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CREDIT DELIVERY TO PHILIPPINE RURAL ENTERPRISES:

ISSUES AND POLICY FRAMEWORK

by

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I. INTRODUCTION

The current Philippine development plan has as a principal component an agriculture and rural-based and employment-oriented development strategy. Throughout the postwar years, the bias has been in favor of import substitution, and later an export-led growth strategy. The economic and financial crisis of 1983 drove home a painful lesson: that in the absence of a determined and sustained effort to increase rural incomes and reduce poverty and income inequality in the countryside, the urban-biased and industry-cum-export-oriented strategy would fail. And fail it did as the economy registered negative growth for the first time in history.

A number of reforms have been introduced to remove the bias against agriculture and rural development. Tax and tariff reforms, a more realistic exchange rate, and the dismantling of the monopolies over sugar and coconut trading and grain importation were pursued. More serious attention to job creation in the countryside is now foremost in the minds of policymakers. It is in this context that a discussion of rural enterprises is relevant. While different studies (Fabella, 1987; Ranis and Stewart, 1987; Anderson and Khambata, 1981) have considered various facets of rural/small enterprises, like their linkage with general agricultural productivity, their employment creation potential and contribution to output, there seems to be a dearth of studies on the financial requirements of small/rural enterprises and how they cope with financial constraints (Lamberte and Llanto, 1987).

There is very little understanding, for example, of how financial liberalization has affected the access of these enterprises to institutional credit.[1/] In Indonesia, McLeod (1984) noted that small enterprises face a wide array of sources of finance but access to these financing alternatives depends on their track record and maturity.

The objective of this paper is to shed some light on the financial issues affecting rural enterprises in order to be able to draw out some implications for financial policy. In particular, it looks into the credit delivery system for rural enterprises.

This paper consists of four parts. The first part (Section 2) presents information on the contribution of rural enterprises (rural non-farm activities) to employment creation. This is largely based on data from <u>The Integrated Survey of Households Bulletin</u> of the National Statistics Office (formerly, the National Census and Statistics Office) which were used by Fabella (1987). The second part (Section 3) discusses the dimensions of credit delivery to rural enterprises. It looks into the financial resources available in the rural areas, the density ratios of financial institutions in different regions and the access of rural enterprises to these resources. Some fragmentary evidence on their access to formal loans and guarantees is also presented. Section 4 considers the financial policy framework affecting rural enterprises while the last part (Section 5) discusses two approaches to provide financial services to rural enterprises which are currently pursued in the Philippines.

II. EMPLOYMENT CREATION BY RURAL ENTERPRISES

The unemployment rate in the Philippines is high. Mangahas (1986) reports an open unemployment rate of about 13 percent while underemployment is approximately 20 to 30 percent. This is an acute problem and it has influenced the government's decision to seriously consider a development strategy which can provide jobs to a rapidly expanding labor force.

Part of this strategy is the recognition of the role of rural enterprises in providing employment and generating output. It is held that these rural enterprises could very well be strategic vehicles for rural employment creation and, thus, important instruments to reduce poverty and inequality.[2/] Available data (third quarter of 1982) show the importance of the rural non-agricultural sector[3/] in rural labor absorption.

Rural off-farm (non-farm) enterprises account for as much as 30 percent of total rural employment for both sexes in 1977. By 1982 the share had increased to 32 percent.

The share of employment for females in rural enterprises was on the average 48 percent between 1977 and 1982; for males this was about 23.6 percent. The relatively large share of rural

Table 1: PERCENTAGE SHARE OF AGRICULTURAL AND NON-AGRICULTURAL SECTORS IN TOTAL RURAL EMPLOYMENT, THIRD QUARTER OF 1977 AND 1982

	Both Sexes		Male		Female	
Year	Agri	Non-Agri	Agri	Non-Agri	Agri	Non-Agri
1982	68.1	31.9	75.3	24.7	52.7	47.3
1977	70.2	29.8	77.5	22.5	51.3	48.7

Source: Integrated Survey of Households Bulletin, Nos. 48 and 51.

enterprises in total rural employment is partly explained by the fact that the reference quarter (July, August and September) represents a period when agricultural activity slows down[4] and the rural population gravitates towards the rural non-agricultural sector.

