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Review of Small Farmer Access to Agricultural Credit in Nigeria

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The important role of credit in agricultural enterprise development and sustainability has prompted the Federal Government of Nigeria (FGN) to establish credit schemes such as the Agricultural Credit Guarantee Scheme (ACGS) and Agricultural Credit Support Scheme (ACSS) to ensure farmers' access to agricultural credit. Yet, the situation has not improved substantially; based on the 2006 Core Welfare Indicators Questionnaire Survey, it is estimated that only 18 percent of farm households (mainly small-scale farmers) have access to financial services (Akramov 2009). This brief reviews existing knowledge on small-scale farmers' access to credit with particular focus on conditions for accessing credit, the maximum credit provided, repayment of credit, other factors limiting access, and the impact of credit on small-scale farmers.

Background

Agriculture is a major contributor to Nigeria's GDP and small-scale farmers play a dominant role in this contribution (Rahji and Fakayode 2009), but their productivity and growth are hindered by limited access to credit facilities (Odoemenem and Obinne 2010). Credit institutions can be categorized into three groups: (a) formal, such as commercial banks, microfinance banks, the Nigeria Agricultural and Cooperative Rural Development Bank (NACRDB), and state government-owned credit institutions; (b) semiformal, such as nongovernmental organizations-microfinance institutions (NGO-MFIs) and cooperative societies; and (c) informal, such as money lenders, and rotating savings and credit associations (RoSCAs). Enhancing Financial Innovation and Access (EFInA) (2008) notes that 23 percent of the adult population in Nigeria has access to formal financial institutions, 24 percent to informal financial services, while 53 percent are financially excluded.

Methodology

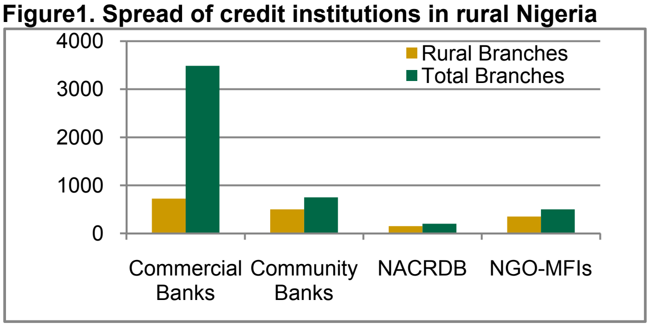
The study is based on a review of literature, complemented by interviews with key informants and focus group discussions (FGDs) to generate quantitative and qualitative data to validate the findings from the literature. The key informants included officials of the Small and Medium Enterprise (SME) Unit of the Central Bank of Nigeria (CBN), Abuja Cooperative Federation (ABCOF), and RoSCAs. Two FGDs were conducted with male and female small-scale farmers in Lafia, Nassarawa State.

Results

Small-scale farmers' access to credit institutions

The ratio of rural branches to total branches of formal credit institutions is low compared to informal and semiformal institutions (Figure 1) and this constitutes a limitation of small-scale farmers' credit access in Nigeria. Okojie *et al* (2010) report that the poor have limited access to financial services, and that the main source of finance for the majority of rural women in Edo state is their contribution to the savings/market associations. This is further corroborated by EFInA (2008) which reports that 24 percent of the adult population in Nigeria has access to informal financial services while 53 percent are financially excluded. The FGDs revealed that friends and relatives are the most important sources of credit to the farmers followed by cooperatives and NGO-MFIs while formal institutions such as banks were not accessible to the respondents.

Figure1. Spread of credit institutions in rural Nigeria



Source: World Bank, 2008

Conditions for extending credit to customers

Access conditions vary from one credit institution to another (Table 1). Informal credit institutions such as RoSCAs and cooperative societies, as well as formal credit institutions, provide credit on the basis of membership deposit. The interviews with key informants confirmed that lending by RoSCAs and cooperatives are deposit-based and make use of peer collateral in ensuring repayment, while CBN's guaranteed loans through commercial banks require customers to have an account with the commercial bank and tangible or intangible collateral security.

The traditional credit providers (i.e., money lenders) usually do not require a deposit relationship, which may be responsible for the high interest charged, as no collateral is required (Ben-Yami n.d.; Okojie *et al* 2010; and World Bank 2008).

