EXTENSION OF PRODUCTION CREDIT BY COOPERATIVES WITH
A PROGRAM FOR WEST PAKISTAN

by

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CO-OP PRODUCTION CREDIT

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ABSTRACT

The basic aim of this thesis is to make a study of the different methods of extending production credit used by cooperatives in various countries including United States, Canada, Japan, Philippines, and India; to evaluate the production credit program of cooperatives in West Pakistan and to determine the causes of its failure; then on the basis of an analysis of the experiences of the above countries in meeting the various problems they encountered in the extending of production credit, to suggest a cooperative credit program for West Pakistan which can meet the member's needs for short and medium term loans.

The cooperative program in Pakistan has been stagnant due to various socio-economic factors. The main internal factors impeding it have been low limits on the amount of credit extended to individual members, dependence on land as security, unlimited financial liability of members, small size of the societies, failure to foster thrift by the members resulting in small savings deposits, and absence of integration of credit with provision of production supplies and the marketing of members' produce.

The Raiffeisen model of small un-limited liability societies has failed in Pakistan. Therefore, organization of limited liability credit societies of adequate size to provide sufficient income to essential expenses has been recommended. However, the successful unlimited liability societies should be left to flourish and obtain the

same government financial investment as limited liability societies. Integration of three main services, namely, credit, supply, and marketing, is absolutely essential but the credit service must be segregated from marketing and supplies, and operated on sound banking principles. Marketing service should be handled on strictly commission basis and purchasing service on the pool order basis through affiliated marketing societies and provincial unions. Members need to pay cash for their production supplies, borrowing it from their credit society when necessary. Crop lien should be the primary security and credit extended on a budgeted and supervised basis in instalments. In order to qualify for a loan, a member of a credit society must also hold membership in a marketing society and contract to deliver his surplus produce to the marketing society for sale. The contract should provide for deduction of the amount of the loan and remittance to the credit society.

The primary credit society will serve as the agent of the marketing society to assemble, store when necessary, and arrange transport of members' produce to the nearest marketing society. It also should order essential production goods for the members from affiliated societies and advance them to members instead of cash, which should be advanced only for cash expenditures which farmers have to pay themselves.

The loan funds of the credit societies should be accumulated through member investment in capital by purchasing shares of stock, accumulation of reserves, and acceptance of deposits. The program should retire the initial government investment in the capital of these societies as early as possible and should aim at a member owned cooperative program. Thrift campaign for members savings and deposits should be carried out by such methods as periodic and seasonal deposit programs, chit funds, home savings schemes, and school savings projects.

Special emphasis should be placed on the education of members and a training program for directors, committee members, and the societies' staff principally through in-service training by government officers and officials of the Union of credit socieities. Members will patronize and participate more actively in their cooperatives when they understand cooperation and know about their own cooperative. Cooperatives can give superior service only when the staff is well trained and understands cooperative principles and practices.

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# INTRODUCTION

"For achieving an optimum production from agriculture, credit is to be assigned a foremost importance. Capital is said to be the life-blood of industry and it is no less important for agriculture."[1]

## Difficulties of Agricultural Credit in Pakistan

The majority of the farmers in West Pakistan are small scale producers whose average holding is 3.7 acres of cultivated land. They have generally but a small surplus left after taking care of their immediate consumption needs to meet their cash obligations to the Government, payment of interest, or the instalment of a loan already taken, some needs for consumer goods etc.

Important features characterising Pakistan Agriculture are low productivity, subsistence farming and even below subsistence level for a substantial part of the farming economy, fragmented holdings, soil salinity and water logging problem, dependence of agriculture on vagaries of nature, primitive method of cultural practices etc. The cumulative effects of these influences have caused a further decline in crop yields.

Needs for financing vary by class of producers and their ability to make use of credit to improve their economic position, kind of security they can offer etc. On the one hand there are cultivators who own or rent medium sized holdings large enough to maintain their

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1 Moquit, A., "The Problem of Agricultural Credit in Pakistan", Quarterly Journal, State Bank of Pakistan, Vol. VII, p. 1, July-September, 1959.

existing production at a moderate standard of living. Credit helps them to keep the production going or raise their level of income. They are considered to be good credit risks because they possess the means of repaying the loans and thus can satisfy requirements of the credit agencies.

But the crux of the problem is financing small scale cultivators who are in the majority and who number into millions. These are the farmers who live in a deficit economy. The subsistence nature of farming unit has resulted in poor farm management and land use and as a result, in low crop yields. Practically no savings or capital formation takes place with these marginal cultivators, many of whom go into debt whenever they suffer reduction of income from a natural calamity or have an unusually large family expense. Lacking alternative opportunity for employment and an annual increase of population between 1.5 to 2.5 percent per annum, there is increasing pressure on the land which prevents increasing the average size of unit for the subsistence farmers.

Increased production is the only solution to ameliorate their economic position. This can be achieved by either increasing the size of each production unit (an extensive approach) or increasing the yield per acre (intensive approach). The scope for the former possibility is relatively limited because of slow industrial developments in the country to provide employment for those giving up farms and the protracted process to transfer excess population from agriculture to industry. Under these circumstances, therefore, an intensive agriculture with improved methods of cultivation, copious use of fertilizer, improved irrigation and plant protection measures are the only remedies to increase yields. This is a matter of the vicious circle because to achieve this requires an application of an appropriate amount of credit.

Financing of these poor risk farmers is the real problem. These millions of farmers are scattered in hundreds and thousands of villages and many of these villages are lacking communication with the rest of the country. Overhead charges in administering, supervising and servicing such small loans will be prohibitive to any credit agency outside the village. This, added to the problems of extreme dependence of agriculture on nature, absense of crop insurance, lack of storage warehouses, commodity exchanges for holding against price fluctuations, or any guarantee of minimum income to producers, has discouraged any institutional financial agency from investing in rural agriculture. Farmers' needs for credit are not only to finance production and marketing but also for family consumption between sowing and harvesting because of inability to accumulate capital.

Evaluating the situation, the concensus of opinion is that affording credit to these farmers would be done best through co-operatives situated in the villages and operated by farmers themselves with necessary guidance by unions of co-operatives, and by Government officers.

The co-operative credit movement remains a minor source despite fifty years of existence under state sponsorship and assistance. Maximum contribution of co-operatives to the credit supplied farmers as determined by the 'Punjab Board of Economic Enquiry Report', does not exceed thirteen to fifteen percent in the relatively most well developed co-operative province of Punjab. In absolute terms, the credit extended from within the co-operative movement itself does not exceed Rs. 40 millions in West Pakistan and even this figure is not a measure of an annual flow since it includes a heavy component of overdues.[2]

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2 Credit Enquiry Commission Report, Government of Pakistan Press, Karachi, Sept. 8, 1959, p. 10.

To describe briefly, the co-operative movement in West Pakistan has been characterised by stagnation in the post partition period attributable partly to such external factors as the diversion of co-operative funds to non co-operative uses, political intervention, weakening of the co-operative departments due to exodus of trained staff after partition, frequent transfer of Registrars, poor selection of officers, and lack of Government support.

Deficiencies internal to the structure of the credit society include a low credit limit for individual borrowers, gradual shift to the security of land, unpopularity of unlimited liability, and dependence on unpaid staff.[3]

Both qualitatively and quantitatively, the movement has been stagnant. As a result of low savings and slow building of resources by the local societies, there has been too much dependence on borrowed funds for loaning purposes by the societies. The ideal of creating thrift among the village community which was one of the main ideals of the movement has failed. The result is a high rate of interest on loan funds which is channeled all the way from the State Bank of Pakistan to the local credit society on the village level. Provincial co-operative banks, the Central banks (District banks) serve as the intermediary tunnels for credit to pass through on its way to the village societies.

Another defect with the movement has been concentration on the provision of credit. Marketing of members produce and supply of goods

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3 Ibid., p. 37.

for production and consumption have been neglected. These three types of internal services were performed by the village banya (local merchant). He was an important though exploitive institution in the prepartition village economic set up who provided credit, marketed farmers produce and supplied consumption credit along with production supplies. Post partition village economy has suffered by their migration to India which reduced very greatly the amount of credit available to villagers. To fill in this gap which is otherwise also essential, the three integrated services for meeting the needs of the farmers are absolutely essential for the successful operations of co-operatives.

Objective of the Study

Evaluating the situation, the only recourse to solve the agricultural problem in Pakistan is to revive the co-operative credit structures, because it appears that only through rural agencies can credit be provided at rates farmers can afford to pay. The purposes of this thesis are, therefore:

1. To make a comparative study of production credit extended by co-operatives in some of the principal co-operatively well developed countries.

2. To evaluate the difficulties they experienced regarding the provision of production credit and loans and the measures taken by co-operatives to meet these difficulties.

3. In the light of their experiences regarding solving some of the problems similar to those in Pakistan, it is intended to correlate their solutions with the solution in Pakistan.

On this basis, ways of conducting loaning operations by the Pakistan co-operative societies will be recommended which it is believed will meet more adequately the needs of farmers for production credit to expand their output of farm products and thereby increase their incomes and provide the basis for capital accumulation and a higher plain of living.

The reason for selecting the United States and Canada for analysis of their production credit program was mainly to learn the basis for successful extension of such credit by cooperatives. Another reason was the availability of an adequate amount of literature in this field both in the University and School of Agriculture Libraries plus ability to secure by correspondence enough literature from these two countries relative to the handling of the problems encountered by cooperatives in extending production credit.

Japan was selected as an Asian country where cooperatives are relatively well developed and multi-purpose village cooperatives have operated relatively successfully over a long period of time. The Philippines were included because of integrating the credit program with marketing and supplies for assurance of repayment of loans. Indian experiences were considered to be of relatively better use because the history of its cooperative movement and the social and economic environment of villages being generally similar to those of West Pakistan.

# CHAPTER I

## COOPERATIVE CREDIT IN U.S.A.

"The credit problems of American farmers are not nearly as acute as those of farmers in many other countries of the world, particularly farmers in the Near East and the Far East. There are numerous sources of credit which farmers can utilise in securing the loans which they need to purchase their farms as well as to provide the credit for production purposes after they have acquired their farms. By all odds, the principal source of credit is still from commercial banks as well as from merchants and suppliers of farm production goods."[4]

The co-operative sources of production credit in the United States are particularly through:

1. The Co-operative Farm Credit System.
2. Several hundred limited liability rural credit unions (patterned after the Raiffeisen societies).
3. Many specialized farm supply co-operatives which extend short term accomodation to their member patrons.

Co-operative credit associations in the U.S.A. are only one of several sources which farmers in the country use for their needs for production credit. Farmers certainly are not under heavy pressure to borrow from the co-operative credit institutions because frequently

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4 Schaars, M.A., Professor of Agricultural Economics, University of Wisconsin, U.S.A., Letter, Jan. 10, 1961, p. 1.

they are in a very good position to get all the credit they need from private lending agencies and at competitive rates. Still the production credit associations which are one of the components of the 'Farm Credit Administration' system affiliated with the twelve 'Intermediate Credit Banks', together with the rural credit unions are serving an important need for farmers generally throughout the country.

Production credit associations furnish about 13% of the total amount of non real estate loans[5] (production loans for short and medium term) used by farmers in the United States. These are co-operatively organized limited liability local organizations furnishing production credit to farmers. Their exclusive function is to provide short term and medium term credit to farmers. They are part of the co-operative credit system which also includes the 'Intermediate Credit Banks', 'Federal Land Banks', 'Federal Land Bank Associations' which furnish long term real estate loans to farmers; and the 'Banks for Co-operatives' which finance co-operative marketing, purchasing and business service associations. All three groups of these banks and associations financing farmers or their co-operatives are co-operatively organized. These banks and the local credit associations are single purpose associations, i.e., they have the exclusive function of making loans.

Table 1 shows the amounts of debts owed by individual farmers and the distribution of this debt to the principal lender groups.

The data on non real estate loans provide a summary of the percentage distribution of loans by the lending agencies for production credit only.

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5 Engberg, R.C., Chief, Research and Information Division, Farm Credit Administration, Letter, Dec. 22, 1960.

TABLE 1

Amount of Loans to Farmers and Percentage of Total Held by Types of Lenders, United States, January 1, 1960 and 1959[6]

| Type of lender | January, 1960 | | January, 1959 | |
|---|---|---|---|---|
| | Amount (millions) | Percentage of total | Amount (millions | Percentage of total |
| | **Real Estate Loans** | | | |
| Federal Land Banks | 2,335 | 19 | 2,065 | 18 |
| Insurance Companies 1) | 2,821 | 23 | 2,661 | 24 |
| Commercial Banks | 1,625 | 13 | 1,512 | 14 |
| Farmers Home Administration | 437 | 4 | 300 | 3 |
| Individuals and others 1) | 5,073 | 41 | 4,628 | 41 |
| Total | 1)12,291 | 100 | 11,254 | 100 |
| | **Non Real Estate Loans** | | | |
| Production Credit Associations 2) | 1,361 | 13 | 1,115 | 12 |
| Federal Intermediate Credit Banks 3) | 90 | 1 | 84 | 1 |
| Commercial Banks 2) | 4,814 | 45 | 4,161 | 44 |
| Farmers Home Administration | 396 | 4 | 405 | 4 |
| Individuals and others | 3,900 | 37 | 3,700 | 39 |
| Total | 10,561 | 100 | 9,465 | 100 |

1) Preliminary

2) Excludes loans guaranteed by Commodity Credit Corporations.

3) Loans to and discounts for financing institutions other than P.C.A.'s only.

Source: Research and Information Division, Farm Credit Administration; U.S. Department of Agriculture.

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6 Engberg, op.cit., p. 1.

Production Credit Associations

The 495 Production Credit Associations and 12 Federal Intermediate Credit Banks comprise one of the major sources of short and intermediate term credit for farmers in the United States. Farmers borrow from their local associations to finance farm production, including such things as purchase of seeds, feeds, fertilizer, fencing materials, drainage and irrigation equipment, machinery, appliances, building repairs, feeder cattle, breeding stock and some family consumption needs.

The funds farmers borrow from their associations are obtained by the Production Credit Associations rediscounting farmers notes with and borrowing from the Federal Intermediate Credit Banks. The Credit Banks in turn obtain their funds through sales of consolidated collateral trust debentures to investors in the financial markets.[7] The services of the Federal Intermediate Credit Banks are available also to other financing institutions making loans to farmers, such as agricultural and livestock credit corporations and state and national banks.

1. Interest Costs:

The discount rates charged associations by the banks are based on and fluctuate with the rates at which their debentures are sold. "The spread between the average rates charged associations by the banks and the average rates paid on debentures outstanding was 0.27 percent in 1954, 0.47 percent in 1955 and 0.05 percent in 1956.[8]

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7 26th. Annual Report on the Work of the Co-operative Farm Credit System, 1958-59, Farm Credit Administration, Washington 25 D.C., Jan. 6, 1960, p. 27.

8 P.C.A. Members and Their Loans, Farm Credit Administration, Washington 25, D.C., Bulletin CR-8, May 1957, pp. 2-3.

The rate of interest charged by a production credit association is the rate authorized by the Federal Intermediate Credit Bank of its district plus the fees and other charges prescribed by the association subject to the approval of the bank. The discount rate which the association must pay to their Federal Intermediate Credit Bank is a major factor in establishing the interest rate which it will charge borrowers. Operating costs and the need for making provision for losses are also considered in determining the interest rate and loan service fees. The more common plan used by these associations charging service fees is a graduated schedule which calls for rates per thousand dollars of loan that decline as the amount of loan increases. The rates and schedule of service fees varies between different associations. But all borrowers from a particular association pay the same interest and the same schedule of service fees.

2. Period of Intermediate-Term-Loans Lengthened:

During the first two decades of the F.C.A. sponsored credit programme, most loans were made for not more than one year. Loans that were for capital and semi-capital purposes were extended by renewing according to the borrower situations.[9] In order to provide greater flexibility in financing intermediate credit needs, the making of loans with terms up to three years was initiated in 1955. Later the Farm Credit Act of 1956 extended the possible term to 5 years. These longer term loans call for regular repayments spread over the term for which the note is written and do not require annual renewal.

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9 Ibid., p. 4.

Since such loans are used for capital and semicapital purposes, supplementary loans with annual maturities are frequently made to cover seasonal credit needs.[10] The purposes for which the intermediate term loans are made include, to buy livestock; to purchase machinery; auto trucks and equipment ; for irrigation equipment and wells; to pay debts; to buy farm real estate; to improve farm land and buildings.[11]

3. Purposes of Loans:

Production Credit Associations make loans for any agricultural purpose , including the financing of operating expenses and capital requirements connected with crop and livestock production, living expenses and family needs, and financing of debts. Most loans are obtained for more than one purpose. Payment for current operating and living expenses, however, accounted for 81 percent of all farmer borrowings and accounted for 59 percent of the total cash advanced during the year as determined in the survey. More than 68 percent of all cash advances were for current requirements.

Capital investments accounted for nearly 18 percent of the total cash advanced. These included buying machinery 9 percent, improvements to land and buildings 3 percent, and purchasing livestock other than feeders to 6 percent.[12]

4. Security for Loans:

Basically the strength underlying every production Credit Association loan is the borrower's repayment capacity. In most cases,

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10 *Ibid.*, p. 4.
11 *Ibid.*, Table 8.
12 *Ibid.*, p. 5.

however, the association requires security in the form of mortgages on chattels or real estate, liens on growing crops or in the form of endorsers or guarantors.[13]

The practice with respect to taking security varies widely among the farm credit districts. Nevertheless, the most frequent type of security was a chattel mortgage or crop lien, or both, either alone or in combination with endorser or co-maker, or a real estate mortgage. Systemwide, such security was taken on about 85 percent of the number and 90 percent of the amount of loans.[14]

For the United States as a whole, 71 percent of the number and about 70 percent of the amount of loans were secured by chattel mortgages or crop liens only. It was recorded as high as 97 percent of the amount in St. Paul district to as low as 31 percent in Columbia district. The wide range resulted mainly from the difference in the practice of taking real estate mortgages as additional security.[15]

An endorser or co-maker alone, or a farm real estate mortgage alone,were the least common types of security taken. Only 1 percent was secured in this way.

5. Budgeted Loans:

Most loans of the production credit associations are made on the basis of a farm budget showing the production expenses and expected income from crops and livestock. The budget thus shows the revenues

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13 *Ibid.*, Table 10.
14 *Ibid.*, p. 7.
15 *Ibid.*, Table 10.

which are expected to repay the amounts borrowed for his entire season's credit needs with a budgeted loan from his production credit association. The member plans and arranges in advance for this important part of his farming business at his convenience.[16] Then he knows he will get money when he needs it in the operation of his business. He makes repayments as he sells his crops and livestock. Since only farmers and ranchers use production credit association's services, P.C.A.'s personnel are experienced in agricultural financing and are well qualified to assist farmers with their credit planning.

Besides permitting a farmer to devote his time to operate his farm without bothering with piecemeal credit arrangements, the budgeted loan saves money for the farmer. This special credit service, provided at no extra charge, permits the farmer to save time and money by paying cash for his purchases and, at the same time, reduce his interest cost because interest is charged on each dollar only for the time it is used.

6. Actual Loan Making:

A farmer's or rancher's application for a loan is acted upon by the loan committee of the production credit association, which is composed of two of the elected farmer directors and the secretary treasurer. These committees endeavor to approve loan applications only in amounts and with repayment schedules that will enable a member to accomplish the purpose for which funds are desired and to repay his loans in an orderly manner under normal conditions.

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16 26th. Annual Report, Farm Credit Administration, op.cit., p. 30.

In most instances, when the loan is closed, the association gives a farmer a check which he deposits in his account in the local bank. He can pay for his supplies or other expenses with his own check. However, some associations, especially those with large livestock loans, give the ranchers authority to issue a 'sight draft' (similar to a check) on the association to pay for livestock purchased. These sight drafts can be issued up to the amount of his budgeted loan. Interest on these loans begins when the sight draft is received by the association.[17]

Some supply co-operatives facilitate borrowing by their patrons to pay for feed, fertilizer, etc. The co-operative submits the notes given to it by the farmers to the production credit association, which advances it the amount of these notes. The farmers then have loans from the P.C.A. which they repay the same as any other. However, they have been saved the negotiating of individual loans from the P.C.A. and have the help of at least a partial guarantee of their loans by the supply co-operative.

7. <u>Farmers Repayment Record Good</u>:

As a result of issuance of loans by the credit committees of the respective P.C.A.'s for production uses only and arrangement of repayment schedules based on the sale proceeds of the farm business, and as a result of favourable production and prices since 1933, the period in which the associations have been making loans, the repayment record has been good.[18] Actual losses of the associations during their

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17 Engberg, <u>op.cit</u>., p. 1.
18 <u>26th. Report</u>, <u>op.cit</u>., F.C.A., pp. 31-32.

26 years of operations, plus provision of estimated future losses on loans outstanding on Dec. 31, 1958, amounted to 22 cents for each $100 of the $16 billion of cash advanced during the period. Most delinquencies have been due to unfavourable weather and/or low market prices for the borrower's products.

8. Farmer Owned Cooperative Credit System:

When the U.S. Farm Credit Administration loan system was established in 1933, many farm leaders wanted it to be set up as a co-operative programme owned and controlled by the farmer borrowers. However, due to the depleted financial resources of farmers resulting from the 1929 financial crisis and the need for nearly 100 percent government financing of the programme, twelve Production Credit Corporations were organized as Government institutions. They supplied most of the capital required by the local production credit associations through purchase of class A stock. In order to assure basic farmer ownership of the P.C.A., it was required that every borrower must own class B shares of stock equal to 5 percent of the amount of his loan. Since most borrowers were very short of cash, it was permitted to add the 5 percent to the principal amount borrowed. Due to the pressing need of farmers for cash, most of them repaid only the production loan and had the stock cancelled. As farm income increased during the period 1940-1955, many farmers became permanent owners of P.C.A. shares equal to 5 percent of their annual borrowing.

Since 1956, borrowers have been encouraged to repay their loans in full, including the extra 5 percent to cover the purchase of shares.

Furthermore, some supply co-operatives have purchased shares in a P.C.A. so that loans could be obtained for their members to pay for production supplies.

These measures have resulted in a large number of P.C.A.'s building up sufficient member capital to supplement the reserve accumulated from annual earnings to be able to repay the Production Credit Corporation the money it had advanced for class A shares.