Nevertheless, this is indicative of the significance of rural enterprises not only as a source of additional income but also as a provider of rural jobs.

Table 2 gives the relative importance of rural enterprises in the employment of the labor force. They were able to absorb more than 20 percent of total labor in the periods cited. The labor absorption of males is higher than that of females in both periods.

Table 2: PERCENTAGE SHARE OF RURAL ENTERPRISES (RES) IN TOTAL LABOR FORCE EMPLOYED, THIRD QUARTER 1977 AND 1982

RES	Both Sexes	Male	Female
1982	22.5	11.8	10.7
1977	20.2	11.0	9.9

Source: The Integrated Survey of Household Bulletins, Nos.48 and 51.

If we look at the distribution of employed persons in rural enterprises classified by the different industry groups, we note that the community, social and personal services category has a 10 percent share followed by wholesale and retail trade (7.8 percent), manufacturing (7.0 percent), transportation, storage and communication (3.2 percent), construction (2.7 percent) and others (mining and quarrying, electricity, gas and water and other services) with 1.4 percent share (Table 3).

The available evidence points to the significance of rural enterprises in absorbing rural labor which could have spilled over into and exerted tremendous pressure against the urban job markets. We also emphasize their contribution to the rural household's income, most especially during slack periods. However, it should be noted that the rural enterprise's own objective function is not employment creation per se but the creation of more output and wealth which at the same time reduces mass poverty and income inequality.

Table 3: PERCENTAGE DISTRIBUTION OF EMPLOYED PERSONS IN THE RURAL AREAS BY MAJOR INDUSTRY GROUP, THIRD QUARTER 1982

Industry Group	Employed Persons in Rural Areas (Total Percent)
Rural Workers	100.0
(a) Agriculture	68.0
(b) Non-Agriculture	32.0
- Community, Social & personal	9.9
- Wholesale and retail trade	7.8
- Manufacturing	7.0
- Transportation, Storage and Communication	3.2
- Construction	2.7
- Others	1.4

Source: The Integrated Survey of Household Bulletin, Third Quarter 1982

III. DIMENSIONS OF CREDIT DELIVERY TO RURAL ENTERPRISES

Credit for rural enterprises has several dimensions. We concentrate only on three important aspects, namely: (a) the rural credit delivery system, (b) bank resources together with savings mobilized in the rural areas, and (c) access of rural enterprises to formal credit. Unless otherwise indicated, we use in this section data collected from Central Bank statistics by a group of consultants[5/] who prepared a study on the strategies for the expansion of banking services in the rural areas.

The rural credit delivery system is composed of two broad categories: (a) formal institutions (mostly banks) and (b) informal credit sources (mostly moneylenders). The former are composed chiefly of the rural banks, private development banks, thrift banks and the commercial banks. The latter category consists of individual moneylenders like grain traders and input suppliers, the pawnshops, cooperatives and credit unions. This category will not be treated for lack of aggregative data.

Credit Delivery System

At the end of 1986, the country had a total of 5,946 offices of banks, non-bank financial intermediaries (NBFI) and non-bank thrift institutions (NBTI) of which 3,698 or 62.2 percent operated in rural areas. Banks made up approximately 60.2 percent of these financial offices. About 69.6 percent of the total banks operated in the rural areas (Table 4).

The national density ratio defined as the ratio of the total number of financial offices to the total number of municipalities and cities was about 3.7 in 1986 and 3.3 in 1981. In the rural areas, it was 2.3 in 1986 and 2.1 in 1981. While these may seem to be acceptable ratios, it must be noted that the banks are not uniformly and equally distributed across regions. There is a high percentage of municipalities in some regions without banks, especially in Western Mindanao (76 percent), Eastern Visayas (67 percent) and Central Mindanao (63 percent). On the average about 41.5 percent of all municipalities are without banks (Table 5).

