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IMPACT OF MICRO FINANCE ON AGRICULTURAL SECTOR

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ABSTRACT

Agriculture has been the backbone for any developing countries. Agriculture plays a key role in providing raw materials for the service sector and less developed world. But the finance is the major problem for agriculture sector so micro finance can help to increase production and growth. Amidst the issue, microfinance contributes great towards agricultural modernization and increased production in developing countries. This paper seeks to evaluate the impact of microfinance on agricultural production. The study recognized that microfinance is positively related to agricultural production and shows a significant impact on output levels. Major challenges identified with credit access include unavailability of collateral securities, small loan amounts and delay in the release of agricultural loans. The major challenge with credit administration is the lack of understanding of the loan acquisition process among farmers. The formation of active farmer-based organizations, educating farmers on the loan acquisition process, encouraging farmers to save, and encouraging Microfinance Institutions (MFIs) and other development partners to sufficiently finance agriculture were recommended. It is envisaged that such efforts have the potential to reduce income inequality thus contributing towards the achievement of the millennium development goal of poverty reduction.

KEYWORDS: *Microfinance Institutions (MFI), Impact, Developing countries, Agricultural, Production.*

Introduction

Agriculture is an inevitable associated to the economies of developing countries as it plays a key role in providing food to the population and supplying other sectors with raw materials for production of goods and services. Agriculture is a major sector of the economy because its impact heavily on poverty reduction and industrial promotion through the supply of inputs. Higher production from a farmer's increases access to food and enhances household food security that result is improving the nutritional needs of society. For those who purchase food, higher production generally means lower food prices and consequently access to a greater quantity of food in the market for a given income level. Poverty is deepest among food crop farmers, who are mainly traditional small scale producers. Despite the significance of the agricultural sector to poverty reduction and overall development but the agriculture is characterized by low production and badly functioning markets for outputs. Small holder farmers rely on elementary methods and technology. Small farmers have limited skills and inputs such as improved seeds that would increase yields. Peasant and subsistence farming with the use of undeveloped technologies have been very primary in the agricultural sector, resulting in low levels of production. Although the sector contributes significantly to the Gross Domestic Product (GDP) of the country, its per capita contribution is very insignificant. Thus, the overall production has not been up to the level that will ensure that the sector makes the needed impact.

The gross effect of the situation described above is that, most of these farmers lack economies of scale as a result of the small scale production, resulting in a high per capita cost and generally low production levels. Finance or capital has been identified as been inadequate to expand production in the sector especially by the low- income earners or farmers who hold small farms. Microfinance has a very important role to play in addressing the numerous constraints bedeviling the agricultural sector. The United Nations Capital Development Fund (**UNCDF)** has shown that microfinance plays three key roles in development (UNCDF, 2004). It helps very poor households meet basic needs and protects against risks, it is associated with improvements in household economic welfare and it helps to empower women by supporting their economic participation and so promotes gender equity.

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Microfinance Facilities

Microfinance is the financial services provided to the poor in the form of deposits, loans, savings, payment services, money transfers and insurance with the primary aim of helping them. And engage in or expand their livelihood activities that, reducing poverty and quickening development. They highlight that such beneficiaries are often people who are not included in the formal financial systems. Due to some barrier like distance, illiteracy, untouched area and many more which have not been mentioned or outlined and also add that such credit when accessed, is returned in small agreed installments usually according to be within the capacity of the beneficiary. In the area of micro finance various approaches and methods are used in the delivery of financial services and these falls under three broad categories formal, semi-formal and informal institutions.

Objectivs of the Study

The situation therefore requires a research into the area of microfinance and agricultural production. The study therefore aimed at unfolding the realities between microfinance and agricultural production with the following specific objectives:

- To identify the challenges involved in accessing credit.
- To know the importance of agriculture finance.
- To suggest recommendations to agriculture growth through microfinance.

Research Methodology

The work is descriptive and analytical in nature. It is simple but pragmatic. The study is mainly based on descriptive and secondary sources. We have made the study based on secondary data collected from the various publications research report, papers, books etc.

Review of Literature

Dr. Satish Chandra[1] in his publication "**Agricultural Price Policy in India**" (2017) stated that agriculture price in India suffer from violent fluctuations due to so many factors such as vagaries of nature and the traditional outlook of farmer's social class etc. the agricultural price policy has to take care of all such fluctuations so as to provide a logical condition for rapid growth. It is controversial whether in the real world price fillip will substantially enhance the productivity because the consumption of the agriculturist is responsive to income elasticity of demand in agricultural sector.

Ministry of Statistics and Programme Implementation[2], **Central Statistics Office** Oct. (2016), "**Manual on Agricultural Prices and Marketing**" stated that agricultural prices and marketing have enormous economic and political implications. In India, where agriculture continues to provide employment and incomes, agricultural prices and marketing have profound effect on the levels of live-in. It is the concern with both the level of agricultural product prices and wide fluctuations which led the government. In this context, the policies relating to agricultural sector, particularly those relating to the pricing and trade are receiving the utmost attention of planners, economists, farmers and trade organizations.

