking systems in rural areas (FFTC:2007).

As an alternative to the adoption of innovative methods, Yaron (1992) raised the need for applying mobile banks that can be taken as techniques to reduce administrative costs of delivering financial services. A more recent case study by Gupta and Shroff (2003) in India implied the need for opening satellite branches. It understands the nature of the ecological conditions and inherent environmental risks in drought vulnerable regions and, then, views stationery branches as incompatible in rural areas. Moreover, fixed branches

are not functional to reach the population in highly dispersed populations. Through opening of satellite branches that may be available for service periodically "...*weekly market days*...", the rural people can meet their credit needs and provide small saving schemes to the bank as well.

There are conclusive ideas on the need to build institutions to create viable rural financial markets. Targeted credit has always been considered to promote dependence on the beneficiary. Thus, interventions in rural financial markets should be temporal and targeted at supporting institution building. However, the lack of adequate emphasis is the characteristics of supply-led credit institutions (Yaron: 1992). In view of this reality, there is need to consider other lending institutions such as commercial banks.

2.2.2. Commercial Bank and Other Sources of Credit

Even though non-bank financial institutions have certain salient aspects, they also present adverse features in their services to the rural poor as compared to provision of credit services by banks. For instance, MFIs are known to provide credit at a higher interest rate. For MFIs, which are mostly credit driven, effective interest rates reach as high as 120% (Kellogg Foundation: 2002). Yaron (1992) also argued about the existence of perceived shortage of credit in the rural market that led to the interventionist approach by governments in the form of subsidies and directed lending. Such perceptions create market distortions in the rural credit market as the real demand and supply are not at equilibrium. The main mechanisms for the execution of such policies of the government were specialized financial institutions that use donor and aid funds. However, most state operated and donor supported agricultural credit operations were unsuccessful and the results were below expectations. As the transaction and processing costs are high for small farmers to borrow from commercial lending institutions, only large scale farmers can participate in the process. In developing countries, due to the absence of strong formal credit markets, informal lenders begun to flourish and monopolize the credit market. Nonetheless, the informal credit market by itself has variety of limitations including limited diversification of loan portfolio and limited geographic coverage that fails to guarantee adequate supply in the market. Some times, due to their monopoly

position, the informal lenders charge very high interest rates on loans and, hence, are socially undesirable.

Thus, institutionalized lending to small holding farmers seems inevitable. Commercial banks, as actors in the financial intermediation, have roles to play if adequate incentives are created in line with their profitability objectives. In the assessment of Indian agricultural credit, Golait (2007) noted the role of competition and the quest for higher profits driving commercial banks to explore new ways of lending such as contract farming, extending credit for the various stages of agricultural production and other intermediaries. These incentives also help to facilitate the expansion of commercial bank credit to agriculture. Thus, the credit need of smallholding farmers in terms of the positive as well as negative attributes is crucial to see the gap with commercial banks.

2.2.3. Credit for Small Holding Farmers

In order to bring sustainable growth for small holding farmers, credit facilities should be offered in various forms to meet the multifaceted needs. Gupta and Shroff (2003) identified about four classes of loans. The first sort of loans is for survivals which help farmers to recover from hardships and are inherent in drought stricken areas. The second type of loans is for urgent needs to meet socio-economic commitments such as marriage and festivals. Third in line is loan facilities used for productive purposes such as fertilizers and improved seeds where institutional credits can intervene as likelihood for repayment of such loans is relatively high. The fourth type of loans needed by small holding farmers is those to be used for recurrent and operating needs and is usually smaller in amount. Such types of loans fill the income gap between production and harvesting seasons.

Mukwereza and Manzungu (2003) commented that institutions entrusted with provision of credit service should be viable in order for agricultural credit to impact the rural economy on a sustainable basis. Basically, the institutions should strive to ensure proper disbursement of funds and collection of repayment. An institution providing financial services should work on the following activities;

- Staff development activities to enhance the credit delivery process
- Decentralized structures to speed up the credit delivery process
- Establish system for proper monitoring of utilization of funds
- Ensuring collection of funds and take legal action when appropriate
- Supporting clients through education as *"fore-closure does not indicate a progressive lending policy."*

Golait (2007) further discussed the benefits of creating linkage between Small Holding Group (SHG) and banks on the existing banking infrastructure implying the need for cooperation between various supporting institutions to augment credit to small holding farmers.

2.2.4. The Role of Supporting Institutions in Small Scale Agric-Credit

Gupta and Shroff (2003) argued that membership based organizations such as cooperatives have positive contributions towards credit expansion. They are considered useful in remote areas as their membership is composed of voluntary staffs, which can use their knowledge when making loan assessment, and create community peer pressure for loan repayments, and demand low level of institutional set up and infrastructures. These organizations, whether formal or informal, can play a vital role in expanding financial service to rural areas. By partnering different farmers' associations, transaction cost of lending can significantly be reduced as it makes dealings with groups as a single processor rather than numerous and scattered farmers.

Yaron (1992) also presented empirical evidences that attest the success of credit delivery systems that create and involve other supporting institutions. According to the assessment made in South Korea and Taiwan, loan collection records exceeded 90% through integration with cooperatives. The basic reason for such a higher collection performance was the "*...Strong village cooperative systems and social cohesiveness...* ". Despite the fact that agriculture is high risk sector as compared to other economic activities, knowledge and application of the right incentives and legal enforcement structures help to expand credit delivery and improve the repayment rates.

As a prime actor to realize development of communities through their various incentives, governments also have the responsibility to involve in such processes. Odhiambo (2007) emphasized the role of the government in terms of the need for public sector investments in rural infrastructures that enhance more efficient performance and less dependence on government subsidies. Kellogg Foundation (2002) noted that rural investments are one of the important contributions that governments should facilitate for the development of the sector. Investments can be in the form of rural roads, water supply, electricity, health and education. Infrastructural developments improve the economic and financial returns of private investments increasing the potential of farmers to borrow as it also facilitates improved collection and viability of financial institutions, directly and indirectly. In addition, it also prepares the ground and lays the foundation for financial institutions to pursue foreclosure procedures on defaulting borrowers. Therefore, the cumulated efforts of the various actors are essential to ensure the survival of financial institutions participating in the rural markets. Golait (2007) discussed the role of policy makers by citing India as a case in point. Policy makers can also play important role by creating conducive environment, and putting policies and making appropriate interventions that enhance efforts by ensuring prudential banking practices.

As a model of favorable government intervention in the credit market, Olaitan (2006) remarked on the experience of the agricultural credit guarantee scheme in Nigeria, which was established in 1977 where the Federal Government and the Central Bank of Nigeria created a joint fund with 60:40 ratios to provide guarantee for credits extended to finance agricultural activities. In default scenarios, 75% of the outstanding balances of credits are paid from the allotted guarantee fund to the financer less any realizable income form sale of collaterals. However, the scheme was not with out obstacles. The major challenge was the lack of participating banks in the scheme as banks found it unprofitable to borrow short term deposit and extend long term loans. Other impeding variables for the scheme include; lack of adequate capital, farmers' refusal to repay loans, poor project appraisal by banks, sufficient collateral and cost of administering the loans. The Nigerian experience demonstrated the need for cooperation between banks, the government and other institutions partaking in the process to bring efficiency with mutual benefits.

Pearce (2004) also presented the intervention by NGOs in the rural credit market. It showed evidence that NGOs play roles in rural credit delivery as banks tend to become more risk averse and reluctant to extend credit for agricultural economic activities. These inabilities of banks to meet the financial service needs of rural population have given way to an increased role for non-governmental organizations (NGOs) in the provision of rural finance in general and try to fill the gap. CGAP (2005) also presented the role of donors as a crucial ingredient for the success of many financial institutions financing agriculture. Flexible and high quality technical assistance to financial institutions helped in adapting loans to rural clients. However, donors should avoid acts that may distort the market and focus on capacity building of local people. This shows the constraints are not limited to borrowers only but the supporting institutions as well leading to the need to assess it.

2.2.5. Constraints in Small Scale Agric-Credit Delivery

Andrews (2006) described agriculture as a sector with unique set of challenges for financers, especially in extension of loan facilities to that of small holding farmers. The challenges have varying nature that affect both the lenders and farmers, and emanate from factors that are both internal and external to borrowers and financial institutions. Hence, understanding the problems and their causes can be a step to the viable ways out. Other financial institutions, apart from commercial banks, share the fact that micro-credit intervention for poverty alleviation and income generation is not without challenges and constraints. The challenges may prevail in the form of high interest rate, absence of regulatory framework and advances by NGOs without sustainability of the programme.

According to Stiglitz and Weiss cited in Komich and Ohlmer(2007), there are two types of credit constraints that farmers face. The first known as *'redlining'* refers to institutions' exclusion of farmers from credit privileges instead of offering them other contractual requirements such as higher interest rates and collaterals to compensate for the relatively higher magnitude of risk assumed from individual counterparties. The second form is *'credit rationing'*, by which farmers with the same characteristics, are discriminated as some getting loans and others being denied.

Gupta and Shroff (2003) mentioned the great mismatch between how official lenders perception of rural credit and the rural poor view of it. The perception difference had led to the multifaceted problems of small holding farmers who could not have adequate access to agricultural credit to satisfy the various needs from production of primary products to delivery in market. According to CGAP (2005), determinants of agricultural revenue in the rural economy are covariant. Generally, delivery of credit for small scale agriculture is challenging in areas where the population is less dense, distance between clients is great, transportation networks are poor, and small financial transactions due to low level of income. Particularly, agricultural credit is risky as it is difficult to depend on cash flows rather than collaterals due to factors such as natural calamities, fluctuating market prices, unpredictable low yields, lack of market, and loss from poor storage conditions.

It is worthwhile to separately treat what the lenders, borrowing farmers and other supporting institutions including the government are responsible for in materializing the envisioned agricultural credit regime for the rural community.

i. Borrower Related Challenges:

Zeller et al cited in Komich &Ohlemer (2007) classified farmers in to four groups based on the behavior they exhibit in relation to credit constraint. The first is referred as voluntary non- borrowers who willfully reject borrowing as they may be risk averters or want to use only up to what they earn. They may also exhibit prudential approaches in their access to credit. The second groups known as non-rationed borrowers are distinguished as those who want to borrow the combined credit facilities available from all lenders. Rationed borrowers compose the third group whose credit appetite is so high that they want to borrow more than what the credit market can offer at a time. The last but not the least is involuntary non-borrowers with no access to credit. Borrowing costs for such borrowers are so high that they perceive their position as highly unlikely to get access to credit.

According to Pearce (2004), small holding agricultural borrowers pose high credit risk, and create high operating and transaction costs for formal financial institutions. Besides, lack of collateral has been the classical reason for failure of the credit market in the rural areas to create buffer in case of default. According to Gupta and Shroff (2003), most farmers hold their assets in the form of live animals such as goats, poultry and cows. This gives farmers the chance to reshuffle capital forms, seasonally. Banks consider this conversion of assets as misutilization of borrowed funds out of the loan agreements. However, if a farmer continues holding a particular asset, he/she will lose the particular activity or settle for loss. Moreover, Farmers do not have sufficient savings to create capital and assets that can be held as collateral for borrowing.

In addition, Komich &Ohlemer (2007) emphasized information asymmetry in credit market as a challenge in lending decisions. Lending institutions often need information on such areas as credit performance, transaction and deposits, cash flow statements and other information valuable to evaluate the credibility of the borrower. Nevertheless, most rural borrowers do not keep record of their performance as they may not have such commercial oriented engagement. This led the bank to require high collateral to secure extended funds and compensate for the lack of information about the particular borrower which by it self is a problem.

Mukwereza and Manzungu (2003) remarked on the crucial nature of building knowledge of the potential of the production areas and the resources of farmers during the process of credit application, monitoring of farmers production activities and transportation of farmers produces. Tripartite arrangements with agro- processors or marketers serve as mechanism to resolve the market as well as the transportation challenges. Intermediaries set the required quantity and quality of produces and extend the corresponding level of support for farmers such as obtaining inputs at a discount and economies of scale during distribution. Adams et al (1987) also argued that contractual arrangements between, financial institutions, producers and sellers reduce price risks, enhance production quality and endures repayment of borrowed funds. Therefore, the partnership enables commercial banks to rely on the intermediaries in extending financial resources to

farmers. Accordingly, the concept of financial products delivery system has advantages for farmers with out their own financial resources.

The high operating costs in the process of delivering the necessary credit is another problem for financial institutions. This is mainly attributed to the small size of borrowers and the dispersed settlement of rural population.

ii. Lender Related Challenges:

Formal financial institutions such as banks pursue relatively stringent lending policy and procedure. The stringency helps to reduce credit risk by discriminating borrowers but ends up in excluding the rural population by creating "social access barrier". In addition, the low educational level and the need for formal documentation also bar the small holders from accessing financial resources. The rural community face high access cost as the formal financial institutions are urban based with almost all their branch networking in the urban setting (Goodland et al cited in Pearce:2004). According to Golait (2007)'s conclusions of the assessment in India, agriculture credit was still inadequate and the banking sector was hesitant on various grounds to deliver credit to small and marginal farmers. Furthermore, the concerted effort by different concerned bodies to strengthen the flow of agriculture credit by exploring new innovations, product designs and new methods of delivery and processes is fundamental.

iii. Other Institutions Related Challenges:

According to Koza et al (2004), one of the reasons for the absence of rural agricultural credit is the policy prohibition to use land as collateral. It is common knowledge that land is the main resource and asset for farmers. Yet, land in most developing countries is the property of the public and individual propriety is not attached to it. Therefore, it can not be taken for registry as lien for loans. Moreover, land holdings are too small in size that sustainability of production could not be guaranteed.

Poor contract enforcement scenario due to weak institutional capacity is another dimension of the problem. It is a common problem in many developing countries that

leads to high enforcement cost and takes long time through the bureaucratic mechanisms. As a result, even though a borrower has collateral to offer, it may be declined from qualifying for the facility in fear of the shortcomings. (Pearce: 2004).

Andrews (2006) noted the political intervention of governments through various methods by giving subsidies that resulted in *"crowding out effect"*, directed lending, and undermining the payment morale of borrowers through debt forgiveness and interest rate reductions. Andrews argued that:

> *"... the provision and design of agricultural finance have largely been driven by pressures to finance farm production and raise rural living standards, rather than build sustainable infrastructure for rural finance. When the government officials face a perceived choice between promoting the maximum outreach of rural financial services by building sustainable institutions and using institutions to channel finance in direct support to technology adoption, subsistence food production and rural infrastructure development, regardless of long term sustainability, they usually opt for the latter, at the expense of sustainability."*

Lack of credit culture in the rural market has been the tradition through farmer debt pardoning if such debt threatens the land tenancy of smallholdings. This signals the reluctance from the government side to enforce strict loan recovery that erodes the confidence of financial institutions.

2.2.6. Small Scale Agric-Credit in Developing Countries

Agriculture in developing countries is predominately small scale. The very low size of land holding leads to low level of operating capital and low investment in depreciable assets. Consequently, the sector has been provided with little financial resources as compared to other sectors. The nature of the sector led to 70% to 80% of the small holding farmers to be denied access to credit. The rationales for the absence of credit make a vicious circle of argument. Credit has not been provided to the agricultural sector as it is unproductive and, on the other hand, agriculture is unproductive and the existing

potential for profitability could not be exploited because it is not supported with sufficient capital (Kahlon and Singh: 1984).

According to Yaron (1992), short term and long term agricultural credit demand has led to the expansion of formal agricultural credit institutions in most developing countries. The need for adoption of agricultural credit has been initiated by farmers' requirement for timely availability of agricultural technologies and inputs. However, commercial lending institutions have been extending credit only to large scale farmers and ignored the small holding farmers due to the high processing and transaction cost and lack of adequate security. The tendency led to the development of informal credit institutions that do not require the fulfillment the constraints with the formal institutions. Komich & Ohlemer (2007) state that credit markets in developing countries are inefficient. The prime reasons for market imperfections include: interest rate ceilings imposed by governments, expansion and dominance of informal credit suppliers, large transaction costs incurred by borrowers, information asymmetry and moral hazard problems.
There have been attempts to provide rural credit in general and agricultural credit in particular for small holders in developing countries. Some institutions extending the credit obtained funds from external sources such as external donors. Still, others were forced by the government to lend at concessional interest rates below market rates. In addition, rationing credit facilities for agriculture had also been ignoring competition as a variable. Hence, establishment of specialized agricultural financial institutions created by the state have also been imperative. (Komich &Ohlemer: 2007).

