OLD WINE IN NEW BOTTLES?
RURAL FINANCE AND SOCIAL FUNDS IN ARGENTINA

Esteban Tapella [1]

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For further information contact:
ORPAS - **Institute of Social Studies** - P.O. Box 29776
2502LT The Hague - The Netherlands - FAX: +31 70 4260799
E-mail: **workingpapers@iss.nl**

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ABSTRACT

This article briefly explores how rural financial approaches have been evolving over the past three decades as development paradigms shifted from large State intervention to adjustment and liberalisation policies. Particular attention is given to the question about how rural credit programmes can combine social objectives (high outreach) with financial performance. To provide this analysis with an empirical foundation, the case of the Social and Agricultural Programme (PSA)[2] in Argentina is assessed. The study demonstrates that PSA resulted in a high outreach level but low recovery rates. Based on the financial analysis, recommendations are presented as the policy implications of the study.

[2] PSA is the major national policy for the peasant sector in terms of coverage (beneficiaries and provinces), budget and projects. Although there are studies on PSA, none of these focused deeply on its credit system.

1. INTRODUCTION

Over the past two decades, globalisation, the emergence of a new international agro-food regime and world-wide liberalisation policies have drastically transformed Latin American and Argentinean rural society. Structural changes in Argentina resulted in two simultaneous and contradictory effects. On the one hand, there was an exceptional increase in technological change, production and exportations. On the other hand, by looking at the agrarian structure and social indicators, results show concentration of economic power, worsening of distribution of wealth, hence an intensification of domestic inequalities and weakening of the already precarious position of peasants[3] (Maletta, 1995; Kay, 1994, 2000; Spoor, 2000; Lattuada, 2000).

Accompanying structural reforms, a significant change in the conception of rural finance has taken place, shifting from subsidised agricultural credit towards more liberal market-led approaches. In this process, two important responses to structural changes need to be highlighted. First, in the field of rural finance, microfinance institutions (MFIs) emerged and spread, aimed at targeting low-income farmers while at the same time trying to pursue financial viability. Second, in the field of social policies, social funds (SFs) or rural development programmes were implemented to offset the negative impact of structural adjustment policies among targeted groups of rural poor.

It has been acknowledged that MFIs have specialised since the 1980s, providing loans and savings services to those small farmers usually excluded from existing formal financial services. They achieved high repayment rates and relative financial independence (Hulme & Mosley, 1996; Coffey, 1998; Morduch, 1999 and Hulme, 2000). In addition, every country in Latin America has implemented some kind of SF, targeting the extremely poor (Cornia, 1999; Stewart & Van der Geest, 1995 and Glassner *et al*., 1994).

However, despite these efforts, two basic issues still remain under debate: (1) the degree by which the rural poor really have access to financial services; and (2) the ability of lending institutions to be sustainable. Apparently, the more rural finance institutions or credit programmes focus on poverty alleviation, the more difficult it is to achieve financial

[3] In this study the '*peasant*' refers to the small farmer or *minifundista* who produces for both self-consumption and local markets, engaging only workers in short seasons like the harvest. They have a precarious land tenure situation, small-scale production (low capital and technology) and use intensively family labour.

viability. The higher the financial performance is expected, the more institutions tend to 'exclude' the poorest farmers. How to link these extremes is the core issue. The study of PSA in this article therefore focuses around this debate and analyses the extent to which PSA was able to combine outreach to peasants with financial performance[4].

This paper has three major parts. Section two briefly reports how different rural financial perspectives were evolving during the 'pre' and 'post' adjustment era with regards to the Latin American context. Sections three and four explore the case of PSA in Argentina. This programme emerged in the 1990s as a SF, but adopted a typical credit policy of the 1960s or 1970s, without learning from microfinance experiences; a case of putting *old wine in new bottles*. For this reason, PSA is critically assessed by looking at it both as a 'social fund', as well as a 'rural credit policy'.

Concluding remarks show that PSA has succeeded in reaching the targeted population. However, its main objectives as a social fund (to mitigate rural poverty) compelled the programme to adopt a very inefficient subsidised credit policy. Welfare concerns were prioritised at the cost of extremely low repayment rates resulting in the collapse of the rotating fund. The policy implications of the study are built on the financial analysis. As a result, a set of successful microcredit practices is taken on board in order to improve PSA's current credit policy and financial performance.

2. CHANGING PARADIGMS ON RURAL FINANCE

For a long time, governments, international aid organisations, non-governmental organisations (NGOs) and development banks have invested vast amounts of resources to provide credit to peasants and commercial farmers in order to accelerate development. Meanwhile, the question of how to best develop effective and efficient rural financial policies has been debated as development perspectives were changing. Since the 1950s, two perspectives have crystallised from which two distinct financial policies have been developed (Ellis, 1996; Vogel & Adams, 1997 and Alvarado, 1996).

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[4] '*Outreach*' refers to the extent by which a programme provides financial services to a large number of small (targeted) farmers. '*Financial performance*' mainly refers to the ability of the programme to provide durable services on a cost-recovery basis. See Yaron (1992a, 1992b), Christen *et al*. (1995), Rhyne (1998) and Woller *et al*. (1999).

First, the period 1960s to the early 1980s can be explained by one development model, where subsidised credit policies prevailed under a grater state involvement in the economy. In this period, rural development programmes or special development banks provided credit and technical assistance to small farmers in order to adopt 'green revolution' technologies and increase productivity. Also called the *'productive' approach*, this perspective underlies supervised or directed credit policies.

For this perspective to emerge, it was assumed that the peasant sector (poor but potentially productive) would improve their situation if they had access to credits under 'soft' contractual conditions (Aguilera, 1997). In this sense, a kind of 'vicious circle' of poverty would be broken with rural credits (Rivas-Guerra, 1995 and Ellis, 1996:155).