A fundamental principle of the Farm Credit Administration is to encourage and develop co-operative lending institutions with farmer ownership as the ultimate objective. Very substantial progress has been made in this respect both as to the P.C.A.s and the Federal Intermediate Credit Banks which supply their loan funds. Most of the P.C.A.s have become completely farmer owned by building up members' investment in shares and accumulating reserves from earnings. The requirement that members must own shares equal to at least 5 percent of the amount they borrow has been an important stimulus to the accumulation of adequate member investment to enable the associations to meet the needs of farmers for production credit from association funds supplemented by discounting member notes with the Federal Intermediate Credit Banks. Substantial member investment is essential in order to give the investors who buy the consolidated debentures of the credit banks at low rates of interest confidence in the safety of their money. As of November 1, 1959, a total of 454 Production Credit Associations were completely member owned. Since then many more have repaid all the Government money originally advanced them by the Production Credit Corporations. On November 1, 1959, the Government capital still retained by P.C.A.s was about $4 million compared with $90 million when the programme was started in 1933.

Most production credit associations have attained a strong financial position. The P.C.A.s in operation on January 30, 1959 had a bombined net worth of $269 million on that date. Should any association find need for capital beyond the amount the members are able to supply, it can borrow its requirements from the revolving fund of the Farm Credit Administration. There is $60 million in this fund at the disposal of the Governor of the FCA. Any new group establishing a production credit association to supply the needs of its members for production loans can apply to him for an advance from this fund to invest in its class A stock to enable it to qualify to discount member's notes with the Federal Intermediate Credit Bank serving the area.

Pursuant to Farm Credit Act of 1956, Production Credit Associations started on January 1, 1957 to acquire ownership of the Federal Intermediate Credit Banks. Up to June 30, 1959, P.C.A.s had purchased $13,112,000 of class B stock of these banks. They are also acquiring additional capital stock as the banks pay their patronage refunds out of earnings. Such additional capital stock ownership by these associations amounted to $ 7.4 million by June 30, 1959.[19]

Government capital in the Federal Intermediate Credit Banks will all be retired over a period of years as capital and reserves are built out of purchases of capital stock by P.C.A.s and accumulation of earnings retained by the banks. When all Government capital has been retired, all capital stock of the banks will be owned by P.C.A.s In this way, the members of the local P.C.A.s will become the ultimate owners of the agencies supplying their needs for production credit on a cooperative basis

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19 The Cooperative Farm Credit System, Circular 36A, Farm Credit Administration, Washington 25, D.C., p. 9.

under their democratic control.

Appraisal of the Production Credit Associations:

The co-operative credit system in the United States encountered the following types of problems in the early years of its development. The discussion has been substantiated by some comments made by Professor Marvin A. Schaars of the University of Wisconsin who is a leading authority on the subject.[20]

Types of Problems Experienced in the Past and Their Solutions:

The production credit system sponsored by the Farm Credit Administration was designed to meet, among others, the following problems of credit societies.

1. Insufficient funds for extension of credit or loans to members.
2. Inadequate security for repayment of loans or credit.
3. Delinquencies due to unfavorable weather and market situations.

1. Insufficient Funds for Extension of Loans:

The historical background for setting up production credit associations was the great depression of 1929 and the early thirties when large numbers of commercial banks went bankrupt and were obliged to liquidate their assets by calling back their loans. This forced the farmers to sell livestock and crops at very low prices which resulted in a tremendous economic set back. Merchant credit, also dwindled because

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20 Schaars, op.cit., p. 2.

of the inability of banks to renew their loans to business concerns. There was thus no source left to provide farmers with adequate amounts of production credit. Recognizing this serious deficiency, the federal government assisted farmers by establishing production credit corporations under the Farm Credit Act of 1933, to foster the development of local production credit associations to advance short term loans for crop and livestock production.

a. Governmental Capital Supplied:

Recognizing the farmer's inability to invest at that time, the "federal government made a plan to assist the farmers to help themselves. Under this program, the government furnished capital for a Production Credit Corporation in each of the twelve Farm Credit Districts, which in turn would supply the original capital, help organize, and give supervision to local production credit associations organized by farmers. Every borrower would purchase stock and become a part owner of his local association."[21]

A revolving capital fund of $120,000,000 was authorised to set up and finance the 12 production credit corporations. Each P.C.C. was to have $7,500,00 and was empowered to finance and supervise local production credit associations which would borrow from intermediate credit banks. "P.C.C.'s were not to lend direct to farmers but to provide each P.C.A. with capital not less than $5,000 but up to 20 percent of the volume of loans. Such capital was represented by non-voting class A stock preferred as to assets and sharing equally with class B stock in

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21 Arnold, C.R., "Farmers Build Their Own Production Credit System", Farm Credit Administration, Circular E-45, Washington 25 D.C., August 1958, pp. 16-17.

dividends. Each borrower, on the other hand, was required to take and keep 5 percent of his loan in class B stock. Class A stock may be sold to investors in the community. The local P.C.A. was required to build up a guarantee fund to at least 25percent of the paid-in capital before payment of dividends."[22] The members were encouraged to repay the investments made by the production credit corporation in the local P.C.A.s.

The system of financing worked out very successfully through the members' investments in the capital stock of their associations. Most of the P.C.A.s are now member owned and most of the Government capital has been retired. From these retired funds, the government has made available $60 million of revolving capital to the Governor of the Farm Credit Administration to invest in A and C classes of stock of any association in need of capital resources.

b. Borrowing in Central Money Markets:

P.C.A.s make loans to their members from their own capital and reserve funds. They offer the promissory notes of borrowers to the intermediate credit bank serving the area for discount. The bank buys all the P.C.A. endorsed members notes which it considers will probably be repaid on schedule. The intermediate credit banks borrow whatever money they need for this purpose from investors in the central money markets. In this way, P.C.A.s are able to obtain as much money for reloaning to members as the intermediate credit banks consider will be repaid them.

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22 Ibid., p. 17.

2. Inadequate Security for Repayment of Loans:

At the time of the establishment of the P.C.A.s a major difficulty in extending production loans was the security problem. The general security for most of the loans accepted by the commercial banks and other credit institutions was the tangible security of land, usually in the form of a mortgage. Because of the loss of equity ownership in the land by many farmers after the 1929 depression and the declining value of land and farm products, even land security became inadequate even for mortage loans. Besides, young farmers who went into the ownership of newly acquired land had already pledged their land for long term loans which left them with no other tangible security to obtain loans for production. Therefore the P.C.A.s had to have some other kind of security for their loans.

a. Chattel Mortgages and Crop Liens:

The newly set up P.C.A.s introduced the two very convenient types of security of chattel mortgages and crop liens which worked out very successfully and set the pace for the commercial banks and other institutional credit sources as acceptable security for production loans. Now a majority of the production loans extended by the credit agencies are on chattel mortgages and crop liens which together account for 71 percent of such loans in the U.S.A., as mentioned earlier.

It should be pointed out that P.C.A.s have had additional security for many of their loans over and above chattel mortgages or crop liens in "the form of the increasing equity of farmers in their land due to the rising land values for about 25 years since the P.C.A.

system was established. Since three-fourths of the farmers have practically no mortgage debt, the security for the P.C.A. loan in the form of chattel mortgages, crop liens, cosigners on paper, etc. has presented no real problem as the farmer's equity in his land provided ample collateral."[23]

3. Delinquencies:

The problem of delinquency in repaying P.C.A. loans has been very small due to limiting the amount loaned to borrowers relative to their ability to repay from sales of products.

a. The loans extended are adjusted to the total production needs of the farmer for an entire year rather than to individual loan needs as they arise, as was done years ago. These are called 'budgeted loans', which provide for an entire season's credit. In a bad crop season, the period of the loan and repayment is extended. In this way farmers are financed for continuing their production operations even after a crop failure so that almost all loans are eventually paid in full.

b. A loan application to the P.C.A. is acted upon by a loan committee consisting of two farmer directors and the secretary treasurer. They do not grant loans in excess of the borrowers ability to repay.

c. Furthermore, the P.C.A.s have operated largely during a period of rising farm prices and this has helped the repayments record to be remarkably good. In 26 years of operation, losses have accounted to only 22 cents out of each $100 of the $16 billion of cash advanced.[24]

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23 Schaars, op.cit., p. 2.
24 Ibid., p. 2.

4. Other Difficulties:

a. In the early period after their establishment, the associations faced the problem of attracting a large volume of business in order to lower the unit costs of operating a credit society. They solved this difficulty by extending the area served by each association. Two or more P.C.A.s were merged so that the number of borrowers per association increased to where the interest and inspection fees more than covered annual operating expenses.

b. Other measures for soliciting patronage were principally of an educational nature (meetings of members, field service calls on individual farmers, publicity materials, radio broadcasting, etc., to point out to members and potential members the services of the cooperatives.[25] Members of federal farm loan associations, marketing and purchasing cooperatives, were invited to borrow their production credit needs from the P.C.A. serving the area.

Factors Responsible for Success of Production Credit Associations

On the basis of his observation of the operation of production credit associations over a period of many years, Dr. Marvin A. Schaars[26] considers the following factors contribute to their successful operation.

1. The cooperative credit associations extended loans on competitive interest rates and thus attracted substantial numbers of borrower members.

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25 Ibid., p. 3.
26 Ibid., p. 2.

2. Working with farmers on farm production programmes (advising, counselling and suggesting good farm management practices) enabled borrowers to use their loans profitably.

3. "Budgeted loans" related to planned production programsso that the loans were not in excess of sales returns and a regular payment schedule was worked out in relation to the sale proceeds of the farm business in advance of granting the loan.

4. Employing capable managers, field service men, and qualified office personnel who evaluated the business and production capacity of farmer members and adjusted the loans accordingly.

5. Associations operated in sufficiently large economic units to keep operating costs at a minimum.

6. Regular audit of accounts, adequate reporting to members, good annual meetings, and conducting the association in line with good cooperative principles and practices.

Factors Responsible for Membership Support

Dr. Schaars attributes the widespread support of P.C.A.s by the members to the following factors.[27]

1. Keeping members well informed through the following media:

   a. Annual meetings where members gather and receive reports on the work of their P.C.A.

   b. Printed annual financial statements available to all members.

2. Having numerous members serving on county membership committees, boards of directors and special committees.

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27 Ibid., p. 3.

3. Member investment in class 'A' and 'B' stock of the association.

4. Active solicitation of business by the association through personal calls at the farm, radio and newspaper advertising etc.

Extent to which the Credit Cooperatives Meet the Farmer's Requirements for Production Credit

The production credit provided by the P.C.A.s accounts for 13 percent of the total amount used by farmers in the U.S.A., as reported earlier. This is not because cooperatives are not able to meet the requirements of the farmers but because they are able to get credit at many other sources at just as low a cost as at the coops. P.C.A.s and credit unions will get more farmer patronage as a result of the more aggressive solicitation program they are following.

In the opinion of Professor Schaars, credit cooperatives are prepared to meet the full credit needs of deserving farmers. Through access to the central money markets by way of the intermediate credit banks, they can secure whatever amount of money is needed to make loans to applicants who demonstrate ability to repay what they borrow.

## PRODUCTION LOANS BY SUPPLY COOPERATIVES

The second important source of production credit supplied by cooperatives is through many specialised local and regional supply cooperatives. "These supply cooperatives may be ones which sell petroleum plus feed, seed, fertilizer, hardware, insecticides, household appliances and farm machinery. More specifically, the method of extending credit would tend to vary by products. Petroleum, feed, seed and hardware tend to be provided to farmers on open account credit more often than farm machinery or fertilizer.[28]

"Credit needs of farmers have increased greatly in the last two decades in the U.S.A. Technological advancements in agriculture and mechanization on the farm have added to the cost of farming. These advances, while contributing to the production efficiency, requre the use of more and more cash, or its equivalent in credit. This greater need for credit is reflected in rising amounts of accounts receivable on the books of many farm supply cooperatives."[29]

Although credit is available to most farmers through P.C.A.s, the'Farmers Home Administration', local banks and other lending agencies, these institutions have not eliminated the demand for store or open account credit.

### Preference for Open Account Credit:

There are numerous reasons why many farmers buy on open account rather than borrow from a lending agency and pay cash.

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28 Koller, E.F., Professor of Agricultural Economics, University of Minnesota, Letter of Jan. 24, 1961, p. 1.

29 Bailey, J.M., Pursell, A.H. and Engberg, R.E., "How Cooperatives Use Credit Agencies to Meet Patron Needs", Farm Cooperative Service, U.S.A., General Report 52, Dec. 1958, p. 1.

1. Some farmers prefer open account credit because they look upon it as credit without an interest charge.

2. Some prefer it because of its convenience and its lack of 'red tape', as compared with submitting financial statements or signing notes or mortgages required by the specialised credit agencies.

3. "Credit also became a matter of convenience. When the farmers purchased only a few supplies occaionally, he picked them up when he went to town for groceries and paid cash for them. With larger purchases usually delivered to the farm, it was often not convenient to pay cash.

"When the goods were delivered, the farmer might be away from home or he might be in the field. If merchandise could be left, this saved considerable time for the delivery men and mailing a check becomes much more convenient for a farmer."[30]

Farm supply cooperatives have generally tried to limit open account credit to an accomodation period, such as 30 days. Frequently, though, they have extended even beyond 60 days. This has sometimes tied up the coop's operating capital which is needed for other purposes.

Aging of Accounts Receivable:

Collecting accounts as they became due has long been a difficult problem for cooperatives. If they are not collected on schedule it becomes increasingly difficult to collect them without loss. A study of 52 supply cooperatives was carried out by the University of

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30 Robins, C.B., and Rickey, L.F., "Controlling Open Account Credit in Feed Cooperatives", Farmer Cooperative Service, U.S.D.A., Circular 24, September 1957, pp. 1-2.

Minnesota in 1959-60 to determine their credit practices.[31] A rising trend in the aging of accounts receivable was observed as under in Table 2.

TABLE 2

Comparison of the Age of Accounts Receivable of 17 Farm Supply Co-operatives in Minnesota, 1950-1959

| Year | Under 30 days | 30 days to 6 months | 6 months to one year | Over one year |
|---|---|---|---|---|
| | | Percent of Total | | |
| 1950 | 47.3 | 41.8 | 5.7 | 5.2 |
| 1959 | 32.8 | 46.8 | 10.4 | 10.0 |

The authors give no clear explanation for the higher percentages of the older accounts but one factor appears to be the failure of managers of smaller purchasing cooperatives to make collections as accounts fell due. It was also evident that in 1959 the payment of more accounts was postponed until after crops were harvested and sold. This suggests that members were prevailing on their cooperatives to allow them longer term open account credit for fertilizer and other crop production expenses than was customary a decade earlier. If cooperatives find they can extend this type of seasonal production

31 Amann, V.F., and Kohler, E.F., "Credit Problems in Farm Supply Cooperatives", Minnesota Farm Business Notes, University of Minnesota, November 1960, p. 2.

credit without serious losses, the question will arise as to whether it is more economical and convenient for the farmer than borrowing from a lending agency and paying cash for his production supplies.

Credit Extension and Collection:

It was observed in the Minnesota Survey by Amann and Koller that the credit policy was generally determined by the board of directors. Extension of credit and enforcement of credit policy was the manager's responsibility. Most associations authorised truck driver-salesmen a specified limit to the amount of credit to be allowed individual patrons.

A farmer's capacity to pay based on his past record and his present payment ability, was the main qualification for receiving credit. Manager's interview with the customer, enquiring with the local merchants and bankers, credit bureaus, and contact with the petroleum supplier, to verify the credit record of the customer were the other factors for deciding the qualification of the applicant to receive credit.

"Financial responsibility for credit losses was placed on the manager in 15 cases and on the truck drivers in 6 cases. This was done by withholding a certain percentage of the latter's monthly commissions as a reserve for losses. At the end of the year, the doubtful accounts were charged off against the reserve and turned over to the employee and became his property for collection.[32]

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32 Amann and Koller, op.cit., p. 2.

Purchasing cooperatives in Minnesota had various programs for controlling accounts receivable and fostering payment thereof, as found by Amann and Koller.

1. "In 29 associations a cash discount was allowed on bills paid within 30 days.

2. In 6 associations, 2 percent interest was paid on money deposited with the association to prepay the bill.

3. In 21 associations, an 8 percent interest charge was made against an account outstanding more than 30 or 90 days.

4. Other practices included sending out statements, using attorneys, etc. Personal call by the manager was stated most effective for collection of accounts receivable."[33]

<u>How Supply Cooperatives Use Lending Agencies to Meet Patrons Needs for Production Credit</u>:

Open account credit, being the most important method by which supply cooperatives provide production credit to their members, presents the problem of difficulty in collecting outstanding accounts on time. The problems of delinquency and losses from uncollectable accounts are serious from the standpoint of tying up capital, absorbing time and energy of the manager, and draining funds away from the operating capital of the cooperatives.

The Minnesota study by Amann and Koller showed 1.5 percent of accounts to be complete losses. When the gross margin of the cooperative

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33 *Ibid.*, p. 2.

is about 10 percent of sales, a loss of this size (15 percent) is serious and adds substantially to the costs borne by the members who pay their bills. Moreover a large amount of operating capital was tied up. Consequently managers try to encourage patrons to borrow from different available credit agencies. They do this in various ways.

1. Borrowing and Discounting Patron's Notes:

With a variety of financial sources available, a supply cooperative can use some of its own working capital, or obtain funds from farmers, banks for cooperatives and commercial banks to finance the delivery of supplies to members on credit. Patrons time purchases can also be financed through the facility of P.C.A.'s, credit unions and commercial banks by discounting member's notes. Federal intermediate credit banks assist in such financing by discounting farmer's notes for eligible lending agencies. These arrangements are of particular significance to local farm supply cooperatives because they offer alternative methods of channelling much of their open-account credit to specialized credit agencies.

2. Assist Farmers to Obtain Loans:

Local supply cooperatives may arrange with particular agencies to make loans to their members to pay for specific production supplies. The following are examples of such arrangements.

a. Some local supply cooperatives make it possible for the farmer to borrow directly from the regional supply cooperative. The farmer makes his purchase at the local cooperative and the local will discount the note it receives from the farmer with the regional cooperative.

b. Certain cooperatives that enter into production and marketing contracts with their members also may arrange for P.C.A.s to provide credit to these members for particular production expenses. The contract provides that the P.C.A., as the local lending agency, will pay loan proceeds to the cooperative to cover the cost of baby chicks, feed and medications furnished by the cooperative to the producer up to an agreed maximum amount for any individual producer. The cooperative then obtains from the producer his signed note and a chattel mortgage in favour of the P.C.A.

Then the cooperative advances supplies to the producer as needed during the producing period. Finally, the producer repays the loan from the proceeds of egg sales. The cooperative will guarantee the P.C.A. against loss up to 10 percent of the maximum amount of individual notes for production loans.[34]

3. Prepayment by Patrons:

Some cooperatives encourage farmers to prepay their supply purchases. Under this plan 2 percent interest is usually paid the farmer on the prepaid funds. This two percent is credited to the farmer's total deposit. For example, if a farmer deposits $100, his account will pay for the purchase of $102 worth of products.[35]

4. Contract with P.C.A. for Loans to Members:

A new method of financing being tried by many of the supply

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34 Bailey, Pursell, and Engberg, op.cit., p. 3.
35 Koller, op.cit., p. 2.

cooperatives is entering into a contract with the P.C.A. to make loans to patrons to pay for their purchases of supplies. Two general plans are being tried under these arrangements, under which the P.C.A. is protected against serious losses by either a guarantee or a special reserve provided by the supply cooperative.

a. Guarantee Plan:

Here the P.C.A. agrees to accept all loans below some agreed size and for an agreed total amount. The maximum amount varies but generally ranges between $400 and $1000. The P.C.A. is guaranteed against loss on such loans by the cooperative. Larger loans are handled as individual lines of credit and must be acted upon individually by the P.C.A. loan committee. The larger loans may or may not have the cooperative guarantee, depending upon the specific arrangements made.

b. Reserve Plan:

It is synonimous to the guarantee plan except that the cooperative does not guarantee the loan. Instead, it establishes a special reserve fund for an amount the cooperative and P.C.A. agree upon. The amount of reserve is a percent of the total amount of the loans handled. The rate is usually 5 percent. If there are losses in excess of this reserve, they will be born by the P.C.A.[36]

After the loan is made, the P.C.A. services it and the borrowers make principal and interest payments direct to the P.C.A. The supply cooperative shares some responsibility for the loans made under both

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36 Ibid., p. 4.

the guarantee and reserve plans. In both plans, the cooperative assists in the purchase of the required amount of B stock in the P.C.A. by its patrons.

With these arrangements, patrons who need credit can arrange for it at the time they buy their supplies, avoiding a separate trip to a P.C.A. or a bank. The necessary papers can be signed and other arrangements made with little or no more inconvenience than if the cooperative itself were furnishing the credit. The cooperative, in turn, does not have to tie up funds in accounts receivable that can be used much more effectively in more useful operations. Furthermore, it puts credit servicing in the hands of experienced people.

5. Loans by Cooperative Sponsored Credit Corporations:

Credit corporations are organized and supervised generally by the regional sales and marketing cooperatives. Some of these corporations serve the members directly by obtaining funds through rediscounting of farmers notes or borrowing from the intermediate credit bank, or other agencies. Some of these associations finance only cooperative members by funds borrowed from banks or cooperatives. The rate of interest in either case is sufficiently high to cover the cost of borrowed funds plus operating expenses and reserves.[37]

Relationships Between Supply Cooperatives and P.C.A.s:

P.C.A.s are themselves farmer cooperatives, As such they are especially interested in adapting their credit services to the needs

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37 Ibid., p. 6.

of patrons of other farmer cooperatives. Various P.C.A.s enter into different arrangements with supply cooperatives according to local needs and preferences.

On the other hand, many local farm supply cooperatives have employed a variety of methods to acquaint their members with P.C.A. credit so that they will borrow in order to pay cash for supplies. In an extensive examination of credit control practices of local supply cooperatives in various areas of the U.S.A., conducted by Farmers Cooperative Service of the U.S. Department of Agriculture, they found the cooperatives used the following methods for encouraging farmers to make greater use of the local P.C.A.

1. Cooperatives acquainted patrons with P.C.A. services.

2. Cooperatives arranged appointments for patrons and P.C.A. representatives.

3. P.C.A. representative, upon request, reviewed the cooperative's accounts receivables for the names of potential borrowers.

4. Cooperatives arranged to have P.C.A. representatives take some part at annual meetings, or at least attend them to get recognition.