Glance at the results of such practices in Africa by Koza et al (2007) witnessed mixed results. Some banks became totally insolvent and ended up to be rescued at larger public cost. Some agricultural banks in Benin, Togo, and Senegal Cote d'ivorie have collapsed. On the other hand, some banks were able to survive and meet their intended objectives in some countries such as Benin and Cote d'Ivorie. Countries succeeded in employing the excess liquidity in the banking sector for the export of Cocoa in the 1990's.

Yaron (1992) reasoned that the adoption of several innovative resolving mechanisms apart from the traditional banking products and forms of collateral were the factors

behind the success of the previous agricultural credit provisions. Arrangements such as group lending through homogeneous lending groups and cooperative membership enabled the availability of credit for small farmers. The studies show both the dark and bright sides of agricultural credit evidenced by the experience of several countries. There is a possibility of bringing agricultural credit to success for the development of small holders' economy and, on the other hand, there are costs of the adverse effects from the resultant mismanagement.

CHAPTER III

3. RESEARCH METHODOLOGY AND THE STUDY AREA

3.1. RESEARCH METHODLOGY

3.1.1. Research Method

The basic research method chosen for the study was explanatory. This method was chosen to identify and explain the challenges with their causes of the variables affecting agricultural loan delivery. Moreover, the effects of the problems on the agricultural loan delivery and recovery in the context of *Ada'a Liben woreda* were explained.

3.1.2. Sample Design and Frame

The issue of access to credit requires consideration of different variables as it incorporates the contribution of various stakeholders. With such understanding, the concerned individuals and institutions were contacted to seek expert opinion in addition to collection of data from farmers. Accordingly, selected individuals from commercial banks, cooperatives and farmers composed the sample for the study. The executives and credit experts from the state owned Commercial Bank of Ethiopia and the privately owned Bank of Abyssinia were specifically selected to represent the commercial banks. The basis for choosing the two banks was their relative exposure to agricultural credit delivery in the area, as learnt from the literature. As the issue of credit requires access and operational knowledge of bank lending policies and procedures, four individuals (The Commercial Credit Committee Chairman and Credit Assessor from head office, and *Bishoftu* Branch Manager and Loan officer) from CBE and four Individuals (Credit Department Manager and Deputy, Credit Department Manager) from BoA were selected through purposive sampling technique and were subject to professional opinion assessment. From the intermediaries, management representatives of *Ada'aLiben Woreda* Cooperative Promotion Commission, *Erer* Farmers Cooperatives Union and Primary Cooperatives were the subject of this study. Accordingly, heads of both the *Woreda*'s Cooperatives Promotion Commission and *Erer* Farmers Cooperatives Union were contacted for the key informant discussion. On the other hand, from the 47 Primary

Farmers Cooperatives found under the umbrella of the Union. 4 primary cooperatives (*Dukem, Godino, Kajima* and *Udee*) that operate in the *Ada'a Liben Woreda* were selected using multi-stage purposive sampling. The criteria used to select the sample primary cooperatives include: year of establishment, membership size and aggregate loan amount taken. Individuals who were responsible for financial matters of the four primary cooperatives were chosen for key informant discussion using purposing sample technique. Finally, considering the limited time and financial resources, aggregate numbers of 100 individual farmers who were end users of the loans and composed 2% of all members of the four primary cooperatives were selected for survey to gather data and seek opinion.

3.1.3. Data Collection Techniques

The data collection process was carried out in two ways. First, opinions were sought from the selected individual key informants from commercial banks and the intermediary primary cooperatives, their Union and the Cooperative Promotion Commission. To conduct the discussion with the informants, two independent interview guidelines were prepared, one for the commercial banks and the other for all the remaining informants. The checklist helped to structure the flow of opinion and to be consistent with the conceptual framework. It also included questions designed to capture description of the institutional approaches followed in the agricultural loan delivery process in general and the case area in particular. Second, structured questionnaires were administered on the sample farmers who were also members of the selected cooperatives. The questionnaire was organized in to eight parts to assess the socio-economic profile, asset ownership and facts about borrowing experience of farmers.

To conduct the survey, four data enumerators were recruited and given orientation on how to interpret the questions for respondents. Accordingly, pilot survey was conducted on sample farmers from the *Dukem* Primary Cooperative by taking 15 individual farmers. After making the proper modifications on the questionnaire, the survey was carried out on a total sample of 100 farmers who were also members of the primary cooperatives based on the established sample proportion.

3.1.4. Sources of Data

The study was undertaken by using data from primary as well as secondary sources. The primary source inculcates all the data and opinions received from the individual farmers, who are also members of primary cooperatives, through the structured questionnaire. Furthermore, the key informant discussion with representatives of the sample commercial banks, Cooperative Promotion Commission, *Erer* Farmers Cooperative Union and the four sample primary cooperatives gave first hand information about their involvement in agricultural lending process. To complement the data from intermediaries, unpublished data on the profile and loan amount of primary cooperatives were sought. The secondary data source includes information from the annual reports of the National Bank of Ethiopia, the Union's brochures and both banking and cooperative society establishment and regulation proclamations.

3.1.5. Data Analysis Technique

The research adopted both qualitative and quantitative data analysis methods. The qualitative method was basically used to analyze the descriptive data that were collected in the form of individual opinion. On the other hand, the quantitative methods were used to analyze data that involve numerical values. To analyze numerical values, statistical tools such as measures of central tendency and measures of dispersion were used, in addition to the simple ratio and percentage analysis. The statistics were used to show the state of variables such as annual income, expenditure, saving, loan amount, age, land size, yearly production and stock share.

3.2. THE STUDY AREA

3.2.1 Physical Characteristics

Ada'a Liben is a *woreda* in the East *Shewa* Zone of the *Oromia* Regional State bordered by *Akaki* in the West, *Gimbichu* in the North, *Lume* in the East and *Dugda-Bora* in the South. Geographically, the *woreda* has total area of 1,610.56 square kilometers, *Bishoftu* being the *Woreda*'s capital. The *woreda* is also rich in natural resources having *Erer* Mountain, the highest point in East *Shewa* Zone, which reaches 3,100 meters high followed by mount *Ziqualla* that elevates 2,989 meters above sea level, in addition to the five rivers (*Awash, Modjo, Belbela, Wedecha* and *Dukem*) and the ten crater lakes. In terms of climatic zones, around 90% of the *woreda* is found in the sub-tropical agro-climatic zones while about 5% is covered by tropical and temperate climatic zones. To see pictorial description of the *Woreda*, refer Figure 2.3.

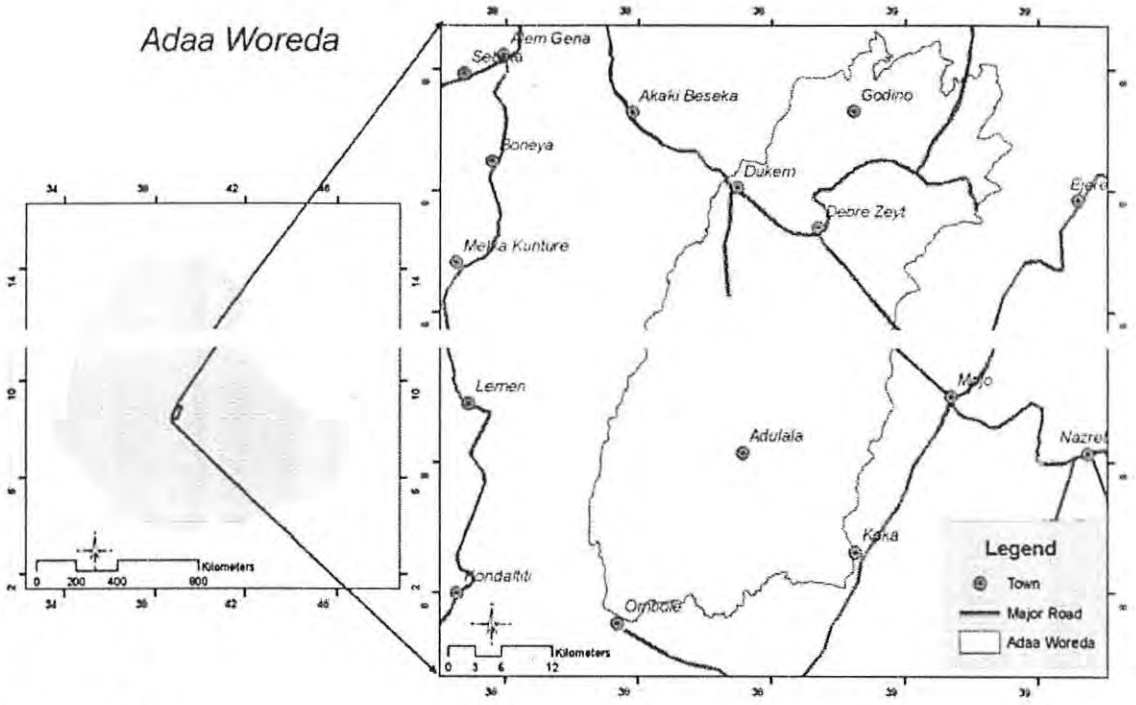
3.2.2. Demographic Characteristics

According to the *Oromia* Regional State Government, Population-wise, *Ada'a Liben Woreda* is one of the densely populated *woredas* in East *Shewa* Zone. According to the 2007 National Census as presented by UNFPA (2008), the *woreda* had a total population of 308,153. The urban population accounted for 33% while the remaining 67% were rural dwellers. In terms of age composition, 42%, 54% and 4% of the total population belong to the 0-14, 15-64 and above 64 years stratum. Gender-wise, the female compose 52% of the urban and 48% the rural population while the male shared 48% of the urban and 52% of the rural population. The average family size for the *woreda* was 5, the same figure being determined for both urban and rural areas. The population density was 154 individuals per square kilometer. (URL: http://www.oromia.gov)

3.2.3 Economic Activity

Ada'a Liben is one of the top cereals producing *woreda*'s in *East Shewa* Zone such as *'Teff'* and Wheat. Particularly, the *woreda* is known for its *'Teff'* production that has been branded as, *'Ada'aTeff'*. There are around 42 Farmers' Associations with around 26,525

Figure 2.3: Arial Map of Ada'aLiben *Woreda*



Source: ILRI

CHAPTER IV

4. DATA DESCRIPTION AND ANALYSIS

In order to answer the research questions, the study followed certain methodology to collect data and analyze the information to arrive at a meaningful conclusion. The data gathered and opinion sought from various sources is analyzed by triangulation from different sources. Thus, this chapter is devoted to the description and analysis of the survey results.

4.1. SOCIO- ECONOMIC PROFILE OF RESPONDENTS

To understand the social-economic structure and composition of respondents, the survey included certain questions related to personal profile, income and expenditure, land size, production and stocks, and fixed asset holdings. Such queries complement the study by discovering the correlations between variables related to various respondents' characteristics and borrowing experience. Accordingly, the following sub-sections are entirely dedicated to the discussion of respondents' socio-economic profile.

4.1.1. Demographic Structure of Respondents

The survey result shows that 98% and 2% of the respondents were male and female, respectively. As all the respondents were members of selected cooperatives who were agricultural input borrowers, the major gap in gender proportion reflects the patriarchal orientation of families where the male takes in charge of the family's affairs such as assuming the risk of loans. In terms of religion, 91% of the respondents were Orthodox Christians while 9% were Muslims. Ethnicity-wise, 75% of the respondents were composed of '*Oromo*' while the remaining 25% were '*Amhara*'. Given the fact that the study area is under the jurisdiction of the *Oromia* Regional State, the high proportion of '*Oromo*' dwellers could be self explanatory. Another dimension of respondent composition was the level of education. Farmers' level of awareness was assumed to enhance their understanding on the need and use of credit so that longer borrowing

experience, good repayment habit, and hence smooth relation with lenders could be established. Thus, 88% of the respondents were below 8th grade, 9% were 10th complete and 3% were diploma holders. This, in a way, indicated the maximum expectation from majority of respondents to possess basic reading and writing skills. Marital status was considered as another factor that impacts the repayment behavior of borrowers on the grounds of family stability and the associated degree of responsibility. Accordingly, 94% of the respondents were married while 3%, each, were unmarried and divorced. Age-wise, the sample was composed of adults above the age of 25, of which, 88% were above 36 years and 33% were above 41 years. The energetic and working age group of 25-30 shared only 8% followed by 4% of the 31-35 years. The young farmers seemed to have no access to credit services rendered through cooperatives. Lenders seemed to be reluctant to include young farmers in credit services due to lack of adequate resources such as land and/or oxen to be eligible for borrowing. Another reason could be that the young farmers themselves did not appear before the primary cooperatives asking for loans. (For further reference on demographic structure of respondents, see Annex I)

4.1.2. Farmers' Income and Expenditure

To see the overall performance of different income generating activities, the study considered certain variables such as income and expenditure. As the ultimate objective of enabling farmers to access credit is to assist them boost their income, and hence; have a better standard of life to this end, analyzing the respective performance was logical. Likewise, respondents' habit of keeping record of their own income and expenditure from time to time was important. The survey showed that all (100%) of the respondents kept record of their income and expenses from various activities with 98% keeping own records without external assistance. However, farmers did not have systematically produced and organized information that would help lending banks to project future financial needs and resolve information asymmetry problems. Thus, farmers may need assistance to systematically identify and organize transactions by hiring professional book keepers, for one thing to compensate for their low educational level. Lenders and other associations such as multipurpose farmers' cooperatives also need to work on such areas by educating farmers and giving technical assistance.

A relevant dimension of assessing economic performance was the source of income which critically determines smallholdings' access to credit. As lenders require assurances on the full return of their lent money, source of income is one component of the creditworthiness assessment, especially when the loan is availed for productive purposes. Correspondingly, among the production options such as cereals and oil seeds, the survey showed that all respondents were cereal producers as a principal line of production. The finding was consistent with the conclusion made by *Oromia* State Government that *Ada'a Liben* as one of the prime producers of cereals such as *'Teff'* and wheat, among all the *woreda*'s in East *Shewa*. The discussion with the Cooperative Promotion Commission and Head of *Erer* Cooperatives Union indicated the reputation of the *Woreda* for the production of *'Ada'a teff'*, and hence, has lucrative market for its produces.

However, farmers may have other supplementary income sources, in addition to the principal cereal production. Table 4.1 shows 12% of the sample respondents worked on animal fattening as a source of income while 2% undertook diary farming to earn better income. The remaining 16% rent their cattle to other farmers and 20% got income through other means such as horse-driven carts.

Table 4.1: Alternative Income Source

No.	Source	Yes		No		Total (%)
		Number	%	Number	%	
1	Diary Farming	2	2	98	98	100
2	Animal Fattening	12	12	88	88	100
3	Renting Cattle	16	16	84	84	100
3	Selling Labor	4	4	96	96	100
4	Other	20	20	80	80	100

Source: Own Survey, 2009

To complement for the economic profile assessment, respondents' disclosure of the level of income, expense and savings, if any, was made. Accordingly, the annual mean income for the sample was determined to be Birr 24,213 with standard deviation of Birr 15,178. Considering the range of Birr 71,000 with maximum of Birr 75,000 and minimum of Birr

4000, the sample seemed dispersed. In terms of expenditure, the mean annual expenditure for subsistence was Birr 15,462 with standard deviation of Birr 8,763. The respective range of expenditure was Birr 51,000 with maximum of Birr 54,250 and minimum of Birr 3,250. The sample statistics show the low disparity in terms expenditure for subsistence as compared to that of income. A residual effect of the income and expenditure values is the level of average annual saving that farmers keep from all activities. Thus, the mean annual saving for the sample farmers was Birr 4,119 with standard deviation of Birr 3,501. The corresponding range for savings of Birr 20,750 was determined from the maximum of Birr 20,750 and minimum of zero. The measure of dispersion for saving was relatively higher than those of income and expense indicating the variation in saving capacity of farmers. In fact, in the worst cases, farmers could undergo deficits by borrowing from other sources rather than positive saving. (See Annex VI for summary of the statistical figures)

4.1.3. Land, Production and Stock

Land is the basic resource for primary level production activities such as farming. The difficulty for farmers to lead a decent life is apparent with out the adequate size of land for farming. Keeping all factors such as the use of fertilizers and improved seeds constant, the mere increase in land size is likely to boost production through extensive farming. Thus, land size is a critical component in the smallholdings' effort to access credit. In addition, land is a type of asset which farmers can make money by exploiting the various opportunities it creates such as: pledging it as collateral provided that the land tenure system allows private ownership. In Ethiopia, nevertheless, the prohibition of private land ownership and trading that originated from the pro-socialist *'Derg'* regime and continued in the Ethiopian People Revolutionary Democratic Front (EPRDF) led Federal Democratic Republic of Ethiopia (FDRE) government.