Sudip Mitra and Jagjeet Singh Sareen[3] (2016),'**Adaptive Policy Case Study :Agricultural Price Policy in India''** analyzed some specific policy instruments under APP form an adaptive policy perspective. The objective of the government's price policy for agricultural products is to set remunerative prices with a view to encourage higher investment and production. Theoretically, APP accounts for various economic factors, such as the rate and quality of economic growth, in identifying and promoting the optimal crop mix. This, consequently, ensured appropriate allocation of resources in the agriculture sector, capital formation, and inter-sector terms of trade.

V N Mishra and **Peter B R Hazell**[4] (2016), "**Price and Non-Price Factor in Agriculture Investments**", the author aimed that we give too much emphasis to the price factor and not enough to the role of public investment while interpreting the result. Indeed he accuses us to of being very obsessive in underscoring the role of prices. His comments seem misplaced when viewed within the broader context of our papers.

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1 Chandra, Satish (2017) Agricultural Price Policy in India, Chaugh Publications, Allahabad.
2 Ministry of Statistics and Programme Implementation, Central Statistics Office Oct. (2016), Manual on Agricultural Prices and Marketing
3 Sudip Mitra and Jagjeet Singh Sareen (2016),'Adaptive Policy Case Study :Agricultural Price Policy in India''
4 V N Mishra and Peter B R Hazell (2016), Price and Non-Price Factor in Agriculture Investments.

Ibrahim and Bauer (2013) concluded that agricultural investment should be increased for ensuring efficient and sustainable technology to increase farm profit and microcredit fill the gap between the actual fund of the farmer for production and the required agricultural investment.

Wadud (2013) found that microcredit, farmer's education and experience help to utilise input more efficiently in the cultivation process in Bangladesh. Thus farmers can reduce food insecurity in the family level.

Saleem and AliJan (2011) suggested that farmers with access to microfinance are significantly more efficient than their non-borrowing counterparts and also revealed that land fragmentation, family size, household wealth, on farm-training and off–farm income share were the main determinants of inefficiency in the farm productivity.

Islam (2011) also suggested ensuring access to microfinance to increase TE in agricultural production. Unfortunately, small farmers cannot get access for bank credit in many countries because of mortgage, high formality, lengthy procedure and unavailability of concerned institutes at farmers' close position. Hence, microfinance emerged as a noble substitute for informal credit and is considered to be a powerful instrument for poverty alleviation among people.

Osei-Mensah and Adams (2009) suggested that state must continue support to ensure access in cheap and adequate capital especially in the form of concessionary loans to support non-agricultural micro enterprises. Hence microcredit can fill the gap. If farmers get loan at high time then, they can use inputs efficiently and can increase productivity also.

Khandker (1998) found that microcredit could be source of self employment and higher consumption, wealth and assets of the beneficiary group. The credit not only improves the agriculture productivity but also raises the purchasing power of the farmer.

Discusstions

Specificities of Agricultural Finance

The agricultural sector is different from other economic sectors in a number of ways. Activities are generally located in isolated areas with low population density and poor infrastructure. They are dependent on weather and production cycles, income is seasonal and monetary income is limited. Agricultural prices are disreputably volatile and few farmers can offer guarantees that are legally or financial acceptable. Table 1 shows list of Micro Finance Institutions with loan portfolio for agriculture and other small industries. With its extensive branch network Bandhan Bank has been able to ensure maximum client outreach and has the highest client base of 65 lakhs. SKS microfinance once again comes a distance second followed closely by SKDRDP which follows self help group – bank linkage model of microcredit.

Table: 1 List of MFIS with Loan Portfolio as of March 2015

S. No.	Name of MFIs	Gross Loan Portfolio (in Crore)
1	Bandhan	9524
2	SKS	4155
3	Janalakshmi	3774
4	SKDRDP	3570
5	Ujjivan	3274
6	Spandana	2665
7	Equitias	2144
8	Satin Creditcare	2141
9	Share Microfinance	1603
10	Grameen koota	1447

Source: e-books

These specificities demand financing mechanisms adapted to the diverse needs and services of rural households:

Short-term: input financing at the beginning of the crop year (seeds, fertilizers, pesticides), additional labor, feed, storage facilitates, processing, etc.

Medium and long term: equipment for intensification, commercialization (transportation), storage (buildings), perennial crops (investment, renewal, maintenance), (re)constitution of herds, land purchase.

Non-financial services: monitoring demand, technical assistance and extension.

Understanding how to best meet these financial needs and finding ways to mitigate the risks associated with them are added challenges that further hinder the expansion of financial services for agriculture. Moreover, as microfinance is increasingly integrating into conventional financial markets, the sector has no choice but to apply cost-covering interest rates. Such rates often contradict the expansion of rural coverage and agricultural finance due to the low profitability of the activities financed. All these factors explain the relative lack of interest in agriculture on the part of urban and peri-urban zones. Consequently, liberalized markets coupled with contractual innovations-elements promoted under the new paradigm-have not fulfilled their promises vis a vis rural and agricultural finance.