5. Cooperatives and P.C.A.s jointly sponsored advertisements in local newspapers emphasizing the complementary services of each.[38]

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38 Bailey, Pursell, and Engberg, <u>op.cit</u>., p. 3.

## FINANCING BY RURAL CREDIT UNIONS

The third important cooperative source of production credit in the United States is several hundred rural credit unions (patterned after Raiffeisen societies).[39] "These unions are savings and lending institutions, organized and operated for the mutual benefit of their members. Their objective is twofold:

1. To promote thrift among members.

2. To mobilize rural savings and thereby provide a steady source of credit for members who need to borrow.

There were a total of 575 rural credit unions serving 150,000 members in January 1959.[40]

Many credit unions have been sponsored by supply and marketing cooperatives. Assets of these unions range from a few thousand to a few million dollars.

The type of credit services provided by these unions varies from one to another. For example, the Poultry Producers Federal Credit Unions, San Leandro, California, serves farmer-members and employees of the Poultry Producers of Central California. This credit union makes loans to members to finance purchases of feed, supplies and equipment. The credit union secures its loan funds from:

1. Savings of members.

2. Deposits by cooperatives.

3. Loans from local banks.

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39 Schaars, op.cit., p. 2. (farmer cooperative credit societies)
40 Pursell, A.H., Using Your Rural Credit Union, Farmers Cooperative Service, U.S.D.A., Washington, D.C., Educational Circular 16, Sept. 1959, p. 1.

4. Members notes rediscounted by the Federal Intermediate Credit Bank of Berkeley, California.[41]

Another type of service performed by credit unions is to have its fieldmen assist members work out a production plan and budget for their farmers before the start of the crop year. On the basis of this budget, planned for the whole season with the assistance of the fieldman, the union approves the loan.

Advantages and Limitations of Credit Union Financing:

There are several ways in which rural credit unions fit into the program for financing farmers production credit.

1. The credit union is flexible in operation and adaptable to the varying patron credit needs of the sponsoring farmer cooperatives.

2. Close working relationships with sponsoring organizations provide opportunity for increased membership and patronage for both organizations.

The main limitation of credit unions is the difficulty of raising a substantial amount of capital within a short period of time after its organization. However, in many states credit unions can borrow money from the State Central Credit Union, local cooperatives, and other sources.[42]

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41 Bailley, Pursell and Engberg, op.cit., p. 7.
42 Ibid., p. 8.

PRODUCTION LOANS BY MULTI-PURPOSE COOPERATIVES

Production loans also are supplied by some cooperatives which perform several functions such as supplying production requirements like seed, feed, fertilizer, petroleum products, marketing and other types of services to the members. In the credit phase of their activities, such cooperatives have the usual problems of any other type of agency which sells supplies on credit. More recently, integration of functions has further emphasized combining approved production practices with obtaining the supplies and services modern farmers need and then with marketing the products farmers grow. These integrated operations performed by cooperatives under farmers' control on through the marketing channels necessitate provision of more capital, assumption of various kinds of risks. They often make it possible for the cooperative to employ more competent management, etc. as the result of the larger total volume of business.

To analyse the impacts of integration of various services in one cooperative on credit problems, the Farm Credit Administration made a few studies of centralized and local cooperatives operating on this basis. "The first association selected for the study was the Central Carolina Farmers Exchange, Durham, North Carolina, commonly known as "CCFE". The services performed by the association are divided into three broad classes:

1. Provision of farm supplies.

2. Marketing of farm products.

3. Furnishing farm business services.[43]

The association has a good record of business performance. Initially the association was started as a typical local farm supply cooperative. It now includes a wide variety of marketing and related business activities.

A. Highlights of Operations:

CCFE was started in 1930 to purchase and process farm supplies to reduce the cost of production and to promote and develop markets for poultry, eggs, livestock, milk, grain and seed in order to increase farm income of the members. It was organized initially with subscribed members' capital of $2,400 and a supplemental loan of $10,000 extended by a bank at Durham, N.C., with 400 farmer members.

"Since organization, total assets have reached $3.9 million, net worth provided by farmers has increased to $3 million, yearly volume of business of marketing and purchasing stood at nearly $18 million in 1957."[44] In addition, a number of farm services such as livestock slaughtering and meat processing, trucking and bulk delivery of feed also are provided. Membership in 1957 was 13,000, which included a large portion of the farmers in the Pierce county area in which it functions. The association has built 8 service stores, a processing plant for broilers, and facilities for marketing eggs (commercial and hatchery), livestock, grain and seeds. In addition, there are expanded and developed production supply services. These include

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43 Abrahamsen, M.A., and Engberg, R.C., "Integrated and Related Operations, Central Carolina Farmers Exchange", Farmers Cooperative Service, U.S.D.A., Washington, D.C., General Report 44, June, 1953, p. 1.

44 Ibid., p. 7.

manufacturing feed, hatching chicks, distributing fertilizers, insecticides, seeds, and adding general farm supplies and appliances. Moreover, it provides credit to farmers and assumes many production and marketing risks.

B. Integration of Enterprises within One Cooperative:

Broilers:

The degree of integration varies by enterprise. A great degree characterizes the broiler enterprise which is almost completely integrated. It provides chicks, feed, poultry supplies, and supervision under "Growing Agreements" to some 350 selected growers. The terms of the contract provide that producers obtain chicks from the cooperative's hatchery, and feed through its mill. Moreover, the feed service program provides visits once a week by an association poultry expert and coordinates production with processing and marketing requirements.

a. Credit and Contract Provisions:

Since 1937, growers have pressed for credit sales for supplies rather than cash, which was the prior practice. Initially the members were charged $2 more a ton for feed and $1 more per 100 chicks than those who paid cash. This extra charge covered risks, financing costs, and the additional supervision necessary for the credit plan. In 1952 and 1953, other feed manufacturers and their dealers began to offer farmers contracts under which they paid growers 5 cents a head or $50 a thousand to produce broilers. The feed dealer furnished medicine and marketed the birds. In effect, they guaranteed the growers against loss.

In 1953, the Exchange tried a 50-50 basis of risk sharing which proved unattractive under unfavourable broiler prices. In 1956, the association worked out an incentive payment plan whereby an increased payment was guaranteed to producers who achieved more efficient conversion of feed into meat. As the producer reduced the cost of production per pound of meat, his payment per bird increased on the following basis:

| Cost of production per pound | Payment per head | Payment per pound of meat sold |
|---|---|---|
| 20 cents and over | 4 cents | 0 |
| 19 to 19.99 | 5 cents | 1.5 cents |
| 18 to 18.99 | 6 cents | 1.8 cents |
| 17 to 17.99 | 7 cents | 2.1 cents |
| 16 to 16.99 | 8 cents | 2.5 cents |

The cost of production was determined for this agreement by taking all the cumulative costs of baby chicks, feed, medicines and sanitation supplies furnished by the association, which was divided by the total number of pounds of broilers sold. The growers are paid on the per head basis, or the per pound basis, whichever gives them the greater return.

b. <u>Cost of Financing</u>:

Growers financed on this basis pay $ 8-10 more a ton for feed and $3 more per 100 chicks than those who buy on a cash basis.[45] This gives enough margin to the association to cover the price of feed,

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45 Difference between this charge and the original $ 2-3 charge is to take care of the greater losses under the new program during periods of low broiler prices.

chicks and supplies and the sale of the broilers to cover the actual cost of these items sold to the growers plus the incentive payment and losses, which have become frequent due to low market prices for broilers. The association at all times, though, encourages cash payment for supplies. It also gives volume discounts to the members purchasing larger amounts at one time but only when payment is made immediately.

3. Measures to Avoid Losses:

The association's gains are carried to a reserve fund and losses to the association are charged to this fund. An important problem associated with this programme is the pricing of feed and chicks plus the incentive payment and the usual patronage refund to the growers to make the contract more attractive in contrast to those offered by competitors. The special broiler operation reserve fund is kept on a relatively even keel, with a minimum of long range average losses to be absorbed by the total operations. Other safeguards for avoiding losses include careful selection of growers. The main qualifications are honesty and dependability, plus ownership of appropriate facilities and resources for efficient production, and a good record as a producer.

Growers are required to sign a contract to market their poultry through the exchange. For high quality production, they must obtain all their supplies and have the whole operation supervised during the entire period of production by the association to minimize the risk of losses from poor management practices.

2. Chick Hatchery:

To get quality chicks for broilers, the CCFE has set up its own hatchery. It now provides chicks for laying flocks as well as for broilers.

The eggs the cooperative hatches for growing commercial laying flocks are purchased from specialised breeders. For the hatchery eggs for broiler chicks, the coop pays a premium price about that for eggs for consumption ranging from 30 to 40 cents a dozen.

a. Growers Charged for Credit:

About one third of the hatchery flocks are financed by CCFE and the flock owner pays for the chicks and feed for 8 weeks. After that the cooperative finances feed, medication, and other supplies. When the birds begin producing hatching eggs in about 6 months time, the exchange uses 85 percent of the sale proceeds from the eggs to cover the accumulated charges for feed and other expenses of the programme. These growers pay 6 percent on outstanding balances and 5 cents a hundred pounds more for feed than do strictly cash buyers.

b. Financing Commercial Egg Production:

Producers of table eggs also are financed under contracts. The association furnishes feed, laying type chicks and supervision, and markets their eggs under the "Farm Fresh" brand. When the pullets begin producing eggs at 5-6 months, the total cost is about $1.75 a bird. The association applies 85 percent of the egg proceeds toward paying the grower's account to which current purchases offered and supplies are charged. This practice usually pays for the hen in 14 months. On their accounts, growers pay 6 percent on outstanding balances and 5 cents more for each 100 lbs. of feed than the growers who pay cash strictly. Under a written agreement, financed growers must market their eggs through the exchange.

4. Financing Livestock Production Supplies:

A partial integration is carried out for livestock production. The Exchange furnishes the growers with production supplies and equipment on a basis similar to that for broiler production. The cooperative also tried pig feeding on an experimental basis.

For the dairy farmers, the association provides 60 percent of their feed and dairy equipment and the use of bulk milk cooling tanks. The Exchange does not, however, market its members' dairy products. Besides, the association also buys grain for its feed mill from its members but does not finance any of the feed grain producers. However, it does furnish many farm management aids to encourage the use of certified or pedigreed seeds and approved production practices.

C. Financial Appraisal of the Associations:

Problem of Credit Control:

The association was not facing any serious financial difficulty in financing its broiler and egg programs. But since the accounts receivable amounted to $900,000 according to the 1957 audit report, it was recommended that the association employ a credit manager.

2. Financing Contract Production Advantageous:

"Cooperatives generally have resisted financing credit sales, including the type required in integration. The experience of CCFE, however, suggests that when proper safeguards are taken the cooperative may finance growers producing broilers and eggs under contract to the advantage of its patrons and without excessive risks. There are several reasons why at least short time risks appear limited."[46]

3. Safe Financing:

First, since the members are required to market all their broilers through the association, it can control the sale of the birds and is in a position to deduct from the farmer's proceeds the amounts required to meet his obligation.

Second, even though the growers are owners of chicks, and buy the feed and supplies, the association's contract enables it to influence quantity and quality and this adds to the safety of financing.

Moreover, the selected growers are carefully screened for suitable facilities, resources, and experience before acceptance. Under such circumstances, the cooperative has definite advantages in granting credit.

"Several methods of financing credit sales are open to cooperatives. Some have organized their own credit corporations which take over the credit function. In some cases this separate agency is a credit union. In either case, the financing agency may obtain funds by rediscounting producer's notes with a federal intermediate credit bank or by borrowing from commercial banks. Under certain conditions, it may also borrow from a bank for cooperatives. Another approach is

46 Abrahamsen and Engberg, op.cit., p. 29.

to work out arrangements with a production credit association or a local bank for furnishing needed credit directly to patrons."[47]

But in certain cases, none of the above mentioned arrangements seem desirable as in the case of CCFE. In that case, if the cooperative has enough members, equity and a standing credit with a bank for cooperatives or a commercial bank, it may decide to finance producers directly. This may be done in two ways. Chicks, feed and other supplies may be sold to the grower on credit, in the manner followed by CCFE. Such credits are carried as accounts receivable.

On the other hand if the cooperative retains the title to the chicks grown, the grower becomes merely a custodian and no credit is extended to the grower in the real sense. "The advances by the cooperative for chicks, feed and other supplies, represent expense outlays or investments rather than credits, and therefore must be carried in that manner rather than as accounts receivable."[48]

The experience of CCFE suggests that where a multipurpose cooperative undertakes to finance the producer through advancing him production supplies or credit, under a contract which requires him to market through the association, this operation should be recognized as a separate service to members and given as much skilled attention as any other enterprise. It should be organized as a separate department with a competent credit manager in charge. When organized in this manner and when production and marketing are supervised and controlled effectively under contracts, such a service can be provided members and farmers with perhaps even less risk than some other types of operations.

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47 Ibid., p. 30.
48 Ibid., p. 30.

## CHAPTER II

## COOPERATIVE CREDIT IN CANADA

Cooperative credit in Canada for all purposes, including production credit, is mainly provided through credit unions. There are also numerous retail cooperatives which sell commodities such as feed and fertilizer, petroleum products, building supplies, farm implements, food stuffs, etc., on a credit basis.

The open account credit by supply cooperatives presents problems in collecting outstanding accounts similar to those of the United States. Cooperative pruchasing associations place restrictions on the amount of credit sales to each individual member, and on the length of time before payment. But there appears to be a need for other credit services to some kinds of patrons who need credit for periods up to one year, or even two years, particularly in communities depending on irregular agricultural income for their existence, like Saskatchewan province, for instance. Therefore, an attempt is made to encourage members to secure their credit needs through credit unions or through chartered banks.[49]

Since the credit unions are the principal source of production credit supplied by cooperatives in Canada, a brief evaluation of their operations in Saskatchewan province is made in order to analyse the basis of their success with regard to their loaning operations.

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49 Turner, H.A., The Control and the Cost of Customer Credit, Department of Agriculture, Regina, Saskatchewan, Bulletin No. 95-E, 1943, p. 46.

Credit Unions in Saskatchewan:

A credit union, or "caisse populaire", is a cooperative society organised for the purpose of promoting thrift amongst its members and creating for them a source of credit for provident or productive purposes. In addition, it educates the members in matters of finance and mutual help.

To accomplish these objectives, the members agree to save by purchasing from time to time shares valued at five dollars each, and to pay for them either in a lump sum or in instalments. Savings may also be in the form of deposits. From the above capital subscriptions and these savings deposits, loans are advanced to members only at a rate of interest which is determined by the board of directors only, and which may not in any case exceed one percent per month on unpaid balances.[50]

A. Organization Procedures

The union can be organized by any ten persons of a group having a common bond of occupation, association or living within a well defined community, either rural or urban. Cooperative associations may be members with a right to one vote as a member at the annual meeting. Credit unions in Saskatchewan have been organized by rural community groups, including farmers and village residents, with the members belonging to different professional occupations.

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50 Credit Unions, Department of Cooperation and Cooperative Development, Regina, Saskatchewan, Canada, 1958, p. 3.

The organization of a union is preceded by a thorough study of literature and study courses which are supplied by the University of Saskatchewan, and the cooperative union of the province. Assistance is also provided by the field staffs of the Department of Cooperation and Cooperative Development and the credit union league, as well as by officers of public relations federations and district representatives of the wheat pool. After the studies on the part of the probable members and leaders, an application is submitted to the Registrar of Credit Unions, Department of Cooperation, Regina. If the representations made are satisfactory and the organization appears economically feasible, the preliminary application is approved by the Registrar.

Among the main factors determining the feasibility of the organization of a credit union are:

1. A group well informed regarding the principles and practices of such a society.

2. A strong demand for credit union services.

3. Availability of a capable treasurer with a suitable place for business.

4. Incorporators and prospective officials willing to accept their full share of responsibility for a community effort of this type.

A representative of the department attends the organization meeting after incorporation. Subsequently, careful instructions are given to the officials regarding the details of operations and duties of the various committees are fully explained and discussed. A number of the inspection staff of the department visits the union within six months after incorporation to render assistance in various technicalities of operation.

B. Membership:

For eligibility to membership, a person must belong to the group the union serves, and must be elected by the board of directors. A membership fee of twenty five cents is usually charged to each member. Each member agrees to save systematically and regularly from his income, monthly, seasonal or other regular basis, rather than stipulated monthly deposit. However, many credit unions operating in rural areas have adopted a systematic plan of savings based on a percentage of income derived from sale proceeds of grain, livestock and dairy products. The regular, systematic saving on a seasonal basis is the very essence of cooperative thrift and the foundation of the credit union. This has proven true in Jordan, Indonesia, and other countries in addition to Canada.

The credit union legislation provides that ninety days and thirty days notice is required to withdraw shares and deposits respectively and fifteen days notice required by the chartered bank for withdrawal of all or any portion of money deposited in the savings department. But in practice, the money can be withdrawn on demand. Because of this practice, maintenance of cash liquidity becomes very essential. Each union is thus required to maintain a cash reserve of at least ten percent of its liabilities to its members in respect of shares and deposits. The other provision kept for liquidity is that the union cannot loan more than twenty percent of the resources of a credit union in long term real estate loans.

C. <u>Management</u>:

Management of the union is carried out jointly by an elected five member board of directors, a credit committee of three members appointed by the board of directors and a supervisory committee of three, one of whom is appointed by the board of directors and the other two elected by the members. Their various responsibilities are set forth in the by-laws. The three way administrative system by committees is one of the reasons for the success of the credit unions. The treasurer is a salaried manager. No official except the treasurer and his assistant receives a salary.

D. <u>Operation</u>:

The funds of a credit union are usually deposited in the Saskatchewan Cooperative Credit Society or in a chartered bank. Loans may be made up to $200 without security, or in the case of credit unions with resources in excess of $200,000, loans up to $400 can be made without security. Assignment of shares or deposits may be taken as security as well as a co-signer or endorser. The liability of members is limited to the unpaid amount of the shares subscribed for in writing.

The revenue of a credit union is derived primarily from the interest collected on loans made to members. There is also revenue derived from investments, such as government bonds, shares and deposits in the Saskatchewan Cooperative Credit Society, shares and guaranteed investment certificates, of the Cooperative Trust Company, as well as from other sources. The net earnings of the union, after paying all expenses, including interest, is presented at the annual meeting for apportionment. The Credit Union Act provides that there be set aside as a reserve fund against uncollectable loans and probable future losses, all entrance fees, fines collected from members, and at the end of each fiscal year, at least twenty percent of the net earnings. This is done from year to year until such reserve fund is equal to at least ten percent of the assets of the credit union from time to time.[51]

The act also specifies that a dividend of not more than five percent be paid to the members annually on all fully paid up shares, and that five percent of the net earnings be reserved for educational purposes.

E. <u>Savings</u>:

Savings may be put in a credit union in two forms, namely share capital or deposits. The share capital savings are of more permanent type. Farmer members are encouraged to adopt the habit of saving a portion of their income from the sale proceeds of their farm produce, including livestock and livestock products. Many unions provide life insurance for all members with the amount proportioned to each member's savings as well as covering his loans. This provides an incentive to the members to build up their share capital and borrow against it when in need of temporary credit rather than withdraw their savings.

F. <u>Loans by Credit Unions</u>:

Loans are granted for provident or productive purpose. A provident purpose includes loans for the payment of educational expenses,

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51 <u>Ibid</u>., p. 9.

medical bills etc. A productive purpose is one which will leave the borrower better off economically or will assist him in earning his income.

The character of the appliant, his ability to repay and the security offered are the factors which determine the granting of the loans. In the case of a farmer, terms of repayment are generally arranged according to his seasonal income, such as sale proceeds of grain, livestock and dairy products.

1. Purpose of Loans:

Besides, providing for emergencies, one of the main purposes of the loans is to make the members cash buyers of goods and services. One test of the usefulness of the loan service is to determine whether the cash cost of an article plus the credit union interest charge is less than the instalment purchase or credit price of the same article.

The purposes for which loans are made by a typical rural community credit union include loan payments, buildings and improvements, farm machinery and repairs, purchase of livestock, consolidation of debts, operating expenses, other farming expenses, endowment contracts, living expenses, (food, clothing etc.). A credit union is designated thus primarily to meet the needs of the members for short-term or seasonal credit.

2. Meeting Credit Needs of Farmers:

The twenty two years of progress made by the credit unions in Saskatchewan Province has shown that they can meet all the legitimate short term credit needs of the farmers. In the agricultural section of the economy, credit for farmers has been recognized as essential, in one form or another. Therefore, a credit agency has to be provided to the community which can carry the burden of providing credit. Otherwise, farmers are forced by circumstances to buy necessities from merchants at high time prices which cover the costs and losses involved in this type of book credit. In order to avoid the high cost of merchandise credit, and to secure substantial economic and social benefits for themselves, farmers are advised to form their credit unions and to obtain credit at cost. Thus is credit provided by those who use it with the aid of other thrifty members of the rural community. This is one of the significant contributions made by the credit union movement.

Credit Unions and the Cooperative Movement:

Where supply cooperatives have adopted a policy of unrestricted credit, the outcome almost invariably has resulted in financial difficulties. Combination of merchandise and credit on the same counter has shown alarming consequences in Canadian experience, as well as in other countries. The following suggestions have been made based on the observations and experiences of many Canadian cooperative associations in finding a solution to the credit problems.[52]

A. Shifting the Provision of Credit:

"There is a decided shift from credit by trading associations to credit through local credit unions since the unions are especially designed to handle credit problems."[53]

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52 Ibid., p. 15.
53 Ibid., p. 15.

B. Manager's Position:

The manager of a supply cooperative should not be called upon to differentiate between member patrons as to who should or who should not receive credit. His function is to merchandise. The presence of a local credit union tends to consolidate the patronage of the cooperative association by eliminating the problem of credit from the customer relationship. All members buy for cash at the same price on an equitable basis.

In most cases, besides, the manager does not make a thorough analysis to determine whether the patron is considered a good credit risk and consequently the cooperative takes losses that never should have been suffered.

C. Members Buy for Cash:

A member can pay cash to the cooperative for purchasing supplies by making arrangements with his credit union beforehand. This is the soundest method of buying when a farmer does not have sufficient cash resources to pay for whatever he needs. Some credit union members now have arrangements for the issuing of withdrawal vouchers against their deposit account to cover payment for goods and supplies purchased through their supply cooperative.