Bank Resources in the Rural Areas

The rural areas have on the average only 16 percent of total bank financial resources (1983-1986) while Metro Manila has 84 percent. In absolute terms, bank resources in rural areas have not significantly risen in this period, averaging ₱56.1 billion. As of end of 1986, 9.1 percent were in Luzon, 5.6 percent in the Visayas and only 3.8 percent in Mindanao, for a total 18.5 percent share of rural areas in total resources.

Rural banks have most of their resources in the rural areas (98 percent), while thrift banks (composed of private development banks, savings and mortgage banks and savings and loans associations) have 34.2 percent. Commercial banks have 15.5 percent of their resources in the rural areas.

With respect to savings, approximately 27 percent have been mobilized by the banking system in the rural areas from 1983 to 1986. The rest, about 73 percent, have been mobilized in Metro Manila (Table 6). Commercial banks were able to absorb 79.4 percent of total rural savings as of end of 1986, while rural banks mobilized only 7.1 percent, thrift banks, 11.3 percent and specialized government banks, 2.2 percent.

Access of Rural Enterprises to Formal Credit

There is no direct evidence concerning the access of rural enterprises to formal (bank) credit and this represents an information and research gap. Nevertheless, we present in this

Table 4: DENSITY RATIOS OF FINANCIAL OFFICES TO TOTAL MUNICIPALITIES AND CITIES, PER REGION
As of end of 1986

Region	Banks	NBFI	NBTI	Total No. of Financial Offices	Total No. of Municipalities & Cities	Density 1986	Ratio[a] 1981
I - Ilocos	270	74	3	347	176	2.0	1.9
II - Cagayan Valley	108	22	-	130	116	1.1	1.2
III - Central Luzon	393	279	3	675	121	5.6	4.5
IV - Metro Manila	1,089	1,098	61	2,248	17	132.2	111.7
IVa - Southern Tagalog	511	321	4	836	221	3.8	2.8
V - Bicol	146	43	1	190	115	1.7	1.7
VI - Western Visayas	254	123	2	379	130	2.9	2.9
VII - Central Visayas	216	113	3	332	132	2.5	2.3
VIII- Eastern Visayas	90	27	-	117	142	0.8	0.7
IX - Western Mindanao	73	35	1	109	103	1.1	1.1
X - Northern Mindanao	163	46	1	210	122	1.7	1.6
XI - Southern Mindanao	182	78	1	261	85	3.1	3.1
XII - Central Mindanao	85	25	2	112	121	0.9	0.9
Total Philippines	3,580	2,284	82	5,946	1,601	3.7	3.3
Total Rural (Excluding Metro Manila)	2,491	1,186	21	3,698	1,584	2.3	2.1

[a] Density Ratio = $\frac{\text{Total No. of Financial Offices}}{\text{Total No. of Municipalities and Cities}}$

NBFI refers to - Non Bank Financial Institutions
NBTI refers to - Non Bank Thrift Institutions

Source: Central Bank of the Philippines

Table 5: PHILIPPINE BANKING SYSTEM'S GEOGRAPHICAL COVERAGE AS OF END OF 1986

Region	Total No. of Municipalities	% of Municipalities Without Banks
I - Ilocos	176	35.8
II - Cagayan Valley	116	50.8
III - Central Luzon	121	8.3
IV - Metro Manila	17	0.0
IVa - Southern Tagalog	221	23.1
V - Bicol	115	41.7
VI - Western Visayas	130	20.6
VII - Central Visayas	132	40.9
VIII - Eastern Visayas	142	66.9
IX - Western Mindanao	103	75.7
X - Northern Mindanao	122	52.8
XI - Southern Mindanao	85	40.7
XII - Central Mindanao	121	62.6
Total Philippines	1,601	41.0
Total Rural (excluding NCR)	1,584	41.5

Source: Central Bank of the Philippines.

