Agricultural Sector Development: Problems and Issues

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Agriculture is by far the most important sector for Pakistan's economy. The forward and backward linkages to the rest of the domestic economy, to the international trade and with poverty alleviation are very strong. A bad year for agriculture due to drought or other natural calamities has extremely adverse effect on GDP growth, living standards of the population, price level, exportable surplus and balance of payments. Thus the dichotomy of agriculture vs. industry or services sectors is totally false as agriculture forms the backbone of the whole economy.

We should be grateful to our uneducated and illiterate farmers who have transformed this country of 140 million population from a deficit to a surplus country. Very few developing countries have been able to achieve a sustained growth rate of 4 percent for agriculture sector and Pakistan is one of them. No doubt we have to further improve and enhance our productivity in this sector but we should be proud of the contribution the farming community has made to the country's economy.

I would like to focus this morning on the measures the State of Pakistan has taken to accelerate flows of credit to this sector.

First, unlike other sectors of the economy agriculture credit is regularly supervised by the SBP. Targets are assigned to ADBP and to commercial banks and those who fail to meet these targets are taken to task. Agriculture Credit Advisory Committee meets every six months and carries out reviews and resolves issues pertaining to agriculture credit delivery.

Second, ADBP was provided a special line of credit for agriculture by SBP at a subsidized rate of 6% which it lent to farmers at the rate of 14% thus earning differential of 8%. There has been gross misuse of this subsidized financing and the loan portfolio of ADBP is full of stuck-up and non-performing loans. It is not pricing but access to credit which is the constraint for the small and medium farmers. Recently the lending rate to ADBP has been aligned with the T-bill rate but in effect agriculture credit still receives a preferential rate compared to other sectors.

Third, the end-use funding cost to farmers is still quite high despite this lower interest rate credit provided to ADBP. This is due to inefficiencies, high administrative costs and provisioning of bad debts. The administrative cost alone is about 4% due to inadequate capital base, poor asset quality, weak internal controls and infected loan portfolio. We are therefore embarked upon a major restructuring of the ADBP. A new Board of Directors consisting of private sector representatives well versed in farming from all the four provinces has been formed recently and empowered to carry out the badly needed reforms. A Portfolio audit is also underway to ascertain the current status of the ADBPs portfolio and then take remedial measures.

Fourth, the private banks have also been encouraged to get involved in extending credit to agriculture sector either directly or through syndication with other banks or through on-lending to ADBP, Rural Support Organization and UNGOs. I am pleased to report that at least Rs 2.5 billion has been disbursed by these banks in the first year of their credit operations to support agriculture sector.

Fifth, commodity financing which was so far the exclusive domain of the public sector has been opened up to the private sector. The same rate of financing – 12% p.a. – which is available to the public sector is also allowed to the private sector despite the higher risk inherent in the latter mode. But initially we have to provide a level playing field to the private sector operators so that they can penetrate into this market and compete with the public sector procurement agencies. We hope that this competition will ensure remunerative prices to producers.

Sixth, one of the main issues confronting the farmers today is that prices of their commodities do plunge immediately after the harvest. There are no facilities for on-farm or off-farm storage like other countries where the farmers can deposit their produce and pay a rental. They will then withdraw and sell only limited quantities at prices acceptable to them. This saves them from making distress sale at lower than announced support prices in the post-harvest period. For this purpose, the SBP has allowed private sector to obtain financing from commercial banks at a preferred rate of interest i.e. 12 percent.

Seventh, the Export promotion policy has identified seven thrust areas of development exports. Three of these areas are the output of agriculture sector i.e. Fruits and Vegetables, Fisheries and Livestock products. Special incentives and financing are available to the producers, processors and exporters of these commodities.

Eighth, the SBP has established a regulatory and legal framework for Micro Credit Sector development in the country. Khushali Bank has set up branches in 30 cities and its recovery rate is 98 percent. The first private sector bank in this sector – First Micro Finance Bank – has also started functioning under the sponsorship of Aga Khan Development Network.

Ninth, the SBP has advised the commercial banks to extend financing to the newly emerging Corporate Farms I would like to clarify that these farms will not displace the small and medium farmers but will make use of new technology, best practices, economies of scale to boost productivity. We hope that these practices will then be adopted by small and medium farmers enhancing the overall productivity of agriculture sector.

Tenth, we still are not fully satisfied with access to credit by the rural communities for all their needs – farming and non-farming. Cooperative banks have ceased to be an effective instrument. The SBP has therefore appointed a Committee on Rural Finance to come up with comprehensive recommendations to improve the access and delivery of rural finances.

Finally and most important the SBP has expanded the scope and coverage of agriculture credit to make it attractive for commercial banks to lend to the farming community. I will dwell on these steps in some detail.

(a) The entire value chain of agriculture – from inputs, equipment, machinery and implements, production, storage, marketing, transport, processing to distribution, has become eligible under the supervised agriculture credit scheme.

(b) All fresh credit lines to ADBP and Cooperatives are to be priced at the minimum average rate on T-bills. The prime objective of market-based interest rates is to encourage commercial banks to lend their funds to ADBP. In the long-run, greater competition amongst banks in terms of lending to agriculture should bring down lending rates.

(c) In the past commercial banks were not allowed to lend outside their narrow territorial area that was specified by SBP. In certain cases, this provided banks with an excuse not to lend. The removal of this rule should enable commercial banks to lend on purely commercial basis. More importantly, this will also give farmers the option to choose the bank of their choice.

(d) In order to improve credit flows to farmers, SBP has allowed them the facility of revolving credit which means even if farmers are unable to adjust their previous loans fully, they can still avail fresh credit. Earlier, banks were only allowed to sanction credit to farmers who repaid their previous loans fully and on time. It is hoped that will help improve farmers' ability to meet their credit needs.

(e) To facilitate commercial banks meeting their mandatory targets, they are now allowed to count their equity stake in corporate farms as part of their lending. They can also include lending to micro credit institutions, recognized NGOs and Rural Support Organizations. Most importantly, however, commercial banks can also use their lending to ADBP as part of their mandatory targets.

(f) The limit on credit against personal securities has also been raised from Rs 50,000 to Rs 100,000. This should help those farmers with limited access to collateral.

(g) We have added 45 new items to the list of items eligible for agriculture finance. For example, diesel oil for tractor, production loan for minor crops, fixed capital for storage of raw agriculture / farm produce and reclamation of land etc.

Apart from these measures, SBP has also revised the methodology used for estimating agriculture credit needs by provinces. More than 45 items or activities have been added to this list.

In the end, I would like to wish the Conference the best of luck in your deliberations and hope that you will come up with practicable and workable recommendations. I can assure you, on my part, that the SBP will take these recommendations seriously.