D. Financing Credit Needs:

It is difficult for a supply cooperative to find a manager who can balance credit needs of individual members and salesmanship of goods and services. A credit union enables the people to educate themselves in methods of financing their credit needs independent of the fortunes of management of the business cooperative. By assembling their individual savings in a cooperative loan fund in their local community, they mobilize their money and thereby minimize the amount which it is necessary to borrow from outside. Some communities accumulate surpluses which can be loaned to other groups needing funds to expand output and income.

E. Credit Unions Serve Dual Purposes:

1. Loans to Cooperative Members:

Experience in Canada also indicates conclusively that credit is expensive, and generally speaking, the business cooperatives are not designed to carry on a credit service. This is function of credit agencies, such as banks, loan companies, financial institutions, and credit unions. These organizations are designed to provide credit, and are better equipped to handle it on an efficient, low cost basis, with minimum losses from uncollectable loans.

Thus, the policy advocated in Saskatchewan is for members of supply cooperatives to pay cash for their purchases and to borrow any needed funds from credit unions.

2. Loans to Supply Cooperatives:

A credit union may also give a supply cooperative independent financing to some extent since the credit union act allows a cooperative association to become a member of a local credit union. Cooperative associations may also join the Saskatchewan Cooperative Credit Society and the Cooperative Trust Company. This enables supply cooperatives to obtain loans so that they can buy for cash at all times and thus make further savings for their members while maintaining a satisfactory financial and credit relation with wholesalers and others.

The Saskatchewan Cooperative Credit Society:

The Saskatchewan Cooperative Credit Society, Limited, is a federation of both credit unions and cooperative associations and functions as a central credit union (or bank) for its corporate members. It acts as a depository for the funds of its members and enables them to borrow to meet their requirements. The society reallocates the surplus funds of certain unions with surplus deposits to the legitimate demands of others which need more funds for loaning their members. It thus keeps the members' funds productively employed. It is empowered to rediscount the notes given to a union by its members and function generally as a central credit institution for all its associated members.

By virtue of the provisions of the Cooperative Guarantee Act, the provincial credit union is empowered to apply for government guarantees in respect to portions of certain loans it makes to cooperative associations and credit unions. "The act specifies that the maximum liability of the Saskatchewan treasury on account of guarantees given to the society shall not at any time exceed $1,000,000."[54] This makes it easier for the society to obtain funds from lending agencies and investors at lower rates of interest than would otherwise be possible. By a further amendment of this act in 1958, "the guarantee portion shall not, except with the approval of lieutenant governor in council, exceed

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54 Credit Union Guarantee Act of 1953, Province of Saskatchewan, Regina, R.S.S. 1953, p. 3455.

fifty percent of the loan."[55]

"The society offers a service to its member organizations in the field of administering redemption or sinking funds. Credit society serial certificates bearing interest at 4 percent are issued to all organizations depositing funds with the society for this purpose."[56]

Inspection, Supervision and Auditing of Credit Unions in Saskatchewan:

The Department of Cooperation, through its Credit Union Service Branch, is required to inspect each credit union at least annually and to provide a general advisory and supervisory service. The credit union act also provides that any credit union with resources of $100,000 or more may, if the members desire, appoint an auditor to conduct an annual audit with report to the members accordingly. Any credit union with resources of $200,000 or more shall be required to appoint an auditor. The purpose is to encourage the credit unions that have sufficient income, to appoint auditors as an additional safeguard and to make this a mandatory requirement for each credit union with resources above a certaih minimum. In this way, the larger credit unions help to provide themselves with services designed to protect the interests of their members, thus supplementing the services provided by the government supervisory section.

Problems Encountered in Cooperative Credit and Their Solution:

The cooperative credit movement in Saskathcewan encountered

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55 Credit union act amendment, March 18, 1958, p. 1.
56 Credit Unions, op.cit., p. 21.

several types of problems in its successive stages of development. The ways of meeting these problems successfully has been amply substantiated by some of the comments made by Mr. B. N. Arnason, Deputy Minister and Registrar, Province of Saskatchewan, Canada, who has had wide experience in the field and who is at present providing leadership in the provincial cooperative program of Saskatchewan.[57]

A. Shortage of Funds:

The basis of establishing credit unions was the inadequate funds possessed by farmers to finance their production expenses. Credit unions were the cooperative agencies, organized to promote thrift and pool the savings of community groups with the aim to provide an adequate amount of production credit to the farmer members.

B. Cooperatives Mobilize Capital:

In the early periods of their establishments, credit unions face the problem of inadequate funds to loan their members, as was experienced by the P.C.A.s in the United States. The credit unions in Canada obtain funds through the following measures.

1. Foster Capital Investment in Shares:

Members agree to save and purchase from time to time shares valued at 5 dollars each, and pay for them either in a lump sum or in instalments. In many cases, members are required to invest in share capital a certain percentage of the sales proceeds of their farm products.

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57 Arnason, B.N., Deputy Minister, Department of Cooperation and Cooperative Development, Regina, Saskatchewan, Letter, March 17, 1961.

2. Thrift and Saving Programme for Deposits:

Credit unions provide very convenient banking facilities for the farm community and receive their surplus incomes in saving deposit accounts. By a process of education, farm family members are stimulated to practice thrift. Thus, regular systematic saving on a seasonal basis is the very essence of the cooperative credit program of the unions. A substantial part of each member's savings is deposited in his union and this is available when he or other members may have need for funds.

3. Interchange of Surplus, Savings through Provincial Credit Society:

Saskatchewan Cooperative Credit Society serves as a central bank for its corporate member unions. The society is a federation of both credit unions and cooperative associations. The concentrated funds in the society are profitably utilized by loaning them to the unions and associations which need additional funds. The member union or association can rediscount their members' notes with the provincial union and thus draw loanable funds for them. The existence of such a central credit association serves a dual purpose. Credit unions and cooperative associations can keep their surplus funds profitably invested through the society and receive interest on money which would otherwise remain idle. On the other hand, unions and associations with a scarcity of loanable funds are accomodated by borrowing from the society on the collateral of their members' notes. In this way, there takes place an interchange of surplus savings between the credit unions.

4. Limited Government Guarantee to the Credit Society on Loans:

The surplus amounts deposited with the central cooperative credit society are secured to the limit set by law on the government guarantee of loans by the society to member associations and credit unions.

C. Delinquencies in Repayment of Loans:

As in other countries, delinquencies have been a problem with the credit unions in Saskatchewan. There are two principal reasons for delinquencies.

a. Crop failure due to weather and insects.

b. Restricted delivery quotas for wheat.

The following measures have been adopted by the credit unions to safeguard against delinquencies and to maintain their solvent liquid position.

1. Central Reserve Fund:

In order to maintain the solvent position of individual credit unions, the unions have jointly sponsored a central reserve fund in the Saskatchewan Cooperative Credit Society, to which they contribute 5 percent of their annual net earnings. Credit unions in financial difficulties can draw upon this reserve and safeguard the members equity interests in their unions. This reserve fund enables such unions to meet requests for withdrawals during periods when borrowers are unable to repay due to forces beyond their control.

2. Adjusted Terms of Repayment:

The Cooperative Department of Saskatchewan in its inspection program draws to the attention of officials of credit unions the need to press delinquents to settle their loan obligations. Delinquencies which are due to crop failure or restricted delivery quotas on wheat often result in terms of repayment adjusted to their incomes. Also in their normal loaning operations, care is taken to loan the amounts to the members according to their repayment capacities and the repayments are scheduled from the sale proceeds of their grain, livestock, and dairy products.

D. Credit Control by Supply Cooperatives:

Similar to the problem of supply cooperatives in the United States, the Canadian experience also corroborates the view that where cooperative associations have adopted a policy of unrestricted credit, it has increasingly resulted in financial difficulties. Thus, supply co-ops have found it necessary to adopt measures to limit the amount of credit extended to individual patrons and to secure payment of money due.

1. Managers Job is Merchandising:

In Saskatchewan, they also have found that it is generally beyond the scope of a cooperative manager to differentiate between credit-worthy and non-credit-worthy members. His function is primarily to merchandise the supplies handled for members. The presence of a local credit union tends to consolidate the patrons of a cooperative association by eliminating the problem of credit from the trading relationship. Members pay cash for their supplies and those who need credit, borrow from the credit union.

2. Cash Trading Policy:

Leaders of marketing and purchasing cooperatives have sponsored many credit unions in order to:

a. Encourage their members to borrow from credit unions and pay cash for their supplies.

The business cooperatives make arrangements with the credit unions to pay directly to them for the purchases members make, against charge slips transmitted to credit unions which have granted loans to the members.

b. Assure productive utilisation of their loans.

The farmer receives a minimum of cash from his credit union loan. All the supplies and services he obtains from cooperatives are advanced to him and charged to his loan account in the union. This minimizes the possibility of directing loans to non-productive uses.

Factors that Contribute to Success of Cooperative Credit Program:

The following factors have contributed to the success of the cooperative credit program in the Province of Saskatchewan, according to the analysis of Mr. B. N. Arnason, Deputy minister of the Department of Cooperation and Cooperative Development.

A. Make Loans from Available Funds:

1. Loan Members Savings:

One of the important factors contributing to the success of credit unions in Saskatchewan is the extension of loans to the members mainly from accumulated funds, primarily desposits and share capital.

Credit unions, therefore, in the early stages start with short term production loans only. Gradually they extend intermediate term loans when their deposits have increased and they have sufficiently built up their resources. Some of the financially stronger unions also provide loans for the purchase of land, but for their sound working and to maintain their liquidity, they are restricted by law, to lending not more than 20 percent of their deposits in long term loans. Thus, the cooperative credit program grows primarily from its own resources with but incidental outside funds.

2. Encourage Thrift and Savings:

The encouragement of savings by coop members and their deposit in credit unions, plus investment in shares in these unions, has served to mobilize rural savings into the cooperative credit program. Farmers have come to recognize that agriculture has to rely mainly on their own savings for meeting farmers' needs for production credit, that only limited funds can be borrowed from urban centers through the credit union.

3. Pooling Savings through Central Credit Society:

The existence of a central provincial pool of savings, through the Saskatchewan Cooperative Credit Society, has added to the financial strength and services of the credit unions. From this co-op bank, surplus funds deposited by some societies are made available to those credit unions and business cooperatives that need additional funds for meeting the needs of their members.

B. Good Management of Credit:

Extension of credit has to be handled carefully if the legitimate needs of farmers are to be met and losses are to be avoided. Trained and experienced personnel are required. Thus Saskatchewan business cooperatives that extend credit to members employ such specialized personnel as well as credit unions.

1. Limited Accomodation Credit by Supply Cooperatives:

Supply cooperatives in Saskatchewan generally have adopted the policy of cash trading, but in many, the members still demand accomodation credit for 30 days. Most of these cooperatives encourage their members to pay cash for their supplies and to borrow from the local credit union when they need money to pay for their purchases. To safeguard against losses due to uncollectable accounts, the managers of supply cooperatives generally are required to have special training in the extension and control of credit.

2. Most Production Credit Supplied by Credit Unions:

As the result of the Saskatchewan program of encouraging business coóperatives to follow the cash trading policy, much of the production credit supplied to their members is obtained from credit unions. These are specialized credit agencies that are well qualified to handle the extension of credit successfully. They can do a more effective job of screening applications to avoid granting loans that will become delinquent, and of securing repayment of loans not paid on schedule.

3. Careful Extension of Loans by Credit Unions:

Loan applications received by credit unions are processed carefully. Credit committee members are trained to differentiate between credit worthy and non-credit-worthy members. The treasurers of credit unions receive careful training in appraising loan applications so that they can point out significant facts to the loan committee regarding the prospects for repayment of loans, if granted. Consequently, the losses from uncollectable loans suffered by credit unions in Saskatchewan have been negligible.

C. Members Education:

The education program regarding cooperation and credit carried on by various agencies in Saskatchewan has been an important factor in the success of cooperative credit program. It has lead to members generally understanding cooperation and how cooperatives operate so that members recognize the importance of their cooperatives adhering to sound loaning practices, as well as the importance of the thrift program encouraged by cooperatives generally. Members of supply co-operatives have voted to adopt the cash trading policy as a result of the education program.

In the opinion of Mr. B.N. Arnason, perhaps the most important factor responsible for the success of the program is the tradition of cooperative self help in the province of Saskatchewan which has lead to greater cooperative growth in proportion to population than in any other province in Canada.[58] Through the education program this tradition has been utilized to develop member support for the various kinds of cooperatives offering services to farmers.

D. Supervision and Auditing:

An important factor supporting the member education program regarding the safety of depositing savings and investing in shares of

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58 Arnason, op.cit., p. 4.

credit unions has been the government inspection and supervision of credit unions. This has been a vital factor in the fine record of no member losses. Periodic auditing of accounts has fostered honesty on the part of credit union and coop employees. These things build member confidence in their cooperatives.

E. Advice, Guidance, and Training:

The field service advisors of the Department of Cooperation and Cooperative Development, plus the fieldmen for the federations of business cooperatives and the Credit Union League, have guided the leaders, officials, and staff of cooperatives in the proper handling of the business of their organizations. Training programs for personnel have helped them to perform their work more efficiently and effectively. Appraisal of the factors contributing to the success of the cooperative credit program in Saskatchewan gives an important place to the guidance, advice, and training which have been furnished the societies by both the government and the federations and unions of cooperatives.

CHAPTER III

# PRODUCTION CREDIT BY AGRICULTURAL COOPERATIVE ASSOCIATIONS IN JAPAN

There are at least three things in common to be found, without an exception, in any rural village of Japan: the village hall, a school, and an agricultural cooperative association. The agricultural cooperative association is an organization upon which the farmer's economy leans.[59]

## Types of Agricultural Cooperatives:

General policy favored the establishment of one general purpose cooperative in each village or town which would combine the four services of credit, marketing, purchasing, and processing. Yet the farm people are permitted to form any other type they wish, according to the law. Numerous cooperatives have been formed to market special products such as fruits, eggs, milk, etc. or to process sweet potatoes into starch, fruit into jam etc. Therefore, the agricultural cooperatives of today are classified into two categories: General purpose cooperatives and specialized cooperatives. These cooperatives are further classified into two types: Capital stock cooperatives, and non-stock cooperatives, both with limited liability.

## General Purpose of Agricultural Cooperative Associations:

There are 12,400 general purpose cooperatives in Japan which

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59 Ashikaza, T., Agricultural Cooperative Associations in Japan, Agriculture, Forestry and Fisheries Productivity Conference, Tokyo, Japan, Agricultural Development Series No. 6, July 1959, p.5.

are the most common type. These are organized with capital stock and limited financial liability for the members. Because most farmers in Japan are not specialized, the general purpose village cooperative associations occupy the predominant position in the Japanese agricultural cooperative system. This is different from America and Europe where the production of agricultural commodities for market is often specialized in definite areas so that more of their cooperatives market particular products.

The general purpose agricultural cooperatives are established under the guidance of the Ministry of Agriculture and Forestry in accordance with the provisions of the Agricultural Cooperative Associations Law of 1947 when a group applies for such assistance. They have advantages in that their organizational structure includes almost all the farming population, and on the management side, they can utilize for financing their business services part of the savings deposits that are made by the farmers. On the other hand, they have shortcomings in that they are organized mainly for rice and wheat raising farmers and not for farmers producing speciality products, such as fruits and vegetables, milk, and poultry products. Farmer members cannot be sure their savings deposits are fully protected, and because several departments are operated under a single management, it is difficult to operate all departments efficiently.[60]

These unit cooperatives, both general purpose and special purpose, are federated into prefectural and then national federations,

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60 Ashikaga, op.cit., p. 37.

forming a three stage systematic organization, mutually binding, with the membership systematized vertically and horizontally. A general purpose cooperative in a village or town participates in several federations on the prefectural level at the same time. Through these federationsthey are indirectly affiliated automatically with corresponding national federations.

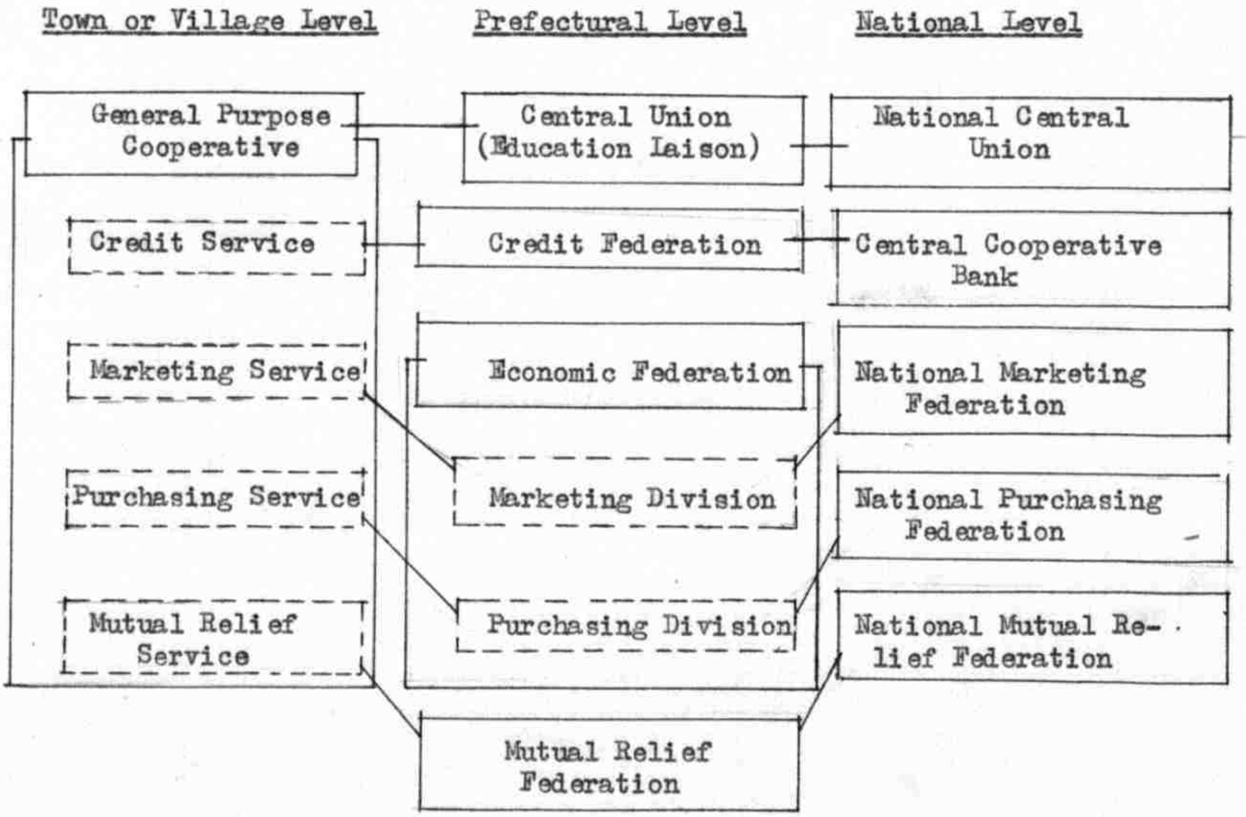
National Setup of Cooperative Organizations in Japan:

The cooperative structure in Japan is organized from the bottom up, that is, with local cooperatives at the base of the organization pyramid and the national federations at the top. Local cooperatives are members of area, and prefectural federations, which in turn are members of the national federations. Each federation is controlled by its members to assure democratic control of the cooperative structure by farmers. This organizational structure is shown in Figure 1 below.

FIGURE 1

Organization of Farmer Cooperatives

in Japan




As indicated in Figure 1, village general purpose cooperatives usually are members of three prefectural level federationsin order to obtain needed services. Credit federations according to the Cooperative Law, can perform only banking and loaning services. The prefectural economic federations provide both marketing and purchasing services, for the local general purpose cooperatives. The mutual relief service of the local cooperatives is related to the prefectural federation which furnishes crop and livestock insurance.

At the national level, there is a nation-wide federation for performing each of the major services required by lower level cooperatives and federations in the fields of credit, education and laison, marketing, purchasing and insurance. This is in accordance with the Cooperative Law which limits a national federation to the performance of a single major function. These federations are controlled democratically by the representatives of the organizations comprising their memberships.

Prefectural Economic Federations:

After the second world war, federations of general purpose economic services were divided into marketing and purchasing federation working independently. These federations are united again into one economic federation at the prefectural level, in order to improve the service rendered to local general purpose cooperatives. The economic federations market mostly rice and wheat for the local cooperatives. They provide wholesale service for both farm production supplies and staple consumer goods, including staple food stuffs, clothing and household supplies.

National Federations:

The credit federations of the 46 prefectures are all members of the Central Cooperative Bank, which serves as their national federation and their channel for securing funds from the National Bank of Japan. The National Marketing Federation handles mostly rice and wheat and serves as the laison for cooperatives with the staple foods program for the government. The National Purchasing Federation buys both household and farm production supplies on a nation-wide scale.

The National Federation of Agricultural Purchasing Cooperative Association, not only deals in farm supplies but owns other facilities like rubber factories, feedstuff factories, and invests capital in other enterprises, such as the manufacture of agricultural chemicals and household medicine, in order to assure supplies of these items of the kinds preferred by farmers. Besides, the National Federation has close ties with some of the fertilizer manufacturers and other industries through which it purchases with an agreement to put cooperative trade marks on the packages. The cooperative members are psychologically encouraged through the "Buy from cooperatives" campaign to buy and use goods that carry their co-op trade mark, which is now a great factor for boosting the purchasing service of agricultural cooperatives.[61]

Of the varieties of items handled by cooperatives, the principal item is chemical fertilizer which amounts to 39 percent of the total volume of commodities handled by the general purpose cooperatives. The prefectural economic federations and the National Purchasing Federation also handle large amounts of chemical fertilizer.

There are several reasons why fertilizer occupies such an important place in the purchasing business of cooperatives. One is the decontrol of fertilizer in 1950 and the ensuing adoption and popularization of the unconditional consignment system and the pooling system under full utilization by the cooperatives.

The attestation system and the agricultural note system have also facilitated the supply of fertilizer to farmer members who do not have to make cash payment until their crops are marketed.

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61 Morita, op.cit., pp. 62-63.

Purchasing Activities of Agricultural Cooperatives:

Purchasing business is one of the most important functions of the local agricultural cooperatives. These multipurpose cooperatives supply farmer members with commodities of good quality at reasonable prices, thereby contributing to lower cost of production and improvement in their standard of living. It also checks excessive profits by monopolistic enterprises and profiteering by local merchants.