Table 6: SAVINGS MOBILIZED BY THE BANKING SYSTEM END OF YEARS, 1981-1986 (₱ Million)

Year	Total Savings Mobilized	Savings Mobilized in MetroManila	Savings Mobilized in Rural Areas	% Share in Rural Areas
1986	164,277	112,829	51,448	31.3
1985	163,418	120,277	43,141	26.4
1984	146,442	109,100	37,342	25.5
1983	136,304	102,365	33,939	24.9
1982	113,385	a/	a/	
1981	115,540	88,966	26,574	23.0
Compounded Yearly Growth Rate (%)	8.4	5.4	18.7	

a/ not available.

Table 7: LOANS OUTSTANDING OF THE BANKING SYSTEM IN RURAL AREAS END OF YEAR, 1981-1986 (₱ Million)

Year	Loans Outstanding in Rural Areas	Loans Outstanding in Agriculture	Loans Outstanding in Non-Agri Sectors	% Share of Agriculture
1986	24,420	15,634	8,786	64.0
1985	18,385	16,867	1,518	91.7
1984	27,400	20,250	7,150	73.9
1983	29,665	27,728	1,937	93.5
1982	n.a.	24,075	n.a.	n.a.
1981	24,647	21,466	3,181	87.1

a/ The extreme year-to-date variation is suspicious so the data should be taken with caution.

Source: Central Bank of the Philippines

sub-section indirect information on rural enterprise availment of bank credit.

The indirect evidence is given by the amount of loans granted and outstanding in the non-agricultural sector in the rural areas. Only data on outstanding loans are available at this point and are reported in Table 7. The bulk of the loans outstanding in the rural areas are loans for agriculture. Those given for the non-agricultural sector presumably are those for the first three rural major industry groups cited in Table 3 above. They received an average of 20 percent during the period.

Another way of assessing the access to credit by rural enterprises is to analyze the loan portfolios of the financial institutions principally involved in countryside lending. These are the rural banks[6/] whose major clients are farmers, merchants, cooperatives and other rural-based borrowers. The data for rural banks for the last five years show a concentration in agricultural loans (about 84.3 percent of total loans) with the balance going to commercial and industrial loans (Table 8).

Table 8: OUTSTANDING LOANS OF RURAL BANKS, BY TYPE
END OF YEAR, 1981 TO 1986
(₱ Million)

Year	Total	Sector: Agri	Comm'l	Ind'l	Others	% Agri-cultural
1986	6,790.5	5,471.7	566.6	187.7	564.4	80.1
1985	6,636.4	5,555.8	449.0	160.5	471.1	83.7
1984	7,022.5	6,039.9	443.9	197.2	341.5	86.0
1983	7,648.0	6,514.9	484.6	226.8	421.7	85.2
1982	6,668.8	5,770.3	383.9	208.0	306.6	86.5
1981	5,485.6	4,662.5	269.9	359.2	194.0	85.0

Source: Central Bank of the Philippines, Rural Banking System in the Philippines 1981- 1986.

Presumably the latter category consists of loans to rural non-agricultural enterprises. The agricultural loans were largely for crop loans (57 percent), mostly production credits for palay, fruits and vegetables, sugarcane and coconuts. Non-crop loans are principally for livestock and poultry, fishing and swine. The data show a strong bias for production-oriented credit despite the fact that post-harvest operations such as processing, storage and marketing are important economic activities which require financing.

The impression one obtains from the aggregate data is that the rural areas are net savers, since the share of savings mobilized (averaging 27 percent) is greater than the share of lending in rural areas (averaging 18 percent); therefore rural areas are net suppliers of funds for urban-based projects. Given this situation, the rural enterprises may not be able to avail of all the credit they require[7/] since the bank resources flow out of the rural areas and are used by urban-based enterprises.

This may be too facile a conclusion, however, because the rural deposits may "flow out" in search of a higher marginal return that urban-based projects may be able to provide. Furthermore, the resource outflow may also be due to the lack of effective demand in rural areas.

On the other hand, some loans intended for agricultural projects and rural-based borrowers are actually booked in Metro Manila (80 percent as of end-1986) so are included in Metro Manila statistics. The practice seems to be to book a loan, whether for an agricultural or a non-agricultural project, a rural or urban borrower, in Metro Manila or other commercial centers like Cebu City and Iloilo City because the head offices of the banks are located there where the loan transactions are consummated.