Regarding the use and means to get land, Table 4.2 exhibits that the main source to get land for 68% of the respondents was from the government grants followed by 18% and 7% of the respondent who rent and buy from other farmers, respectively. On the other

hand, 21% used other sources such as gift from relatives and family inheritance. The mean land size for the sample stood at 2.7 hectares with standard deviation of 1.44 hectares. The size of land in the sample ranges from a maximum of 6 hectares to minimum of 0.5 hectare of land. The survey indicated that land was a problem in the *woreda* that, in turn, had repercussions on the borrowing capacity of farmers.

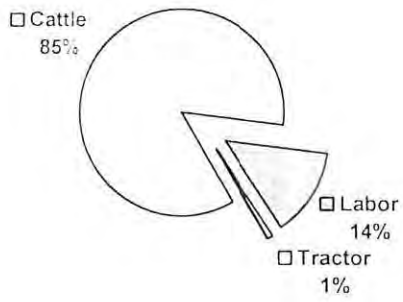
Table 4.2: Means to Access Land

No	Source	Yes		No		Total
		Number	%	Number	%	
1	Government Grant	68	68	32	32	100
2	Bought from farmers	7	7	93	93	100
3	Rented from farmers	18	18	82	82	100
4	Other source	21	21	79	79	100

Source: Own Survey, 2009

The means and volume of production are very crucial elements that contribute to farmers' eligibility to borrow and assist lenders to determine borrowers' repayment potential. Institutional lenders follow procedures to project the amount of income earned from a particular engagement. As part of the production process, farmers' means of production for the principal economic engagement in the sample was assessed.

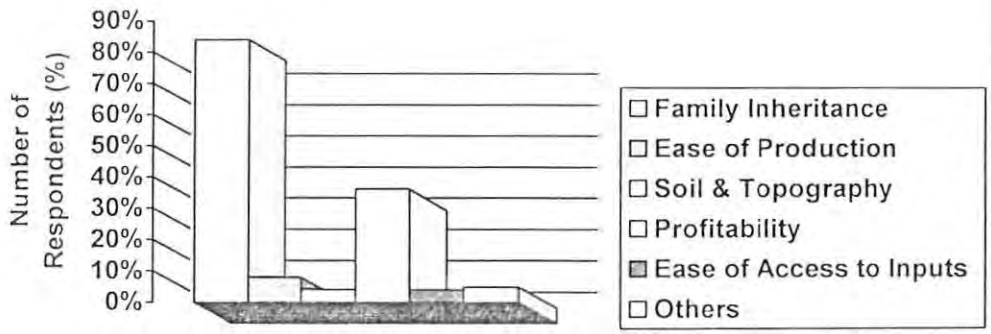
Figure 4.1 : Means of Principal Production Activity



Source: Own Survey, 2009

Figure 4.1 depicts the production means that sample farmers adopted to carry out their principal production i.e. cereal production. The survey result shows that 85% of the respondents were engaged in cereal production using cattle i.e. oxen-driven farming system, and 14% used labor, on top of the use of cattle. Only 1% of the respondents claimed to use tractor services for farming. However, the key informant discussion with the Chairman of *Erer* Cooperatives Union revealed the availability of tractor services for farmers included under member primary cooperatives. Meanwhile, the findings did not correspond with the claim as the number of farmers using tractor services was insignificant. Since modernizing the traditional agricultural system is a corner stone for development of the sector; increase in volume of production, improved productivity of farm lands, and diversification of production activities, were issues which still need to be addressed. Considering the unique geographic advantage of the *woreda* leading to acquire a famous brand name for the produce (*"Ada'a Teff"*) and create attractive market potential, the Union could have done more by offering farmers with such related services.

Figure 4.2: Reason for Choice of Principal Production Activity

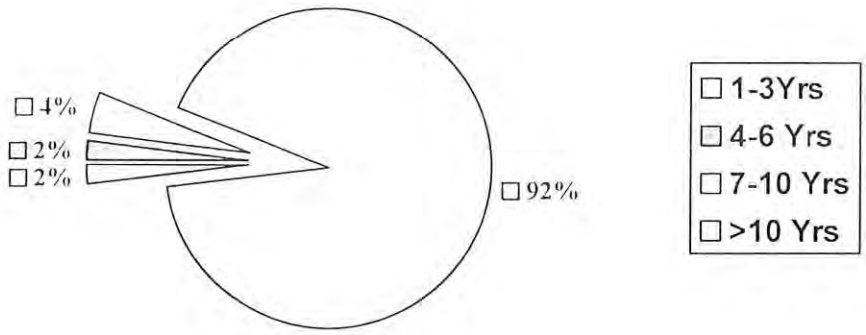


Source: Own Survey, 2009

Figure 4.2 exhibits a perspective on the rationales behind farmers' inclination towards their current principal line of production. Such queries were intended to unravel the motivational factors to engage in profitable lines of production that, in a way, shows farmers entrepreneurial capability and create confidence on lenders. In view of the

stringent lending procedures of commercial banks in Ethiopia which generally demand strong linkage between the quality of income sources and amount of loans, raising the queries was deemed important. The study, then, shifted focus to farmer's base of choice for particular production such as family inheritance, ease of production, nature of soil and topographic factors, profitability of the crops and ease of access to inputs. As a result, significant share of total respondents took up on their current principal production as part of family inheritance (84%) followed by profitability (36%). While relatively small in proportion, ease of production (8%), soil and topography (4%), ease of access to input (4%) and others (5%) such as absence of other choices and illiteracy indicated by respondents as the basis for picking their primary production. The predominance of following the lead of family activity may be due to children's inheritance when they reach an age to live by themselves.

Figure 4.3: Experience on Principal Production Activity



Source: Own Survey, 2009

A person or an entity's experience in a particular endeavor is equally as important as the choice of the line of production. The sheer length of time in the production cycle could enable the individual to understand and manage the risks arising out of a certain activity. Especially, in rain fed agriculture, the subjective and traditional knowledge of farmers to reasonably predict the embedded risks can not be underestimated. With this conception,

figure 4.3 reveal that 92% of the respondents had experience in cereal production for over 10 years, 4% of the respondents had 6-10 years of experience while the remaining 2%, each, had been in the same line of production for about 4-5 years and 1-3 years. This shows that most borrowing farmers were more experienced and middle aged, as 88% of total respondents were above the age of 35. The age factor seemed to help lenders and other intermediaries to develop trust and see stability in farmers, as guarantee for the loans. In terms of amount, the mean annual production for the sample was 26.07 quintals of cereal with standard deviation of 15.3 quintals. The production ranges from 65 quintals to the maximum and 4 quintals to the minimum per annum. As a result, the sample average production per hectare of land stood at 9.8 quintals with standard deviation of 3.3 quintals of cereals. From the change perspective, the level of production for 71% of the respondents increased with in the last three years while 18% decreased and the remaining 11% observed no change. As part of the justification for decline in production, table 4.3 shows that 89% of the respondents were constrained by shortage of land, 25% and 23% of the respondents faced lack of fertilizer and drought as core problems hampering their productivity, respectively. Last but not least, the absence of capital that was emphasized by 5% of the respondents adversely affected production.

Table 4.3: Problems Affecting Production of Farmers

No.	Problems	Response (%)		
		Yes	No	Total
1	Lack of Fertilizer	25	75	100
2	Lack of Capital	5	94	99
3	Shortage of Land	89	11	100
4	Drought	23	77	100

Source: Own Survey, 2009

The discussion with primary cooperatives unveiled that respective '*Kebeles*' conduct survey on the adequacy of individual farmers' land holdings for loan purpose. The survey is carried out before the loan application for fertilizers or improved seed is accepted. The *Kebeles*' assessment enables the lender to estimate adequate quota of inputs based on

land size and minimize the prospect of over financing. The limitation of this approach towards adequate loan delivery was reflected in the survey result as shortage of land was the core problem contributing to lack of fertilizers as the second most pressing problem. In fact, 72% of the farmers who faced shortage of fertilizers also had problem of shortage of land, which in turn accounted for 20% of the total number of farmers with land shortage.

Complementary to the adequacy of production was the level of stocks to be set aside from yearly production. Basically, farmers face two options to pursue after a harvesting cycle is completed. First, all the produce could be sent to the market so that relatively quick cash return can be sought. Some of the reasons for selling all the produce could be; the attractive market conditions, lack of storage space, inadequate production and/or the high cost of storage. As a second option, farmers may keep stock of a certain proportion of their produce so that it can be used for consumption and/or wait until prices get higher in the market. Indeed, the possible purposes for deciding to keep stocks may include: price speculation, animal feed, own consumption and lack of attractive market. The level of stock also determines the amount of finance required to bridge the finance gap between the periods of harvesting and collection of sales proceeds. Thus, in view of this rationale, the survey attempted to assess stock holding habit of farmers and the associated challenges there to. Accordingly, 90% of the farmers customarily keep stock of their yearly produce while 10% immediately sell out the produce to the market. In fact, the discussion with primary cooperatives and their union revealed the practice of buying produce from individual farmers after the harvesting season to search for higher price.

Table 4.4 shows farmers' rationale behind holding stock from portion of their annual produce. Consumption (97%) stood out as the most important reason for keeping stock of yearly produces, followed by price speculation (69%), feed their cattle (12%) and lack of market (1%). In conclusion, as the entire sample was selected out of cooperative members who had the opportunity to sell produce to the respective cooperative associations and had stronger, though indirect, bargaining power to get higher prices, market problem seemed to have minimal effect on individual farmers coupled with the favorable brand name attached to *'Ada'aTeff'* and wheat.

Table 4.4: Reason for Holding Stock

No.	Reasons	Response		
		Yes	No	Total
1	Price Speculation	62	28	90
	% age	*69%*	*31%*	*100%*
2	Animal Feed	11	79	90
	% age	*12%*	*88%*	*100%*
3	Consumption	87	3	90
	% age	*97%*	*3%*	*100%*
4	Lack of market	1	89	90
	% age	*1%*	*99%*	*100%*

Source: Own Survey, 2009

The survey indicated that farmers kept mean stock up to 51.2% of annual produce with standard deviation of 25.7%. With respect to the length of time needed to keep stocks, the study revealed that 78% of the total respondents held stock for about 7-12 months while the rest, including respondents who did not keep stock at all, sell their produce within 3 months of each harvesting season.

In a bid to determine how far farmers can hold on to keeping stocks from every production season, questions were raised on the changes of stock proportion for the past three years. Accordingly, Table 4.5 shows that about 73% of respondents registered growth, 12% recorded decline and 14% remained constant. The data indicated the reliance of farmers on keeping stocks for either consumption or price speculation purposes. Farmers' intentions to keep stock of portion of their annual produce for speculation showed the weak bondage between cooperatives and their members in terms of marketing produces.

Table 4.5: Trends in Farmers Ability to Keep Stock

Question	Reply	Changes in Trend of Storage in the Past three years			Total
		Increased	Decreased	Constant	
Hold Stock	Yes	66	11	13	**90**
	% age	*73.3%*	*12.2%*	*14.4%*	***100%***
	No	0	2	8	**10**
Total		**66**	**13**	**21**	**100**

Source: Own Survey, 2009

3.1.4 Farmers' Asset Profile

As mentioned earlier, the form and value of asset that individuals own is an indicator of their creditworthiness. Institutional lenders such as banks consider quality and value of assets as the basis of lending decision since assets can be used as collateral to secure loans. Besides, means of sustainable production could be determined from assets. This implies that individuals without the acceptable types and value of asset are subject to exclusion from borrowing before they can even make applications. The prevailing stringency in the bank lending system seems to close all doors for flexibility beyond collateralizing the prime type of assets often found in the urban areas. This situation becomes more pronounced when it comes to agricultural loans for smallholding farmers who comprise the majority of the country's poorest with insignificant level and quality of asset ownership and low opportunity to create wealth. Thus, the paradox creates divergence between farmers demand for credit and bank's market selection for lending.

Thus, survey was conducted on farmers' ownership of major type of assets, which specifically included house and cattle. Table 4.6 depicts the fact that 97% of the respondents had their own houses while 2% rent and one of the respondents resided in a relative's house. To assess the condition of houses, their age, and the number and amount of renovations made in the past three years were taken as variables. Likewise, annex I shows the mean age of houses in the sample was 16 years with standard deviation of 7 years. The maximum age of 44 years and the minimum age of 1 year gave the range of 43

years. In terms of renovation of houses, the mean frequency in the three years was 1 time with 0.8 times in standard deviation. The maximum number of renovation made in three years was 3 times while not renovating was the minimum. Money-wise, the mean renovation expenditure in three years was Birr 2,692 with standard deviation of Birr 2,013. The expenditure ranged between not spending at all and maximum of Birr 10,000 in three years.

Table 4.6 : Source of House Ownership

Type of House	Response (%)		
	Yes	No	Total
Own House	97	3	100
Rented from Individuals	2	98	100
Relatives House	1	99	100
Government Rented House	0	100	100

Source: Own Survey, 2009

Regarding respondents' house quality, Table 4.6 shows 97% were made of mud walls while 2% were constructed from brick stone. Considering the requirements banks put to ensure collateral marketability, the survey result suggested the less likelihood of narrowing the expectation gap in view of farmers credit demand and banks credit policy stringency.

The other major category of asset for small holding farmers was ownership of cattle, which is used as means of production as well as income generating activities. Hence, Table 4.7 depicts the ownership of Cow/Oxen, Donkey, Sheep/Goat, Poultry, Mule/Horse and Bull/Heifer by 88%, 68%, 30%, 17% and 8% of respondents, respectively. The mean number of Cow/ Oxen in the survey was 7 with standard deviation of 4 Cow/Oxen owned by respondents. The range was composed of maximum of 20 and minimum of 1 Cow/Oxen owner. Besides, ownership of Sheep/Goat and Poultry with mean of 9 and 11 and standard deviation of 5 for both was counted, respectively.

Table 4.7 : Summary of Cattle Ownership

Cattle	Summary of Responses				
	Respondents	Mean	Standard Deviation	Minimum	Maximum
Cow/oxen	100	7	4	1	20
Sheep/Goat	68	9	5	2	25
Poultry	30	11	5	2	20
Donkey	88	1	1	1	4
Mule/Horse	17	1	1	1	3
Bull/Heifer	8	2	1	1	2

Source: Own Survey, 2009

The mere size of assets at a point in time may not give reliable picture of farmers' adequate ownership of assets unless it is supplemented by trends in the respective changes. Table 4.8 depicts the increase in number of Cow/Oxen for 64% of the respondents while 31% remained constant and only 5% registered decline. In terms of number of Sheep/Goat, 66% of the respondents registered increase while 4% declined and 29% remained constant for the past three years. Considering the number of poultry, 53% showed increase, 7% decrease and 40% observed constant for the three years.

Table 4.8: Change in the Number of Cattle

Assets	Change in the Past Three Years			
	Increase	Decrease	Constant	Total
Cow/Oxen	64(64%)	5(5%)	31(31%)	100(100%)
Sheep/Goat	45(66%)	3(4%)	20(29%)	68(100%)
Poultry	16(53%)	2(7%)	12(40%)	30(100%)
Donkey	15(17%)	1(1%)	72(82%)	88(100%)
Mule/House	3(18%)	1(6%)	13(76%)	17(100%)
Bull/Heifer	2(25%)	2(25%)	4(50%)	8(100%)

Source: Own Survey, 2009

In a nut shell, the economic description and analysis in terms of financial performance, production, stock and asset holdings for the sample gave reflections on the farmers' economic base. The variables were discussed based on the assumption that they have associational linkage with eligibility for credit.

4.2. ASSESSMENT OVER SMALL SCALE AGRICULTURAL CREDIT IN ADA'A LIBEN WOREDA

4.2.1 Small Holders Access to Bank Loan

Credit is an essential resource to the over all development of an economy in general and serve as important input to boost agricultural production in particular. It gives farmers the momentum to access new technological services including improved seeds, fertilizers and pesticides. Input access, in turn, contributes towards the improvement of the corresponding farm productivity. In addition, credit gives farmers the freedom to bargain over the primary produce markets so long as they have alternative source of fund to consume until such time that they earn a better profit from the market. In general, credit options give farmers far reaching benefits towards improvement of their standard of living. Nevertheless, the long standing problem that created the gap between the financial needs of small holding farmers and lenders' priority market, especially that of banks, had to do with the modes of delivering the funds and ensuring the proper and full repayment of the loans in a manner that is cost efficient for both transacting parties. Searching ways that mutually satisfy the needs of all transacting parties is very critical.