According to a survey made by the Ministry of Agriculture and Forestry, it can be said in general that prices of single chemical element fertilizer and feedstuffs charged by the cooperatives are about the same or a little higher than the prices charged by the private dealers, while for mixed fertilizer, urea, and mixed feeds, cooperatives prices are lower than merchants. Some cooperatives pay patronage refunds which serve to reduce the net cost of supplies to the members.

Some local cooperatives have combined special services and technical guidance in the use of fertilizer, testing soils, and servicing agricultural machines. But these latter services are provided by only a few associations. Annual fees paid by members cover only part of the cost of the technical guidance service so that most of the balance has to be paid by the purchasing department.

Financing Farmers' Purchases:

Most of the seeds, fertilizers, agricultural chemicals, and farm machines and tools are purchased by agricultural producers through local cooperatives. But the farmer's financial position is not always sufficient to pay cash for all the purchases they want to make. In such cases, there are two ways in which a cooperative responds to the farmers' needs:

1. Members are allowed to charge items and settle their accounts after marketing their products, usually selling through the cooperative.

2. Loans made to members upon adequate security by the credit department. Members are required to borrow when the amount of credit they need is substantial and the time of repayment will be after a number of months, as for fertilizer for which payment is made when the crops produced with it are sold.

Farmers can borrow at lower interest rates on Agricultural Bills secured by their anticipated delivery of rice to their general purpose cooperative for marketing. Under the Japan Foodstuff Control System, each farmer legally can sell his rice only through the marketing agency he has designated. Thus, he can pledge the anticipated payment for his rice crop as security for a loan up to the stipulated percentage of the value of his crop. The credit department of each general purpose cooperative is authorized to issue an Agricultural Bill, (special form of promissory note) against this special collateral.

1. <u>Agricultural Bills</u>:

These bills enable the cooperative to obtain funds needed by their members through the following steps:

a. The association issues a promissory note to the prefectural credit federation, using the farmer's Agricultural Bills as collateral.

b. The prefectural credit federation discounts the note at the Central Cooperative Bank For Agriculture and Forestry.

c. When necessary, the C.C.B. offers the note and supporting Bills as security to obtain loans from the Bank of Japan.

For loans secured by Agricultural Bills, farmers pay their local cooperative, 3 percent higher rate of interest than the discount rate of the Bank of Japan. Each intervening agency takes 1 percent to cover its handling expenses.

2. Ordinary Loans:

Farmers who need to borrow more money to pay for production supplies than they can secure under the Agricultural Bill System have to pay higher rates of interest. This is because when their cooperative borrows from the prefectural credit federation on ordinary security the interest rate is higher due to the higher rate the federation has to pay for its funds. The national program of promoting thrift uses higher interest paid on savings deposits to encourage such deposits. Consequently, the credit federation has to pay higher rates to attract deposits from the cooperatives and federations and to borrow from the Central Cooperative Bank.

Members pledge their savings deposits in the local cooperative as security for repayment loans. Often the interest they pay when they borrow for 6-9 months is less, or no more than the interest they earn by having their savings on deposit all through the year. Members generally market their staple products through their cooperative and can pledge these anticipated sales proceeds to assure payment of loans.

Problems  Co-op Credit and Their Solution:

The problems experienced by local general purpose cooperatives in Japan since World War II in extending production credit to farmers and the ways in which these difficulties have been met are worth examining for ideas that might contribute to improving and strengthening the cooperative credit program in Pakistan.

1. Inability to Repay Deposits to Members:

During the spring of 1950, over 200 local general purpose cooperatives were forced to suspend re-payment of deposits which members needed to withdraw. This situation threatened to undermine the confidence of members so that special measures had to be taken. The reasons for inability of these cooperatives to return the money requested by members was explained to members; officers of local cooperatives were advised to collect as much as possible of over-due loans and to sell inventories of supplies in co-op stores to secure the money needed by members for planting their crops.

The basic cause of the difficulty was that inexperienced new directors of many local general purpose cooperatives had used money deposited by members following sale of their crops to buy substantial quantities of various goods that had previously been in short supply. They expected that the members would buy these goods during the winter so that there would be cash in the treasury when the members needed their money for paying production expenses in the spring. But the members bought better quality goods at lower prices from the merchants and the stocks of co-op goods remained on the shelves. There was little cash in the treasury of the co-op for returning deposits to members upon request.

This situation caused the Agricultural Cooperative Section of the Ministry of Cooperatives to have the Minister issue a Government Ordinance setting forth the amounts of capital which members should invest in their cooperatives and regulating the use of money deposited in the credit divisions of general purpose cooperatives. These regulations were designed to:

1. Induce members to invest the capital needed by their cooperative to pay for its facilities and carry on the business services performed for members.

2. Severely limit the amount of the money deposited by members in the credit division of general purpose cooperatives which could be used to finance the economic services desired by members so that the credit division could make loans requested by members and repay deposits upon demand.

Accordingly, the Ordinance[62] stipulated the standards that must be observed in fund raising and in the use of funds by the general purpose cooperatives. The main points of this ordinance are as follows:

1. The amount of capital paid in by members shall exceed the total amount of the association's fixed assets plus the amount subscribed to the capital of other agricultural cooperative organizations.

2. The division of funds between credit business and other business services, shall be clearly defined and the amount that can be transferred from the credit division to economic undertakings is limited to not more than 20 percent of the total of ordinary savings and fixed term deposits.

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62 Ashikaga, <u>op.cit.</u>, p. 46.

3. A fixed amount of savings deposits is to be set aside as a reserve for refunding deposits withdrawn by members.

4. A standard is provided to govern the amounts of loans that can be made by individual cooperatives and the prefectural credit federation.

5. A limitation is set on the uses which can be made of surplus funds.

Local cooperatives which adhered to these regulations greatly improved their financial position and ability to extend credit and loans to members within a few years. By the end of 1953, the amount of the paid-in capital of local general purpose cooperatives had more than doubled. Deposits, and particularly fixed term deposits for longer than 1 year had increased very substantially so that the total loan funds of these cooperatives were greatly expanded. In terms of total funds, the amount used in the non-credit divisions of the multi-purpose cooperatives was about 12 percent, on the average, at the end of 1958.[63] At that time, a Japanese agricultural economist calculated that about 80 percent of all the funds borrowed by farmers were supplied by their accumulated savings deposited and invested in general purpose cooperatives and in the postal savings system. Farmers indirectly regained the use of their postal savings deposits through the Central Cooperative Bank.

2. Inadequate Investment in Cooperatives by members:

As indicated in the preceding section, one of the big reasons

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63 Ashikaga, op.cit., p. 48.

why general purpose cooperatives faced difficulties in meeting requests for withdrawal of the deposits in the spring of 1950 was that a large part of the money on deposit in the credit division was being used to finance the business operations of the cooperatives. Money was being diverted from the credit service because the cooperatives did not have sufficient paid-in share capital to cover their investment in facilities needed for the marketing, purchasing, processing, and other business services and supply the operating capital for these services.

This problem was met in two ways. The ordinance prescribing financial regulations for cooperatives already mentioned, required them to have sufficient paid-in member capital to cover the investment in facilities and the usual operating capital needed to carry on the business services. This standard for member financing of cooperatives provided the basis for an intensive educational and capital investment campaign carried on jointly by the cooperative section of the Ministry of Agriculture, the federations, and local cooperatives. This campaign resulted in the remarkable growth in member investment in cooperatives mentioned in the previous section.

Some local cooperatives followed an additional plan for stimulating members to increase their investment in shares and their deposits in the credit division. They provided in their rules regarding loans to members that the amount any member could borrow should not exceed a stated number of times the amount of his share holdings and his deposits. The more he wanted to borrow, the more money he was required to have in his coop. Over a decade, the cooperatives gradually reduced the multiples of share holdings and deposits toward a limit of 10 times the sum of a member's investment and deposits. Thus, members who wanted to borrow, were induced to invest in more shares of capital stock and to increase their savings deposited in cooperatives.

3. <u>Inadequate Loan Funds</u>:

Most cooperatives in Japan perennially are unable to meet all the requests of members for loans, particularly intermediate and long term loans to expand production, due to shortage of loan funds. Commercial banks have such a keen demand from commerce and industry for loans that they rarely make loans to farmers. For the same reason, it is very difficult for the Central Cooperative Bank to obtain funds except from the Bank of Japan, and then in rather limited amounts.

To meet this difficulty, cooperatives and federations in Japan, have prevailed upon the government to establish special programs for loans to farmers for intermediate and long term loans with the applications handled by cooperatives. General purpose cooperatives, usually limit their loans to short term (generally less than one year) and to intermediate terms of two or three years. Pursuant to the regulations in the ordinance issued by the Ministry of Agriculture, the amount that can be loaned for longer than one year is limited to the amount of long term deposits and special reserves of the cooperatives for such purposes. This has stimulated the cooperatives to encourage members to make long term deposits and to build up reserves in order to meet more of the requests for intermediate term loans for financing the purchase of farm machinery, and land improvements.

Some credit federations have arranged with the prefectural government to deposit a substantial part of the taxes collected in the spring in these federations. This money can be loaned to farmers for 6 months to help finance crop production and then withdrawn by the government to pay its expenses the latter part of the year.

The inability of cooperatives to borrow from sources outside the cooperative movement sufficient amounts to supplement their own funds to meet the needs of their members has given continuing stimulus to the campaigns for building member investment in their cooperatives and increasing their deposits therein. Japanese farmers place major reliance upon capital accumulation in agriculture to meet their needs for credit. The continuing growth of such savings and investment is indicated by the percentage of capital utilized by farmers originating in agriculture increasing from about 60 percent in 1951 to about 80 percent in 1958.

CHAPTER IV

# COOPERATIVE STRUCTURE OF THE PHILIPPINES

The agricultural credit and cooperative development program of the Philippines was launched in 1953. The program was specially designed for small scale tenant farmers who had practically no access to any source of institutional credit for lack of mortgagable real property customarily required as collateral for loans. Before the initiation of the program, 86 percent of the farmers in the Philippines needed credit assistance. The farmers belonging to this group posed trouble because they held a decisive position in the social economy. Three factors were responsible for holding the masses of farmers down to a state of misery and deprivation. They were exploted by the land owners as share croppers; squeezed by the moneylenders with exhorbitant rates of interest; and taken heavy toll from by the middlemen, who served as intermediaries to sell their produce. These dealers took the lion's share of the price paid by the consumers.[64]

## The ACCFA Program:

In 1952, the Philippines Congress passed a Republic Act 821 to establish a liberal credit program especially designed to meet the needs of the small farmer. An administrative agency was also created to carry on the program. This agency was known as the "Agricultural

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64 Agricultural Credit in The Far East, Proceedings of the First Far East Agricultural Credit Workshop, Manila, Philippines, June 1-14, 1956, pp. 65-66.

Credit and Cooperative Financing Administration", popularly known as ACCFA. The act also known as the ACCFA charter, laid out four general and interrelated objectives.

1. To extend liberal credit to small scale farmers, in order to release them from usuary and to enable them to acquire essential tools for production.

2. To promote the organization of cooperatives among farmers actually engaged in agriculture to facilitate production, processing, storage and marketing of their products locally or abroad.

3. To establish producer controlled systems for orderly marketing so that the profits of agriculture may accrue to the farmers through their cooperative associations.

4. To place agriculture on economic equality with other industries and to elevate the level of living of the rural population.

A. The Small Farmer:

The original definition of small scale farmer, put a limit of 6 hectares maximum area for the eligibility of a farmer for loans, but the revised act No. 821, put a limit of 24 hectares of cultivated land ownership for eligibility. The bigger holding limit, provided greater safety for the loans than smaller holdings.

B. Credit Without Collateral:

The ACCFA system of credit in which collateral is not required is very unique in the world. Section 18 of republic act 821 provides, "Credit extended to small farmers, either with title or no titles to their lands, whether tenants or part owners, should be based upon the anticipated productive capacity of farmers in so far as repayment probabilities are concerned. The ability of such a borrower to provide security in the form of land or other tangible security, should not be the primary deciding factor in approving or disapproving a loan."[65]

Beside extension of credit, the ACCFA program also includes financing of cooperative associations for the purpose of developing a producer controlled marketing system. To achieve this objective, ACCFA is authorized to extend facility loans to such associations. Moreover, the law gives this agency broad supervisory authority and powers over all agricultural cooperatives.

ACCFA Loaning and Financing Operations:

The credit and financing programme of ACCFA is carried out through various types of loans. As a matter of policy, no loan application is considered unless the applicant has entered into a marketing contract with the cooperative association of which he is a member in accordance with the provision of section 35 of act no. 3425. The contract has to be registered and a copy filed in the office of the municipality where the association has its principal office and where a book for that purpose has to be kept. This record book shows the date of registration of the contract, the names of the parties, amount, and kind of produce to be marketed, and the period of the contract. No charge or fee of any kind is to be made for registration.[66]

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65 Ibid., p. 66.
66 Republic Act No. 821 as amended by Republic Act No. 1285, Government of the Phillipines, June 15, 1955, p. 10.

A. Types of Loans:

ACCFA loans are classified into two general types with various kinds in each category.

1. Loans to individual farmers, or personal loans.
   a. Production loans.
   b. Farm improvement loans.
   c. Facility loans.
   d. Commodity loans.
2. Loans to Cooperatives (FaCo Mas), or cooperative loans.
   a. Facility loans.
   b. Merchandising loans.

B. 3. Production Loans:

These are the most risky and most needed loans, intended to finance farm operations from the time the land is plowed to the time the crop is harvested and sold. Items allowed under this loan are grouped into:

i. Seed and land preparation.
ii. Transplanting.
iii. Subsistence.
iv. Fertilizer and pesticide.
v. Harvesting.

a. Budgeted and Supervised:

The whole amount of loan is approved in advance, but released in instalments, in accordance with an approved schedule which coincides with the budget for the farm, substantiated by the applicant's schedule of farm operations, or that prevailing in the locality. Payment to borrowers of subsequent instalments is conditioned on the proper use of the previous release as certified by the local ACCFA agent or the FaCo Ma (farmer's cooperative marketing associations). Where it is found that a previous release was misused or diverted to non-productive purposes, or the farmer did not plant, or the condition of the crop indicates a very poor harvest, subsequent releases are either reduced or completely withheld.

A special characteristic of this loan is, therefore, that it is budgeted and supervised. This feature has been adopted to insure the proper use of the loan, to train the farmers in scientific farm management, and to reduce risks. The main basis of granting the loan is the productive capacity or the expected production of the borrower, as this can be determined by area cultivated, record of previous yield, crop sharing arrangement. In addition, the character and reputation of the borrower, are considered.

The maximum amount allowed for a production loan is 60 percent of the value of the storable produce that he pledges in his marketing agreement, computed on the basis of usual yields and predetermined price per unit. For palay (rice), for instance, the ACCFA set an average price of 8.00 Pesos for carean (44 kilos net).[67]

b. Maturity and Interest:

Production loans mature 270 days after the first release, at 7 percent interest. The interest may be computed either on the actual time the money was used by the farmer, or at a straight 4 percent or

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67 Agricultural Credit in the Far East, op.cit., p. 67.

.04 for every Peso borrowed regardless of time the money was used within the maturity period.

4. <u>Farm Improvement Loans</u>:

These are partially secured medium term loans advanced for the purpose of purchasing work animals, farm implements and tools, such as plows, harrows, carts, etc.; and farm improvement purposes, such as fencing materials, fertilizer, etc. A maximum of 300 Pesos per farmer is allowed. The basis of granting such loans is similar to that of the production loans, that is, 60 percent of the value of the pledge at a given base price. Maturity ranges from one to three years. Interest is 7 percent. For both production and improvement loans, a farmer may be granted a maximum of 2,000 pesos.

5. <u>Commodity Loans</u>:

The first two types of loans are granted for production and consumption purposes. After the farmer has harvested his crops and delivered the produce to the cooperative warehouse for storage, milling and marketing, he may secure another loan, a commodity loan. With this loan, the farmer can liquidate his crop or farm improvement account and have cash for immediate needs while he is waiting for his produce to be marketed. This way, financing is made from planting to planting, covering the whole cycle. The loan is limited to 80 percent of the current market value of the commodity or produce stored in the cooperative warehouse. It is a fully secured loan which makes it one of the safest kinds of credit accomodations during periods when prices are stable. The maturity period is 120 days, renewable at 6 percent interest.

6. Facility Loans:

This type of loan is given to individual farmers, groups of farmers, and cooperative associations. It is intended to enable the farmers to acquire farm machinery, and enable FaCo Ma to establish essential facilities and installations needed for efficient storage, processing and marketing of farm produce, including warehouses, processing plants with accessories, trucks, tractors, threshing machines, containers like sacks, etc., office building and equipment like typewriters, adding machines, etc.

Security for such loans, when given to small farmers, is real property having an assessed value equivalent to the full cost of the facility together with the facility itself. Maturity of the loan is 10 years at 8 percent interest.

7. Merchandising Loans:

One of the primary functions of a FaCo Ma is the marketing of the members' produce. For this purpose the cooperatives are encouraged to operate commodity stores from where the cooperative sells the members' farm produce. Also, through these stores, members get certain production items under the crop and farm improvement loans. These supplies are released in kind as a matter of policy, after procurement on a wholesale basis.

A farmer's cooperative marketing association (FaCo Ma), may avail itself of this loan by fulfilling certain conditions, among which are:

1. Satisfactory management and handling of accounts.

2. Sufficient volume of business and membership support.

3. Adequate value of assets owned by the FaCo Ma.

Real estate or security bond equivalent in value to the amount of the loan applied for is required. The loan is given for 120 days to one year, depending on purpose, at 7 percent interest.

B. Processing and Collecting of Loans:

Two documents are the basis for the processing of applications by farmers for loans:

a. The application form, and b. The marketing contract.

1. Application Form:

On the application form, the following information is required: Size and location of farm, kind of crop raised (loans are made on specific crops), tennure conditions, normal yield per hectare, crop sharing arrangements, number of dependents, marketable surplus, other sources of income of the family, and the outstanding indebtedness of the applicant.

2. Marketing Contract:

The applicant has to be a member of a FaCo Ma, and the signer of a contract to market his products through the cooperative. The applicant pledges to deliver a certain specific quantity or amount of produce within a seasonal time after harvest. The amount and value of the pledge are the basis of determining the amount of loan which may be extended to the applicant. The amount pledged in the marketing contract must conform with the data given in the application.

The marketing contract, when registered with the local municipal treasurer, gives ACCFA a preferential lien on the produce of a farmer who obtains a production or farm improvement loan.

3. <u>Procedures for Processing Loans Applications</u>:

Initially the processing is done by the three local farmers who are members of loan committees of the association. These men are familiar with the circumstances and characters of the farmers of the locality. The committee, after scrutinizing the loan application, submits its recommendations as to the appropriate action to be taken. From them, the application goes to the secretary-treasurer of the FaCo Ma who, in turn after going through the application, submits his recommendations to the association's board of directors. At this stage, or even before, the ACCFA cooperative agent goes over the application and makes his own recommendations.

The FaCo Ma transmits the individual applications in batches with a consolidated list or schedule and its recommendations in each case to the ACCFA provincial office where the ACCFA loan examiner analyses the applications and transmits them together with the consolidated schedule on which he places the amounts he recommends for approval to the loans and credit department of the ACCFA.

The department finally submits its recommendations to the ACCFA board of governors which approves the loans.

3. <u>Release of Loan Funds</u>:

Upon approval by the ACCFA board of governors, loans are released to the FaCo Ma concerned, upon fulfillment of certain conditions. Two requirements are common to all types of loans:

a. Resolution of the stockholders, authorising the FaCo Ma to incur the indebtedness and designating the officials to sign for and on behalf of the FaCo Ma in negotiating the loans with the ACCFA.

b. Fidelity bonds of the secretary-treasurer and the manager.

For different types of loans, specific documents are required[68] in regard to the specific type of security provided by the borrower.

The route of the loan funds from the ACCFA to the FaCo Ma or the individual members is as follows:

a. When the loan is a personal one, the money goes from ACCFA to the provincial director to FaCo Ma secretary-treasurer, and finally to the member.

   i. The release of production loans is budgeted and supervised. The ACCFA may suspend or stop further release, if at any stage it finds any evidence of improper use of the loans.

   ii. For the farm improvement loans, for the purchase of work animals, the initial amount is equivalent to the combined bonds of the manager and the secretary-treasurer of the FaCo Ma is released and subsequent releases are made in the form of replenishments of the initial amount against evidence of purchase and transfer of carabaos[69] to the individual farmer concerned.

This procedure has been adopted to:

i. Insure the proper use of the loan funds and minimize possible misappropriation.

ii. To stagger the procurement of carabaos to avoid undue rise in prices that may be induced by sudden demand for this valuable work animal.

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68 Ibid., p. 69.
69 Carabaos are the type of water buffaloes used extensively as draft animal in the Philippines.

b. In the case of a facility loan, which is a FaCo Ma loan, the general procedure is for the check to be written out and delivered directly to the firm or company from whom the facility is purchased. In certain types of facilities, like a warehouse or a rice mill, which have to be constructed or installed, the release of the loan is scheduled in accordance with the progress of construction. Usually the loan is released in three instalments--at the start of the construction, midway, and when construction has been completed.

c. In the case of merchandise loans, a credit is established in favour of the FaCo Ma but withdrawn in the form of commodities which are procured at wholesale by the Central Cooperative Exchange. The CCE thus gets the commodity in volume and thereby gets the best prices, which in turn benefits the farmers who get the supplies at a relatively low cost.

5. Mechanics of Loan Collection:

Shortly before the harvest, ACCFA issues each FaCo Ma, a statement of accounts on crops and farm improvement loans that are due for collection from the farmer members. The FaCo Ma in turn sends out individual statements to its members as a reminder to deliver the produce they pledged in their marketing contract.

The indebtedness of the farmers is met technically as soon as he delivers the full amount of the pledged crop in the association's warehouse. The loan is not liquidated however, until full cash payment of principal and interest has been made.

Liquidation may be effected immediately upon delivery of the crop pledged by the farmer taking a commodity loan and applying the proceeds to the crop loan and/or farm improvement account. If he so desires, the farmer may also decide to sell outright to the FaCo Ma, if this has funds, or to an outside buyer, if the FaCo Ma or the farmer has one, and from the proceeds derived from the sale, settle the account. Another alternative is for the farmer to wait until his crop is finally marketed. In the last case, however, the maturity date may be extended and additional interest collected.