Nevertheless, there seems to be no hard information on the real status of the access of rural enterprises to bank credit and the statements made in this sub-section should be taken as tentative.

IV. FINANCIAL POLICY ENVIRONMENT

The policy environment affecting rural enterprises covers a wide ground and is a large subject to tackle. Thus, we concentrate our discussion on the financial policy environment affecting the overall enterprise.

The general impression is that rural enterprises have limited access to institutional finance. It seems that most of these rural enterprises provide their own start-up and later working capital. Anderson and Khambata (1981) reported that in a 1978 survey of 80 small scale enterprises, composed of household and manufacturing establishments with over 20 workers, the majority of the respondents stated that they used their own savings to start the business. Only 5 percent availed of institutional sources. Some borrowed from friends and relatives.

In the case of small manufacturing enterprises, a 1977 survey undertaken by the National Cottage Industries Development Authority in Ilocos, Philippines showed that 22 percent of rural households obtained loans from the financial institutions; 65 percent financed their own investments and the other 13 percent used informal sources, including NACIDA itself (Anderson and Khambata, 1981).

Other observers (e.g. Meyer, 1988) have noted that these types of enterprises receive little credit from formal institutions and self-finance most of their working capital, while informal lenders provide them with short-term loans at interest rates higher than normal bank rates.

On the assumption that it is the availability rather than the cost of credit that matters, a possible difficulty with informal sources is their limited capacity to sustain the recurrent needs of this clientele. Hiemenz and Bruch (1982) stressed that informal loans are usually given in small amounts and have short pay-off periods. Added to these is the limited capacity of informal sources for local savings mobilization, refinancing and term transformation. This indicates that formal finance may become a critical factor as the rural enterprise evolves into a more sophisticated user of funds and producer of goods and services, and requires greater access to bank resources. This suggests a process of evolution or maturation so that at a particular point of time a rural enterprise may need more formal relative to informal credit.

It is argued here that the lack of formal credit is not necessarily symptomatic of capital market distortion "which penalizes small enterprises" (Little, 1987). Rather it could be interpreted as a "filter that eliminates the dishonest, the incompetent" (ibid.) and the non-viable loan applicants.

The upshot in this case is not a problem of lack of formal credit per se but the lack of readiness or "maturing" of rural enterprises for formal credit.[8/]

The implication is that the barriers to the access to formal credit must be overcome. Barriers from within the rural enterprise which render it less creditworthy must be removed. These bottlenecks include lack of management and technical expertise, inexperience of personnel, weak product line and distribution system, and their small asset base.

Barriers from without the rural enterprise may consist of financial and economic policies at the macro level which determine the operation and growth of the capital market and the efficiency of financial intermediation. Financial reforms which reduce the intermediation cost and stimulate financial deepening and capital market efficiency will be needed. At the same time, policies that provide ample access to electric power, markets and land would strengthen the competitiveness of rural enterprises. The provision of infrastructure, water and basic economic services in the rural areas all serve to increase the creditworthiness of the rural sector.

At the micro level of both banks and rural enterprises, the most significant wedge that frustrates financial transactions refers to transaction costs. These costs can arise from both the characteristics of rural enterprises and the unfamiliarity of banks with lending to them. Cuevas and Meyer (1988), reporting upon research in progress, identify the importance of borrowing transaction costs as a determinant of loan demand in rural areas. They hold the view that the more significant price signal to rural borrowers seems to be the transaction costs involved rather than the explicit interest rate charged.

On the bank side transaction costs have two components: (a) administrative costs and (b) the cost of default risk. Administrative costs refer to the screening, evaluation, processing and delivery of loans. The perception of default risk is increased when banks feel that a given rural enterprise is not viable and creditworthy. Provision for probable loan losses and actual bad debts must be made to cover the cost of default risk.

