

The banker, the farmer and the gem-cutter

(The Nation, Bangkok, 14 and 18 October 1991)

The Bank for Agriculture and Agricultural Cooperatives (BAAC) is the government's main source of credit for small-scale farmers. It lends to over 60 percent of Thailand's farmers, for their farming enterprises. But farmers do other work too, and BAAC wants to be able to support its clients' non-farm activities. Should it be allowed to widen the scope of its operations?

Consider Mrs. Sumalee Maniphak. As a rice farmer she is typical of the village of Nong Manao, Muang District, Ubon Ratchathani province. She has a 30 rai plot, slightly above the average for the province. She gets an average yield.

Like an increasing number of farmers in the Northeast, Mrs. Sumalee became dissatisfied with her income from rice growing. Despite following the extension officer's advice her income has increased only marginally. She began to look outside traditional farming activities for a way to upgrade her family's living standard. She experimented with a small village retail operation but was not successful.

In 1987 she established a gem cutting and polishing business in her house. She bought two machines for 3,000 baht each, and hired two village girls. At first that was not successful either. The buyer rejected many of her finished gems, and she had no idea how to improve their quality and no way of contacting alternative buyers.

And she had no way of borrowing money to improve or expand her business. As a farmer, she had borrowed from the BAAC for many years to finance her paddy farm. Yet BAAC refused her request for a loan for the gem business because the bank's charter restricts it to lending for farming activities.

Sumalee's story is increasingly common, and reflects the far reaching changes that are under way in rural Thailand. Already, Northeastern farmers earn on average almost two thirds of their net household incomes from non-farm or off-farm activities, according to the Office of Agricultural Economics (OAE). Many would argue that a gradual transfer of resources into non-farming activities is in the region's best interests, because of the limited potential for growth in the farm sector. And small



enterprises like Sumalee's gem business can create significant numbers of year-round jobs.

Yet, as Sumalee discovered, there are formidable barriers to setting up and financing a small rural non-farm enterprise. A farmer could call on several agencies for assistance with a new project, including BAAC. Equivalent agencies hardly exist for non-agricultural enterprises. So few people try, and among those who do the probability of failure is high.

CARE

Sumalee's luck changed when she contacted CARE, a non-government organization. Since 1988 CARE has run a Small Enterprise Development project in Ubon, with the intention of filling a gap in the provision of services for non-farm activities.

With no experience or model to base their work on, CARE began by making a general survey to establish what kinds of enterprises might qualify for their help. They made a second survey, in collaboration with the provincial administration, to find out in more detail what kinds of help the businesses needed.

Sumalee needed better technical skill for herself and her staff, and better market contacts. CARE



Credit

Credit remains a problem. Many of the enterprises which CARE has assisted have relied on their own resources, by choice or necessity. Sumalee is an example. Others do not have the funds to buy equipment or raw materials, and the lack of credit is the main constraint on their enterprise.

Mr. Samran Thongsan has a small motorcycle repair business that he runs from a rented shop. Mr. Koson Saisuk makes metal tops for pick-up trucks. Mr. Phaitoon Kanhalim has a bakery, and supplies local shops with peanut brittle and other cookies. All of them needed loans of 50,000 baht or so to make their work premises weather proof, to buy equipment or to establish a revolving fund of working capital to buy raw materials. None of them approached a bank. They knew BAAC could not help. They had no idea how to approach the commercial banks and were quite sure that if they did they would be refused.

CARE's solution was to lodge a guarantee fund with the Bangkok Bank. The bank in turn undertook to lend up to three times the value of CARE's deposit for enterprises which CARE recommended to them. In effect, CARE acts as the bank's credit officer. Staff members identify enterprises, appraise loan applications, pass suitable ones on to the bank and CARE guarantees loan repayment. The bank has accepted 80 or 90 percent of CARE's proposals.

The arrangement has worked well, according to CARE and Mr. Apichai Ratanasin, the manager of Bangkok Bank's Ubon branch. But it is not a permanent solution to the credit problem. The total amount of credit available is limited. Even with the existing scale of the Small Enterprise project, Mr. Pinyo screens out about half his loan requests before sending them to the bank in order to stay within the agreed credit limit.

More seriously, the eventual goal is to phase out the project and have each enterprise stand on its own feet. There is no evidence that commercial banks will continue to finance even the existing project-supported enterprises unless their loan requests meet the bank's normal requirements. There is no evidence either that the bank's lending policies have changed to make them more sympathetic to requests for fairly small loans in relatively remote areas. Such loans are expensive to administer and unattractive to

brought her to Bangkok to visit several factories which contract work to outworkers. She was able to choose between them and establish a better deal than she had had with the local buyer. And the company sent a trainer to help in the village. More recently CARE arranged for the Department of Industrial Promotion's Ubon office to attach a gem expert to Sumalee's business for three months.

"We have only four field workers, so we can't do much ourselves," says Mr. Pinyo Weerasuksawat, Field Coordinator of the CARE project in Ubon. "But we can coordinate, and arrange for services which the farmers could not get by themselves."

In three years, CARE has supported 1,640 households with non-farm enterprises in 30 villages spread over 12 districts of Ubon.

The needs and CARE's approach have varied from enterprise to enterprise and from village to village. Brush makers in Ban Hua Saphan, Khlong Jiam district have formed a successful cooperative, with assistance from the Community Development Department. They appointed members as the quality control officer, and marketing officer.

In contrast the potters of Ban Tha Tao Hai in Muang district have met several times to try to cooperate, so far without success. CARE has instead focussed on technical problems such as kiln design to try to improve the quality of the pots and reduce wastage.

Many otherwise promising enterprises have little management or accounting ability, resulting sometimes in gross misallocation of resources. Simple accounting training has enabled them to streamline their operations and identify sources of losses.

commercial banks.