Complementary to the modes of delivering credit services to small holding farmers is the access to information on banking services and that of the proper credit products. Access to information on banking credit services can be facilitated through the various available media in the vicinity of the respective farm community. However, there are also obstacles that hamper this opportunity to spark motivation and the subsequent decision to use the services.

Accordingly, Table 4.9 presents summary of sample questions with the aim of discovering the available means to get information in the study area such as word of mouth from friends, relatives and others, in addition to the electronic media including radio and television. Furthermore, the banks' promotional endeavors, the assistance by government DAs or extension agents and farmers cooperatives themselves can play roles to disseminate information on the various advantages and disadvantages of banking

credit. As a result, 83%, 73% and 42% of the respondents got banking information through word of mouth, Radio and Television, respectively. On the other hand, the role of banks' promotional endeavors, the assistance by government extension agents and the cooperatives were accepted only by 9%, 9% and 3% of the respondents from the survey, respectively.

Table 4.9: Means to Access Bank Credit Information

No	Means to get Information	Response (%)		
		Yes	No	Total
1	Radio	73	27	100
2	Television	42	58	100
3	Word of Mouth	83	17	100
4	Bank's Promotion	9	91	100
5	Extension Service Agents	9	91	100
6	Cooperatives	3	97	100

Source: Own Survey, 2009

Farmers' ability to access credit information and increase their awareness level on the benefits of using credit can be impeded by numerous factors. Table 4.10 shows that majority of the respondents restrained from commenting that there were critical problems hampering the smooth path to get credit information. Only 19% and 14% of the respondents emphasized the problems of accessing electronic media and other obstacles, respectively. Inadequate infrastructural networking which involves the absence of telecom and road services was mentioned by 9% and 1% of the surveyed farmer-borrowers, respectively. The fact that the study area is approximately 45kms away from the capital, Addis Ababa, showed the existence of a relatively better opportunity for accessing infrastructures so that farmers can seek the necessary market information.

Table 4.10: Obstacles on Access to Bank Credit Information

No	Obstacles	Response (%)		
		Yes	No	Total
1	Absence of Road	1	99	100
2	Absence of Telecom	9	91	100
3	Absence of Electronic media	19	81	100
4	Other Obstacles	14	86	100

Source: Own Survey, 2009

The level of infrastructural development by itself, however; may not give assurance that farmers get credit services from banks. First, farmers may be constrained by the lack of available financial services for various purposes. One aspect of such problem is the inadequate level of infrastructural development that hinders both the farmers and the lending institutions from communicating. Second, institutional constraints may not be prevalent but individual farmers may refuse to borrow due to various individual reasons.

Indeed, among other things, farmers' willingness to borrow may depend upon the purpose of the loan to which they want to borrow. The loan purpose is one of the prerequisites in any lending-borrowing relationship. Lenders opt to ensure that borrowers have specific purposes to which they devote the borrowed funds. On the other hand, borrowers have certain activities for which they require the finance. Reconciling the divergent needs of both actors (i.e. lenders and borrowers) and creating common ground for mutual benefit has prime importance. Accordingly, 25 (81%) of the respondents needed the fund to start both on-farm and off-farm related business activities and 6 (19%) opted to use the fund for the purchase of fertilizers. Farmers' desire to purchase more fertilizers, additional land and engagement in animal fattening included the on-farm purposes. The tendency of farmers to aspire for more fertilizers, in addition to the amount loaned from the respective primary cooperatives, was attributed to the shortage of land, based on which the level of fertilizer needs are determined. On the other hand, respondents also chose direct bank borrowing for off-farm purposes that include buying horse pulled carts and opening shops. However, it seemed impossible to meet these purposes as banks, BoA and CBE, did not have rooms in their credit policies for

individual treatment of small holding farmers. In fact, the credit policy of the Commercial Bank of Ethiopia has stated that no individual borrowing is allowed for small holding farmers unless loan application is made in group.

Table 4.11: Purpose of Preferring Bank Credit

No	Purpose	Response	
		Number	% age
1	Purchase of Fertilizer	6	19
2	Consumption	0	0
3	Transport Product to Market	0	0
4	Paying overdue rent	0	0
5	Paying Overdue Loans	0	0
6	Other Purposes*(Purchase of cart & land, Opening shops and animal fattening*)	25	81

Source: Own Survey, 2009

In line with the need of farmers to bank credit is their attempt to ask for loans. It gives their actual experience on the matter and enables to make decision either to continue borrowing or detach from such notions. Hence, only 17% of the total respondents made attempt to ask for direct borrowing from banks in the *woreda* while 83% of the respective sample made no attempt to ask for direct lending from any bank, so far. Table 4.12 shows that 82% of the respondents who approached banks to ask for loans returned with some demands from the lenders while 18% of the respondents faced total rejection. The table also explicates the fact that none of the respondents were eligible for direct acceptance or got approval with demanding requirements. Thus, the opportunity to borrow for individual small scale farmers appeared narrow.

Table 4.12: Reply Received for Direct Loan Application

No	Reply Received	Response (%)	
		Yes	% age
1	Total Rejection	3	18
2	With Demanding Requirements	0	0
3	With Some Requirements	14	82
4	Acceptance	0	0
	Total	17	100

Source: Own Survey, 2009

Another way to see farmers' access to borrowing from banks is to understand the rationales for preferring banks to other sources of loans. The source and type of borrowing may range from the simple friendly extension of funds for purposes such as organizing social events with no interest expense to the large sum institutional borrowings that charge relatively higher cost of fund. Therefore, farmers should have the option to place their choice on a particular point on the continuum. Nevertheless, borrowing from banks, which is the focus of this study, can be opted on several grounds. Among other things, one can prefer to borrow from banks due to the relatively less costly nature of the loans, seeking for the other associated banking services, the trust for work which is built upon professionalism out of its formal and institutional nature, accessibility to the business areas of the borrower and other reasons. With this in mind, Table 4.13 revealed 30% of respondents' preferred borrowing from banks due to its accessibility while 11% of the respondents based their preference on the low interest rate that banks' charge for lending and the trust of farmers on the works of banking institutions. From observation, it was learnt that there had been two branches in the *Woreda*, the Commercial Bank of Ethiopia, and Construction and Business Bank for long time. Recently, with the participation of private banks in the financial sector, the number of bank branches in the *woreda* grew to six. The ratio for the total population to bank branches for the *woreda* in general stood at 41,379. According to NBE (2008), the national population to bank branch ratio reached 136,108 people for one branch as at June 30, 2008. Thus, the *woreda* had the relative advantage in accessing bank branches with wider opportunity to get banking services.

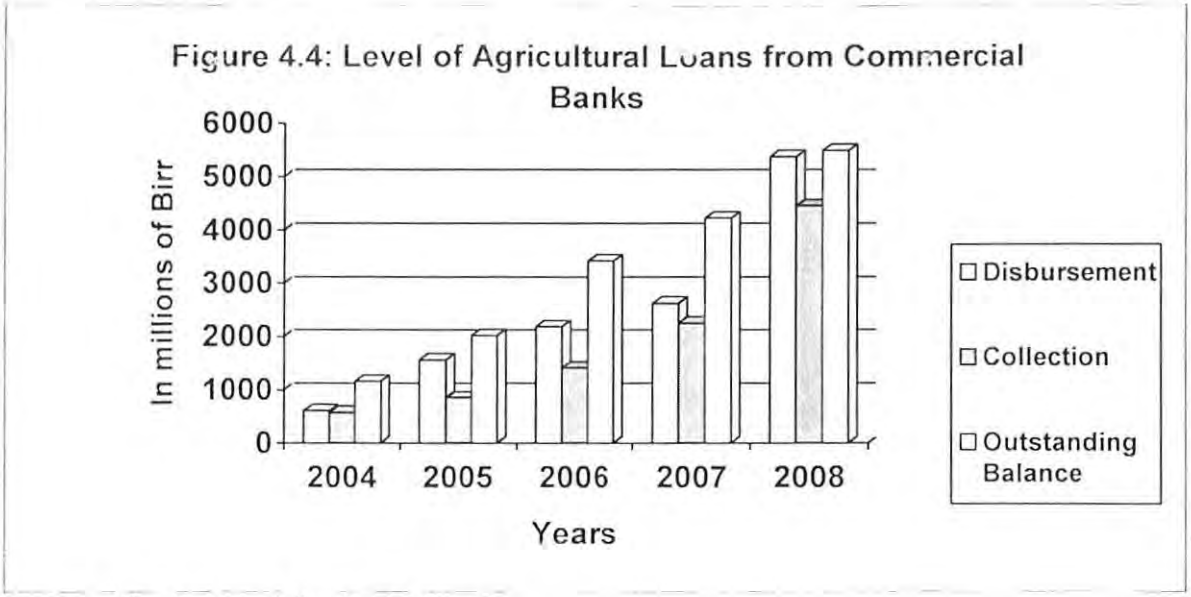
Table 4.13: Reason for Preferring Bank Credit

No	Reason	Response (%)		
		Yes	No	Total
1	Low Interest Rate	11	89	100
2	Accessibility	30	70	100
3	Trust for Work	11	89	100
4	Other Reasons	2	98	100

Source: Own Survey, 2009

4.2.2 Origination of Small Scale Agricultural Credit

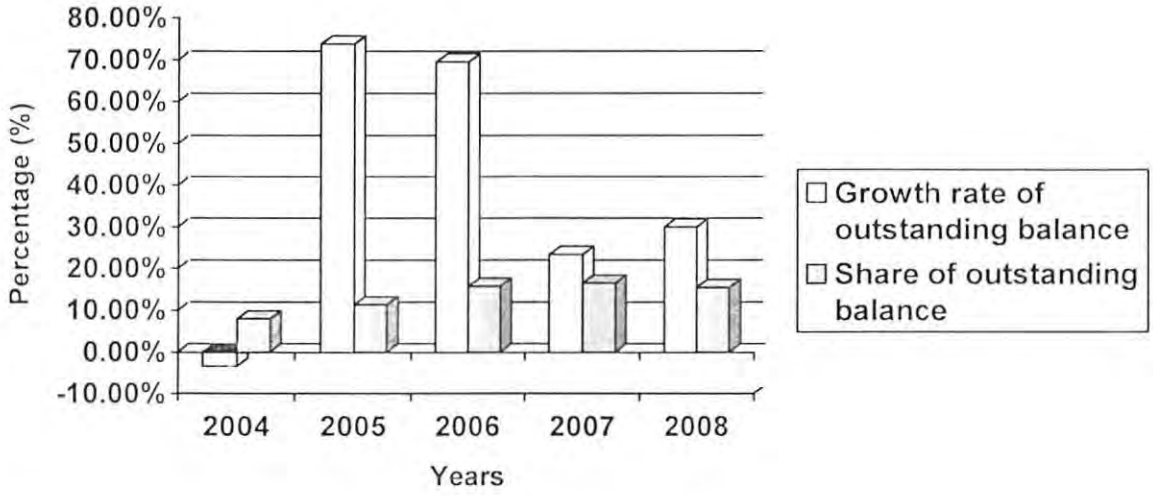
To begin from the broader picture, consideration of the national credit allocation trend to the agricultural sector from commercial banks in Ethiopia is vital. Hence, figure 4.4 presents the fact that total disbursement for the sector shot up from Birr 602 million in 2004 to Birr 5.371 million in 2008.The average annual growth rate over the five years was 72% with the highest growth rates of 159% and 105% registered for the years 2005 and 2008, respectively. On the other hand, collection rose from Birr 572 million to Birr 4.443 million in 2008 with average annual growth rate of 55% and registering marked growth of 97% for 2008. Owing to the more than proportionate growth of disbursements over collections, the accumulation of accrued interest and other reasons, the residual annual outstanding balance grew from Birr 1.162 in 2004 to Birr 5.481 in the year 2008 with annual average growth rate of 39%. The maximum outstanding loan balance growth of 74% and 69% were registered for the years 2005 and 2006, respectively, mainly due to the divergence between the growth rates of disbursements and collections. However, it is still difficult to conclude that the amount of fund allocated to the sector is at an adequate level. Additional variables such as the yearly arable land increment, the population growth rate, and the number of agriculture related activities that need financing should be taken in to account.



Source: The National Bank of Ethiopia

Another dimension to see the attention given to the sector in terms of capital injection from the banking sector was the share of agricultural loans from the total loan portfolio of banks. Figure 4.5 exhibits the share of the respective loans from the total loan portfolio and the yearly percentage growth of such loans through 2004 to 2008. Accordingly, the share of agriculture loans to the total loans rose from 8% in 2004 to 17% in 2007, though it declined to 15% in 2008. In terms of growth, agricultural loans shot up from -3% in 2004 to 74% in the year 2005. However, the growth rate for agricultural loans continuously declined to 23% in 2007 and revived to 30% in the year 2008.

Figure 4.5: Growth Rate & Share of Outstanding Agric-Loan Balance from Commercial Banks



Source: The National Bank of Ethiopia

In conclusion, it seems evident that the share of agricultural loans in the credit portfolio of commercial banks was increasing from year to year. Except for the year 2008, the past five years witnessed the significant growth of agricultural loans from commercial banks in Ethiopia. It is worth to note that the share incorporated all type of loans extended to the sector including those lent out to small holding farmers and other large agricultural investors. Even if it requires further scrutiny to determine the share of small holders that would have direct implication for the objective of this study, it is grossly indicated that the overall trend of loan provision in the sector has been increasing.

An equally important issue in the credit delivery for smallholding farmers is the form of credit. Credit forms determine the mode of transferring the funds from lenders, especially from the banking sector. In the two-tiers lending system, other concerned institutions, with the desire and responsibility to help the poor, also involve in the credit delivery process by filling the gap between lending institutions and the end users. Institutions such as the government, Primary Cooperative Associations and their Unions serve as intermediaries between the financing banks and the end user of the loans, i.e. the farmers. The government may provide the financing bank with the necessary collateral

requirements on behalf of the end users for replenishment in case of default. The Primary Farmer Cooperatives facilitate the use of the fund extended from banks and give assurance that the funds are properly utilized for the intended purpose. Despite the demerits brought about by the institutions' intervention such as corruption and nepotism, the two tier system has been a better and practical approach that presents strong control over the flow of funds from the original source to the end user, and ensured its full repayment.

In the study area, recent agricultural loans taken from commercial banks were entirely used for the purchase of agricultural inputs. The key informant discussion with head of the *Ada'a Liben Woreda* Cooperative Promotion Office and the Chairman of *Erer* Farmers Cooperative Union unveiled that bank borrowing in the *woreda* follows the two-tier approach, where other intermediaries intervene to transfer the loans to the end users in the form of fertilizers, improved seeds and chemicals. Farmer Cooperatives Unions negotiate the adequate level of loans with the concerned regional government offices which guarantees the loan from the respective bank. The main and longstanding lender of agricultural input loans in the *woreda* was the state owned Commercial Bank of Ethiopia. The credit procedure of the bank also stipulated some requirements for smallholdings in that loans are to be given for the purpose of purchasing agricultural inputs such as fertilizers, agro-chemical and improved seeds. Loan for small holders is also defined in the credit procedure as:

> *"...Loans extended to farmers with small land-holdings who use oxen-drawn local plows and low-level technology. The term of the loan for smallholding farmers is short, not exceeding one year".*

Moreover, the credit procedure prescribed the following requirements for small holders to be eligible for agricultural loans:

- *Organize themselves into an association and acquire legal personality from the concerned government;*
- *Establish accounting and farm-record systems;*

- *Employ a Manager and an Accountant/Bookkeeper; and*
- *Present a minutes of resolution passed by at least three-fourths of the members of the General Assembly of their cooperative/association*

The credit procedure clearly stipulates the prohibition of individual loans for small holding farmers.

To understand the credit delivery process in the *woreda*, figure 4.6 illustrates the loan origination from commercial Bank of Ethiopia until it reaches the end users or farmers. The credit need of farmers is assessed by the respective *Kebeles* and reports are sent to the primary cooperatives. The base of the assessment for input loan eligibility is the size of land a particular farmer owns. After receipt of the evaluation report, the primary cooperatives' loan committees make their own assessment of individual farmer eligibility for loans by considering past track records, land size and other parameters that indicate creditworthiness. Then, supporting letters are sought from the Cooperative Promotion Commission as testimony of primary cooperatives' eligibility for loan application. In such a manner, the documents attesting the input needs of farmers would be consolidated and sent to the *Oromia* Regional Finance Bureau for loan request from the Commercial Bank of Ethiopia. The regional government, through its president, makes the application to the bank and, after approval; the Union concludes the loan contract with the bank. The approved fund, then; will be directly advanced to the input suppliers while the unions will receive the inputs. In the two-tier lending approach, the role of Unions, as intermediaries, is limited to the distribution of the purchased inputs to the respective primary cooperatives that, in turn, will pass down the inputs to individual farmers based on the assessment made by *Kebeles*. The lending bank directly advances the fund to input suppliers upon agreement with the Unions. In other words, the farmers' direct linkage with the original source of fund is highly detached. Indeed, the survey also revealed that clients of the primary cooperatives did not even know the source of the inputs they took on loans.