Consequently, rural credit emerged as an 'instrument' (in order to access seeds, fertilisers, labour, technology, land, irrigation systems) aimed at reducing poverty by increasing productivity and incomes (Braverman & Guash, 1986:1253).

Despite good motivations, policies that emerged from this approach were sectoral (i.e. limited to specific regions or groups) and have been unsuccessful, at least in the financial sense, since they lost an inordinate volume of capital with each passing year (Hulme & Mosley, 1996:2). With the fiscal crisis, inflationary and debts problems during the 1980s, this approach was seriously questioned. Fungibility problems, high transaction costs, lack of saving services, low recovery rates, limited access of rural poor, and dependency in government resources, constituted the main causes for its decay (Braverman & Guasch, 1986:1256-7 and Ellis 1996:162-3).

Based on a complete break with the previous paradigm and stimulated by the adoption of liberalisation policies since the 1980s, a new perspective on rural finance emerged; the *'financial market' approach*. Subsidised credit evolved into rural finance, encompassing the financing of both farming and rural non-farm activities, as well as integrating the issue of local savings mobilisation. Market interest rates increasingly prevailed, loans became demand driven and institutions were evaluated on a cost-recovery basis. There was a tendency to reduce State intervention by allowing financial markets to play the most dominant role (Hulme & Mosley, 1996; Braverman & Guash, 1986:1254 and Rivas-Guerra, 1995).

At least two main problems of this perspective have to be stressed. First, although credit and saving services were very important, they had limitations to (1) increase productive capacity, (2) adopt technologies and develop new skills, (3) start up new activities (employment generation) and (4) reduce poverty (Hulme & Mosley, 1996; Dawson & Jeans, 1997:6 and Berger, 1989). Secondly, the pressure on institutions to be efficient and sustainable resulted in a shift from productive initiatives to commercial, processing and consumption loans. Additionally, there was a tendency to select low-risk activities and more viable farmers (Dawson & Jeans, 1997:7-8), as well as a preference for smaller short-term loans (Otero, 1997:29). In many cases policies resulting from this approach failed to reach the poor.

Despite these two major streams ('productive' and 'financial market' approaches), it has to be emphasised that after structural adjustment programmes, different perspectives were experienced and are still debated.

As a response to liberalisation policies and the withdrawal of the state, a *first generation of MFIs* emerged. Also called microcredit institutions (MCIs), they evolved in many legal forms, such as NGOs (some transformed into regulated institutions), credit unions, co-operatives, commercial banks and in combination with State-led programmes. They received the label of 'micro' due to the small size of their transactions and savings deposits, and 'finance' because they were aimed at providing safe and reliable financial services to the poor (Microfinance Gateway Library, 2001).

MFIs shared several features with the financial market approach. They attempted to spread the financial market sector, including a broad range of services (e.g. credit, savings and insurance). They also persisted in high repayment results, positive interest rates and the intention of building up sustainable institutions. Since the middle 1980s several MFIs like *BancoSol* in Bolivia, *K-Rep* in Kenya, *BRI* in Indonesia and *Grameen Bank* -now in 66 countries (Grameen Bank, 2001)- emerged and expanded in developing countries.

These policies were positively evaluated in terms of beneficiaries and the high recovery rates they got (Dawson & Jeans, 1997 and Chavez, 1997:102-9). However, also negative results have to be mentioned. First, the precondition for institutions to be sustainable generated a tendency to select the 'best' borrowers, consequently, excluding those 'non-viable' producers or more risky crops (Morduch, 1999:1598-601; Hulme, 2000:26-8 and Galarza & Alvarado, 2001:20-1). Second, credit was still too scarce and saving facilities very limited to play a stronger role in development (United Nation Secretariat, 1998:5; Coffey, 1998). Third, although MFIs achieved high levels of repayment, only 5 per cent of world-wide institutions are financially sustainable (Morduch, 1999:1587 and Hulme & Mosley, 1996:8).

Since the late 1990s and based on the problems of MFIs mentioned above, a *second generation of MFIs* (also called 'innovative financial institutions') seems to be emerging (Hulme & Mosley, 1996:10). In this approach, a re-regulation of financial services is believed to contribute at re-conciliating efficiency objectives with welfare concerns; or productive and re-distributive impact with financial sustainability (Seibel, 1998 and Lapenu, 2000).

Spite some positive experiences, one could ask: is there a 'real' second generation of MFIs, which reach the poorest of the poor *and* achieve financial sustainability? Is microfinance a single path or a mixture between two divergent ends: namely, poverty reduction and the development of a healthy microfinance sector?

In fact, beyond different approaches and actors involved (donors and internationals institutions, researchers and policy makers, NGOs, MCIs and peasant organisations) there seems to be a permanent debate between two historical streams. On the one hand, the 'institutionalists', who emphasise on the spread of financial institutions, professionalisation, sustainability and profitability, prioritising financial performance over depth of outreach (Otero & Rheyne, 1994). On the other hand, the 'welfarists', who focus on direct poverty alleviation, even at the cost of low recovery rates (Woller *et al.*, 1999:1). This debate is very relevant for the analysis of state-led rural development programmes, designed as targeted policies to mitigate rural poor in a context of structural changes and increasing poverty.

For the PSA's case, both outreach level and financial performance are considered important objectives (PSA, 2001:15-19). The first objective fulfils government expectations as regards a social policy; the second is a pre-condition for sustainability which allows for an expansion of coverage.

Given these concerns, it is worth asking: Is PSA an expression of the second generation on MFIs? Has PSA, in fact, reached poor peasants and, at the same time, achieved financial sustainability? Or, on the contrary, has the programme simply wrapped old-style subsidised credit policies in an innovative social fund framework? Is this just a case of '*old wine in new bottles*?'