Credit available to small-scale farmers

It is estimated that only 2.5 percent of total Commercial Bank loans and advances is directed at agriculture (CBN 2008). The average loan size granted by microfinance institutions as reported by Anyanwu (2004) was ₦8, 800. Loan amounts ranged between ₦5, 000 and ₦13, 762. This is close to the ₦8, 206.90 reported by the CBN (2005) as the average loan size granted by NGO-MFIs. Oke *et al* (2007) found that the average loan size from NGO-MFIs institutions to farmers in southwest Nigeria was ₦23, 551.25, while actual loan amounts ranged from ₦5, 000 to ₦90, 000.

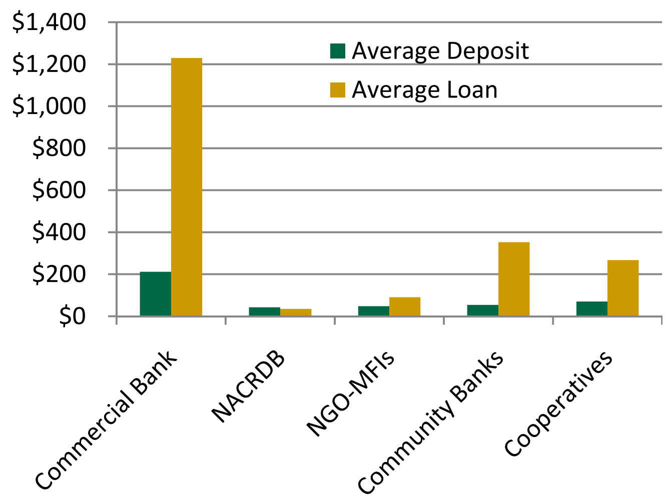
Table 1. Conditions for lending among credit institutions

Type of institutions	Credit institutions	Conditions for lending
Formal	Commercial banks	Deposit-based Strict and complex rules Physical collateral
Formal	Microfinance banks	Deposit-based Simpler rules Physical collateral
Formal	NACRDB	Deposit-based Flexible rules Peer collateral
Semiformal	NGO-MFIs	Deposit-based Flexible rules Peer collateral
Semiformal	Cooperatives	Deposit-based Flexible rules Peer collateral
Informal	RoSCAs	Deposit-based Informal rules Peer collateral
Informal	Money lenders	Non-deposit-based Informal rules Informal collateral

Source: Generated by author from interviews with key informants

Interviews with the key informants revealed that the maximum funds available for small-scale farmers from RoSCAs vary from time to time and is dependent on the membership strength and the total contribution by the group at that particular time. This situation is similar with cooperative societies where members are entitled to borrow double the size of their savings. However, the maximum available credit under the ACGS without tangible security is ₦20, 000, while it is ₦10, 000,000 if tangible security is provided. This further confirms the findings from literature with respect to the maximum available credit from formal institutions (Figure 2).

`Figure 2. Average deposits and loans granted to all categories of customers by credit institutions in Kaduna



Source: World Bank, 2008

Affordability of credit to small-scale farmers

One of the principal characteristics of informal credit as stated by Okojie et al (2010), and Anyanwu (2004) is the higher interest rates imposed on loans relative to those by the formal banking sector. But this applies more to the informal credit institution (money lenders). Credit from cooperative societies generally attracts interest rates of less than 10 percent, while for some informal institutions such as RoSCAs no interest is charged.

The average loan repayment rate is as high as 89.7 percent for NGO-MFIs (Oke *et al* 2007). However, loan default with respect to subsidized public credit from a formal institution (NACRDB) accessed by farmers in southwest Nigeria was 77 percent (Adejobi and Atobatele 2008). It is asserted that most of the defaults arose from poor management procedures, loan diversion, and unwillingness on the part of some clients to repay loans (Oladeebo and Oladeebo 2008). Siebel (2004) stated that loan repayment rates among RoSCAs are generally high even when linked to semiformal and formal sources of credit, and they are also more sustainable because they adhere to the indigenous principles of self-reliance, viability, sustainability, and outreach. Public credit is subsidized and therefore attracts a low interest rate. Ironically, its repayment rate is low as borrowers erroneously believe that credit from the government is not supposed to be repaid (CBN 2005 and Ben-Yami n.d.). The FGDs highlighted that the terms and conditions of repayment of public credit are not often well spelt out, and as a result, they are often mistaken for grants. FGDs also revealed that when the respondents had access to credit from cooperatives and NGO-MFIs, repayment rate was generally high, with women being more committed to the payment. Using repayment rate as a measure of credit affordability, one can conclude that credit channeled through informal and semiformal avenues is likely to be repaid.