The money collected is remitted to the ACCFA by the local FaCo Ma in the form of checks through its provincial branch. The secretary-treasurer of the FaCo Ma, receives the cash collections and remits the same to the ACCFA.

If full payment is made, the account is closed, otherwise the collection of the loan goes on until full payment is made. Where circumstances allow it, legal action is taken to compel payment of overdue accounts.

6. Incentive to Loan Repayment:

In the second year of ACCFA's operations, it introduced the system of classifying FaCo Ma's members into:

(a) Privileged members.

(b) Non-privileged members.

The first group consists of members who paid their previous loans in full and complied with their marketing agreements. Non-privileged members are those whose payment record is below 100 percent. The latter group includes new members.

For privileged members, ACCFA has adopted a policy of approving automatically new loans to the amount they had the previous year, plus 20 percent for expansion purposes. This policy is intended to induce farmers to pay their loans on time.

With respect to old(non-privileged) members, eligibility to new loans is determined by careful screening to find out the real cause for non-repayment, and the capacity to repay outstanding accounts and such additional loans as they may obtain. Essentially, the same procedure is used in the case of new members. Present plans call for the use of deposit figures of the previous harvest season as the basis for estimating ceilings for production loans. In the case of a share tennant, or a leasehold tennant, loans may be granted through the guarantee of his landholder or landholder-lesser who shall be paid by ACCFA a collection fee of 2 percent upon remittance to ACCFA of the amount collected by him.[70]

7. <u>Insurance of Loans</u>:

From all crop and farm improvement loans, the ACCFA withholds 5 percent as insurance against delinquencies, and this is treated as forced savings. The amount is returned to the members concerned, after settlement in full of their loan accounts, but in the form of stock certificates or additional investment of the members in the capital stock of their FaC Mas. This deduction builds up the capital

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70 <u>Agricultural Credit in the Philippines, 1960</u>, Prepared by the Agricultural Credit and Cooperative Institute, College of Agriculture, U.P. College, Laguna, Philippines, Third Far East Agricultural Credit Workshop, Saigon, Vietnam, October 24--Nov. 5, 1960, p. 24.

of the FaCo Mas and at the same time increases individual investments and the stakes of individual members in their associations. The policy does not prevent ACCFA from garnisheeing the 5 percent to cover delinquencies.

Organizational Structure of FaCo Mas:

Farmers cooperative marketing associations are primary multi-purpose cooperatives on the village or town level. The policy is to organize provincial and national level federations specialized according to specific crops or services. For future developments it is also proposed to convert provincial federations into central cooperative banks.

Services of FaCo Mas:

The various services performed by the local general purpose cooperatives include the following:

1. Credit:

The cooperative serves both as a screening and a distribution apparatus for cash loans and loans in kind to farmer members. The FaCo Ma also guarnatees the payment of the loans granted to its members.

2. Warehousing and Marketing:

The FaCo Mas operate as warehousing and marketing agencies of the farmers. FaCo Mas also operate processing facilities to serve the members, like rice mills. The principal crops stored and marketed are palay (paddy), Virginia tobacco, corn, peanuts, onions, potatoes, vegetables.

3. Purchasing and Merchandising Commodities:

Commodity buying is one of the earliest and most popular as well as lucrative fields of cooperative services. Most FaCo Mas today operate stores which serve as distribution outlets for both consumers goods and farmers produce. The ACCFA grants merchandising loans to cooperatives to help finance these operations.

4. Miscellaneous Services:

There are other services of varying importance performed by the FaCo Mas. These include setting up funds for emergency loans (sickness, death, etc.), securing technical guidance for farmers in matters of production, pest control, fertilizer, etc., and other incidental services.

Problems of the Loaning Program:[71]

The seven years of loaning operations of FaCo Mas have shown poor collection of loans and a high incidence of delinquencies. The number of privileged members has gone down since 1957-58. The privileged members recorded in 1957-58 were 37,296, but in 1958-59, the number shrank to 31,711 and in 1959-60, they went down to as low as 11,537. Even the commodity loans which are supposed to be fully secured and should ordinarily show 100 percent repayment, recorded 88.07 percent repayment.[72]

A. Problems Related to ACCFA:

1. A summary of the factors responsible for the problems that now face these cooperatives is given below.

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71 Annual Report of Cooperative Department, FY 1959-1960, AFFCA, Manilla, Credit Division Report, pp. CTD 9-13.

72 Ibid., Fig. 1, and p. CTD 8.

1. Reported Anomalies in the ACCFA:

Reports of anomalies being committed by people connected with ACCFA have produced a hostile reaction from the public, specially from farmers. Early termination of cases against guilty persons erase in the minds of FaCo Ma members whatever they might have heard about the ACCFA's sincerity.

2. Lack of Loan Funds:

Due to lack of funds, one of the solutions recommended is that ACCFA should liquidate some of its capital properties and launch intensified collection efforts by dispersing ACCFA personnel throughout the critical areas during harvest time.

3. Indifferent Attitude of ACCFA fieldmen:

Personal differences among the fieldmen in the administration and indiscriminate transfers and postings of these men have not had a healthy effect. They have resulted in low collection of ACCFA loans.

4. Too Much ACCFA participation in the Affairs of Cooperatives:

Many of the FaCo Mas organized are not an outcome of voluntary organization by members based on a background of education and recognition of felt needs but were forced and induced by the ACCFA. What could have been done, perhaps, was to start pilot cooperatives in a province and let the idea thrive and prosper by the successful demonstration, and let the people in adjoining areas form one after being stimulated and then educated.

B. Problems Related to FaCo Mas:

1. Failure of FaCo Ma Officials and Loan Committee Members to Collect Loans:

Most FaCo Mas placed too much dependence on the ACCFA fieldmen for loan collection and this produced poor results and low recovery of loans. FaCo Ma officials and loan committees should have been made responsible for the collection of the due accounts by themselves. This would put more people on the job instead of one ACCFA fieldman, and satisfactory results would be produced at the harvest time when members have the means to pay. They could be induced to pay by the officials of their local cooperative.

2. Dishonesty and Incompetence of FaCo Ma officials:

This factor has been mainly responsible for the inefficient working of so many of the cooperatives and for their poor financial condition. Removal and suspension of such officials is the solution, plus prompt and vigorous action to recover the money misappropriated.

Due to poor system of auditing of the accounts of FaCo Ma officials by the ACCFA's fieldmen, there was a recorded loss of 14 million pesos as of Dec. 31, 1959 when only 61 percent of the cooperatives were examined. The actual total misapplication was estimated to amount to nearly 22.5 million pesos. Findings of the ADL-ACCFA credit committee show that small farmers are good debtors and their repayment of personal loans is above the rate of repayment even for secured loans. Hence, strict checking of the accounts by the ACCFA fieldmen is recommended.

C. Problems Related to Members:

1. Lack of Proper Understanding of ACCFA's market and Credit Program:

Education of members is essential to have them realize their responsibilities toward patronizing their cooperatives by discharging their obligations to deposit their marketable surplus in the cooperative warehouse. They should be taught how cooperatives succeed when the members participate and help their cooperative to operate at low cost so it can make savings for them.

2. Non Credit Worthiness of Borrowers:

Many bad credit risk farmers have been advanced loans. To avoid this problem, a proper evaluation by the fieldmen of the character, capacity and other circumstances of applicants is essential before approval of loans. Members of loan committees have to be convinced that when loans are made to farmers who cannot, or will not, repay the amount borrowed, every member of the cooperative, including himself, has to absorb his respective share of the losses.

CHAPTER V

# EXPERIENCE OF THE INDIAN COOPERATIVE CREDIT PROGRAMME

## Cooperative Movement in India

In India, the cooperative movement was initiated to help farmers finance their own operations rather than become indebted to the money lender. Credit societies were started after enactment of the "Cooperative Credit Societies Act), in 1904. But the cooperative movement, restricted to credit only, grew very slowly. While the societies were both for thrift and credit, the thrift side was ignored and the members relied on them solely for credit. This resulted in a small volume of deposits so that the societies became too heavily dependent on the government as a source of loanable funds.[73]

With further establishment of credit societies in the villages, it was realized that the mere provision of credit was inadequate to meet the real needs of farmers, and therefore the societies should go a step further and supply other requrements. The credit society also should help him to get seed and other production requirements, and also arrange to market his produce. As Mr. Varde puts it, "In order to help the farmer get out of debt to the money lender, it is necessary not only to give him credit but to give him some of the services that the

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73 Sen, S.R., Institutions and Credit Problems in India, Proceedings of the International Conference on Agricultural and Cooperative Credit, University of California, Berkeley, Aug. 4 to Oct. 2, 1952, pp. 725-26.

money lender was performing.[74] This led to the development of multi-purpose societies. This broadening of the program came during the second world war and the post partition period when many such societies were developed. In spite of this stimulated growth, the movement has touched only a fraction of the people and there is a heterogeneity in response in the different provinces.

A. <u>Structure of the Co-op Movement</u>:

There is a pyramid type of structure of the cooperative movement in India. The primary credit societies, which are the base of the movement, are usually federated into unions or central (district) cooperative banks, and these again into a provincial (state) cooperative bank, functioning as an apex institution for a whole state. These societies and banks supply in the main short-term and, to some extent, medium term credit.

Primary agricultural credit societies and multipurpose societies together totaled 166,543 cooperatives. As of 1957-58, they had a membership of 10,221,000. Share capital of Rupees, 282 million, deposits Rs. 86 million, and working capital of Rs. 1337.5 million. This indicates that cooperatives now provide 5 percent of agricultural credit in India. Other data showing an average figure per society for 1957-58 as follows: Number of members 61; share capital, Rs. 1,695; deposits, Rs. 513; deposit per member, Rs. 8.4; working capital, Rs. 8,031; loans advanced per member, Rs. 94; and overdue loans as a percent of loans

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74 Blaisdell, T.C., Jr., et. al., <u>Farm Credit in Underdeveloped Areas</u>, International Conference on Agricultural and Cooperative Credit, University of California-Berkely, 1953, p. 43.

outstanding, 21 percent.[75]

B. Organization and Membership:

Any 10 adult persons living in a village intending to promote mutual economic interests in accordance with cooperative principles, can register the group as a cooperative society with limited or unlimited liability, as they choose. The membership and range of operations of a society with unlimited liability are relatively restricted due to the desirability of intimate mutual knowledge of resources and integrity of members. The provincial (state) and central (district) banks are organized on a limited liability basis and have generally mixed membership of individuals and societies.

1. Funds:

The funds of the societies consist of entrance fees and share capital subscribed by the members, deposits, loans, reserves, and other funds and subsidies, grants, etc., given by the state governments. Generally a maximum limit is laid down in the by-laws in regard to the amount of shares which a member can hold. The society, as required by law and its by-laws, sets aside a certain portion of the net earnings to the reserve fund (one fourth under the 1912 act) before any dividend on shares or patronage refund on services is paid. The liabilities which a society with unlimited liability can incur by way of borrowings and advances from non-members are determined by the general meeting

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75 Abrahamsen, M.A., A Look at Agricultural Cooperatives in India, Farmer Cooperative Service Circular 28, U.S. Department of Agriculture, Washington, April 1961, p. 21.

of members every year. In the case of a limited liability society, the amounts of borrowings by the society are also restricted by the by-laws. In Bombay, for instance, societies with limited liability provide in their by-laws that liabilities shall not exceed eight times the total amount of its paid-up share capital, accumulated reserve funds and building fund minus accumulated losses. Banks, of course, also set limits on the amounts they will loan various societies. The government also generally prescribes certain minimum liquid resources to be kept by societies for meeting their liabilities. The primary societies are able to get loans from the central (district) banks and the latter, in turn, from the provincial (state) bank as mentioned earlier. The Reserve Bank of India functions as a banker's bank and a lender of last resort. It grants concessions to the cooperative credit institutions both in regard to the period of accomodation and the rate of interest.[76]

2. <u>Loaning Operations</u>:

Loans can be granted by societies only to their members, or to other societies with the sanction of the Registrar of Cooperative Societies. In Madras state a society can also make loans to its depositors on the security of their deposits. A maximum borrowing limit is fixed for every member in the annual general meeting. Further, every form of security which an agriculturist can possibly offer, his real or immovable property, his chattels or moveable property, his personal credit or general reputation for thrift and honesty, and the signatures of two other members as guarantors for repayment of the

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76 Sen, op.cit., pp. 43-44.

loans, is accepted as security. But the most predominant form of security is land. Under the Cooperative Societies Act of 1912, the sanction of the Registrar is necessary for loaning money on the security of moveable property. Under the Madras state act, this sanction is not necessary when money is lent by the society on the security of agricultural produce stored in an acceptable warehouse.

3. Period of Loans:

The period is fixed according to the purpose of the loan, though the period for similar loans is different in different states. In Madras, the societies with unlimited liability can extend loans up to 5 years, while for the limited liability society the corresponding period is three years. In Bombay province short term loans are allowed for one year or until next harvest, whichever period is shorter. Intermediate loans for purchase of implements for three years and those for land improvement can run for five years.

C. Multipurpose Societies:

The development of multipurpose societies was encouraged first by the Agricultural Credit Department of the State Bank of India in the late 1930's. It was then recognized that other needs of the farmers besides credit must be provided relative to marketing farm products and providing production supplies. The idea of meeting these varied needs through one overall local society rather than through several uneconomical small scale societies, performing different functions, has gained headway.[77]

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77 Abrahamsen, op.cit., p. 29.

When these developments occur, the general practice is for a primary credit society to take on these additional functions, and often to expand its area of operation to include several villages. The multi-purpose society, therefore, provides credit, markets farm produce, and supplies to members production supplies like fertilizer, seeds, insecticides, and related items.

In Madras, the "Controlled Credit Scheme" parallels the work of the multi-purpose societies. Loans are advanced by rural credit cooperatives for growing specified crops on condition that the produce raised with the loans will be delivered to the marketing societies with which the credit associations are affiliated for sale. The loans are recovered out of the sale proceeds.[78]

The large size societies now being set up in India, under the new reorganization scheme in various states, are primarily single purpose credit societies affiliated with a supply and marketing society. This trend is based on the recognition that credit and trading activities cannot be safely combined in one institution because losses in the trading sphere will affect the credit side, leading to losses and eventually to the inability of the society to give the loans for agricultural production for which it is primarily intended.[79]

The primary multi-purpose societies are generally affiliated with the district marketing or purchasing organization, or both. These

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78 Blaidsell, et. al, op.cit., p. 45.
79 Hough, E.M., and Das, K.M., The Cooperative Movement in India, Oxford University Press, London, Fourth Edition, 1959, p. 239.

reliance on honorary services for even day to day work, with resultant inefficiency in management.[80]

A more detailed enumeration of the handicaps of the movement, i.e., the intrinsic factors which have retarted its development are given in Dr. E. M. Hough's publication, "The Cooperative Movement in India".[81] These factors are poverty and malnutrition, the widespread indebtedness, high percentage of illiteracy, lack of business experience, uneconomic holdings, antiquated methods of cultivation, inadequate transportation and storage facilities, price fluctuation, unregulated markets, exploitation by money lenders and middlemen. Other weaknesses of the movement have been almost exclusively dependence on borrowed funds, and the inadequate linking of credit with thrift and other cooperative services; the tying up of funds in long term loans; delinquencies in repayments; and numerous defects of management.[82]

New Developments to Meet the Problems of the Credit Societies:

The main difficulties experienced by the primary credit societies in India are:

1. Inadequacy of financial resources.
2. Lack of trained staff.
3. Firm hold of money lenders and middlemen on some of the members.
4. Lack of a strong educational programme to foster systematic saving by villagers.

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80 All India Rural Credit Survey, General Report, Vol. II, Bombay, India, 1954, p. 246.
81 Hough, op.cit.
82 All India Rural Credit Survey, Vol. II, op.cit., p. 247.

Many of the primary societies are uneconomic units, as mentioned earlier, and their deposits are meagre. They have, therefore, to depend on the central cooperative financing agencies to a very large extent for their loan funds. In the new set up, therefore, the share capital financial base of the societies, whenever necessary, is strengthened by contributions made to the share capital by the state governments to give them greater financial strength. Lack of trained staff, and consequently mismanagement at the hands of untrained secretaries and managers, have been stumbling blocks in the successful operation of the societies. This problem was taken up by the government by organizing a network of training centers under the auspices of Central Committee for Cooperative Training. The hold of money lenders on the members of primary credit societies is being loosened gradually by legislation and by the spread of the ideals of cooperation among the rural people, backed up by increased funds for the societies to expand their lending operations. Despite this, the private money lenders still account for a very large percentage of the total credit supplied to farmers today,[83] because there is no agency that meets the needs of villagers for credit.

2. Linkage of Primary Credit Societies to the Primary Marketing Society Serving a Mandi (Local Market) Area:

Integration of credit with marketing and supplies, has not so far been much of a success in India. The difficulties of the average primary society, lack of the business acumen and shrewdness to handle

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83 Chary, P.N.T., Reserve Bank of India, Agricultural Credit Department, Bombay, India, Letter, March 15, p. 2.

the marketing of members produces, have retarded the development of successful cooperative marketing operations. The society cannot afford a secretary or manager who is well conversant with the produce markets and who can protect its interests from the shrewd designs of traders and middlemen. It can, however, undertake supply of seeds, fertilizers and implements and also essential consumer commodities to their members against payment of cash. The setting up of separate organizations for the purpose of marketing the produce of members of primary credit societies has, therefore, been favoured in India. Thus, while the function of credit and the distribution of supplies may be entrusted to the primary credit societies, marketing may be entrusted to a separate organization. However, the credit societies should be affiliated to the marketing society in the area so that the loans granted by the credit societies may be recovered through the marketing society. As alternative, the marketing society may also undertake the supply activities.[84]

Integrated Rural Programme in India:

On the basis of the recommendations made by the "All India Rural Credit Survey Committee Report", in relation to some of the handicaps discussed earlier, the second 5 year plan for India 1956-61, envisaged the future basis of the cooperative credit programme under the following features. The new set up of credit societies is being carried out according to the following recommendations.

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84 *Ibid.*, p. 2.

A. Large sized societies serving groups of villages are to be organized having a membership of 500, a minimum share capital of about Rupees 15,000, and a total annual business of Rs. 150,000. The object of forming large sized societies is to make them economic and self sufficient units. These societies will be of limited liability type.[85]

B. The rural credit societies are to be affiliated to the primary marketing society serving a mandi (local market) area. Credit societies will collect the produce of their members for disposal through the marketing society. Furthermore, they will obtain the farm production supply requirements of their members from the supply department of the marketing societies and distribute them to their members.

C. Loans are to be advanced by the credit societies on the basis of the production program of the cultivators and their anticipated output of crops. Members of credit societies will be persuaded to agree in advance to market their produce through the affiliated primary marketing societies.

D. Primary marketing societies, as well as large sized credit societies, are to construct their own warehouses to facilitate the storage of agricultural produce. Warehouses also will be constructed at important marketing centres by the state and central warehousing corporations to facilitate cooperative marketing.

E. The Central Government, through the Reserve Bank of India, is to play a crucial role in the integrated scheme of cooperative

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85 Cooperative Developments in India 1953-54 to 1955-56, Report to the Third Indian Cooperative Congress, All India Cooperative Union, New Delhi, April 4, 1958, p. 4.

credit. To enable the cooperative movement to fulfil effectively these objectives, an outlay of Rs. 470,000,000 has been allocated by the Central and state governments for cooperative developments during the second 5 year plan period. A quantitative target for the number of different types of societies has been worked out which includes 10,400 large sized credit societies.

Financing the Cooperatives:

A. Building up Members Investments:

One of the chief defects of the cooperative credit societies has been the lack of members' deposits and investment, as mentioned earlier, which made them dependent on the central banks, and these in turn on the provincial banks for loanable funds. One method of increasing the investment of members of primary credit societies in their capital under the new set up is to link the members' borrowings to their shareholdings. For instance, for every Rs. 100 borrowed by a member from his society, he is required to hold shares worth Rs. 10 in the society. In the case of some marketing societies, a compulsory deduction is made, say 1 percent from the sales proceeds of each member and the amount kept as a deposit with the society concerned for being converted into shares at a future date. In the case of a supply society, the patronage refund on purchases, payable to each member is converted into shares and issued in his name.

B. Loanable Funds:

Funds for loaning may be raised either in the form of share capital or deposits or loans. Methods adopted to increase the share capital have already been explained above.

In order to collect more savings deposits from members and non-members, a few primary credit societies have introduced schemes like the recurring deposits, chit funds,[85a] home savings, etc., and all these measures have met with varying degrees of success.[86]

As regards loans, in order to enable central financing agencies to lend more to primary societies, the committee on cooperative credit which examined the problem recently, has recommended as follows:

1. The following criteria may be adopted by the Reserve Bank for granting short-term accomodation for agricultural purposes to state cooperative banks on behalf of the central banks:

a. The distinction made at present between 'normal' and 'exceptional' limits, may be removed so that the normal credit limit to which A and B class central banks (district banks) will be eligible, will be 4 times and 3 times their owned funds respectively.

b. In addition to the above, an A class central bank may be sanctioned a limit not exceeding twice its owned funds and a B class bank equal to its owned funds on the following conditions:

For the amount outstanding against a bank out of the limit sanctioned by the Reserve Bank in excess of the normal limit, as indicated in (i) above, the bank should show outstanding loans against societies for agricultural purposes for twice the amount borrowed. In other words, of the excess of loans outstanding against socieities for agricultural purposes, over and above the normal limit, only 50 percent can be from funds provided by the Reserve Bank, the other half being provided by the bank out of its own resources.

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85a A program of periodic saving of member subscribers for a fixed period of time during which each member can borrow an amount which is repaid by his periodic payments.

86 Chary, op.cit., p. 2.

C. A class C central bank may be sanctioned a limit up to 3 times its own funds against the guarantee provided by the government. The limit may be raised to 4 times in special circumstances.

The Reserve Bank may sanction an additional medium-term credit limit to a central bank up to twice the increase in fixed deposits and share capital registered during the year prior to that for which the limit applies, provided however that the normal and the additional limits do not together exceed twice the owned funds of the bank.[87]

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87 *Ibid.*, p. 3.

# CHAPTER VI

## EVALUATION OF COOPERATIVE CREDIT IN WEST PAKISTAN

The cooperative movement in the Indian subcontinent has been predominantly a credit movement. The history of the movement in Pakistan was same as that of India till 1947 when the country was separated. Therefore, the overall structure of the cooperative institution is practically the same, with some modifications that occured during the last decade. Cooperative credit societies were first established in 1904 on the Raifeisen model of unlimited liability. Their basic purpose was to relieve rural indebtedness.