3. THE CASE OF THE SOCIAL AND AGRICULTURAL PROGRAMME IN ARGENTINA

3.1 The Context for the PSA to Emerge

It is necessary to briefly situate the study of this state-led rural credit programme in the context of the dramatic structural changes that took place in the region since liberalisation policies were adopted. This reforming scenario and its impact on the Argentinean rural structure constitute key inputs for analysis of PSA.

Undoubtedly, structural adjustment policies, the adoption of an export-oriented development strategy and the internationalisation of agriculture through the intervention of transnational corporations and agribusiness have accelerated the modernisation of sub-sectors of agriculture and transformed social actors and their relationships in the rural society.

Argentina shares with other countries in Latin America almost the same trends, where a dualistic process has taken place. On the one hand, between 1990-1998, the evolution of the agricultural sector in terms of new technologies and increase of production and exportation has been exceptional. The country has had continued and positive rates of agricultural growth, maintaining the contribution of the primary and agro-industrial sector at around 30 per cent of the GNP. For example, between 1992-1997, the production of cereals and oilseeds in the *Pampas* increased 33.2 per cent and the productivity went up 7 per cent (Lattuada, 2000:2-6). On the other hand, the participation of the peasantry in the economy decreased, open competition produced unequal growth (some regions became more viable than others) and rural poverty increased (Maletta, 1995:144 and Hicks, 2000).

The peasant sector and capitalised family producers are vanishing as a consequence of globalisation, deregulation and the involvement of Argentina in MERCOSUR. The integration with Brazil is pushing agricultural producers towards more profitable export crops (*reconversión*). In this process, small farmers face many difficulties in adjusting to the new patterns as they have serious limitations regarding land and technology or access to capital and credit (Manzanal, 1999). Only the fertile *Pampas* export sector (cereals, oilseeds and beef) and, to some extent, other middle-size farmers with regional productions (wines and fruit) could catch up with the conditions imposed by the new agro-food regime, while the rest became 'non-competitive' or 'non-viable' farmers (Paz, 1999).

Structural reforms have accelerated the process of 'depeasantisation' and 'proletarianisation'. The number of agricultural units of production decreased considerably since 1988, where -according to the agricultural census (INDEC, 1988)- the number of peasant households was around 200,000 units. The census was not implemented again, but according to Manzanal (2000), who estimated the peasant population on the basis of secondary data from different local and regional studies (Forni & Neiman, 1994; Murmis, 1995 and Tsakoumagkos, 1997), by 1999 the number of *minifundistas* hardly exceeded 150,000 households[5].

In response to the negative impact of structural adjustment and following World Bank recommendations, Argentina has implemented different *social funds* (SFs)[6] to offset the social costs of liberalisation policies and alleviate rural poverty. By targeting different 'types' of producers and rural poor (*minifundistas*, women, children and rural proletariats) the government has designed different strategies, including the provision of subsidised credits, rural extension services and marketing support. PSA has emerged as a SF and a rural credit programme within this context.

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[5] Other sources testify to this trend. In *La Pampa*, one Argentinean province, the milk sector increased its production between 1991-1997, but during the same period the number of producers decreased by 50 per cent and almost all small producers disappeared (Lattuada, 2000:18). In *Tucumán*, another Argentinean province, between 1988-1996 the number of sugar-cane *minifundistas* (*cañeros*) decreased by 31.5 per cent and their proportion of temporary off-farm labour greatly increased (Giarraca *et al*., 1999:3-7).

[6] *Social funds* were designed as mechanisms through which resources could be allocated according to a pre-determined selection criteria, to demand driven sub-projects proposed by public, private or voluntary (formal or informal) organisations (Carvalho, 1994:1). They started as temporary anti-cyclical programmes but, as the economic stagnation persisted, they became semi-permanent or permanent policies, shifting from 'compensatory' (*Social Emergency Funds*) to 'promotive' measures (*Social Investment Funds*) (Cornia, 1999:12 and Tendler & Serrano, 1999:13). These 'social policies' shared practically the same features: targeting mechanisms (to obtain a high impact per capita); important degree of administrative autonomy, decentralised and privatised delivery of services; demand-driven schemes based on participatory projects, and external financial support.

3.2 PSA Revisited: Institutional Profile and Beneficiaries

As a common trend, the peasant sector[7] in Argentina has not received loans from either the public or private banks. For them, the main sources of 'financial' support have been the national and provincial welfare State (until the 1980s), targeted programmes (since the late 1980s), local or regional NGOs and the informal sector (Manzanal, 2000 and SAGPyA, 2000).

PSA started at the end of 1993 as a targeted programme for peasants. Depending on the National Agricultural Ministry and currently running, it is the major state-led rural policy for peasants in terms of budget, and the first one to cover 21 provinces (Manzanal, 2000). Between 1993-2000, PSA has transferred to the peasant sector $30.6 million in credit. It has assisted 38,121 households (almost 24 per cent of Argentinean peasant population) that participated in 5,892 projects, providing basically credit, training, technical assistance and marketing support (ProgPSA, 2001).

Although credit has been the major attraction for its beneficiaries, PSA is presented as a rural development programme. Two main objectives are explicitly defined: (1) to contribute to the increase of peasant household incomes; and (2) to promote the participation and social organisation of the peasant sector in decision-making processes over policies and programmes (PSA, 1994).

3.2.1 PSA as a Social Fund

PSA has adopted the neoliberal 'style' of social policies and shares the typical principles of SFs implemented in the 1990s (targeting strategy, decentralisation, participatory schemes, and well-qualified staff).