Before the approval, however, the bank secures written letter of undertaking from the Ministry of Finance and Economic Development (MoFED) stating the Ministry's

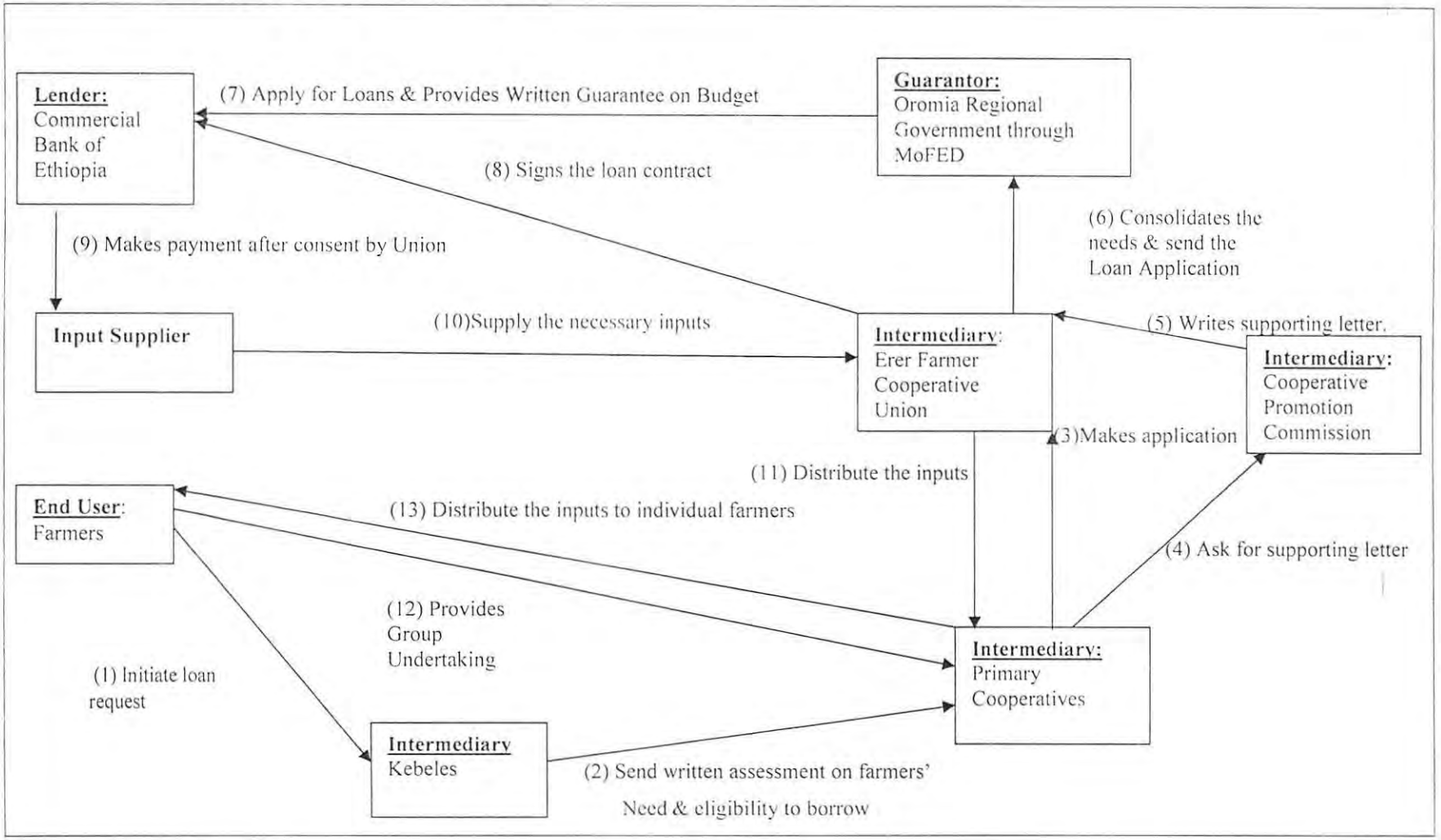
commitment to reimburse for defaulted loans from the subsidy budget of the regional government up on submission of claim by the bank. This type of collateral relieves the bank from engaging in collection activities as it is considered as Cash Substitute collateral. In fact, it significantly loosened the relationship between the bank and the concerned bodies when it comes to the collection process, negatively affecting the level of expertise that cooperatives could use on loan collection procedures.

The key informant discussion at the Commercial Bank of Ethiopia revealed that the Bank in general charges 8.5% interest rate per annum for regional government loans. However, this loan price is shared between the bank and the *Oromia* Regional Government as 6.25% and 2.25%, respectively. The latter is intended to cover the costs incurred by the regional government's facilitation role from origination to the collection of all loans. The minimum lending rate for other types of loans is 8.5% which gives the impression that the foregone 2.5% is a subsidy for the farmers. On top of that, the discussion revealed that farmers face additional 2.5% interest charge by primary cooperatives to cover their own operational costs. Thus, the total interest rate applied on the loans for the end users reaches 11%. However, this rate is still significantly lower than the rates charged by other institutions such as Micro-finance Institutions. Moreover, the loans are short term in nature and are expected to be repaid with in one year of the harvesting season. Similar to the union, primary cooperatives do not have cash receipts during loan origination. Rather, they take the inputs on loan basis from the Union and distribute them to the member farmers for use. In return for taking loans, farmers are also expected to sign on documents as assurance for taking the inputs on loan. This lays the legal ground to pursue after farmers in case of default. The key informant discussion with the Union Chairman revealed that primary cooperatives permit participation of non-member farmers to take input loans by requiring payment of Birr 10, as registration fee. In this way, farmers are eligible for input loans acquired from bank funds but can not take union funds and do not participate in dividend payments. It was explained that such a practice has been adopted mainly due to the government's desire to fulfill farmers' input need in the case area.

Generally, the loan origination process passes down two layers. First, Commercial bank of Ethiopia lends the fund to *Erer* Farmers Cooperative Union, which receives the loan in

input forms from suppliers, by pledging the *Oromia* Regional Government's Budget. Second, the primary cooperatives lend the inputs to individual farmers by asking group undertaking to serve as security for the loans. Thus, the original lender and the individual farmers do not have direct contact.

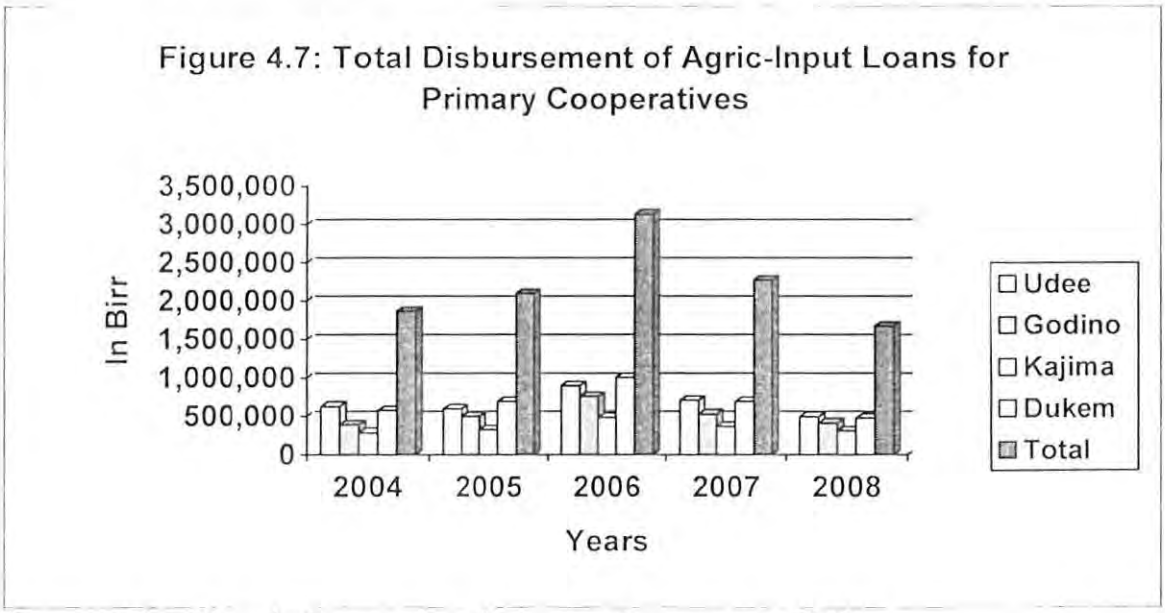
Figure 4.6: Process of Agric-Input Loan Origination



Source: Own Survey, 2009

To get a closer look at farmers' overall access to agricultural input loans, data on the total disbursement of loans for selected primary farmer cooperatives in the *woreda* were considered. Even though agricultural credit service, by definition, encompasses various types of credit services from the basic agricultural inputs to the large scale investments The predominant type of loan in the case area was loans to purchase of inputs such as fertilizers and improved seeds. Such type of loans are short term in nature (Usually for one year) covering only one production cycle. Thus, in terms of accommodating the diverse credit needs of farmers, it is difficult to conclude that credit service was adequately available in the *woreda*.

Figure 4.7 shows the result of the assessment made on the trend in change of agricultural input loans for the selected primary cooperatives in the *woreda*. The total yearly disbursements increased by 13% and 67% for the two consecutive years from 2004 up to 2006, respectively, and declined by 27% for the remaining two years to 2008.



Source: Ada'aWoreda Cooperative Promotion Commission, 2009

In individual terms, sample respondents were asked to disclose their yearly total borrowing from the primary cooperatives. Since the purpose of the loan is for the purchase of agricultural inputs, farmers borrow once in a year time. One can not take additional loans for another season until the outstanding balances of the preceding year

annum followed by 26% of the respondents in range of Birr 1000 to Birr 2000. On aggregate, 81% of the respondents took loans amounting below Birr 5000. Age-wise, 70% of the total respondents who were above the age of 36 years took loans amounting below Birr 5000. On the other hand, 17% of the respondents took loans above Birr 5000. The survey reflect that the loans are concentrated for respondents who were middle aged and for amounts below Birr 5000.

Table 4.15: Summary of Loans Taken by Age

		Average Amount of Loan From Cooperatives						
		1000-2000	2001-5000	5001-7000	7001-10,000	10,001-15,000	>15,000	Total
Age	25-30	3(12%)	4(7%)	0(0%)	1(8%)	0(0%)	0(0%)	8(8%)
	31-35	1(4%)	3(5%)	0(0%)	0(0%)	0(0%)	0(0%)	4(4%)
	36-40	10(38%)	16(29%)	1(100%)	6(50%)	0(0%)	0(0%)	33(33%)
	41-45	6(23%)	12(22%)	0(0%)	2(17%)	2(50%)	0(0%)	22(22%)
	>41	6(23%)	20(36%)	0(0%)	3(25%)	2(50%)	2(100%)	33(33%)
Total		26(100%)	55(100%)	1(100%)	12(100%)	4(100%)	2(100%)	100(100%)

Source: Own Survey, 2009

All farmers included in the survey were borrower-clients of Primary Cooperatives. Moreover, assessment over respondents' borrowing from sources other than banks unveiled that 2% were clients of microfinance institutions while 5% were borrowers from other sources including usurers, friends and relatives. Table 4.16 shows farmers' composition in terms of credit forms where 97%, 81% and 77% of the respondents took fertilizers, seeds and chemicals on loan, respectively. Only 16% took loans in the form of cash. The discussion with chairman of *Erer* Farmers Cooperative Union revealed that loans were given to farmers in the form of seeds, chemicals and fertilizers in addition to the other services. Thus, 16% of the respondents who borrowed in cash were presumed to be from cooperative's own funds, as bank originated funds were entirely allotted to the purchase of inputs.

Earlier, it was discussed that the Primary Cooperatives' Credit Committee scrutinizes applicants' repayment track records and membership status based on the assessment

received from the respective *Kebeles*. The *Kebeles'*, on their part, make assessment of individual farmer's need for inputs determined based on land size and type of production. Such working procedures were uniformly applied to all Primary Cooperatives in the *woreda*. This has the advantage of controlling the proper use of loans against directly giving the cash to farmers. Besides, farmers enjoy the benefit of purchasing the required inputs in bulk at a relatively lower price through increased bargaining power rather than purchasing the items from individual retailers.

Table 4.16: Forms of Credit

No	Forms	Responses (%)		
		Yes	No	Total
1	Cash	16	84	100
2	Fertilizer	97	3	100
3	Seeds	81	19	100
4	Chemicals	77	23	100
5	Others	2	98	100

Source: Owen Survey, 2009

The extent of farmers' borrowing experience in terms of the number of years that credit has been used as farm input was another dimension. Such queries show a perspective on the impact of farm credit that assist the production process by enabling farmers to have access to the necessary agricultural inputs and improved technologies. It also indicates the change in production from time to time with the change in borrowing capacity of farmers. Table 4.17 depicts the claim by 89% of the respondents who use agricultural inputs on credit basis from the corresponding farmer cooperatives for 3-5 years. The borrowing experience of 6% and 5% of the total respondents was for 1-3 years and more than 5 years, respectively.

Table 4.17: Farmers' Borrowing Experience in Years

No	Years of Experience	Response	
		% age	Cumulative % age
1	1-3 Years	6	6.0
2	3-5 Years	89	95.0
3	>5 Years	5	100.0
	Total	100	

Source: Owen Survey, 2009

Age-wise, Table 4.18 presents the response of 11% of total respondents who were aged below 35 years and have borrowing experience for 3-5 years. It is reflected that most of the young and energetic section of the farm community did not have access to borrowing services. The table also shows that 55% of the respondents were aged between 36 and 45 years, among which 91% were borrowing from cooperatives for 3-5 years. Besides, among the 33% of total respondents who were aged above 41 years, 85% had borrowing relationship with primary cooperative for more than 5 years. The basic determinant to get access to credit services was the availability and size of land. This led to the conclusion that the young male group of the farming community does not have access to land that, in retrospect, perpetrated their subsequent exclusion from borrowing services. However, the system seemed to have both positive and negative repercussions. It might be advantageous considering the fact that lending services should always follow ways to ensure sustainability of financial services in the rural credit market. On the other hand, the approach might result in the discrimination of some segment of the society such as the young and women. Credit should be given to the potentially more productive section of the society who has the potential to grow fast and change the old system of doing farming business. However, the lending practice in the case area seemed to work the other wise.

Table 4.18: Farmers' Borrowing Experience by Age

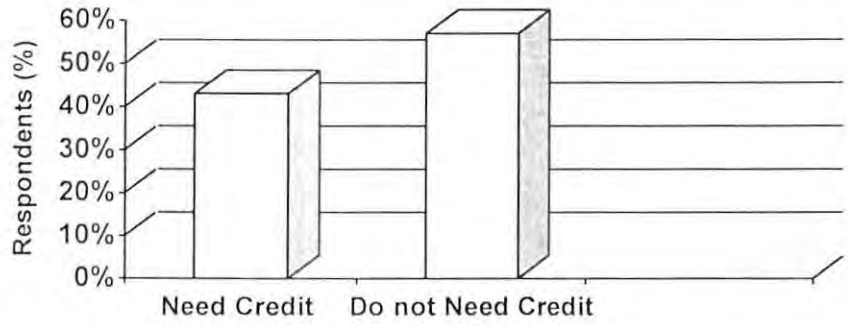
No	Age	Borrowing Experience			Total(%)
		1-3 Years(%)	3-5 Years(%)	>5 Years(%)	
1	25-30	0	7	1	8
2	31-35	0	4	0	4
3	36-40	2	30	1	33
4	41-45	1	20	1	22
5	>41	3	28	2	33
	Total	6	89	5	100

Source: Owen Survey, 2009

Chapter two of the study deliberated on the need to create demand driven credit services for small holding farmers. The past failures of the rural credit market were partly attributed to the supply driven nature of credit delivery, particularly those initiated by governments for various political motives. In fact, curbing such intentions was at the heart of the argument that the state should not directly be involved in rural credit markets. Extension of credit should always base the specific needs of farmers. Farmers, whether individually or in group, should be given the chance to express their specific purposes for which they need credit. It helps not only to ensure the safe repayment of borrowed funds but also develops their entrepreneurial capability of the farm community.