Factors limiting access to credit

According to Okojie et al (2010), the lack of bank accounts, collateral, and information regarding the procedure for accessing credits from banks limit rural women's access to credit from formal institutions. Adejobi and Atobatele (2008) suggested that loan default could limit access to credit, while Agnet (2004) opined that the complex mechanism of commercial banking is least understood by the small-scale farmers, and thus, limits their access. Rahji and Fakayode (2009) blamed the limitation on imperfect and costly information problems encountered in the financial markets; credit rationing policy; and banks' perception of agricultural credit as a highly risky venture; while Philip *et al* (2009) stated that high interest rate and the short-term nature of loans with fixed repayment periods do not suit annual cropping, and thus constitute a hindrance to credit access. Oji (n.d.) mentioned the location of banks in urban centers as a limiting factor, among others earlier mentioned. Adegbite (2009), citing Ezike (1984), Nweke and Onyia (2001), and Kodieche (2002), stated that financial lending Institutions in Nigeria often shy away from giving loans to farmers because of the high cost of administering such loans and the perceived high default rates among farmers.

An interview with the ACGS Fund desk of the SME Unit of CBN suggested that small-scale farmers' low access to credit institutions is due to the requirement for collateral and the perceived high risk and uncertainty of agricultural production. An interview with a cooperative official corroborated the notion that unstable markets tied to uncertain harvests increased lenders' perceptions of risk in lending to small-scale farmers. Other interviews suggested that credit is misallocated to nonintended beneficiaries in government-backed credit programs. FGD indicated that loan default ranks highest among the factors limiting small-scale farmers' access to credit, followed by high interest rates, poor credit information, and poor market structure, which impedes the sales of farm produce.

Impact of credit on small-scale farmers' holdings

Quantitatively demonstrating the impact of credit on small-scale farmers is often very difficult because it is difficult to capture and analyze all of its benefits (Accion International n.d.). However, Okojie et al (2010), in an interview with self-employed women in Edo State, found that microcredit has had positive impacts on the businesses and family life of rural dwellers that have had access to NGO-MFIs. Feijo (2001) also found that there was a positive impact on the lives of farmers who benefited from the credit facilities of the Program to Support Family Farming (PRONAF) in Brazil, based on the measurement of productivity growth of their main crops. Oyeyinka and Bolarinwa (2009), studying the impact on beneficiaries and nonbeneficiaries of the NACRDB smallholder loan scheme in Oyo State, found that yield, income, and access to improved farm inputs of beneficiaries were higher compared to that of nonbeneficiaries. Other impacts included improvements in facilitating economic transactions, managing day-to-day resources, accessing services that improve quality of life, protecting against economic vulnerability, making productivity-enhancing investments, and leveraging assets. Finally, participants in the FGD posited that timely credit provision facilitates the timely acquisition of farm inputs, which help farmers improve their livelihood.

Conclusion

It may be concluded that small-scale farmers have relatively more access to informal and semiformal credit institutions than to formal credit institutions, in spite of the higher volume of credit at the disposal of formal institutions. In addition, the high repayment rate of loans recorded by informal and semiformal institutions could indicate that the loans are granted at affordable rates to the small-scale farmers and that subsidization may not be necessary. It was also found that access to credit is likely to help improve the well-being of the beneficiaries.

In view of the above findings, the following is recommended:

- Assessing the potential ability of traditional institutions to provide credit in the absence of collateral could help improve access.
- Supporting facilitation of the transfer of credit from formal institutions through MFIs to small-scale farmers could help improve access and repayment rates. Developing awareness of agricultural insurance among small-scale farmers and strengthening the ability of agricultural insurance institutions to carry out their mandates will lower the risk faced by financial institutions in lending to small-scale farmers.
- There is a need for further research into the determinants of access to or exclusion from financial services in Nigeria, as well as the efficiency of policy instruments such as ACGS and ACSS in improving farmers' access to credit.

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