This programme deliberately attempts to reach peasants by targeting them as direct beneficiaries. The *target population* are small farmers (*campesinos* or *minifundistas*), and

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[7] In Argentina the peasant sector never had the same relevance as it has had in Bolivia, Mexico or Perú, mainly due to its geographical heterogeneity. Argentina has five large and different regions: the Northwest, Northeast, Cuyo, Patagonia and the *Pampas*. The *Pampas* has the most fertile and well-watered grasslands, while the *Interior* (the other four regions) has worse conditions regarding soil quality and seasonal patterns of rainfalls. The dominant role given to the *Pampas* for Argentina to integrate socially and economically into the world order, has historically neglected the peasant and the *Interior* realities (Manzanal, 1990:137-8 and Sawers, 1996:26-7).

the ‘eligibility’ criteria are defined with very clear and strict parameters of capital, work and income (PSA, 1994, 1998a).

PSA also adopted a very *decentralised* structure. At national level the Agricultural Ministry administrates the programme. At the provincial level, Provincial Units (integrated by public and private local institutions as well as two peasant representatives), are in charge of evaluating productive projects and demands for loans, as well as articulating the programme with other local policies for the sector.

Peasant *participation* is also encouraged at different levels. PSA adopted a demand-driven scheme, in which potential beneficiaries design productive projects formulated by groups. Beneficiaries are supported by rural extension workers, who assist them in organising the group, formulating the project and -once the project is approved- providing technical assistance during field visits and group meetings. PSA also encourages beneficiaries to participate in entities like Provincial Units and meetings at local, regional and national levels, where they contribute to decision-making processes (PSA, 1994, 1998b).

As other SFs in Argentina that emerged as temporary institutional programmes, PSA has not really been institutionalised, that is, there is no law that determines its existence as a permanent service for peasants. Despite its high degree of administrative and technical autonomy, PSA depends on budgets that are yearly defined and approved by the national parliament.

3.2.2 PSA as a Credit Policy

PSA emerged in the 1990s, at the time when microfinance perspectives had spread world-wide. According to its institutional structure, objectives, policy instruments and methodology, it mainly presents the characteristics of the ‘productive approach’ on rural finance, in which subsidised credit is considered a means to increase productivity and incomes. PSA credit policy is aimed at ‘[...] mitigating rural poverty by increasing productivity and improving the marketing of agricultural activities developed by *minifundistas* throughout their association in small enterprises (EPAs)’ (PSA, 1998a).

Although rural credit is very important (an average of 50 per cent of PSA’s expenditure), it is provided within a package of other non-financial fully-subsidised services: (1) *technical assistance*, (2) *training*; and (3) *marketing support*. The provision of this ‘pack age' of services is oriented to fulfil government expectations, mainly defined in terms of social impact: higher incomes, more self-employment, and less rural-urban migration. This puts PSA closer to the 'welfarist' approach, and consequently shapes its methodology.

The programme has designed three lines of credits to support different types of activities. First, consumptive projects (*autoconsumos*), subsidies lower than $200 to be 'repaid' in kind by delivering part of production to community institutions. It represented 12.4 per cent of total funds for credit transferred between 1993-2000, reaching 45.6 per cent of the total number of beneficiaries, and had an average 'loan' size per household of $160. Second, credit for traditional crops and lower risk activities (*proyectos tradicionales*). This represented 80.4 per cent of the total credit delivered and reached 50 per cent of households. Third, credits for innovative or experimental activities (*proyectos innovadores*), which involved 7.2 per cent of total credit and reached 4.4 per cent of households. The maximum loan size per family is $1200 and the average was $ 692 per household. The group membership was on average 6.5 farmers per project, just more than the minimum determined by PSA regulations (PSA 1998b and ProgPSA, 2001).

PSA can be also characterised as a 'directed credit scheme'. Credit is seen as an instrument to increase agricultural capital and productivity. It is directed towards supporting certain agricultural investments in both capital assets and working capital; including a 'negative' list, where prohibitions on the use of loans (for example, land and wages) are stated (PSA, 1998a).

Conditions to access credits also characterise PSA as a 'directed' approach, since it defines many specific requirements. First, producers have to join a group, formulate an associative project and establish their organisational regulations (group lending methodology). Second, they must stipulate the use of the credit (as detailed as possible), present a recommendation letter signed by a local authority who supports the group and add a technical assistance plan aimed at introducing technologies and supporting the associative work (PSA, 1994, 1998a).

PSA´s credit policy also represents a 'supervised' scheme, in which beneficiaries must demonstrate that they used the credit correctly. In addition, they are 'obliged' to participate in technical assistance activities to reduce project-failure risks (PSA, 1994, 1998a).

As many other state-led credit policies, PSA defined very 'soft' conditions. It adopted a 'subsidised' interest rate of 6 per cent per year (for traditional activities) and 4 per cent (for innovative or experimental crops). Conditions of repayment are generally defined for long periods (between 1 to 7 years), and special concessions (rescheduling and debt forgiveness) for extremely poor groups or very risky projects are taken into account.

PSA has regulations for cases of default, but -in practice- none of these mechanisms have been applied, mainly because staff did not believe that they would achieve their objectives. For instance, it was thought that increasing interest rates –for overdue loans- would lead to falling repayment rates rather than acting as an incentive to compliant behaviour. In addition, the follow up of credits through legal enforcement would be seen as contravening the 'principles' of a social programme aimed at reducing rural poverty (Martinez-N., 1996 and Benencia, 1997.

Although financial performance was not an initial priority, PSA designed a 'rotating' fund to deposit repayments and support new credits. It is operated by the central administration, who sends funds to provinces through the same procedures used for budget funds. PSA regulations state that loans recovered in each province can only be used to support new credits in the same province. However, in some cases (caused by budget constraints) rotating funds were delivered to support other activities such as technical assistance or administrative costs.

4. PSA EVALUATED: LESSONS FROM THE FIELD

In this section, the programme is assessed in terms of its ability to combine welfare concerns with financial sustainability. This analysis is made by looking at both social and productive results (PSA as a SF) and financial performance (PSA as a credit policy).