Microcredit Ceiling and Purpose

Beneficiaries were in groups where the bank officials explained that for group lending, the bank expects a low risk because in the case of repayment difficulties by some members of the group, other group members take responsibility. The bank is therefore confident that with group lending, the default rate is almost zero hence, the need for higher amounts for group borrowing. The major purpose for which loan was provided to farmers was basically to help them expand their farm activities, increasing output and income levels. This finding tallies well with the results of Yeboah (2010) and Mason (2013) who found that microcredit is often given for the purpose of business establishment, expansion and ultimately reduce poverty and create wealth.

Inquisitive further, the credit officer explained that farmer households dominate in the areas where they operate and also form the majority of poor households. The overall goal therefore is to provide them with a means that will help them move out of poverty. For them, microfinance is seen as the surest approach to reducing poverty if only other institutions such as the District Agricultural Development Unit and the District Assembly collaborate effectively to provide supervision to farmers in the utilization of such credits.

Production Levels

Here attempts have been made to analyze the relationship between microfinance and output levels as well as the extent to which the credit facility has contributed to output.

Challenges in Accessing Agricultural Loans Collateral Securities and Other Criteria for Credit Qualification

One key challenge raised by farmers which was equally raised farmers' difficulty to fulfill the criteria for accessing loan facilities. Most of farmers described the process as bulky, tiring and time wasting. However, few farmers do not see the process as cumbersome. This finding is an affirmation of Quaye (2011) who concluded a major constraint in accessing credit by Small and Medium Scale Enterprises (SMEs) in developing country are the lack of collateral securities. A key observation made was that almost all farmers who found the process to be easy had educational levels up to JHS/Middle school. It was therefore likely that they understood then process and applied for loan ahead of time. Generally, the waiting time was between 3-24 weeks. Referring to the demographic characteristics discussed earlier, only 9.7 percent of farmers had up to JHS/Middle School education and therefore find it difficult understanding the process and drafting application letters ahead of time.

For the issue of collateral securities clients were expected to have savings with the financial institution (which almost all farmers did not have prior to the loan facility), and others were required to form groups in order to access the loans while group members serve as guarantees for loans granted and are therefore liable for repayments on behalf of defaulting members. Farmers indicated that in trying to fulfill these requirements, so much time is wasted which and the credit finally come late which results in a situation where the maximum benefits are not realized. As mentioned earlier, majority of farmers (89.7 percent) indicated delay in the release of loan facilities however, the measures put in place are to hire the services of laborers on credit basis and pay them later when they receive the loan facility. The danger here is that in circumstances where laborers refuse such agreements, farming activities are brought to a halt until the loan is received which invariably impacts production negatively.

Conclusion and Recommendations

The study established that microfinance played an important role in increasing agricultural production. It was also revealed that despite the unimaginable desire for agricultural loans, actors in the area are challenged with factors such as lack of understanding of the loan acquisition process and unavailability to collateral securities. Based on the major findings of the study, the following recommendations were suggested.

MFIs should assist farmers to form active Farmer Based Organizations

From the study, it was revealed that one of the major challenges of accessing credit is the unavailability of collateral securities which is a requirement for accessing loan facility. It was also revealed that where farmers do not have physical properties and individuals to serve as guarantors, they are asked to form groups in order to access the loan facility. Forming active FBOs will therefore enhance access to credit.

This can be achieved through the following:

- Register Farmer Groups with the District Agricultural Development Unit
- Link farmer groups to the microfinance institutions and organize regular meetings for members to discuss relevant issues relating to their activities.

Encourage Farmers to Save with the Micro Finance Institutions

The study found that saving was one of the strategies employed by some microfinance service users to enable them access larger loan sizes in the future. Also, for farmers to access credit, they were required to be account owners. In this regard encouraging farmers to save will help them access credit with ease and access larger loans in order to expand their farm sizes realize the associated benefits. To encourage savings, the following specific measures are suggested: Regularly award certificates, present prizes and acknowledge the best and regular savers to motivate others to save, Payment of attractive interest rate or profit margin on savings products so that the savers can compensate for the opportunity cost of their deposits; and organize cooperative day and show role-play/theatre on the importance of saving in cooperative rather than at home or any other places.

Educate Farmers on the Loan Acquisition Process

One of the challenges identified was the delay in the release of loan facilities which was attributed to the lack of understanding of the loan acquisition process. The loan acquisition process briefly includes the application, interview, appraisal of applicant's economic activity and finally, loan disbursement. Farmers described the process as cumbersome and time wasting due to the bureaucratic nature of the process which discourages them from applying for loan facilities. It is therefore suggested that the MFI extensively educate FBOs on the process to help them better understand and apply for loans ahead of time. This will help reduce the problem of delay in release of loan facilities.

Educate Farmers on Effective Record Keeping

The Micro Finance Institutions indicated that due to lack of record keeping and ineffective record keeping where there is, farmers have often failed to pass the appraisal and where they do, they spend so much time gathering information hence, causing a delay. It is therefore necessary that the Micro Finance Institutions educate farmers on proper record keeping to help facilitate the process and enhance access to credit.

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