The Small Industries Finance Organization (SIFO) is a government agency which supposedly exists to supply the kinds of loans which CARE's project members needed. Mr. Pinyo sent SIFO some loan applications. SIFO has virtually no branch network in rural areas. After long delays and some prompting Mr. Pinyo concluded that SIFO had insufficient field staff to get involved.

BAAC

So we return to BAAC. In all but one respect, the situation described above is exactly that for which the government created the bank in 1966. BAAC is a state enterprise, supported financially by the government, and intended to provide credit services where commercial banks are unwilling to work. It provides supervised credit, not usually based on mortgage security because few Thai farmers have mortgageable land documents. And it has field officers in virtually every district in the country who work closely with clients to assess and administer their credit needs. BAAC counts 3.1 million households as its clients.

BAAC's charter enables it to lend only to farmers. The Juridical Council has interpreted this to mean that it can lend only for farming activities. So the government's main source of rural credit can lend millions of baht for, say, a commercial dairy enterprise. But it has to refuse a request from a client with 20 rai of paddy land in Sisakhet who wants to buy a sewing machine so that his daughter can boost the family's income by doing contract dressmaking.

So it is that BAAC has so far been able to lend to Sumalee for her paddy farm, but not for her gem business. While BAAC may like the idea of continuing and expanding upon the CARE project there is little the bank can do to help.

Changes

Various World Bank missions to Thailand have advocated widening BAAC's scope of activities. Now at last there are two signs that things may change.

Starting from October 1990 the BAAC has implemented a Rural Household Industry Promotion Project in collaboration with the OAE. Under the project the bank can lend for farm-related



enterprises, provided they are carried out by farmers. Example activities are producing fruit or vegetable juice, handicrafts based on farm products, pickled or dried fruit and making furniture from rubber wood. The project represents a slight widening of the bank's mandate.

Potentially more important is the proposed change to the Act of Parliament that governs BAAC's activities. The proposal would extend the definition of eligible borrowers to include farmers who have supplementary "farm-related" activities, as approved by the BAAC Board of Directors.

Mr. Pittayapol Nattaradol, BAAC Executive Vice President, believes this change will allow the bank to increase the scope of its operations significantly.

"The bank's intention is not to remove all restrictions to its lending activities," he says, "but to be able to provide full financial services for farmers and farm communities. If an enterprise is somehow related to agriculture, owned by a farmer, and its employees are from farm households, it should be considered farm-related and therefore eligible for BAAC loans."

Mr. Pittayapol admits there will be some grey areas where activities fall around the boundary of the bank's mandate. The Board will have to establish where that boundary lies. Nevertheless if the proposed amendment is passed in its present draft form it may have a big impact on the way the BAAC operates.

At present even though the bank can support farm processing activities, most of the raw materials are supposed to originate from the client's own farm. The business should not depend mainly on supplies bought from neighbours. This restriction would

disappear under the proposed amendment.

Village restaurants will be acceptable because they process food produced by farmers, and serve farm communities. A mango grower who wants to open a vehicle repair service would qualify because he is a farmer and farmers would own most of the vehicles he would service. Mrs. Sumalee's gem business could qualify because she is a farmer and her employees are from farm households.

Under the proposed amendment the restrictions on BAAC will still be tight compared to those governing sister banks in neighbouring countries, such as Malaysia's Bank Pertanian. And the question of BAAC's place in Thailand's newly liberalized banking system remains open. So are the proposed changes too great, or too modest?

Those who believe the amendment is too modest say the restriction to "farm related" activities makes no sense. It will be extremely difficult to define in a practical way. Why not lend to *bona fide* farmers for whatever they want?

Others fear that loans for non-farm activities will be relatively large and cheap to administer. They may be so attractive that the bank will focus on them and forget that its first responsibility is to support agriculture.

This is a concern at the Bank of Thailand. Ms. Suchada Kirakhun of the Economic Research Department says: "Farm related activities should use raw materials from farming. Maintaining this meaning is important, to ensure resources are not diverted away from the farming sector which is vital to the country."

The argument turns on the estimated scale of demand for rural, non-farm loans. Will the BAAC be swamped with applications, or will there be so few that getting involved will not be worth the effort of acquiring new loan appraisal and administration skills?

The little evidence that exists suggests neither fear is justified. In the first six months of its Rural Household Industry Promotion Project the bank made 1,812 loans with a total value of 64 million baht. A little over one third of these loans have been in the Northeast, primarily for handicraft enterprises. These loans have averaged 16,000 baht each, about the same as the overall average for BAAC loans.

Total lending for the first full year will be about 120 million, a tiny percentage of the BAAC's total portfolio of over 40 billion baht.

Demand for CARE's services has increased gradually. After a slow start, clients now come to CARE rather than the other way around. On the basis of these approaches Mr. Pinyo estimates that with unlimited staff they would double their present number of project participants. This suggests there is a real demand for assistance, including credit. But the demand is not enough to jeopardize the availability of funds for farm credit.

Is BAAC capable of handling a greatly widened range of enterprises? Judging from CARE's experience the main needs will be for technical training, market contacts and accounting skills. The bank will also need new models for loan analysis. At least one BAAC branch manager has not lent for farm processing because he has no model to base his loan appraisal on.

The scale of demand may be enough to justify one additional credit officer in each branch, but probably not more. And not enough for BAAC to undertake support services directly. So the bank will find itself in the same position as CARE, training its staff to coordinate assistance rather than provide it.

If CARE's project is considered successful the outstanding question is how to institutionalize its achievements and experience, and extend its activities to cover a bigger area. There are several ways in which this could be done, involving various agencies. Amending the BAAC Act to allow lending for a wide range of farmers' activities would make a great deal of sense to people like Mrs. Sumalee.