The analysis of social impacts has some difficulties, since the outputs have varied according to (1) the Argentinean macro-economic context, (2) the particular local and regional agricultural crisis, and (3) the different ways by which PSA was applied in each province. Despite these limitations the analysis was made based on previous studies[8] and available secondary information.

[8] See, Martinez-N (1996), Benencia (1997), PSA (1998a), Manzanal (2000), Rodriguez-B (2000) and Allub (2000).

4.1 Social and Productive Results of PSA as a Social Fund

Undoubtedly, social concerns in the early 1990s in Argentina, like the negative impact of the debt crisis and structural adjustment policies, have shaped PSA as a policy oriented towards reducing rural poverty. The financial performance (basically repayment and default rates) has been a secondary preoccupation for PSA. The programme has emphasised the number of beneficiaries and groups, level of social organisation and marketing activities, and the ways by which credit increases production, number and type of animals, access to inputs and adoption of technology, i.e. the 'productive' approach. In this sense, PSA had positive results, taking on a crucial role in providing credit to the peasant sector, as it is shown below.

With respect to targeting, PSA data show a high outreach level, since more than 86 per cent of the recipients of credit were within the selected population (Martinez-N., 1996 and Benencia, 1997). Contrary to tendencies in the implementation of targeted SFs (Cornia & Stewart, 1995), PSA obtained a low level of both 'F-mistakes' (failures in reaching the targeted population) and 'E-mistakes' (leakage to non-targeted farmers). In addition, for more than 90 per cent of beneficiaries, it was the first opportunity to access credit and technical assistance (Martinez-N., 1996).

Field studies of SFs generally argue that targeting mechanisms generate psychological costs like 'paternalist' segregation, stigmatisation or deterioration of self-esteem (Sen, 1995:13). A recent qualitative study of PSA (Rodriguez-B, 2000) analysed the incidence of targeting on social capital and local peasant networks. Conclusions show that PSA, far from producing segregation or stigmatisation, has been seen by beneficiaries as a chance for empowering their local organisation and acquiring recognition as citizen and economic actors. Targeting did not 'break' previous friendship networks, even in cases where some member of existing groups were not targeted by PSA.

In relation to participation and decentralisation, both Manzanal (2000) and Martinez-N. (1996) concluded that PSA succeeded in 'opening' spaces for the peasants to participate. Small farmers participate in activities regarding project management and decision-making processes at local and regional levels. The extension of PSA, despite budget constraints, is a response more to pressure on national authorities made by beneficiaries than government priorities for the sector. Moreover, the decentralised scheme facilitated the articulation of PSA with other actors (local government and institutions, peasant organisations and donors) and contributed to partially mitigating the lack of resources (national budget and rotating fund).

In relation with the analysis of the productive, technological and economic results of PSA, some works[9] conclude that, in general terms, credit, technical assistance and special training provided by PSA allowed most of the projects to reach their objectives, in terms of (1) improvement of quantity and quality of production; (2) adoption of new technologies and skills; (3) increase in households assets; and (4) participation in associative schemes for producing and marketing (lowering costs, producing value-added and increasing incomes).

However, at the macro level, PSA presents several limitations and weaknesses (Manzanal, 2000:93-6). First, there are no national, regional or local complementary policies to overcome the problems that the 'market' causes to the peasant sector after liberalisation policies. Second, the volume of credit ($1200 maximum per household) and the technical assistance provided through PSA is insufficient for small farmers to become competitive given the magnitude of structural poverty. Finally, more than 74 per cent of the peasant population in Argentina still lacks access either to PSA or to other social supports. As a consequence, what the peasant sector has lost through structural adjustment, in terms of the loss of production subsidies and cutbacks to health, educational and social policies, is far greater than the benefits received from PSA.

4.2 PSA's Credit Policy, Financial Performance and Sustainability

Many of the strengths and weaknesses of the credit policy adopted by PSA match the problems documented within the 'productive' approach (directed and subsidised credit schemes) that was popular in the 1960s and 1970s. Most of the positive results are those already mentioned above, such as high outreach to the target population; satisfaction of

[9] This analysis is a difficult task. The influence of macro economic variables on the agricultural sector makes it very difficult to calculate the manner by which a micro project might have contributed (or not) to mitigating recession and trends of impoverishment. Additionally, there is no sufficient statistical data (at the starting point and after policy implementation) to demonstrate results in terms of incomes, employment generation or other quantitative variables. Nevertheless, it is possible -at least- to present the most relevant conclusions regarding project results, based on previous qualitative studies. See Martinez-N. (1996), Benencia (1997), Rodriguez-B. (2000), SAGPyA (2000), Allub (2000) and Manzanal (2000).

productive needs and the solution of technical problems; and more participation and social organisation. In the following paragraphs, the analysis focuses on the negative results of PSA's credit policy.

4.2.1 Procedures, Conditions to Access Credit and Peasant Participation

PSA is considered as one of the most efficient SFs in Argentina (Martinez-N, 1996); however, it has very bureaucratic and complicated procedures. As mentioned above, many 'steps' have to be taken to access credit. These conditions are not in balance with the real monetary transfer towards the sector and they give rise to problems such as delivery delays; projects formulated without real participation, resulting on non-appropriate investments; and high increase in transactional and administrative costs (Benencia, 1997).

Although PSA adopted a decentralised scheme, conditions to access credit were almost the same for the whole country, without recognising diverse agricultural systems and regional realities. In provinces with very low rural population densities, strict associative conditions resulted in *ad hoc* groups created solely for the purpose of accessing funds. It resulted in many badly functioning groups, which frequently made all borrowers default when one member failed to repay (Benencia, 1997 and Martinez-N, 1996). For these cases, individual treatment would have been more effective.