In order of magnitude, cooperative credit societies account for a far larger amount of production credit than any other institutional source in West Pakistan. Yet they remain a marginal source of credit supply despite 50 years of existence. Under state sponsorship and assistance, the movement has been stagnant, particularly at the primary level, for a number of years.[88]

The cooperative credit structure has a three way pyramidical pattern. The primary credit societies are at the base serving the villages; cooperative central banks are at the district level, being federations to finance the primary societies; and the provincial cooperative bank at the apex or provincial level. The primary function of central banks (district banks) is to meet the credit needs of societies rather than those of individuals.

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88 Credit Enquiry Commission Report, Government of Pakistan, Karachi, September 8, 1959, p.5.

Two external shocks have been principally responsible for the setback of the movement. Firstly, the depression of the 1930's resulted in large scale defaults as agricultural incomes collapsed and many societies became defunct as their own funds were frozen or wiped out by defaults.

The second shock came when, at the time of partition, all Hindu and Sikh communities migrated from Pakistan to India. Hindus and Sikhs constituted the majority of all cooperative officials in the pre-partition Punjab Province which had had a fairly successful cooperative program. This left a great vacum in cooperative management and deprived the cooperative movement in the area of its experienced leaders. These were hurriedly replaced by untrained and inexperienced officials.

Multipurpose Cooperatives:

Some multipurpose cooperatives were organized in Punjab immediately after partition at the time when the rural economy was shattered due to the influx of refugees from India and due to the unorganized produce markets. Prices of farm commodities had gone down very low. The cooperatives were directed to purchase the members' products and arrange for their sale and also to distribute some essential controlled commodities like cloth and sugar. Several oil mills and ginning factories were also alloted to them for processing, which they had to relinquish when normal trade and commerce were restored. These multipurpose cooperatives could not take a firm root because the above mentioned functions were assigned to them as an emergency measure and not with an idea to develop the cooperatives.

4. Credit Societies:

The primary credit societies are of both limited and unlimited types but the majority are of the latter type. Although they numbered over 11,000 and had 375,276 members in 1958, their total capital was small and they supplied but a very small part of the production credit used by farmers.

A summary of operations of primary credit societies as of 1957-58 is given in Table 2.

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89 Punjab formed an independent province of West Pakistan before the merging of three independent provinces of West Pakistan in 1955.

TABLE 2

Capital and Operations of Primary Agricultural Cooperative Societies in West Pakistan, 1957-1958[100]

(In 1,000,000 Rupees)

| Year | Number of Societies | | Number of Members | | Share Capital Paid Up | | Working Capital | | Reserves and Other Funds | | Deposits | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | Ltd. | Un-Ltd. | Ltd. | Un-Ltd. | Ltd. | Un-Ltd. | Ltd. | Un-Ltd. | Ltd. | Un-Ltd. | Ltd. | Un-Ltd |
| 1957-58 | 90 | 11,154 | 32,008 | 343,268 | 29.44 | 56.22 | 271.65 | 358.88 | 48.02 | 121.52 | 122.11 | 30.11 |

| Year | Borrowed at End of Year | | Loans to Individuals During Year | | Loans Outstanding at Year's End | | Loans Over-due | | Gain or Loss | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Ltd. | Un-Ltd. | Ltd. | Un-Ltd. | Ltd. | Un-Ltd. | Ltd. | Un-Ltd. | Ltd. | Un-Ltd |
| 1957-58 | 72.08 | 148.03 | 141.82 | 173.87 | 147.45 | 298.91 | 24.45 | 100.53 | + 4.43 | + 8.51 |

100 Credit Enquiry Commission Report, op.cit., pp. 21-22.

5. <u>Stagnation of Cooperative Program</u>:

The total membership of credit societies as of 1957-58 was 375,276. Considering the average number of members in a family to be five, the percentage of rural families participating in the primary cooperative credit societies was less than 7% in West Pakistan, which includes areas which were known to be in the forefront of the cooperative movement in the subcontinent.

Total working capital as of 1956-57 was Rs. 62.8 million, having risen from Rs. 29.8 million since 1947-48 when partition took place. The rise is due largely to an increase in outside borrowings without any substantial growth in member investment or savings deposits.

The audit classification reveals that out of 10,985 societies in 1956-57 in West Pakistan, 2,421 societies were defunct and on the verge of liquidation, while another 2,194 societies were nearly defunct. This means that nearly 40 percent of the total number of societies were in a moribund condition and of no consequence for current financing purposes. Of the active societies, there were only 245 in the A class and 1,942 in the B class, i.e., societies which were regarded as in fairly good condition and needing little or no supervision. Another indicator of stagnation at the primary level is the slow growth of membership. In the decade ending March 1958, only 129,282 new members joined the primary credit societies in West Pakistan or less than 13,000 per year. Since the population in the rural areas would have risen in West Pakistan by an average quarter million per year over the decade, an addition of this small number of members means that the growth of the membership did not even keep pace with the rise in population.[91]

In the year 1959, there were 11,453 primary credit societies in West Pakistan. Amount of loans advanced to these societies during the year 1959 to extend to their members on farms was Rs. 26.7 million. These societies in turn advanced loans to their members to an amount of Rs. 38.08 million and recovered Rs. 31.59 million during the year.[92]

The amount, although it represents the largest amount loaned for agriculture by any institutional agency, yet is very modest as compared to the total requirement of farmers in West Pakistan which is roughly estimated to amount to Rs. 3,000 million.

Causes for Stagnation:

A basic cause of the slow pace of development is illiteracy and a subsistence economy where practically no savings take place for capital formation in savings deposits or investments. Very few peasant farmers in Pakistan have sufficient land to produce on a commercial scale for sale in the market. Besides, in spite of more than 50 years of the cooperative program, it still remains mostly official in character and the idea of cooperatives being member controlled and member owned organizations, has not been absorbed into the minds of the people. Other external factors responsible for stagnation in

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91 *Ibid.*, p. 26.
92 Ahmed, M., Educational Assistant Registrar of Cooperative Societies, Lahore, West Pakistan, Letter March 3, 1961.

the post-partition period are diversion of cooperative funds to non-cooperative uses; political intervention, nepotism; exploitation by the economically privileged members; weakening of the cooperative departments due to exodus of trained staff after partition; frequent transfers of registrars (who are almost the skippers in the movement); poor selection of officials; and lack of real government support.[93]

Internal Deficiencies:

The main internal weaknesses of the credit societies which are relevant to the investigation of this study have been reported by the Credit Enquiry Commission Report of the Government of Pakistan.[94] These deserve mention here.

1. Low Credit Limits:

Throughout West Pakistan, a certain maximum credit limit has been set for loans taken by an individual member of a primary credit society on the security of the signatures of two solvent persons. These limits were set in the pre-world war II period and were not revised in the post-partition period when price levels have risen considerably. In the former Frontier and Punjab provinces (now merged into the one over-all province of West Pakistan), an absolute limit of Rs. 300 was prescribed for barani areas (rainfed areas) and Rs. 500 for irrigated areas. Within these ceilings, a member's credit limit was fixed in relation to the varying amount of land taxes he paid on different pieces of land. In the case of an occupancy tenant or a mortgagee with possession, the multiple was 10 times, while

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93 Credit Enquiry Commission Report, op.cit., p.37.
94 Ibid., pp. 28-29.

in the case of a tenant at will, it was 15 times of half the land tax payable on his rental holding. In the former Sind region of West Pakistan, the maximum limit was fixed at 4 times the land tax, including the water tax which was separately charged elsewhere. Since the land tax rates had been fixed 30 to 40 years outside former Sind and since settlement were overdue in many areas, these rates have little relation to the rise in prices over the period. A ceiling of Rs. 300 may have been appropriate for the 1930's but is insufficient for the recent years to meet any of the production credit requrements of the cultivators, such as the purchase of a pair of bullock.[95]

2. Gradual Shift to Land Mortgage Security:

The ceilings on individually loan limits could be doubled, if the cultivator was willing to offer the security of a mortgage on his land. The extension of production credit thus came to depend increasingly on the mortgaging of land. The poor recovery experience of earlier years also impelled many cooperatives to insist upon security of this kind. The extension of the loans, thus, was gradually restricted largely to landed individuals only. The other sections of the population who did not own land were discouraged from joining the societies by the low limits applying to them.

3. Unlimited Liability Unpopular:

Many persons were detered from joining the societies because they were operating on unlimited liability. In the former province of Punjab, for example, the enquiry committee report stated that

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95 *Ibid.*, p. 28.

in case of large number of societies liquidated, the clever members exploited the legal provisions of the laws to evade their responsibility for repaying what they had borrowed personally so that the main burden of settling the debts of the society fell on the non-defaulting members.

4. Dependence on Unpaid Staff:

Another weakness characterising the primary credit societies has been the dependence on untrained and honorary office bearers who either did not exert themselves at all, or only for their own benefits. Very few villagers can read and write so that few ordinary members of credit societies can perform the work of secretary-treasurer. The small income of the society from the low volume of loans extended prevents paying the salary of a trained person.

5. Problem of Delinquent Loans:

Of all the problems of village credit societies, the problem of overdue payments on loans is rated at the top by some people.[96] At the time of partition, the overdues were about 22 percent of the total working capital of all cooperative societies and 33.23 percent of their outstanding loans in West Pakistan. In 1956-57, the proportions had increased to 25.68 and 33.4 percent, respectively. The problem of overdues has remained a regular feature, fluctuating from year to year due to crop failure and unfavourable market conditions. As a result of these fluctuating overdues, the working capital of the societies also fluctuates in the opposite direction.

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96 Khan, A.M., The Problem of Overdues in Farm Credit, Credit Rural and Cooperative, Quarterly Journal of Agricultural Credit Department, State Bank of Pakistan, Karachi, October-December 1960, p. 14.

Other causes attributed to the problem of overdues are, utilization of loan funds by the farmers for non-productive purposes and lack of integration of credit with marketing and purchasing which should have assured repayment of loans from the sale proceeds of the farmer members' agricultural produce. Besides, the loan funds advanced to the member borrowers are quite inadequate to meet their needs for production purposes.

6. Failure to Develop Thrift:

The primary motive behind the movement originally was to create thrift among the rural population. When this part of the program failed, the societies depended mainly on the higher level cooperative credit agencies to secure for them the funds required for extending loans to their members. Consequently, most members feel no personal interest in the credit society because they have no personal financial stake to be safeguarded by collection of loans.

Raising of Maximum Credit Limits:

Recently the credit limits on several loans have been doubled. With land as security, the maximum limit has been raised to Rs. 4,000 in the irrigated areas and Rs. 2,000 in the barani or rainfed area. However, fixation of individual limits in terms of multiples of land taxes, remains the same, so that in effect there is no real increase in the borrowing powers of members who cannot offer land as security. The above credit limit is not in proportion to the production expenses or in proportion to the prices which the farmers get for their products. Hence, the Pakistan Credit Enquiry Commission recommended the repaying capacity of the individual borrowers and the societies' experience of past recoveries as a basis for granting loans and setting the amount to be loaned each applicant.

Recent Developments in West Pakistan:

The West Pakistan Government currently is participating in supplying the share capital of apex cooperative banks, and this money is going down to the primary village societies by the way of bank loans to them. So far, a sum of Rs. 1,1,000,000 has been invested by the government and Rs. 800,000 are expected to be invested in the coming financial year.[97] Large sized credit societies with limited liability are being formed. These societies will each have a paid up share capital of Rs. 10-20 thousand, a membership of 100-200 and hence share capital contribution per member amounting to Rs. 100. The anticipated annual credit business per society is two hundred thousand rupees per year. Out of the sums invested by government as share capital in apex banks, an amount equal to the share capital paid in by members and up to Rs. 10,000 will be made available by the provincial and through district banks to each primary society as an interest free loan. Beside making loans, the societies will also arrange for the marketing of the agricultural produce of the members, through the marketing societies to which they will be affiliated.

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97 Shah, M.H., Registar Cooperative Societies, West Pakistan, Credit Rural and Cooperative, Quarterly Journal of Agricultural Credit Department, State Bank of Pakistan, Karachi, April-June, 1960, p. 11.

About 150 large sized societies have been formed and 600 such societies are planned to be established by the end of 1965. The credit base will thus have been strengthened and primary cooperative societies may then be expected to make loans of over Rs. 150 millions per year as against the present figure of Rs. 25 million.

The State Bank has contributed to the improvement program by giving technical assistance to the Cooperative Department by way of assigning one of its officers as a banking advisor in addition to making funds available for agricultural credit.

Conclusion

In conclusion therefore, following internal factors have been principally responsible for the stagnant growth of the cooperative credit movement in West Pakistan:

1. Low credit limits.
2. Gradual shift to land mortgage security.
3. Unlimited liability has become unpopular.
4. Dependence on unpaid and untrained staff to run the business affairs of the societies.
5. Frequent occurence of delinquencies.
6. Failure to develop thrift and hence low level of member savings and of funds for loaning members.

## CHAPTER VII

## RECOMMENDATIONS FOR IMPROVING THE COOPERATIVE CREDIT PROGRAM IN WEST PAKISTAN

In the rural credit program for West Pakistan, there is no practical substitute for cooperatives as the primary local source of production finance for farmers. As observed in the first five year plan for Pakistan,[98] "No credit organization can be built except at a prohibitive cost to serve the millions of small men in villages, unless they themselves assist it by forming local associations. For a purely commercial agency, the magnitude of the job is too great and agricultural credit will have to be subsidised. For the purely government agency also, the job is too great, without the organized support of the local people, doing their best to help themselves. The best form in which they can organize themselves is the cooperative."

### Recommendations Made by the Credit Enquiry Commission:

Considering the internal shortcomings of the existing cooperative credit structure which have been mentioned in the concluding paragraph of the previous chapter, the Credit Enquiry Commission Report recommends the following criteria to be adopted for the future structure of the cooperative credit program in Pakistan:

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98 The First Five Year Plan 1955-60, National Planning Board, Government of Pakistan, Karachi, December 1957, p. 295.

"There may be gradual establishment of large sized, single purpose primary credit societies covering areas not exceeding in any case the geographical coverage of the union, operating on a limited liability basis and run by paid staff whose salary would be met, in part at least, by the provincial cooperative banks. These cooperative societies should undertake financing of seasonal needs and medium-term needs of the cultivators, not exceeding a period of 3 years on the basis of individual credit limits based primarily on repaying capacity and recovery experience. The primary society should be linked up with marketing societies situated at a higher level. The union level credit societies (recommended large size) may be organized either through voluntary merger of existing primary societies or new societies may be established where primary soceties do not already exist or are in a moribund condition or voluntary mergers do not take place. The departments in both wings of the country should ensure that these societies become truly effective instruments for channelling credit to all credit-worthy members."[99]

Other structural bases of the credit program besides these, have been included in the second five year plan of Pakistan.[100]

1. The primary societies will have individual members.
2. The central banks, to which the primary societies will be affiliated, will have exclusively soceities as members and no individual members.

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99 Credit Enquiry Commission Report, op.cit., pp.37-38

100 The Second Five Year Plan 1960-65, Planning Commission, Government of Pakistan, Karachi, June 1960, pp. 178-180.

3. A single provincial bank at the apex level will have the district or central banks affiliated within it.
4. The central banks will be required to withdraw from any commercial business undertakings.
5. Cooperative institutions would mobilize their own funds by share capital and deposits. They would not become dependent on the State Bank of Pakistan for all their loanable funds.
6. The government may participate in the share capital up to one third of the paid-up share capital of the large size societies.
7. The large size new societies will have a membership of at least 100 persons, paid up share capital of Rs. 10,000, and a loan capacity of Rs. 100,000.
8. Besides credit, these societies would also undertake marketing of produce and the supply of essential requirements for members.
9. The societies should have paid secretaries who would be trained at the cooperative colleges.
10. The management of the societies would endeavour to ensure that loans granted should be used for productive purposes.
11. With the exceptions of payment for hired labor and essential cash production expenses, loans will be disbursed in kind.
12. The village A.I.D. workers, from the government department, may help farmers to determine their credit needs and supervise the utilization of loans effectively.
13. The interest rate on loans must cover the cost of administration.

14. Overdues may be recovered as arrears of land revenue tax by the revenue authorities to facilitate collection of the loans.

15. For the marketing of the member's produce, cooperative marketing societies should be established which should handle the produce of its constituent primary societies as well as of their individual members. The marketing society will undertake the sale of produce, construct godowns at suitable centres, and supply improved seeds and fertilizers and other requirements of the members. The cooperative will issue farmers receipts of the deposit of their products in the warehouses which they can use as a negotiable instrument to obtain a commodity loan from their credit society.

16. Each marketing society will serve 20-30 member primary cooperative societies, market produce, and buy supplies for the farmer members.

17. For the successful operation, credit societies will require members who borrow to sign contracts to sell their produce through the affiliated marketing society. This will facilitate collection of the loan by deduction from the proceeds of the sale of the produce. Members should also be able to obtain loans against products stored in a warehouse controlled by a cooperative.

Evaluation of the Cooperative Credit Program in Pakistan

The preceding section sets forth all of the points included in the program for cooperative credit in Pakistan recommended by the Credit

Enquiry Commission and the First and Second Five Years Plans. For the purpose of evaluation of these from the standpoint of making recommendations for strengthening them to contribute toward more successful operation of the societies, these points have been grouped under five major topics. Following the evaluation of each topic, the recommendations of the writer will be set forth.

Economic Size Local Credit Societies

I. Evaluation of Official Proposals

A. Economic Size Local Credit Societies with Limited Liability

The Credit Enquiry Commission recommended a large size society with limited liability on the basis of the following considerations:

1. Large Enough Volume to Employ Trained Secretary-Treasurer.

One of the causes contributing to the stagnation of the cooperative credit movement in Pakistan is the un-economic small unit of operation. Because of this reason, there had been dependence on the honorary and unpaid staff who showed little interest in the working of the societies which require full time attention. A relatively larger size society, therefore, will meet this deficiency and because of larger scale of operation, the society will be in a position to employ a paid full time secretary-treasurer who can operate the society more efficiently. The other ideas related to the economic sized society are:

a. Operation on Sound Banking Basis:

Hitherto this had been a serious deficiency in the movement. The ideal of a cooperative credit society was also to combine thrift and savings in the community and thereby build up resources in the form of members' and non-members' deposits to stand independent for loanable funds. But due to sole dependence on unpaid honorary secretaries, thrift was neglected and little deposits were built up by the credit societies. A large size society with limited liability can afford to employ trained personnel who can handle members and non-members deposits on a sound banking basis and can manage loaning operations more effectively by proper screening of applications and careful supervision of loans without tangible security to assure high percentage of loan collections.

b. Build Confidence to Foster Deposits:

The official program views with confidence that members will gradually develop faith in the safety of their money deposited with their societies when full time trained secretaries are appointed to manage their deposits and handle loan operations. Thus, the new co-operatives will be able to attract continuing deposits when they demonstrate good management and collection of loans.

2. More Effective Government Supervision:

The government can give more effective supervision to a smaller number of large societies than to a large number of small size scattered societies. With more effective supervision, it is natural that societies can function more successfully.

3. Have Own Warehouses for Crop Storage:

Under the officially proposed set up, a linkage has to be established between the credit and marketing society. The credit society is required to serve as an agent of the marketing society to which it is affiliated to collect members' produce and deliver it to the marketing society for sale. A large size society can afford to build its own warehouse in which to collect members produce and then transmit them in bulk to the marketing society and thus reduce the unit cost of transportation.

4. Large Size Necessitates Limited Liability

Limited liability becomes necessary when the size of a society becomes large. As mentioned earlier, the official program calls for the establishment of large credit societies serving a minimum of 100 members. Farmers are afraid to join a large society with unlimited liability because the amount of risk increases with the enlarging of the number of members whose credit worthiness cannot be determined accurately when granted a loan for the first time. Members must feel sure that there is little or no risk they will be called upon to pay any losses that may be suffered by the cooperative. They know that in a limited liability society they are liable for paying only whatever amount they individually may owe to the society in the event of liquidation.

II. Recommendations

In consideration of the above evaluation, the writer makes the following recommendations:

A. Support for the Official Proposals.

The writer endorses the idea of establishing local credit societies with limited liability especially in view of the fact that substantial farmers who are relatively more credit worthy, will be more willing to join the societies with limited liability. This can be expected even though the liability of members may be fixed at a multiple of their shareholdings because each member can set the limit on the amount of liability he assumes. Besides, a large size society will be able to employ a trained secretary who can operate the credit service successfully.

B. Continuation of Successful Un-Limited Liability Societies

The successful un-limited liability societies may be left to flourish and get the same government financial investment as limited liability societies because they are meeting the needs of the members and there is no valid reason for liquidating them. Un-limited liability credit societies have generally been recommended for areas where small scale farming predominates because of the force of group pressure for all members to repay their loans and the greater willingness of banks to extend loans to this type of society. Such groups as work together successfully desire the same opportunities for participation in the integration program as the limited liability cooperatives.

## Integration of Credit, Purchasing and Marketing

I. Evaluation of Official Proposals

From the very beginning of the cooperative movement a half century ago, it was proposed that a local society must provide at least the three important services of credit, marketing and supply. These integrated services can be provided however, either by establishing separate credit, marketing and purchasing societies, or by merging the functions into one society which may be termed as multipurpose, as was recommended in the 1930's by the Reserve Bank of India (before independence prepartition India).

The official proposal for the new set up is, however, to establish large scale single purpose primary credit societies at the village level and link them to the large size marketing societies at the town or mandi (local market) level which would handle the sale of members produce, delivered through their local credit societies. The details of the official recommendations have been mentioned in points number 8, 15, 16 and 17 of the preceding section.

A. Integration Superior to Multi-Purpose Cooperatives

The official plan for integration of services at the local level instead of multi-purpose village cooperatives corresponds with observation of what has happened with this type of society in other countries, as well as India. Out of experiences of the countries analysed, it was found by the writer that when three functions including credit were combined in one association, it invariably developed a functional conflict of interest. Thus, there may be pressure to increase consumer sales to obtain the advantages of a large volume of business. There is then the temptation to extend credit too far in order to sell more goods. But a more serious problem, in the view of the writer, would be the management of accounts in West Pakistan which would become very complex when credit, supplies and marketing operations are combined in one cooperative society, especially when there is a dearth of trained personnel to operate the societies.