In this regard, attempt was made to see farmers' crave for credit in general. Consequently, figure 4.8 shows only 43% of the respondents were in need of credit in general while the remaining 57% did not need any credit at all. This is presumed to come either out of the age structure of respondents where most were above the working age group of 18-25 who tend to be risk averters, or respondents lack adequate understanding on the benefits of credit.

Figure 4.8: Respondents Need for Credit



Source: Own Survey, 2009

Table 4.19 shows a related finding on farmers' preferred form of creditors. Accordingly, 66% of the respondents opted to take loans from cooperatives while 25% of the respondents preferred that of banks. Only 3% of the respondents preferred micro-finance institutions for borrowing.

Table 4.19: Farmers' Preferred Source of Credit

No	Source	Response (%)		
		Yes	No	Total
1	Suppliers	0	100	100
2	Banks	25	75	100
3	Microfinance	3	97	100
4	Cooperatives	66	34	100

Source: Owen Survey, 2009

An important perspective to understand borrowers' credit appetite was the preferred form of credit. The form of credit was presumed to be a good proxy to determine the purposes for which small holders need credit services. Hence, Table 4.20 presents summary of the survey result that reflects 88% of the respondents' need for credit in the form of fertilizer, 80% in the form of improved seeds and 68% in the form of chemicals. Only 36% and 3% of the respondents needed credit in cash and other forms, respectively. This result suggests that most small holding farmers required credit for activities related to

agriculture only. This attitude might be born out of the fact that farmers were exposed to taking credit for agricultural activities which were supply driven. The discussion with the Cooperative Promotion Commission officials also revealed that there was a practice in the *woreda* to aggressively lend money to farmers for unknown purposes. However, getting access to credit in cash forms give farmers the freedom to choose more profitable activities that helps to diversify the source of income and improve the standard of living. The contradiction between the results that only 43% of the respondents need credit in general against the response of more than 80% of the farmers who needed credit in the form of fertilizers and improved seeds indicate the perception of farmers towards the inputs acquired on loan basis and the fact that such items were not considered as credit. In other words, farmers perceived only taking cash notes as loans.

Table 4.20: Farmers' Preferred Form of Credit

No	Forms	Response (%)		
		Yes	No	Total
1	Cash	36	64	100
2	Fertilizer	88	12	100
3	Improved Seeds	80	20	100
4	Chemicals	68	32	100
5	Others	3	97	100

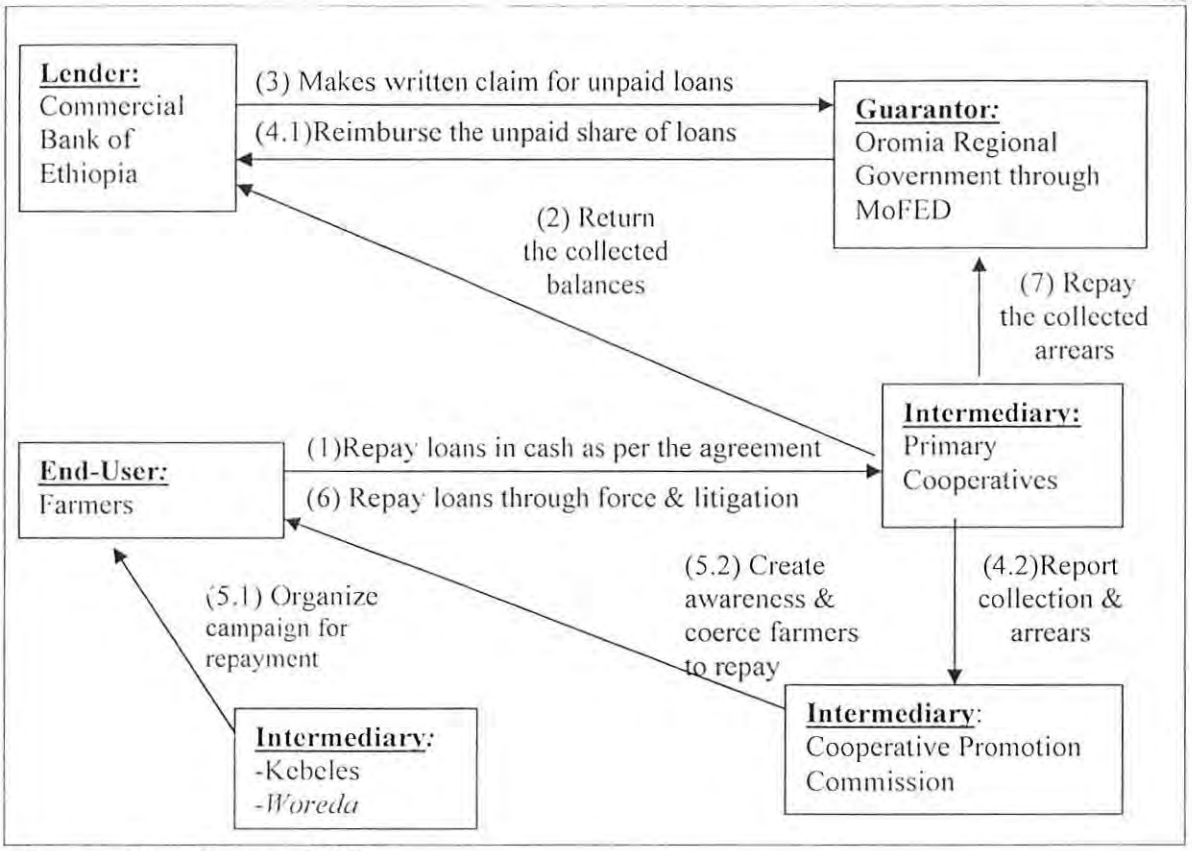
Source: Own Survey, 2009

4.2.3 Collection of Small Scale Agricultural Credit

A crucial stage in the lending process is the repayment phase. Borrowers are expected to honor the contractual agreements by which they are committed to return the borrowed funds through the scheduled stream of payments. It is a stage where most lenders are highly concerned so long as the lending process is concerned. In fact, proper mechanisms to ensure the safe return of the extended funds have been at the heart of all the worries.

With this notion, attempt has been made to review the repayment practice of farm loans in the study area. Figure 4.9 reflects the cycle, the actors and the process involved in the repayment of agricultural input loans back to the Commercial Bank of Ethiopia.

Figure 4.9: Process of Agric-Input Loan Repayment Process

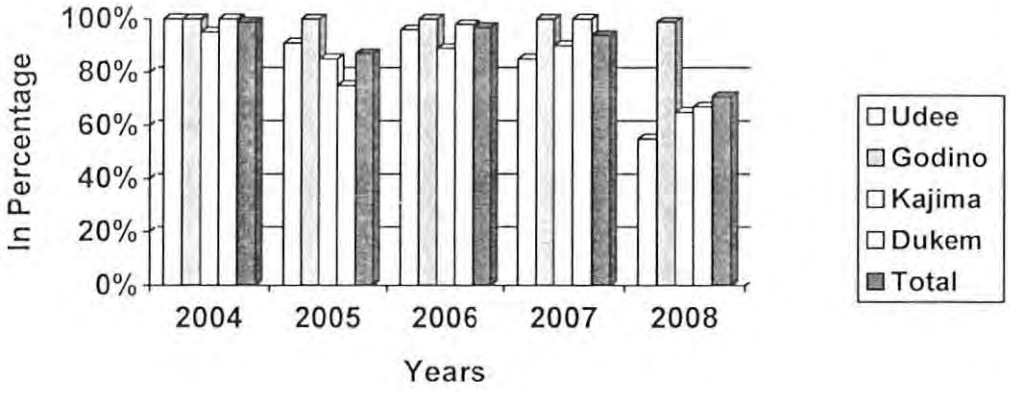


Source: Own Survey, 2009

Figure 4.10 and Annex IV exhibit the loan recovery performance of sample primary cooperatives excluding the accrued interest balances. Accordingly, good repayment performance was registered for *Godino* Multi-purpose Primary Cooperative where the loan recovery rate was above 99% for the five years from 2004 to 2008. On the contrary, *Kajima* Multi- purpose Primary Cooperative was low collection performer with maximum of 95% in 2004 and minimum of 65% in 2008 followed by *Udee* Multi Purpose Farmers Primary Cooperative with the highest collection of 100% in the year 2004 only and minimum of 55% in 2008. *Dukem* Multi-purpose Farmers Primary Cooperative was medium performer from the group with maximum of 100% in the year 2004 to minimum of 67% in 2008. In general, the range for the overall loan recovery performance of the four primary cooperatives was between 71% and 99% from 2004 to 2008, respectively. In fact, the lowest recovery rates for the four sample primary

cooperatives were registered for the year 2008 and the overall recovery rate for individual primary cooperatives showed declining trend since the year 2006.

Figure 4.10:Total Collection of Agric- Input Loan from Primary Cooperatives



Source: Ada'aWoreda Cooperative Promotion Commission

From individual farmers' point of view, the number of months taken to repay total borrowed funds was around 11 months with standard deviation of 2 months. On the other hand, the fourth and fifth loans, chronologically from the latest years, took mean number of 9 months and 8 months with standard deviation of 4 months. A consistent remark made by the key informant discussion with commercial bank credit officials and *Erer* Farmers Cooperative Union chairman states that the loan repayment takes up to one year as applications are usually made at the beginning of each farming season. (i.e. June of each year) and total repayments are expected up to end of April, the following year.

4.2.4 Small Holders Default on Agricultural Input Loans

Significant part of the problem of non-repayment in the area dates back to the loans granted between the years 1996/97 -1999. The then intermediary primary cooperatives were inactive and disbursements were made without proper need and capacity assessment on farmers besides the absence of written agreements. In the worst case scenarios, loans were taken in the name of infant children, in the name of unknown personalities, the nick

name of farmers' cattle and name of rivers. Moreover, in some cases, there were no records of borrowers barring the options to legal acts in times of default. Thus, for such types of defaulted loans, attempt has been made to pursue obligors through the elders and using the social networking.

The discussion with *Ada'a* Cooperative Promotion Officials unfolded the past experience of the *woreda* that availability of credit was largely supply driven. Agricultural input loans were given based on the government's desire that all farmers should have access to inputs either in the form of credit or grants. Indeed, farmers may have their own purpose of seeking credit but largely such needs were not accommodated so far.

In the recent years, the predominately prevailing source of loan non-repayment was the influence of primary cooperative leaders where they use their authority to take more loans and delay repayments. The local government authorities and the militia use their power to intimidate the cooperatives towards their own favor. The key informant discussion also pointed the contribution of losing harvest due to weather condition, relocation, death of farmers as causes for default. In the extreme default cases, the primary cooperatives use two levels of legal actions. For loans amounting to Birr 1,500 and below, the *Kebele's 'Fird Shengo'* handles the litigation process. For amounts greater than Birr 1,500, the respective courts in the *woreda* resolve the cases. In most instances, however; defaulters serve their commitments before the legal sue reaches the court.

Meanwhile, the end users' perception of own default experience is as equally important as the perception of lenders and other bodies involved in the lending-borrowing process. Accordingly, Table 4.21 shows that 92% of the respondents in the sample did not default on their loans while 8% replied they experienced default. However, respondents were presented with questions to indicate the frequency of default where 5 (63%) defaulted just for one time. The remaining 2 and 1 of the respondents said they defaulted 2-5 times and 6-10 times, respectively. Hence, the survey reflected that loan default was not a severe and significant problem in the case area.

Table 4.21: Farmers' Frequency of Default

Type	Default	Response		
		Number	% of total Respondents	% total Defaulters
Defaulters	1 Time	5	5	63
	2-5 Times	2	2	25
	6-10 Times	1	1	12
	Sub total	8	8	100
Non- Defaulters		92	92	
Total		*100*	*100*	

Source: Own Survey, 2009

Different reasons and motives could trigger farmers to default. Naturally, the reasons could be external to borrowers such as crop failures and climatic conditions, though proper farm management and external assistance could bring solutions. Alternatively, internal factors related to the behavior of individual farmers such as not knowing the terms and conditions of the loan and diversion of fund to other personal priorities could also trigger loan delinquency. The repayment terms and conditions should include all covenants of the loan from origination to final settlement of outstanding balances with the corresponding consequences of the loan default. Table 4.22 shows the fact that majority (63%) of the respondents who reported to have defaulted did not know the terms and conditions of the loan. Problems related to climatic conditions attributed to repayment failure by 25% of the respondents. Only one of the respondents declared to have failed to repay by giving priority to other purposes. This implies that most of the problems arose from the lending institutions or the intermediaries' failure in their part to execute the responsibility of ensuring the adequacy of borrowers' know-how on the terms and conditions of the loan agreement. Even if educational level of most respondents (88%) is below 8th grade, techniques of informing farmers that match their level of education could be used to ensure their understanding of obligations.

Table 4.22: Farmers' Reason for Default

Reason for Default	Resp.	Frequency of Rescheduling	Resp.	Type of Rescheduling	Resp.
- Not knowing Terms and Conditions	5 (63%)	- One Time	6(75%)	- Waiver of Repayment	2(25%)
- Diversion to other Purpose	0(0%)	- Two Times	0(0%)	- Additional Grant	0(0%)
- Giving Priority to other Matters	1(12%)	- Three Times	2(25%)	- Reduce Interest Rate	0(0%)
- Climatic Conditions	2(25%)			- Waiver of Penalty	1(12%)
				- Extension of Period	5(63%)

Source: Own Survey, 2009

Based on the assessment to be made on the causes of farmers default, there should always be consideration of alternatives for the amicable settlement of the loans at the lowest possible cost and with the minimum level of hassle. Rescheduling the original loan repayment agreements made between the lender and the borrower is a customary way before legal actions are pursued. After studying the causes of farmers' failure to repay the loans, the appropriate method for rescheduling of the original agreement is done.

Table 3.22 shows that 75% of defaulters in the sample were given a one time rescheduling for defaulted loans followed by 25% of the respondents who were privileged for three time rescheduling. In terms of the type of rescheduling, 63% of the respondents were entertained with extension of period to permit more time for repayment followed by 25% whose expected repayment was waived for some time. Only one of the defaulters was eligible for waiver of penalty. Finally, it was found that none of the farmers in the survey were sued before the court for failure to repay debts. However, this should not imply that there are no defaulters in the case area at all as the key informant discussions and the recovery rate trends indicate the existence of loan delinquencies in the *Woreda*.

In any credit delivery endeavor, the lenders' effort to assist borrowers on how to use the fund and the related engagement areas that are likely to impact the loan repayment process are crucial. Depending on the nature of the activity, therefore; borrowers get assistance on how to run the business and discharge their commitments regularly and

timely. In the case of agricultural loans, borrowers may need the technical assistance of various entities at all stages of the agricultural production process. It may range from managing the farms and using fertilizers to marketing the outputs and serving the loan obligations ultimately.

It was evident from the key informant discussion that cooperatives get no assistance from banks at all. Bank of Abyssinia used to provide loans in the area using USAID's fund as Cash deposit at the Bank as collateral before five years while Commercial Bank of Ethiopia has been a prime provider of agricultural input loans until now. However, both banks did not extend either direct assistance to the farmers or any of the intermediaries on how to use the borrowed funds and regularly repay loans. The key informant at the Commercial Bank of Ethiopia mentioned the fact that the bank once provided written guideline on how to compute interest repayments to all regional governments. Given the width of assistance required, this can not be taken as ample assistance. It was observed that all the Primary Cooperatives, their union and the Cooperative Promotion Commission need assistance from the banks. The advisory could be on the operational details of the country's laws that govern the lending process and the actual technical know-how on the lending operations, even if individual farmers are not contacted. In fact, as intermediaries, the primary cooperatives were also involved in the lending process from originating the loans to the end users, keeping documentation of the securities, following up on the respective member farmers and ensuring repayment of the loans. In other words, the lending process that primary cooperatives follow is a smaller version of the lending process by the commercial banks.

To substantiate the claim that should farmers get assistance, farmers were presented with questions to solicit the source and area of advice. Likewise, Table 4.23 shows that 96% of the respondents get assistance from primary cooperatives while 18% and 10% were contacted by government DAs and the cooperative union, respectively. In terms of advice area, 91% and 56% of the respondents claimed to have gotten advice on how to repay loans, and how to manage farms and use fertilizers, respectively. Only 6% replied that they got advice on how to market products. However, none were approached by bank representatives for advice.