In addition, the 'positive list' that determines which type of investment can be obtained with loans, does not include certain assets (e.g. land) that in some cases might contribute to solving structural conditions of poverty. As a consequence, according to internal evaluative reports, PSA had problems of loan fungibility. Moreover, in some cases, credit ceilings were not sufficient to acquire the most appropriate technology for the agricultural system. These conditions sometimes had negative impacts on productive outcomes, resulting in recovery failures.

Furthermore, contrary to the official PSA policy, the beneficiary's real participation in the management of the rotating fund has been limited, since funds were administrated from the Central Unit. According to Cerviño (1999) it badly affected loan recovery, since peasants felt that this fund would never be available in their own province. It also increases transaction costs, including deposits and transfers from provinces to the Central Unit and vice versa.

Finally, the database for credit monitoring (ProgPSA) is not 'friendly' and its operation is quite complicated. As many provincial co-ordinators have stated (PSA, 1996), peasants do not understand and trust in what the system reports, since in many instances the database generated confusions about interest rates and other amounts to be paid. Consequently, institutional trust was deteriorated.

4.2.2 Financial Performance

The financial performance has been a secondary preoccupation for PSA, at least until early 1998, when the increasing demand for credit was not satisfied due to budget reductions and the insolvency of the 'rotating-fund'. Its institutional profile ('soft' conditions, inappropriate legal framework and instruments, and unsuccessful coercive actions) has contributed to a low financial performance. PSA has high default rates and its credit system is absolutely unsustainable, either in terms of operational sustainability (ability to cover operating costs) or financial sustainability (full dependence on external support, mainly the national PSA budget).

To demonstrate this, two steps will be followed. First, by examining PSA expenditure per type of services as a percentage of the total budget per year, the analysis focuses on institutional priorities and trends regarding credit relevance on the programme scheme. Second, by looking at four complementary basic indicators regarding financial systems, real performance is shown more clearly.

- *Credit Relevance in PSA's Expenditure*

Figure 1 compares four basic types of PSA's expenditure: (1) *Loans*, monetary transference delivery through traditional and innovative projects to be repaid in cash; (2) *Subsidies*, monetary transference for self-consumption projects to be repaid in kind; (3) *Extension services*, including technical assistance, training for beneficiaries and staff, social organisation and marketing support; and (4) *Total costs*, involving administrative and transaction costs for extension services, credit and subsidy delivery. Regarding Figure 1, three important tendencies in relation to PSA's institutional profile should be pointed out.

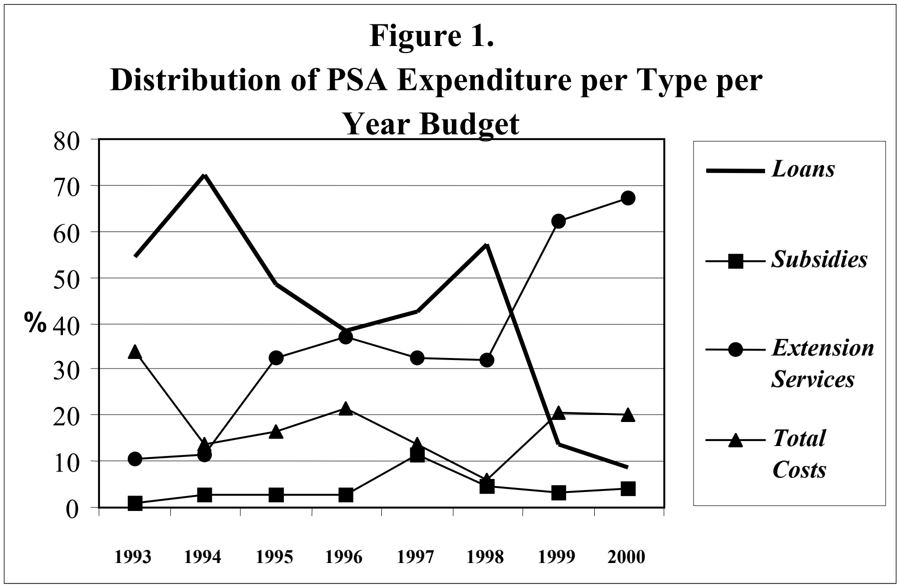


Figure 1.
Distribution of PSA Expenditure per Type per Year Budget

Source: Author's calculations, on the basis of statistical information from '*Prosoc*' database (used by PSA between 1993-97), '*ProgPSA*' and '*PSAren*' databases (used from 1997 until now).

First, it demonstrates that the credit system has been steadily deteriorated, making PSA become a programme which provides basically technical assistance, training and marketing support. PSA started in late 1993, but the real starting point was 1994, when credit delivery rocketed to $8.8 million (29 per cent of total PSA credit delivery between 1993-2000). Since 1994 loan delivery was decreasing in absolute and relative terms, except between 1997-1998 where a light budget increase and the complete use of the rotating fund let PSA to moderately respond to high demand. Important for the analysis is the manner in which the share of extension services has steadily increased, reaching almost 70 per cent of total expenditures in 2000, while credit delivery, which was decreasing, scarcely represented 10 per cent in that year. There are at least three reasons for this result: (1) successive reductions of the PSA budget; (2) low loan recovery rates and consequently lack of resources for credits in the rotating fund; and (3), the institutional profile, which determines that technical assistance is provided for three consecutive years after delivering the credit. Technical assistance tends to grow faster than credit expenditure.

Second, it shows that subsidies were not very significant as compared to total expenditures. However, they were important in terms of coverage, representing 45.6 per cent of the total number of beneficiaries reached by PSA (PSARen, 2001). Moreover, subsidies have taken almost the same value as a percentage of total expenditure per year, even in the periods 1994-1996 and 1998-2000 where loan delivery dropped substantially. In this sense, PSA managed to keep reaching a significant number of peasants within the existing budget constraints. Although this is crucial for a social policy to maintain political support, it adversely affected the rotating fund, since the provision of subsidies allows for in kind repayments.