V. PROGRAMS OR MARKETS[9/]

Two different strategies to provide financial services to rural enterprises are currently pursued in the Philippines: (a) the "financial markets approach" and (b) the "program approach". The first relies on the marketplace to provide the financial services and makes use of a government-sponsored and funded guarantee scheme to reduce lending and default risks for rural enterprises. Under this strategy, the banks screen, process, approve and deliver loans under a guarantee cover provided by one of several guarantee programs of the government. In the case of a rural enterprise, the concerned guarantee agency is the Guarantee Fund for Small and Medium Enterprises (GFSME).

Through the guarantee cover the GFSME assumes a maximum of 85 percent of the default risks (see Table 9 for the features).

If the borrower defaults on his loan, the bank calls on the guarantee and GFSME pays 85 percent of the outstanding loan amount. The distribution of loan guarantees is summarized in Table 10.

From loan guarantees to 27 projects in June 1985 amounting to ₱80.3 million, the guarantees grew to a total of 229 involving ₱433.8 million by October 1987. Note that this growth was achieved in just over two years of operation.

The second approach targets specific institutions or clients and usually provides credit subsidies to the end-borrower and the loan conduits. A good example of the program approach is the government's Agro-Industrial Technology Transfer Program (AITTP) established in 1984. Table 9 summarizes the various dimensions of this program and Table 11 summarizes lending under the program. It is observed that from a total 30 borrowers as of 1985 involving ₱236.1 million, the number of borrowers decreased to only 15 and loans granted to ₱67.2 million as of 1987. However, the program seems to have recovered by March 1988.

While this is not the occasion to evaluate the relative merits of the two strategies, although certainly it is needed, we note some of the issues and implications raised by these strategies in the context of our earlier discussion of rural enterprises.

1. Which approach provides rural enterprises better access to bank resources?
2. What are the social and private costs involved?
3. Which strategy better supports the objective of raising rural incomes and reducing wealth inequalities? Who are the <u>real</u> gainers or beneficiaries?

Table 9: PROFILE OF THE AGRO-INDUSTRIAL TECHNOLOGY TRANSFER PROGRAM (AITTP) AND THE GUARANTEE FUND FOR SMALL AND MEDIUM ENTERPRISES (GFSME) AS OF MARCH 1988

	AITTP	GFSME
Source of Fund	OECF of Japan	National Livelihood Support Fund and CALF for the guarantee cover; Accredited Bank's own funds for lending.
Major Objective	To strengthen the agricultural sector by facilitating the transfer of technology for production and fer of technology processing; developing domestic and export markets; and generating livelihood opportunities for the rural sector.	To help develop the small and medium enterprises sector; to encourage banks to lend to small and medium enterprises using their own funds.
Date/Year Implemented	1984	February 1984
Area(s) of Implementation	Nationwide	Nationwide
Implementing Agencies/Trustee Bank	TLRC/DBP	GFSME/CBP
Lending Channels (if any)	None	Accredited banks

Lending Terms and Conditions:		
Loan Purpose	Acquisition of fixed assets and provision for working capital.	Acquisition of fixed assets; construction of plant facilities; working capital; and payment of existing obligations that are current in status.
Eligible Borrowers	Producers/processors of agri-or aqua-based projects.	Individuals/Enterprises/ Filipino stock corporation with small or medium scale projects engaged in direct production and/or processing of food up to one level of backward or forward integration or linkage.
Loan Ceiling	P21 Million	P8 Million
Security/ Collateral Requirements	Land; land improvements; building; and chattels	Project assets and joint and several signatures of the partners/members or principal stockholders of the corporate borrowers.
Maturity	5 to 15 years inclusive of 1 to 5 years graced period.	5 to 10 years (inclusive of 1 to 2 grace period) depending on purpose of loan.
Interest Rate (% p.a.)	8.75	Varying
Service Charge/ Other Fees	3% of total loan	Origination fee, guarantee and other charges

OECF - Overseas Economic Cooperation Fund
CALF - Comprehensive Agricultural Loan Fund
TLRC - Technology and Livelihood Resource Center
DBP - Development Bank of the Philippines
CBP - Central Bank of the Philippines
Sources: AITTP, GFSME

Table 10: LOANS GUARANTEED BY GFSME
(₱ 000)