Table 4.23: Follow up and Consultation

Advisor	# Yes	Advice Area	# Yes
Cooperatives	96	How to repay loans	91
Suppliers	2	How to manage farm & use fertilizer	56
Government DA/Extension agents	18	How to market products	6
Cooperative Union	10	It did not help at all	0
Other Sources	32		

Source: Own Survey, 2009

4.2.5 Small Scale Agricultural Credit Collateralization

Collateral based lending in the banking sector has been the dominant regime. The majority of commercial banks' loan portfolio is backed by collaterals of various properties. A minute share of the portfolio is allotted to clean based loans. Credit policy and procedures of the two banks considered for the study make no provision for clean based lending and for requests based only on business feasibility. The collateral requirements are stringent for any type of loans. Specific prescriptions on the physical properties of collaterals such as cash, buildings, vehicles and machineries acceptable to back the loans are made. In addition, intangible properties such as personal, group and institutional guarantees are acceptable depending on the type of loans and borrowers.

The Commercial Bank of Ethiopia requires regional governments, providing guarantee on behalf of the small-holding farmers, to present a letter of undertaking from the MoFED to use their subsidy budgets as collaterals. The key informant of the bank discussed the advantage of using such collateral for the full recovery of loans. The type of collateral, which is considered as 'Cash Substitute' as per the National Bank of Ethiopia's directive number SBB/43/2007 on loan classification and provisioning, seemed to relieve the bank from all the effort and costs involved in the process of loan recovery. Even though the loan contract is signed by the Cooperative Unions, the main binding document is the pledge agreement i.e. the regional government's letter of undertaking to surrender part of its budget in proportion to the unpaid sum of outstanding loan. However, due to

the full recovery of loans by the bank. the cooperatives claim that they do not get any support from the bank even on the areas on which banks have specialization such as the techniques to pursue during the repayment campaigns. This may give farmers the impression that the inputs taken on loan are just government fund and not government's borrowing from banks. The practice, in turn, bars the banking credit culture from disseminating among the farmers. The same was true in the case of loans extended by Bank of Abyssinia, before the expiry of the guarantee scheme pledging the USAID's fund as security on 50%-50% basis for loss sharing. The bank extended the loan using the cash deposited by the guarantor with the intention of securing the loans. However, the discussion with BoA's officials reflected on the repayment track record of the borrowing cooperatives where 100% of the loans were recovered during the time.

In addition to the scheme that the Commercial Bank of Ethiopia uses to secure loans, the respective primary cooperatives have their own system of securing individual loans by requiring farmers to offer group undertaking. Thus, a single loan is secured by both the federal government and farmer's group undertaking, revealing the prevalence of double security. First, farmers have to approach cooperatives to ask for input loans in group. The group would serve as collateral as the individuals are cross-collateralized on each others' loans. The group, then, will elect a leader who should be more known and responsible in the community and is economically better than the remaining. It is assumed that the leader will use his influence to prevent farmers from defaulting. Besides, the spouse of each individual borrower, if there is any, commits for the family's liability. As the survey in the area showed, the majority of borrowers (94%) were married indicating the possibility that marriage's consequent responsibility may be used as security for lending. In the case area, no physical properties were used to secure input loans. In fact, it is learnt that the social networking is given higher value than physical properties to secure individual loans. The survey also discovered that 82% of the respondents offered group undertaking to take input loans from the primary cooperatives while 19% gave a personal guarantee that took account of their spouse too.

The discussions with both bank officials and cooperative leaders unveiled the common perception that absence of title deed registration by the respective municipalities was a problem not to use the available properties of farmers, besides the obvious problem of not using land as collateral. The key informant discussion emphasized the low standard of houses that may not qualify for collateral purposes. The survey also showed that 92% of respondents' houses were built from mud walls even if attempts were made to renovate the houses. Besides, the social sanctions not to foreclose houses, the quality of the houses also undermine the respective price of assets to recover loans through foreclosure. Even though cooperatives have not attempted to secure loans with physical collateral, which is much easier to do for them than the commercial banks due to proximity, the lack of municipal propriety system on the houses and other wealth of farmers in most of the rural area would present problem for lenders not to use such collaterals. In fact, inclusion of physical properties for collateral purpose would add more value in addition to using the social networking to secure loans. Therefore, the issue of collateral remains a problem in the *woreda* as well.

CHAPTER V

5. CONCLUSION

Based on the analysis of the data and opinions collected from Commercial Banks, government offices, farmers, and cooperatives and their union, the following conclusions are drawn:

- Regarding the composition of farmers, about 98% were male reflecting the patriarchal orientation of families. Moreover, about 88% of the respondents were married and aged above 36 years. The structure of respondents showed that most farmers taking input loans through cooperatives were middle aged and above. Indeed, loan provision is based on assessing land holding status as a criterion to borrow over which the youth do not have control.

- In terms of land size, the sample shows individual holding of land stood at 2.7 hectare. Besides, the survey revealed that shortage of land was a problem for 89% of the respondents. This led to the problem of inadequate loans evidenced by fertilizer shortage as individual requirements are determined based on land size.

- Regarding farmers access to credit information, respondents revealed their ability to get information through electronic media such as radio and TV, besides the words of mouth. Respondents also played down the impact of possible infrastructural hindrances to access bank information. Thus, farmers do not seem to be affected by lack of information.

- In terms of mode of delivery, farmers get agricultural input loans using the two-tier approach where the government and cooperatives play intermediary roles to ensure the repayment and proper usage of loans obtained from Commercial Bank of Ethiopia. The regional government offers full guarantee for the unpaid sum of loans taken each year through the Ministry of Finance and Economic Development on its subsidy budget. In return, the bank forgoes 2.25% interest

rate per annum for the regional government and charges only 6.25%. This helped the bank to reduce the credit risk emanating from the default of individual farmers and the operation costs related to the loan collection process.

- Type-wise, farmers took loans in the form of fertilizers (97%), improved seeds (81%) and chemicals (77%). No cash contact for both farmers and cooperatives appeared during disbursement. Primary cooperatives and their Union (*Erer* Farmers Cooperative Union) play the role of input distribution and repayment collection. Furthermore, the share of individual loans is small in amount. The mean annual loan for the sample was Birr 3,808 with standard deviation of Birr 3,445. The relative fragmentation of land holdings, based on which borrowing capacity is determined, attributed to the smallness of loans. Thus, banks save enormous amount of operating cost by using intermediaries for disbursement and collection purposes.

- Recoverability of loans has been one of the problems contributing to the low level of credit supply from banks. Key informants indicated the prevalence of institutional abuse of power by the local government authorities and the management of primary cooperatives. From the sample, only 8% failed to serve their commitments, out of which, 75% were one time defaulters. In fact, 63% of the defaulters did not know terms and conditions of repayment and were able to settle after one time rescheduling. Thus, in recent years, loan default has not been much of a problem. Indeed, the heavy campaign works organized with various administrative organs of the *Woreda* contributed to the low default level.

- The existence of regional government guarantee for loans by offering the subsidy budget sought from the federal government has built the Commercial Bank of Ethiopia's confidence to extend credit to small holding farmers. In other words, the government was a key player to enhance credit access to small scale farmers. Contrarily, the guarantee scheme contributed to the withdrawal of the bank from the collection process. The Commercial Bank of Ethiopia extends no technical assistance to the intermediaries in the process of loan collection. Despite the

bank's willingness to lend farmers, its role in the expansion of related banking services seems to be week.

- In terms of collateral coverage, a single loan extended to farmers through the primary cooperatives is secured twice at various levels. First, the regional government guarantee gives assurance of repayment for the banks. Second, the primary cooperatives seek group undertaking for loans taken by individual farmers. The survey also unfolded that 82% and 19% of the respondents offer group undertaking and personal guarantee for loans, respectively.

6. RECOMMENDATION

Based on the analysis carried out and the conclusions drawn, the following points are forwarded as possible recommendations:

- The existing provision of agricultural input loans is mainly based on land size that individual farmers use. However, the scenario may not participate young farmers who have less likelihood to acquire land, and yet, who are relatively a more productive section of the farming community. Thus, concerned bodies who are involved in the credit extension process will need to identify and consider other parameters to assess the creditworthiness of farmers, and hence, promote opportunities for their participation.

- The loan delivery process in the *Woreda* under consideration follows a two-tier approach where other governmental and membership organizations intervene and facilitate the flow of funds from Commercial Bank of Ethiopia to the small scale farmers. However, the bank, which has all the expertise in the lending task, is not involved in the collection process as it secures its loans with cash substitute collateral. Thus, the bank should exert efforts by assisting the intermediaries in the collection process to discharge its social responsibility in addition to its profit making motives.

- Agricultural credit in the *woreda* is limited to the provision of input loans, among the various financial needs of the sector. Even though the default rates and their causes need further study, it appears that banks should endeavor to provide more types of loans that are both on-farm and/or off-farm in nature. This is hoped to supplement the personal income base of farmers and serve as a tool for development.

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Annex I: Demographic Structure of Respondents

Number	Sex	% age	Religion	% age	Ethnic	% age	Education	% age	Marital	%age
1	Male	98.0	Orthodox	91.0	Oromo	75.0	< Grade 8	88.0	Married	94.0
2	Female	2.0	Muslim	9.0	Amhara	25.0	10th complete	9.0	Unmarried	3.0
3		0		0		0	Diploma	3.0	Divorced	3.0
	Total	100.0	Total	100.0	Total	100.0	Total	100.0	Total	100.0

Annex II: Disbursement, Collection and Outstanding Balance of Agricultural Loans in Ethiopia

	2004	2005	2006	2007	2008
Disbursement	602.1	1,560.2	2,188.8	2,621.0	5,371.6
Collection	572.4	851.7	1,409.3	2,254.6	4,443.4
Outstanding Balance	14,564	2,018.2	3,418.0	4,218.4	5,481.2
% Growth of Disburse	*35.6%*	*159.1%*	*40.3%*	*19.7%*	*104.9%*
% Growth of Collection	*3.6%*	*48.8%*	*65.5%*	*60.0%*	*97.1%*
% Growth of Outstanding	*-3.4%*	*73.7%*	*69.4%*	*23.4%*	*29.9%*

Annex III: Disbursement and Collection of Agricultural Input Loans for Selected Primary Cooperatives in Ada'a Liben Woreda

Primary Cooperatives	2004		2005		2006		2007		2008	
	Disburse	Collect	Disburse	Collect	Disburse	Collect	Disburse	Collect	Disburse	Collect
Udee	622,342	622,342	592,712	539,917	897,195	865,333	701,077	597,973	489,671	269,492
Godino	385,343	385,343	495,616	493,661	755,352	755,352	525,045	525,045	407,195	403,832
Kajima	283,582	270,599	318,560	271,078	476,905	423,091	362,585	325,281	303,906	197,343
Dukem	570,022	570,022	687,983	514,177	1,004,642	988,333	684,685	684,685	470,009	312,746
Total	**1,861,289**	**1,848,306**	**2,094,871**	**1,818,833**	**3,134,094**	**3,032,109**	**2,273,392**	**2,132,984**	**1,670,781**	**1,183,413**

Annex IV: Loan Recovery Performance of Agricultural Input Loans for Selected Primary Cooperatives

Performance	2004	2005	2006	2007	2008
Udee	100%	91%	96%	85%	55%
Godino	100%	100%	100%	100%	99%
Kajima	95%	85%	89%	90%	65%
Dukem	100%	75%	98%	100%	67%
Total	*99%*	*87%*	*97%*	*94%*	*71%*

Annex V : Growth of Disbursement and Collection for Agricultural Input Loans for Selected Primary Cooperatives

	2005		2006		2007		2008	
	Disb.	Collect	Disb.	Collect	Disb.	Collect	Disb.	Collect
Udee	-5%	-13%	51%	60%	-22%	-31%	-30%	-55%
Godino	29%	28%	52%	53%	-30%	-30%	-22%	-23%
Kajima	12%	0%	50%	56%	-24%	-23%	-16%	-39%
Dukem	21%	-10%	46%	92%	-32%	-31%	-31%	-54%
Total	*13%*	*-2%*	*50%*	*67%*	*-27%*	*-30%*	*-27%*	*-45%*

Annex VI: Summary of Statistical Outputs

Variables	Sample Size	Minimum	Maximum	Mean	Standard Deviation
Income per Annum	100	4,000.0	75,000.0	24,212.5	15,197.6
Saving per Annum	100	-	20,750.0	4,118.5	3,500.7
Household Expenditure per Annum	100	3,250.0	54,250.0	15,462.3	8,763.0
Amount of Loan From Cooperatives	100	1,000.0	17,500.0	3,808.0	3,440.1
Percentage of Production for Stock	100	-	100.0	51.3	25.7
Land Size in Hectare	100	0.5	6.0	2.7	1.4
Production in Quintal	100	3.5	65.0	26.1	15.3
Percentage of Production for Stock	100	-	100.0	51.3	25.7
Age of House	100	-	44.0	16.2	6.8
Number of Renovations for Houses	100	-	3.0	1.1	0.8
Amount Spent for Renovation	99	-	10,000.0	2,691.8	2,012.8

Annex VII

Addis Ababa University Serial No._____

College of Development Studies

Department of Regional and Local Development Studies

Questionnaire for Farmers

Instruction: The purpose of this questionnaire is to gather data on farmers' borrowing experience from commercial banks. The collected data are to be used for conducting a study for fulfillment of Master of Arts degree in Regional and Local Development Studies, and hence, purely used for academic purpose. Any information to be provided by respondents will be confidential. In a bid to keep logical flows of ideas, the questions are disaggregated into nine sections. Follow the specific instruction for each section. Thank you in advance.

I. Personal Profile:

1. Sex:

   (0) Male (1) Female

2. Age : _____

3. Religion: (1)Orthodox (2)Muslim (3)Catholic (4)Protestant

   Other _____

4. Marital Status:

   (1)Married (2) Unmarried (3) Divorced (4) Single

5. Educational Qualification:

   (1)< 8th Grade (2) 10th complete (3)12th Complete

   (4)Certificate (5) Diploma (6) Degree

6. Ethnic background:

   (1)Oromo (2) Amhara (3) Tigre

   (4)Other (Specify) _____

7. For how long have you been living in the area? (In years)

   (1)< 2 (2) 2-5 (3) 5-10 (4)10-15 (5)15-20 (6)>20

8. Are you head of your family?

   (1)Yes (2) No

9. Household Size:

No.	Relation Ship (Code A)	Age (Code B)	Sex (Code C)	Educational level (Code D)	Marital Status (Code E)	Occupation (Code F)

Code A: (1) Head, (2) Spouse,(3) Son/daughter, (4) sister/brother, (5)aunt/uncle, list if other relationships

Code B: (1) <20, (2) 20-25, (3.) 25-30,(4.) 30-35, (5.) 35-40 and (6.)>40

Code C: (0) Male, (1) Female

Code D: (1) 8, (2) 8-12th,(3) 12th complete, (4.) Certificate, (5) Diploma, (6.) Degree

Code E :(1) Married, (2.)Unmarried, (3.) divorced, (4) Single

Code F: (1.) Farmer, (2.) Student, (3.) Employed, (4.) Unemployed and (5.)Others

10. How much of your income do you save *per annum?*

Maximum: _____

Minimum: _____

11. What was your previous occupation?

(1) Farmer (2) Student (3) Employed (4) Unemployed

(5) Others (Specify) _____

II. The following questions are related to your *land* .You can tick more than once.

1. How do you get the land you work on now?

(1) Leased from government (2) Rented for other farmers (3) Bought from farmers (4) Others (Specify) _____