Third, the data show a relative increase in administrative costs as the total volume of loan decreases. Even when recognising that PSA total costs are high in relation to microcredit standards, since it includes the extension service costs, what is important here is the evidence that they move in an opposite direction to credit volume. Thus, with budget constraints and a low percentage of loan expenditure, total costs tend to be proportionally higher, damaging financial performance.

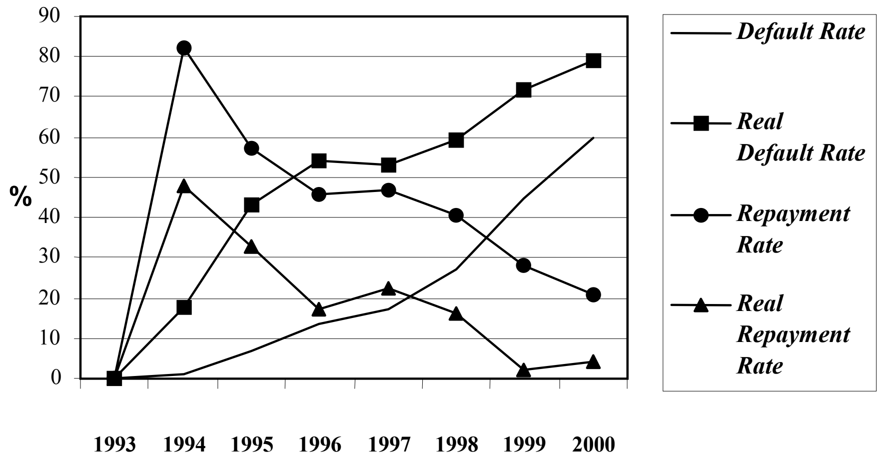
- Loan Recovery and Default Rates

Figure 2 shows the overall tendencies and crucial problems of PSA's financial performance. For the analysis, the data were adjusted and organised according to four indicators, conceptualised as follows: First, the *default rate*, defined and calculated by PSA (ProgPSA database) as the value of overdue loans in one year, divided by the current portfolio. There is a problem however with this indicator; when the portfolio increases reported default rates tend to be lower than real rates. Subsequently, a second indicator had to be created to show the real financial performance, the *real default rate*. In this case, by replacing the denominator with the size of the portfolio at the time that those loans were made, the real default rate was obtained. Additionally, a third indicator was used, the *repayment rate*, calculated by dividing loan volume recovered per year by scheduled repayments plus interests in this year. Since many loans repaid in one year may be long overdue, this indicator does not show the real ability of PSA to recover loans at the time they should be re-paid. Consequently, the *real repayment rate*[10] (complement of real default rate) was used to prove how effective the programme is in recovering loans.

[10] In this study, the incidence of inflation and credit interest rate on the nominal recovery rate is not calculated, since the low inflation rates (an average of 4 per cent per year between 1994-2000) will not influence the extremely low recovery rate trend experienced by PSA, as showed in figure 2.

Figure 2.

PSA Financial Performance:Basic Indicators



Source: Author's calculations, on the basis of statistical information from '*Prosoc*' database (used by PSA between 1993-97), '*ProgPSA*' and '*PSAren*' databases (used from 1997 until now).

Default rates and real default rates have been steadily increasing since 1994. The default rate expressed by PSA hides the real problem of default, at least between 1993-1997 when the availability of funds to support new credits was still high. However, the real default rate testifies that since the very beginning (1994 with 20 per cent) until now (with almost 80 per cent) repayment default damaged the credit scheme.

By looking at the ability of PSA to recover loans the same problems are observed. In PSA, as the history of subsidised credits shows (See Braverman & Guasch, 1996:1256), recovery rates were high at the beginning in 1994, but steadily declined over the programme's life until 2000. Although both repayment rate curves move practically together, the difference between them shows that not only PSA lacks the ability to recover credits but also when it does, it is much later than it should. In addition, rescheduling and debt forgiveness, as well as loans declared impossible to recover, which represent 12 per cent of the portfolio ($ 3.7 millions), are hiding the lack of ability to recover loans.

4.2.3 Why Such Low Loan Recovery Rates?

Evidence presented above shows that PSA's financial performance has been extremely poor. Which factors explain these results? For Benencia (1997), three main reasons answer this question. First, natural calamities, crop failure or low output-price problems. Second, mistakes in assessing the poverty level (or debt-capacity) of potential clients, providing over-sized credits. Third, unwillingness to repay incurred by more speculative farmers who know PSA's limitation to effectively enforce repayments. Additionally, based on peasant reports, the frequent gaps in loan availability created a feeling of 'bankruptcy'. Subsequently, trust in the system was reduced and speculative motivations increased.

Moreover, the political context and contradictory State interventions in Argentina have exacerbated defaults, as shown in two examples. First, the formal credit system (especially State banks) has been historically -also after adjustment policies- very weak in recovering loans. It is not a real problem for borrowers not to pay, since the system has no sanction for those in default[11]. Secondly, '*Programa Trabajar*' (working programme) -another social fund that targets unemployed rural workers and peasants- is implemented in tandem with PSA, providing subsidies for $200 per month during six months without requirements of any productive project. As a result, many peasants might have the same response as one of PSA's beneficiary in the province of San Juan, who said during a field visit in June 1999: 'If they (Trabajar's beneficiaries) do not pay a cent, why should I repay my loan?'

Overall, problems of default in PSA may be attributed to the used credit methodology. However, particular attention should also be given to the historical and political context which shows that in Argentina subsidised credit schemes still remain (Schreiner, 2000). In this context, the 'credit culture' among borrowers and lenders is distorted. Farmers are conditioned to expect concessions and it is difficult to determine whether the government really wants to improve financial performance of state-led programmes.