Item	As of June 30, 1985 No.	Amount	As of June 30, 1986 No.	Amount	As of Dec. 31, 1986 No.	Amount	As of Oct. 31, 1987 No.	Amount
A. By Type of Commodity/Project								
Cereals & Grains	3	2,534	1	2,834	4	6,334	4	6,334
Fruits, Nuts & Veg./Crops	2	3,000	8	22,545	9	25,905	11	31,905
Livestock & Poultry	7	24,950	24	54,265	33	64,090	49	71,542
Fish & Marine	10	23,113	37	96,039	76	162,801	141	282,647
Others	5	26,750	15	39,030	25	51,468	24	41,418
B. By Activity/ Purpose		n.a.						
Production			68	167,049	118	251,339	199	381,467
Processing			17	47,664	27	59,260	30	52,380
C. By Size of Loan (P 000)		n.a.						
2M and below			47	39,090	89	97,245		
over 2M to 8M			38	175,623	55	213,353		
0.2M to 0.5M							40	16,202
0.5M to 1.0M							51	47,527
1.0M to 2.0M							64	102,725
2.0M to 5.0M							65	213,322
5.0M to 8.0M							9	54,070

	As of June 30, 1985 No.	Amount	As of June 30, 1986 No.	Amount	As of Dec. 31, 1986 No.	Amount	As of Oct. 31, 1987 No.	Amount
D. Project Site								
(a) Within Metro Manila	n.a.		n.a.		14	38,276	n.a.	
(b) Outside Metro Manila	n.a.		n.a.		131	272,323	n.a.	
Region 1							12	18,725
2								
3							39	70,484
4							43	70,875
5							4	7,000
6							101	196,482
7							9	20,400
8							1	500
9							1	3,360
10							2	2,700
11							5	12,295
12								
NCR							12	31,026
GRAND TOTAL	27	80,347	85	214,713	145	310,598	229	433,846

n.a. - not available.

Source: Agricultural Credit Policy Council

Table 11: NUMBER AND AMOUNT OF LOANS GRANTED UNDER THE AGRO-INDUSTRIAL TECHNOLOGY TRANSFER PROGRAM BY VARIOUS DIMENSIONS FOR THE YEARS 1985, 1986, 1987 AND CUMULATIVE DATA
As of March 1988

	1985		1986		1987		Cumulative Loans Granted As of March 1988	
	No.	Amount (₱000)	No.	Amount (₱000)	No.	Amount (₱000)	No.	Amount (₱000)
A. By Type of Commodity/ Project								
Cereals and Grains	2	12,173						
Fruits, Nuts and Vegetables	7	39,032	7	63,297	2	2,800	13	83,104
Livestock and Poultry	1	2,500					2	6,500
Fisheries (includes aquaculture)	11	98,107	16	91,972	7	31,100	34	212,920
Industrial Crops (cotton, ramie, cacao, castor beans	4	21,981	4	28,638	3	11,500	13	89,373
Feed Components (cane tops, sweet potato, fishmeal)	3	52,326	1	5,041			8	63,009
Others	2	10,000	1	4,080	3	21,797	4	15,380

	1985		1986		1987		Cumulative Loans Granted As of March 1988	
	No.	Amount (₱000)	No.	Amount (₱000)	No.	Amount (₱000)	No.	Amount (₱000)
B. By Activity/ Purpose								
Production	16	64,612	15	71,694	10	35,500	41	171,132
Processing	14	171,507	14	122,334	5	31,697	33	299,162
C. By Maturity								
Short Term (1 year and less)								
Medium Term (over 1 year to 5 years)	30	236,119	29	193,028	15	67,197	74	470,294
D. By Size of Loan								
Small (0.5M - 5M)							46	147,063
Medium (6M - 15M)							20	173,098
Large (16M-21M)							8	150,133
E. By Type of Borrower a/								
Small (1M - 10M)							50	330,328
Medium (11M - 20M)							14	195,082
Large (21M - 30M)							10	301,329
TOTAL LOANS GRANTED	30	236,119	29	193,028	15	67,197	74	470,294

a/ In terms of total assets.