2. What is the size of your land in Hectare/ Km^2?

_____

3. Have you been using your land for your own work?

(1) Yes (2) No

4. If you ticked "yes" for Q. no. 3, how much of the land has been used for your own work?

_____

5. If you ticked "No" for Q. no.3, what do you do with it?

(1) Rent to other farmers (2) Idle

(3) Others (Specify) _____

6. If you have been renting all or part of your land, what was your reason for renting?

(1) Input shortage (2) Excess land (3) Better profit from leasing

(4) Inability to work (5) Other (Specify) _____

III. The following questions are related to your *Production*.

1. If you are a farmer, specify the particular production activity you are engaged in.

(1) Cereals (2) Oil Seeds (3) Animal Fattening (4) Diary

(5) Other (Specify) _____

2. What means of production do you use for your specific farming activity?

(1) Cattle (2) Labor (3) Tractor

(4) Others (Specify) _____

3. How long have you been engaged in this particular farming activity?

(1) < 1 year (2) 1-3 years (3) 3- 5 years (4) 5-7 years

(5) 7-10 years (6) > 10 years

4. What was your reason for engaging in the job you mentioned under question no.1 above?

(1) Family Inheritance (2) Ease of Production (3) Soil and other

(4) Topographic factors (5) Profitability (6) Ease of Access to Inputs

(7) Other (Specify) _____

5. How much quintal/Liter/number of animals do you get from the selected activity?

_____

6. What were the trends of changes in your production for the last three years?

(1) Increased (2) Decreased (3) Constant

7. Explain the reasons for the changes in production as indicated in your answer for question No.6?

_____

_____

_____

8. What problems do you face in the production process?

(1) Lack of Fertilizer (2) Lack of Capital (3) Storm (4) Shortage of Land

(5) Drought (lack of rain fall) (6) Others (Specify) _____

9. How much of your production do you usually sell after harvesting?

_____

10. What was the trend in the price of items in the last three years?

(1) Increased (2) Decreased (3) Constant

11. Give your explanation for the changes in the price?

_____

_____

_____

_____

IV. The following questions are related to your ability to *Stock*.

1. Were you able to store portion of your production? *(If you ticked "yes', answer only question no.2-8)*

(1) Yes (2) No

2. Have you been able to hold stock every production year/cycle?

(1) Yes (2) No

3. How much of the produce do you store from every production cycle?

_____

4. What was/ were your intention/s for storage?

(1) Price Speculation (2) Consumption (3) Animal feed

(4) Lack of market (5) Other (Specify) _____

5. What was the trend in the amount of your storage for the past three years?

(1) Increased (2) Decreased (3) Constant

6. For how long were you able to store (Experience for the last three years)?

(1) < 3 months (2) 3-6 months (3) 6- 12 months (4) > 1 year

7. Have you been beneficiary in holding stock of your production?

(1) Yes (2) No

8. Give your reasons for the reply for question no.7?

_____

_____

_____

9. If you ticked "No" for Question no.1, what are your reasons?

(1) Good market (2) Lack of Storage (3) Inadequate production

(4) Cost of Storage (5) Others (Specify) _____

V. The following questions are related to your *Income and Expense.*

1. What is your aggregate income *per annum?*

Maximum: _____

Minimum: _____

2. What percent of your income do you allocate for saving?

(1) <10% (2) 10-20% (3) 20- 30% (4) > 30%

3. How much do you spend for your family's subsistence *per annum?*

Maximum: _____

Maximum: _____

4. What other income sources do you have, other than your principal business?

(1) Renting land (2) Renting cattle (3) Selling labor

(4) Other _____

5. How much per hectare/Cattle/labor time were you charging (In cash or in Kind)?

_____

6. How do you keep record of your income and expenses?

(1) Own records (2) Hired Book Keeper (3) Children

(4) Others (Specify) _____

7. How many individuals do you need for your work at a time?

_____

8. Do you work with your family or hire external labor for your activity?

(1) Work with Family (2) Hire labor

9. If you hire labor, how much do you pay for individual labor, on average?

_____ Per hour (1) _____ Per day (2)

_____ Per month (3) _____ Per Year (4)

_____ Other agreements (5)

VI. The following questions are related to your *Membership Status* to associations.

1. Are you a member of any association related to your occupation? *(If you ticked yes, answer questions no. 2-7)*

(1) Yes (2) No

2. If you ticked "yes" for question no. 1, what type of association do you belong to?

(1) Cooperative (2) Women Association

(3) Other (Specify) _____

3. What is the *purpose* of the association you belong to?

_____

_____

_____

_____

4. Do you believe that you are benefited from being a member?

(1) Yes (2) No

5. Give your reasons for your answer to Question no.4.

_____

_____

6. Do you belong to any cooperative association/s?

(1) Yes (2) No

7. If you ticked 'yes' for the question above, which cooperative/s do you belong to?

_____

VII. The following questions are related to *Asset Holdings*.

1. Do you have your own house?

(1) Yes (2) No

2. If you ticked "No" for the question above, where do you live?

(1) Rented house from individuals (2) Relatives (3) Government house

(4) Others (Specify) _____

3. If you ticked "Yes" for question no. 1, what is it made of?

(1) Brick Wall (2) Mud wall (3) Iron sheet wall (4) Iron sheet roof

(5) Others (Specify) _____

4. When was it built? (What is the age of your house?)

_____

5. Have you ever renovated/ maintained your house?

(1) Yes (2) No

6. If you ticked 'yes' for question no. 5, how many times in three years?

_____

7. How much did you spend for renovation in the past?

_____

8. Do you own cattle?

(1) Yes (2) No

9. If you ticked "Yes" for question no. 8, fill the following table?

Code	Type of Animal	Total Number	Change in three years(Increase/Decrease/ constant)	Purpose of Owning
1	Cow/Oxen			
2	Sheep/ Goat			
3	Donkey			
4	Bull/Heifer			
5	Poultry			
6	Mule			
7	Horse			

10. What other means/ asset do you have/ use for your production activity?

_____

VIII. The following questions are designed to assess your exposure related to *Access to credit.*

(Tick more than once if necessary)

1. Do you use loan facilities either in *cash or in kind*?

   (1) Yes (2) No

2. If you ticked yes for question no. 1, in what form do you take the loans?

   (1) Cash (2) Fertilizer (3) Seeds (4) Chemicals

   (5) Others (Specify) _____

3. If you ticked 'yes' for question no.1, from which institutions do you take the loans?

   (1) Microfinance Institutions (2) Banks (3) Saving Associations (4) Cooperatives

   (4) Others (Specify) _____

4. How long have you been using loans if you answered *banks / cooperatives* above? (In years)

   (1) <1 (2) 1-3 (3) 3-5 (4) >5

5. Do you want to borrow money?

   (1) Yes (2) No

6. For what purpose do you need money, besides the purpose for which you already take?

   _____

7. Where do you prefer to borrow from?

(1) Suppliers (2) Banks (3) Microfinance (4) Cooperatives

(5) Other (Specify) _____

8. Give your reason for your reply under question no.7.

_____

_____

_____

_____

9. In what form do you want to take the loans?

(1) Cash (2) Fertilizer (3) Improved Seed (4) Chemical

(5) Other (Specify) _____

10. Give your reason for question no.9 above?

_____

_____

_____

A. *Access to information about credit from banks:*

1. Are you aware of the existence of loans from banks?

(1) Yes (2) No

2. If you ticked 'yes' for question no. 1, how did you know the existence of credit services from banks?

(1) Radio (2) TV (3) Word of mouth (4) bank's promotion

(4) Extension services (5) Cooperatives

(6) Others (Specify) _____

3. How long has it been since you know the availability of credit from banks (In years)?

(1) <1 (2) 1-3 (3) 3-5 (4) >5

4. What obstacles did you encounter to acquire the information?

(1) Absence of Road (2) Absence of Telecom (3) Absence of electronic media

(4) Others (Specify) _____

5. Have you ever tried to request for credit facility from banks, individually?

(1) Yes (2) No

6. If you ticked "yes" for question no.5, what were the replies you got?

(1) Acceptance (2) With some requirements (3) with demanding Requirements

(4) Total Rejection

(5) Others (Specify) _____

7. Do you want to *directly* borrow from banks?

(1) Yes (2) No

8. If you ticked 'Yes' for question no.7, mention the purpose/s for which you want to borrow from banks?

(1) Purchase of fertilizers (2) Consumption (3) Transport product to market

(4) Paying overdue Rent (5) Paying overdue Loans (6) Others (Specify)

_____

9. Do you prefer banks to other lenders?

(1) Yes (2) No

10. If you ticked 'yes' for question no.9, what is/ are your reasons?

(1) Low Interest rate (2) Accessibility (3) Trust for Work

(4) Others (Specify) _____

B. *Collateral position:*

1. Have you been asked to offer collateral for any of your previous borrowing in *cash/ kind* from banks/ cooperatives?

Bank: (1) Yes (2) No

Cooperatives: (1) Yes (2) No

2. If you ticked "yes" for question no.1, what type of *collateral/guarantee* were you asked?

(1) House (2) cattle (3) Crop (4) Group Undertaking

(5) Personal Guarantee (6) Other (Specify) _____

3. Who did require you to offer the type of collateral you mentioned under question no.2?

(1) Government Bureaus (2) Banks (3) Cooperatives

(4) Others (Specify) _____

4. Do you believe that you should offer collateral for your borrowing?

(1) Yes (2) No

5. Do you try to acquire property anticipating it will be used as collateral?

(1) Yes (2) No

6. Do you feel that borrowing from banks will pose any threat on you?

(1) Yes (2) No

D. Credit Repayment and Default Experience:

1. What were the amounts of loans borrowed for fertilizer or other purposes since you started relationship with *cooperatives/Banks*?

   Bank: Minimum_____ Maximum_____

   Cooperative: Minimum _____ Maximum_____

2. How long have you taken to repay the loaned amounts?

Loans	Lender (Code A)	Repayment Terms (Code B)	Purpose (Code C)	Number of months taken to repay loans
1				
2				
3				
4				
5				

Code A: (1) Bank (2) Cooperative

Code B: (1) Monthly (2) Quarterly (3) Semi Annually (4) Annually (5) Lump sum after harvest (6) Other (Specify)

Code C: (1) fertilizer (2) Improved seed (3) Consumption (4) Other (Specify)

3. What repayment terms do you *prefer* for returning debts from *banks/cooperatives*?

   Banks: (1) Monthly (2) Quarterly (3) Semi- annually (4) lump-sum

   Coops. (1) Monthly (2) Quarterly (3) Semi- annually (4) lump-sum

4. Explain your reasons for your reply in question no.3.

   _____

   _____

   _____

   _____

5. What is the trend for the amount of your previous borrowing for the purpose you stated?

   (1) Increased (2) Decreased (3) Constant (4) Abandon borrowing

6. Give your explanation for any of your replies for question no. 5.

_____

_____

_____

_____

7. Have you ever defaulted on any debts borrowed from *banks/ cooperatives*?

   Bank :(1) Yes (2) No

   Coop: (1) Yes (2) No

(Answer questions 8-16 only if you ticked yes for question no. 7)

8. How many times did you default?

   Bank: (1) 1 (2) 2-5 (3) 5-7 (4) 7-10 (5) >10

   Coop: (1) 1 (2) 2-5 (3) 5-7 (4) 7-10 (5) >10

9. What was/were the reasons for your default?

(1) Not knowing terms and conditions of loan agreement/contract

(2) Diversion to other purposes

(3) Crop failure

(4) Giving priorities to personal matters

(5) Climatic conditions (Rain fall shortage, storm, and flood....etc)

(6) Others (Specify) _____

10. What were the measures that are taken as a result of your default?

(1) Land Confiscation (2) Forced to serve for free farming

(2) Cattle and house confiscation

(3) Others (Specify) _____

11. Was there any rescheduling for the defaulted loans?

(1) Yes (2) No

12. How many times did you get rescheduling for each debt?

(1) Loan 1 _____ (3) Loan 3 _____

(2) Loan 2 _____ (4) Loan 4 _____

(5) Loan 5 _____

13. What were the prime reasons considered for rescheduling your debts?

14. What form of rescheduling was applied to you?

(1) Waiver of Repayment (2) Extension of period (3) Additional grant

(4) Reduction of interest rate (5) Waiver of penalty (6) Others (Specify)

15. Were you able to pay after rescheduling?

(1) Yes (2) No

16. Give justification of your answer for question no.15?

IX. The following questions assess your experience related to *other sources of borrowing*.

1. What other sources of borrowing do you use?

(1) Microfinance (2) Iqub (3) Idir (4) NGOs

(5) Others (Specify)

2. If you have been borrowing from sources other than *banks/coops*, fill the following.

Loans	Lender	Purpose	Repayment History*
Loan 1			
Loan 2			
Loan 3			
Loan 4			
Loan 5			

* *Repayment history includes: repaid on time, rescheduled, did not pay at all, other (specify)*

3. Why did you prefer the above sources of credit?

(1) Proximity (2) Low interest rate (3) Small Collateral (4) Flexible Repayment

(5) Low penalty (6) Others (Specify)

4. Are you still a client of lenders other than banks/Cooperatives?

(1) Yes (2) No

5. What problems did you observe from these creditors?

_____

_____

_____

_____

X. The following questions are designed to assess your *overall impression of borrowing from banks.*

1. What general problems do you observe in borrowing from banks?

2. What strong side did you see in borrowing from banks?

3. Give your suggestion on what banks should do to create access to credit?

_____

THANK YOU!

Annex VIII

ADDIS ABABA UNIVERSITY

COLLEGE OF DEVELOPMENT STUDIES (CDS)

DEPARTMENT OF REGIONAL AND LOCAL DEVELOPMENT STUDIES

(INTERVIEW GUIDELINE FOR KEY INFORMANTS OF COMMERCIAL BANKS)

1. Express your personal background (Educational level, prior experience, year of service at various levels in the bank ...etc.)
2. Are you aware of or happen to participate in the bank's operation related to agricultural credit to small holding farmers? Give your opinion of the process?
3. Does your bank have credit policy and procedure for agricultural credit specific to small holders? Give your opinion on the salient features and weaknesses of the policies and procedure.
4. What are the specific endeavors and special considerations by the bank to facilitate access to credit for small holders?
5. What specific reasons can you mention on behalf of the bank for its ***success and failures***?
6. What efforts were there from the bank to pursue training /conduct research /other professional development programs related with agricultural credit? Discuss the outcomes.
7. Do you believe that the existing system/ approach for loan delivery can be applied for agricultural credit in the same way as the other sectors?
8. How do you differentiate between group and individual borrowers for successful operation of credit market? Discuss the merits and demerits of each.
9. Discuss your awareness on existing interest rate, credit rationing or other regulations and laws that impact the farmers' access to credit from your bank, positively as well as negatively.
10. Discuss the bank's experience in interest rate differentiation among products and borrowers of agricultural credit, especially for small holders.

11. Discuss the peculiar issues to be accounted for in appraising small agricultural loan applications by farmers/cooperative/ others.
12. What sort of lien do your often require in agricultural lending?
13. In terms of decentralization, how is the loan approval process for agricultural credit carried out among the different hierarchies in the bank?
14. How do you differentiate the level of credit risk embedded in agricultural credit from other types of credit products you may know?
15. Does your bank happen to adopt innovative mechanisms to facilitate credit delivery in rural market such as *mobile banking*?
16. How do you evaluate the position of small holders in light of ***formal credit delivery*** system/ practice of the bank?
17. What monitoring/ follow up / risk mitigation techniques does your bank/ branch applies to protect its interest from loss arising from small agriculture credit?
18. Have there been loss recovery mechanisms for agricultural loans for small holding farmers? Discuss the outcomes and related reasons.
19. Do you believe that small holding farmers can have access to commercial bank credit in general? Discuss your supporting reasons.
20. How do you see the past failures of lending to small holders? Discuss your personal observations of the contributions of all parties for this failure.
21. What do you suggest should be done in the future to expand commercial bank credit in rural areas?

Annex IX

ADDIS ABABA UNIVERSITY
COLLEGE OF DEVELOPMENT STUDIES (CDS)
DEPARTMENT OF REGIONAL AND LOCAL DEVELOPMENT STUDIES
(INTERVIEW GUIDELINE FOR KEY INFORMANTS OF SELECTED COOPERATIVES, UNION AND OTHERS)

1. Explain about your ***personal information*** (Age, educational background, prior experience...), position, experience in the particular cooperative you belong to?
2. Give brief explanation on the ***process and objectives*** of forming cooperatives?
3. Discuss how the ***governance in cooperatives*** works in terms of ownership and management selection/ appointment.
4. Give your ***opinion on roles*** that cooperatives can play in enabling farmers to have access to credit?
5. Discuss the process with which cooperatives deal with commercial banks for ***credit negotiations***.
6. Discuss the ***mechanisms for individual farmers' access to credit*** from banks with the problems and strengths?
7. Explain your opinion on farmers' ***benefits from cooperative membership*** related with credit, directly or indirectly?
8. What are the roles cooperatives play at ***various levels for farmers*** to get credit?
9. What mechanisms/approach does your cooperative adopts/follows to ensure ***repayment*** of loans? Discuss your justification.
10. Discuss experience of past ***non-repayment of loans from member farmers*** and reasons? What ***measures*** have been taken by banks and the cooperatives or other parties you may know?
11. Discuss the various ***advisory services, process*** and what observations of the outcomes given to farmers related to credit?
12. Discuss the ***services your cooperative provides*** for farmers in addition to credit?
13. Explain you observation of the ***major constraints hampering credit delivery*** from both commercial banks and individual farmers?
14. Discuss your belief about the ***legitimacy of individual farmers' access*** to bank credit and the mechanisms available?
15. Give your ***suggestions, comments or opinion*** on what should be done for credit market flourishment in the rural market.

DECLARATION

I declare that this thesis is my original work and has not been presented for a degree in other university and all sources of materials used for the thesis have been duly acknowledged.

Atikilt Admasu

July 2009