5. CONCLUSIONS AND POLICY IMPLICATIONS

This study has explored how rural financial approaches have been changing over the past three decades, giving particular attention to the question about how credit policies can reach the rural poor, and how they are able to improve financial performance. In the

[11] For example, the Argentinean National Bank determined an 'automatic' rescheduling for overdue loans for more than 150,000 clients to 'reduce' default rates in order to avoid the Bank's privatisation (See *Diario de Cuyo*, 12-08-1996).

context of structural reforms, the study focused on the case of PSA. This is a state-led programme aimed at reducing rural poverty by providing credit, technical assistance and training services to the peasant sector. In this study, two majors aspects of PSA have been analysed; namely the programme (1) as social fund and (2) as a rural credit programme.

Evidence collected in this study indicates that PSA, as a social fund, had quite acceptable results. Although many similar policies in Latin America have been assessed as ineffective instruments to reach peasants and improve their production and technology (Braverman & Guash, 1986:1254-5), PSA has effectively increased access to capital assets and transferred technology to targeted peasants, avoiding leakage to the non-poor farmers. Despite that, PSA has serious limitations in terms of resources and infrastructure to overcome rural poverty and stop the proletarianisation trend in rural Argentina, since it only had resources to reach about 24 per cent of the total target population.

In relation to the credit scheme, results are much more negative. The main conclusion that emerges from the study indicates that PSA did not succeed in combining the welfare impact with financial performance. PSA did not learn from many lessons documented on microfinance, and, being conditioned by rural poverty and social concerns after adjustment in Argentina, it adopted a subsidised credit policy that resulted in low financial performance. 'Soft' credit conditions, an inappropriate legal framework and weak instruments to enforcement repayment are some factors behind very low recovery rates. As a result, the default rate is extremely high and the rotating fund absolutely unsustainable. PSA has very limited chances to spread, and it is fully dependent on external support. PSA placed the 'old wine' of a credit policy of the 1960s and 1970s, in the 'new bottle' of a social policy framework of the 1990s.

Having shown the consequences of this combination, what should be done if PSA credit policy is to be more efficient and the system made more sustainable? Recent experiences provide useful positive lessons that could be learned in order to improve financial performance without shifting the focus on the poor. Based on the analysis of PSA and the study of innovative experiences, nine propositions are put forward as the policy implications of this study[12].

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[12] For key writings and lessons from rural MFIs, see Klein *et al* (1999), Coffey (1998), Alvarado (1996) Christen *et al*. (1995), Jain (1996), Yaron (1992a/b) Otero & Rhyne (1994) and Rivas Guerra (1995).

First, it has to be acknowledged that the worst ‘enemy’ of any financial system is the loan repayment default (Stearns, 1992). Default, rather than a problem of the users or external factors like low prices or natural disasters, is a programme weakness. PSA’s policy of frequent rescheduling and, in certain cases, debt forgiveness was used to hide and ‘alleviate’ default problems, consequently undermining loan recovery and repayment discipline.

Second, PSA’s policy of repayment enforcement has to be effectively implemented to strengthen institutional credibility. For example, in cases of intentional default, PSA could not seize even those assets acquired with loans, due to the limitations of a non-financial institution.

Third, a complementary strategy based on ‘dynamic incentives’ (Besley & Coate, 1995) can lead to higher repayment rates. For example, rewarding farmers with repeated loans and increasing credit size upon satisfactory repayment; or cutting off any future lending when loans are not paid.

Fourth, high transaction costs have a negative impact on financial performance. Although PSA’s costs cannot be attached only to the credit service and -by definition- agricultural lending involves high costs, administrative expenditure in PSA is extremely high in relation to the real monetary transfer to beneficiaries (figure 1). PSA could reduce costs by simplifying its bureaucratic and slow lending procedures.

Fifth, although the group lending methodology contributes to reducing costs and empowering social organisation, individual lending improves loan recovery. In effect, lessons from MFIs show that individual credits provide more flexibility in meeting the loan demand, improve loan quality and reduce default risks (Klein *et al*., 1999). Taking this into account, PSA could introduce more individualised lending terms within existing groups. In doing so, PSA should also improve the assessment of loan repayment capacity and credit worthiness of new beneficiaries to avoid oversized loans (but not exclude least viable farmers).

Sixth, PSA should move from subsidised interest rates to positive interest rates if better performance is expected. PSA´s experience shoes that low interest rates did not lead to higher repayment, and the poorest peasants were precisely those who exhibited better repayment records. For PSA´s case, Morduch’s approach could be appropriated. For him, rather than market or subsidised rates, the interest should be fixed at the level just below rates traditionally charged by informal lenders (Morduch, 1999).

Seven, in rotating fund schemes the sense of ownership in the management increases repayment. This can be facilitated by letting beneficiaries administrate funds (Chavez, 1997). If PSA attempts to reduce default risk and administrative costs, the rotating fund should be transferred (decentralised) towards peasant organisations in each province or region, instead of being managed by national authorities.

Eight, the more financial services satisfy the real demand of peasants, the more they will contribute to supporting the system (Chavez, 1997). Hence, the beneficiary's opinions regarding the optimal ways of improving the credit scheme should be considered[13]. In general terms, they expect from PSA: (1) delivery of credit when demand is expressed; (2) simplicity of lending procedures; (3) flexibility in the use of loans; (4) certainty about repeated and higher loans when repayment record is good; and (5) stringent mechanisms for those who do not repay loans. Overall, such development will increase the trust in the system.

Finally, it has been acknowledged that qualified staff has a positive effect on the effectiveness of credit policies. Therefore, to improve financial performance, the credit management staff has to be trained to learn from new rural credit technologies that were developed in Latin America since the late 1980s. In PSA's case this has been insufficiently done.

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[13] These suggestions were taken from beneficiary's reports in PSA, collected in 10 provinces, from 1997 to 1999. The five most repeated comments (within a sample of 364 group's reports) have been chosen.

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