Source: AITTP-TLRC

4. Which strategy ensures long-term viability of the financial system and in particular the financial institutions?

5. Is there a case for a financial markets approach in view of the "apparent failure" of the government's subsidized credit programs for agriculture?

6. Assuming that market failure in the financial and goods markets can be established, is it optimal to recommend government intervention through specific mechanisms like credit programs?

7. What are the graduation criteria for participants in the program approach? Are they to remain subsidized forever? Or for a limited period of time? What criteria determines when they should graduate into a mature bank-client relationship?[10/]

8. What are the transaction costs that the banks face in trying to gain access to the guarantee funds?

VI. CONCLUSION

This paper tries to shed some light on the issues and financial policy framework affecting Philippine rural enterprises. It discusses the importance of the credit delivery system to these entities and the barriers which prevent access to bank resources. An interesting observation is the view that lack of access to formal credit is a problem of lack of readiness and maturity for formal credit. The paper ends with a presentation of two approaches to the provision of financial services which are currently pursued: (a) the financial markets approach and (b) the program approach. Important questions concerning these approaches are raised with the purpose of stimulating research in this area.

Annex I

DEFINITION OF RURAL AND URBAN AREAS

The same concepts used in the 1975 Integrated Census Phase I were followed in clasifying areas as urban. According to these concepts, urbanised areas consist of:

1. In their entirety, all cities and municipalities having a population density of at least 1,000 persons per square kilometer.

2. Poblaciones or central districts of municipalities and cities which have a population density of at least 500 persons per square kilometer.

3. Poblaciones or central districts (not included in 1 and 2), regardless of the population size, which have the following:

(a) Street pattern, i.e., network of streets in either parallel or right-angle orientation;

(b) At least six establishments (commercial, manufacturing, recreational and/or personal services); and

(c) At least three of the following:

   1. A town hall, church or chapel with religious services at least once a month.

   2. A public plaza, park or cementry;

   3. A market place or building where trading activities are carried on at least once a week.

   4. A public building like a school, hospital, puericulture and health centre or library.

4. Barangays, having at least 1,000 inhabitants, which meet the conditions set forth in 3 above, and where the occupation of the inhabitants is predominantly non- farming or fishing.

All areas not falling under any of the above classification are considered rural.

ENDNOTES

1/ Hiemenz and Bruch (1983) present an interesting study although not specifically focused on rural enterprises. In this paper, we assume that rural enterprises are generally "small" both in terms of assets (less than ₱1 million) and number of workers 1-49. It seems that employment size is the dominant measure (Little, 1987).

2/ Little (1987) argues that the case for promoting any particular type of enterprise is that it uses factors more efficiently, given their social costs. Because small enterprises appear to be more labor-intensive does not necessarily mean they are socially desirable. We do not address this issue but assume that the creation of a job through a rural enterprise is by itself a socially desirable event, especially given large scale unemployment and mass poverty.

3/ In the absence of more detailed information we take the rural enterprises as broadly equivalent to the rural non-agricultural sector. The term "rural" as used in this paper follows the definition of the National Statistics Office given in Annex I.

4/ Planting season starts around late May and is completed by early July (Fabella, 1987).

5/ C. Virata and Associates, SGV and Company, and Estanislao, Lavin and Associates.

6/ The private development banks were excluded in this analysis since 69 percent of their loan portfolio during the period 1981-86 was concentrated in Metro Manila.

7/ It may be the case, of course, that rural enterprises need less bank credit than urban enterprises. More likely, they are unable to compete successfully for these resources in comparison to the risk-return profile for urban clientele.

8/ The other side is, of course, the bank's. There are observations that some financial institutions are not operationally structured to handle this type of formal credit or client. While this should merit equal attention, we confine our discussion to the user's side of formal credit.

9/ This sub-section's title is attributed to Meyer (1988). We do not intend to evaluate the two approaches to providing financial services to rural enterprises. This section merely reports on two applications of these approaches in the Philippines.

10/ Questions number 7 and 8 were suggested by Professor Graham.