B. Advantages of Integration

Linkage of primary credit societies to the marketing societies which also handle production supplies becomes more important under the proposed set up to establish large sized credit societies with limited liability, where close personal supervision of the loans is not possible by the members. Therefore there are two main advantages gained by this linkage.

1. It Insures Productive Uses of Loans

Since loans are to be made mostly in kind, insurance is provided against the diversion of these loan funds to non-productive uses by the member borrowers, as has been a common practice in the past with the farmer members of existing credit societies.

2. Facilitates Loan Collections and Avoid Delinquencies

The proposed marketing contracts for the produce to be marketed through the marketing societies as an essential condition for obtaining loans through the credit societies ensures repayment of loans and avoids delinquencies unless a natural disaster reduces the crop very substantially.

II. Recommendations

To implement the integrated credit program successfully the following procedure should be adopted in West Pakistan, as is being carried out successfully in Cyprus.

A. Marketing Services

The local credit society may handle marketing service of members produce by functioning as an agent of a marketing union to which it may be affiliated. It may assemble members' produce in its warehouse and arrange for transportation to the marketing society. This function may be handled on a purely commission basis per unit of produce handled, and there should be no assumption of risk by the society by taking transfer of title to itself.

B. Purchasing Service

The purchasing service may be handled on a pool order basis by the society. The secretary-treasurer may ask individual members for their specific production requirements and the quantities, which they may enter on a printed form jointly authorising their society to acquire on their behalf their orders, accepting at the same time all responsibility for loss or damages that the society may incur in case the member concerned fails to take delivery of the goods in question on arrival.

The society may then pass on a copy of these orders to the marketing society which would obtain the desired supplies through its provincial union, which will purchase these items locally or import from outside. In Cyprus, the Central Cooperative Bank at Nicosia, which serves as an apex bank, pools these orders from its affiliated local societies and asks for tenders from manufacturing countries. On arrival of the goods, local societies are notified to collect them. The societies in turn inform the members who had ordered the goods, to collect them upon arrival of the truck in the village. Members then may pay cash for the value of goods purchased or they may arrange with their credit society for the said sum on their budgeted production loan arranged prior to the ordering of these goods. They may then sign a bond in the customary form for the value of the goods and thus, in effect, pay cash. In any case, supply of the production goods must be handled on cash basis. Thus the credit societies avoid the problem of book credit or open account credit, which has become a problem in the United States and Canada. These supply cooperatives oblige their patrons to borrow from different agencies and pay cash for their supply purchases beyond an accomodation limit of 30 days. In this way, neither the local societies, nor the central bank, run the risk of accruing any losses from these transactions which are of a commercial nature.

Meeting Financial Needs of Members Successfully

I. Evaluation of Official Program for Extending Loans to Cooperative Members:

The Credit Enquiry Commission recommends repaying capacity of the individual borrowers and the society's experience of the past recoveries of loans extended him to be the main considerations in determining the credit granted a farmer. The recommendation has been made in order to overcome the past deficiency of landed property as security for farmers to obtain an adequate amount of credit to meet their needs for financing their operations. To implement this new program, a radically changed system of security has been worked out by the Commission to provide a convenient form to suit every class of cultivator and acceptable to the credit society. The two common forms of security recommended are:

1. Lien on crop contracted for delivery to a marketing society for production loans.

2. Stored products for commodity loans.

To assure repayment of loans under the crop lieu system, the official program, however, recommends that farmers hold membership in both credit and marketing societies to qualify for loans. Members who borrow would be required to deliver their surplus produce above their consumption requirements to the marketing society which would arrange for the sale with the proceeds turned over to the credit society from which loans advanced will be deducted and the balance credited in the borrowers deposit account.

This system would overcome the fatal weakness in the previous program where there was no positive way whereby the credit cooperative could collect the loans from borrowers. It had to rely on voluntary payment by members. Hence, a large percentage of loans were not paid and later had to be charged off as uncollectable. The system of contract delivery of products to marketing cooperatives with deduction of the loans from proceeds in the Philippines has worked out quite successfully there.

On the security of the products delivered and stored in the warehouse of the marketing society, the members would be advanced commodity loans. To the loaning agency, staple farm products stored in approved warehouses offer an appropriate type of security. The agency will have no difficulty to determine its value, pledged as an asset which is the direct source of the farmer's income out of which repayment will be made. In this way, farmers would get the facility to obtain adequate amounts of loans to meet his seasonal production and consumption requirements. The crop lien will provide security until the product goes in storage when the commodity loan supplies money to pay off the production loan and cover living expenses until the products are sold after prices advance seasonally.

## II. Recommendations

### A. Loans for Only Credit Worthy Members

The official program casually mentions repaying capacity and the past record of a borrower to qualify for a certain amount of loan. But since the appraisal of the prospects for repayment of individual loans is the most crucial factor on which the whole cooperative credit program rests, the subject deserves rather more careful consideration.

The loaning program in the initial stage has to be carried out with proper discrimination and all the borrowers, including tennants and share croppers who are relatively poorer credit risks on account of possessing meagre tangible security, may qualify for loans strictly on the basis of their character, repayment record, productive, and repayment capacity. Otherwise, substantial farmers with better resources would be reluctant to join as members to secure loans at a rather expensive interest charge. When losses from uncollectable loans are charged against the reserves, the society is obliged to raise the rate of interest in order to secure enough net margin to replenish the reserve fund. This increases the net cost of loans to the good credit risk borrowers. They will tend to go elsewhere for loans at lower rate of interest. This would weaken the society and soon put it in the stagnant group.

The solution would be to adopt the method followed in the Philippines program and classify the borrowers into classes principally on the past record of repayment.[101] (Refer to p. 95 and 96) "A" class borrowers may be termed as privileged class and may be entitled to a full amount of credit. "B" class borrowers should be restricted to the bare minimum of credit for production and subsistence under a special reserve program to absorb the losses from delinquencies. "C" class applicants with bad records of repayment should be denied further loans.

B. <u>Protection Against Losses on "Poor Risk" Loans</u>:

1. Unsecured loans, which are relatively high risk loans, should require agreement in the loan contract, that credit cooperatives will withhold from crop proceeds 5 percent of each loan above the principal as a reserve against losses from uncollectable loans. At the end of 5 years, the members would be paid back what remained of their 5 percent retain after deducting the losses suffered on that year's loans.

2. Credit cooperatives should set aside 5 percent of their annual net earnings in a loan insurance reserve in the Provincial Cooperative Bank. When a local cooperative's loans that are losses, as determined by the auditor, exceed the 5 percent retain in their individual

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101 Refer to p. 95 and 96.

allocated reserves, the excess could be collected from the provincial insurance reserve.

C. Supervision and Productive Utilization of Loans:

The purpose of credit is not served unless it is productively utilised by the borrowers and they are able to repay from the sale proceeds of the products for the growing of which the funds were borrowed. In Pakistan, a large portion of the average loan borrowed by low income farmers often is utilised for unproductive purposes, which greatly reduces their repayment ability and results in many delinquencies. It is equally important, therefore, that the loans extended will be used primarily for productive purposes. This necessitates effective supervision and guidance in carrying out the planned program of crop production. This would then improve the repayment capacity of the borrowers and their economic conditions. The following recommendations are made by the writer to foster achievement of this objective:

1. Budgeted and Supervised Loans:

In the experience of the United States and the Philippines, loans should be extended according to the budget plan in order to ensure their proper use and to train the members in scientific planning of their farm operations to increase their net incomes. This would help to reduce the risks of extending loans without land mortgage security or personal guarantors.

For this purpose Extension and Community Development Departments may be required to coordinate in providing supervision and guidance to the farmers to make their production plans and budgets and use improved methods in their production operations. Members with the help of these government officers, or with the help of a trained cooperative employee, should be required to make in advance their production plans and budgets for the whole season. The budget should specify the purpose and time for which loans are requested. The whole amount, after proper scrutiny, may be granted, but released in instalments with the approved schedule coinciding with the farm plan budget. Subsequent instalments may be advanced when the previous release was used according to plan, as certified by the society's agent after making actual inspection. If the loan is found to have been used for other than sanctioned purposes, subsequent instalments are not released and the amount already advanced on the loan immediately becomes due for repayment.

D. Advances in Kind:

Loans which are approved for certain productive items and which are sanctioned in the budgeted loan agreement may be obtained by the borrower either through the supply department of his marketing cooperative, as mentioned earlier, or through local dealers. In both cases, the sales invoices could be charged against the farmer's loan by the credit cooperative on presentation, and direct payments made to the seller for the supplies purchased. In this way, the credit cooperative would insure that borrowers did not divert their loans from the productive uses for which they were granted.

## Financing of Cooperative Credit Program

### I. Evaluation of Official Proposals

In financing the cooperative credit program, it is recommended officially that the cooperative institutions should build up their funds by share capital and deposits. These proposals are designed to overcome the shortage of loan funds that has restrained the cooperative credit program up to the present. Raiffeisen type of societies, on which the old structure was based, did not make any provision for share capital and only a nominal fee was required for bonafide membership. The new proposal would help overcome two serious drawbacks of the previous program. The purchase of a substantial amount of share capital will help develop in the members a sense of belonging and ownership which is so vital for the success of any cooperative program. In addition, it will help the societies to accumulate loanable funds for providing an adequate amount of production loans to individual members. The new large scale credit societies should not be dependent on central banks for their loan capital but obtain an increasing proportion from member capital and deposits. A thrift campaign to mobilize credit society would greatly help in reaching this objective.

## II. Recommendations

### A. Members Owned Cooperative Credit Program

In Pakistan, the Central Government and the state government combined plan to contribute one third of the capital structure of the societies. This is to strengthen their borrowing capacity, particularly if they are able to borrow a certain multiple of their paid-in capital and reserves. But the cooperative credit program must aim to eventually repay the government contributions and make it a member owned program as in Canada, Japan, and the United States. This program may be achieved by members investment in the capital of the society.

For each loan, members must own B class stock equal to 5 percent of the amount borrowed. This percentage may be raised to 15 eventually as rapidly as it is feasible for the members to increase their investments in their society. These shares cannot be redeemed after the member has paid back his loans but may be sold to other members asking for loans. This proposal is similar to the plan which has operated successfully in fostering the building up of capital in the general purpose cooperatives in Japan since 1950, as described in the chapt er on the Japan experience with cooperative credit.

1. Savings Program

a. By way of launching an educational program by the secretary of the societies, members should be taught to make regular small deposits in their societies and invest in their societies by purchasing A class stock for which they may pay in instalments. Large savings deposits should be made from the returns from selling seasonal crops and livestock products.

b. The chit fund and home saving schemes of India should also be adopted.

c. School Savings Program

A very effective method of saving program was observed by the writer in Cyprus during his short visit to survey the cooperative credit movement on the Island in 1960. Schools on the island carry on this saving program by collecting small deposits of the students on behalf of the village credit societies. The teacher in charge of the program gets a certain percentage of the deposits as a commission and to cover the cost of operation. This has proved a very successful program to mobilize rural savings and strengthen the financial position of the societies. The same program has been adopted in Jordan and found successful, as was observed by the writer in 1961; when he visited to survey their cooperative credit program. This program should be adopted in Pakistan as well. It develops the habit of thrift so that adults continue saving and depositing all their earning lives. It leads in time to a very substantial amount of deposit funds in the local credit cooperatives that reduces their seasonal borrowings to a fraction of their earlier requirements from the cooperative bank.

In Japan, 80 percent of the funds loaned to farmers, come from the thrift of themselves and their families, mobilized through village cooperatives, the postal savings system, the provincial credit federations, and the Central Cooperative Bank. The proceeds of the sales of their products marketed cooperatively are credited to their deposit accounts. From the balance remaining after repaying his seasonal crop production loan, the member buys some additional shares and adds to his savings deposits. He leaves enough in his current account to take care of living expenses. He can borrow what he needs for the next cropping season. In this way, farmers are meeting cooperatively by far the greatest part of their needs for credit and production loans.

## Education and Training

### I. Evaluation of Official Proposals

Education and training programs have not found any prominent place in the official recommendations as vital factors in the cooperative credit program. No clear cut program has been ennunciated to carry out the new official proposals.

The task of supervision and audit was the responsibility delegated to the inspectors of the West Pakistan Cooperative Union. Supervision service, as mentioned in the Credit Commission Report, covers not only the testing of the societies for efficiency, but carries a great educational value by imparting working knowledge of cooperatives to the members of societies.[102]

Due to inadequate training and low scale remuneration of the inspectors of the Union, and also of the department, both these functions of education and supervision were not carried out efficiently. The Commission, therefore, has recommended a separation of audit and supervision. Audit service may be transfered to the department and supervision may be left with the Union. In other words, the Union is delegated with the service of education and training. The success of the new program will depend in large measure upon how effective is the education of the membership and the training given officers and staff.

II. Recommendations

The cooperative program cannot succeed with all the best planning unless an extensive and intensive education and training campaign is launched by the department officers and non-government officials (such as inspectors of the union of cooperatives) to educate members, directors, committee members, and officials of the societies, and also for training the staff.

Experience of cooperatives in countries which have made the most advance in proportion of business and credit services handled by cooperatives during the past 30 years, has demonstrated condusively the

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102 Credit Enquiry Commission Report, op.cit., p. 36.

very important role played by education programs for members and training programs for directors, officials, managers, and operating staff. With effective education and training programs, cotton and supply cooperatives have developed in the south-eastern states of the U.S. where the regional tobacco cooperative failed 1925-1930 because of lack of effective member education programs. The cooperative credit program in Cyprus has eliminated moneylenders from almost all villages because of the educational program that stimulated young and old to save small sums regularly and deposit them in the village credit society. The mobilized accumulated savings were and now are loaned to members to meet their needs for credit and loans. In Pakistan, on the other hand, relatives and friends and well-to-do persons and landlords provide the largest source of credit supplied to the farmers. The dependability of these sources is questionable and the amount supplied by these agencies do not meet the full requirements of the farmers. Because the credit societies have not accumulated sufficient member share capital, deposits and reserves, to meet the demands of members for loans, they are still largely dependent on government loans for funds. The reason is the lack of an effective member education program to develop understanding of cooperatives and appreciations of the importance of thrift to the advance of the individual family.

Against intensive high pressure sales merchandizing campaigns by large scale companies, the farm supply cooperatives and marketing societies generally in Canada and U.S. are gradually increasing the share of farmer purchasing and marketing done through cooperatives. This is being done by well trained managers and operating personnel.

Cooperative employees are carefully selected and generally have training for the work they will do. But they continue in regular in-service training programs operated jointly by the individual cooperatives and the federations of which they are members. Specialists from state extension services and government departments assist with these training activities.

A. Member Education

Member education may be handled preferably by an unofficial organization in West Pakistan like the All-India Cooperative Union in India which has undertaken the task of educating members through a specialised branch for which it receives a substantial grant from the government of India.[103]

B. Personnel Training

Officer bearers and committees should, in addition to the normal education on cooperation, receive training in the management, administration and keeping of account books of cooperative societies. These officers can be trained in the following ways:

1. Short training courses should be held at convenient centers which they could attend without too long absence from home.

2. A very effective method of training would be visits of marketing and purchasing cooperative officers and officials of the unions and apex organizations and also to local credit cooperatives. They could train the office bearers of the associations in keeping

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103 Report on the Asian Regional Seminar on Co-operation, Nuwara Eliya, 1957, International Labour Office, Geneva, 1958, p. 163.

the books and on such matters as processing of loans, security etc. These instructions would be more effective and of greater practical benefits if the officials visit them soon after the audit report or inspection report has been submitted. The related shortcomings may be explained and advice and suggestions may be provided to overcome them.

The practice adopted in Canada may be sighted as an example for practical guidance in the Pakistan program. The district representative meets with the officials in round table fashion following his examination of a credit union or within a period of a few weeks, when the report is prepared and submitted to the credit union. This affords an excellent opportunity for the examining officer to discuss in detail the findings as outlined in his report as well as to make suggestions for remedial measures where necessary. Usually the discussion includes the status of the outstanding individual loans, collateral security, and properly drawn documents.[104] This discussion is often followed by sessions with the secretary-treasurers and operating staff regarding proper ways of putting the decisions taken into operation in the work of the society. Continued advisory service of this kind brings about marked improvement in the cooperatives over a period of years.

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104 Fifteenth Annual Report 1959, Department of Cooperation and Cooperative Development, Regina, Saskatchewan, Canada, 1960, p. 57.

# CHAPTER VIII

## CONCLUSION

In order to bring the writer's recommendations for strengthening the program for the development of cooperative credit recommended by the Credit Enquiry Report and the Second Five Year Plan, into focus, they are summarized below. His recommendations for improvement are underscored in order to distinguish them from the official government proposals.

1. There should be established economic size local credit societies with limited liability. The volume of business should be large enough to justify the employment of a paid full time trained secretary-treasurer who can operate the society on a sound banking basis by receiving members and non-members deposits and handle loaning operations efficiently. The society would own warehouses to collect and store members products and finally transport them to the nearest marketing society to which it should be affiliated. <u>At the same time the successful un-limited liability societies should be left to flourish and get the same government financial investment as the new limited liability societies</u>.

2. The single purpose primary credit society at the village level should be integrated with the marketing society at the mandi (local market) or taluka (sub-division) level, which will handle the sales of members' products and also arrange the supply of their production requirements.

Marketing and purchasing services should be handled by the local credit society on an agency basis in conjunction with the area marketing cooperative. Marketing of the members produce should be handled without any assumption of marketing risk by the primary society. The purchasing service should be handled on a pool order basis by purchasing through the marketing society with which it is affiliated and which in turn may purchase through the provincial Union. Members will enter their orders on printed forms and individually accept all responsibility for any loss or damages incured by the society if they fail to take the delivery of the goods they have ordered. The supplies will be handled on a strictly cash payment basis. Members who cannot pay cash must arrange a production loan through their credit society for the items specified in their farm production plans and budgets. Upon arrival of their supplies, members would acknowledge the receipt of the items and deliver the voucher to the secretary of the credit society who would charge the amounts against the members budgeted loans and pay cash to the marketing cooperative to settle the account.

3. The main criteria in determining the amount of credit granted to a borrower would be his repaying capacity and the society's experience of past recoveries. The two common forms of security would be a lien on his crop contracted for delivery to the marketing society and then stored products for commodity loans. Members extended loans on crop lien would hold membership in the marketing society and would be required to make a contract for delivery of their products to it. On the security of products delivered and stored in the warehouse of the marketing society, they would be advanced commodity loans by their

credit society. Members without tangible security will qualify for loans strictly on their character, repayment record, productive (indicated by a farm plan) and repayment capacity. Members would be classified in A, B and C classes of borrowers. "A" class borrowers would be a privileged class and should be entitled to the full amount of credit based on their respective repayment capacities. "B" class borrowers should be restricted to a bare minimum of credit for production and subsistence under a special reserve program to absorb the losses from delinquencies. "C" class borrowers would be denied further loan because of their failure to repay the amount borrowed previously. On unsecured loans, credit cooperatives will withhold from crop proceeds 5 percent of each loan above the principal as a reserve against losses from un-collectable loans. What remained of these retains on that year's loans would be paid back to the members at the end of 5 years, after deducting the losses suffered. Besides, each cooperative will also set aside 5 percent of its annual net earnings in a loan insurance reserve in the Provincial Cooperative Bank. When a local cooperative's loans that are losses, as determined by the auditor, exceed the 5 percent retains in their individual allocated reserve, the excess would be collected from the provincial insurance reserve.

Loans will be extended on the basis of farm production plans and budgets and their utilization will be supervised by a trained cooperative employee. Extension and the Community Development Departments, will be required to coordinate in providing supervision and guidance to the farmers to make their production plans. Loans will be released in instalments. Subsequent instalments will be advanced if the previous release was used according to the budget. If the loan is found to be utilised for other than sanctioned purposes, subsequent instalments will not be released and the amount already advanced would become due for repayment.

Advances for production supplies will be made in kind. Sale invoices of the marketing cooperative supply department, or the local dealers, will be charged against the farmer's loan by the credit co-operative on presentation and direct payments made to the seller for the supplies purchased.

4. Cooperatives will finance their loaning operation mainly by building up their own funds by share capital and deposits. In the initial stage, the State and the Central Government will provide one third of the capital structure of the societies. But local credit societies should require members to increase their investment in share capital so that the government's investments could be repaid by the growth of the societies' capital. Members would be required to own sharesof stock equal to 5 percent of the amount borrowed which would be eventually raised to 15 percent. These shares will not be redeemed after the members have repaid their loans but will be sold to other members who ask for the loans. The long term objective is a member owned and controlled credit system which will have sufficient resources to meet the production credit needs of the members adequately.

Through educational campaigns conducted by the societies' secretary, members would be taught the habit of thrift by making periodic deposits in their credit society. Deposits from the sale of products would be made weekly, monthly or seasonally according to what the farmer markets and when. Other savings program would be carried out by the Chit fund and home savings schemes of India. Members would buy additional shares of stock semi-annually or annually from marketing proceeds or saving deposits.

The school savings program should be launched by the cooperatives in village schools to collect small deposits by the students to go into the village credit societies.

5. Special emphasis will be made on the education of the members and training program for directors, committee members and officials of the societies and the staff. Members education will be sponsored and guided by a nation wide organization as the All-India Cooperative Union in India. The organization would get a substantial grant from the Pakistan Government. Each cooperative should carry on its own education program with the cooperation and support of the Union.

Cooperative's personnel, including office bearers and committees, would receive training in the management, administration, and keeping of account books of the societies through short training courses held at convenient centres, and through in-service training imparted by the visits of marketing and purchasing cooperative officers and officials of the Union and apex organizations. They will train the cooperative officers in book keeping, processing of loans and evaluation of security etc. Shortcomings noted in inspection visits and in annual audits may be explained and advice and suggestions will be provided to help the local cooperative's personnel overcome them.

## Summary

In summary therefore, there should be established a member owned cooperative credit program to meet the farmers production needs adequately, principally through member investment in share capital of the society and savings mobilized through different methods. For operating the society successfully, full time trained and paid secretary-treasurer should be employed. Loans should be extended mostly in kind to assume productive use of the funds. Repayment should be insured by requiring each borrower to contract to deliver his produce to the marketing cooperative for sale with the loan deducted from the proceeds. To foster efficient management, an in-service training program is essential for the cooperatives personnel. Member education is essential to ensure their loyal participation in the savings program and repayment of their loans for the permanent success of the credit program.

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