Saving and Credit Cooperatives: A New Conceptual Approach

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1- **Credit and Saving Cooperatives and Contemporary Problems**

The first credit and saving cooperatives were established in the mid - 19th century, mainly in Germany. Two men are considered as the founding fathers of the credit cooperative movement: Herman schultze- Delitsche, who established a credit cooperative for minor artisans and the urban middle classes, and Freidrich Reifeisen, the founder of the rural credit cooperative. In Italy, Luigi Luzzatti established credit cooperatives which combined the principles established by his two German predecessors. After the consumer cooperative, the credit cooperative is the most common type of cooperative to be found in the modem world, including the Third World. This form of cooperative has been established in both rural and urban districts by labor unions and other organizations, including government bodies. Because of its very abundance, it provides an answer to the most pressing need of large groups of people: the necessity of obtaining monetary credit for various purposes.

Today, it is quite clear that credit and saving cooperatives are facing serious and fundamental problems. Issues at the centre of these problems include such basic concepts as the nature and aim of the cooperative, as well as its structural and the principles on which it operates. We are witness to severe managerial problems. Even worse, among the majority of members of credit and saving cooperatives throughout the

world and, in particular, among their administrators, there is a lack of understanding of everything connected with the processes by which this particular form of cooperative operates. Thus, in the everyday life of the cooperative, a basic, simple formula enabling us to determine its operating and service costs is lacking. Another key problem is the credit and saving cooperative's ability and, in practice, its failure to initiate projects for increasing revenues, both via the use of accumulated savings and by acting as a channel for transferring outside sources of finance to its members. As far as the five above-mentioned problems are concerned, it transpires that credit and saving cooperatives around the world do not properly satisfy their members' needs. In most cases, in fact, the members of the cooperatives, including their administrators, are quite unaware and quite unable to comprehend the problems in question.
The aim of this paper is to throw new light on the above mentioned problems and discuss them from a different angle. A new look at the credit and saving cooperative, particularly in the developing countries, will serve to re-emphasize the overwhelming importance of this form of organization to the economic progress of nations throughout the world.

2. **The Nature of the Credit and Saving Cooperative**

What do credit cooperatives have to offer? Apart from avoiding the difficulty, red tape and sometimes even outright impossibility of obtaining credit from a bank, the answers are many. The credit cooperative satisfies the requirements of its members without undue complications. Thus, it provides them with interest on their respective shares and rewards for participating in its operation. The credit cooperative helps to-prevent or over come poverty. It furthers members' education, as well as a spirit of mutual aid and self-reliance. This form of cooperative also encourages productive activity by providing credit required by its members and, in particular, leads to a greater understanding of democracy and the democratic process. What then, is the credit and saving cooperative?

2.1 **The Saving Aspect**

It is a cooperative which encourages its members to save money and enables them the obtain loans they may require for various purposes from their accumulated savings. This definition provides an indication of the two main tasks of the cooperative. The first task is to enable members to save their money on a regular basis, or according to their needs. The member saves his/her money within the framework of the cooperative. Knowing that he/she will receive a suitable return for his effort, in the form of interest on his savings. Accordingly, in order to encourage savings, it is desirable to pay members interest at a higher rate than that obtainable at any other type of financial institution. The member will then realize that it is preferable to save with his/her own cooperative. Cooperatives in many countries make the mistake of paying interest on their members' savings at a lower rate than that offered elsewhere.

2.2 **The Credit Aspect**

The second task of the cooperative is to grant loans to its members. Loans are granted from the members' accumulated savings. Obviously, not all the members can take out loans, or obtain them immediately or simultaneously. Members are granted loans in accordance with their seniority within the cooperative and the amount of their savings. Generally speaking, the size of loans granted from the cooperative's fund is governed by the liquidity regulations of the country in which it is located. Clearly therefore, the size of loans granted to members does not exceed the total of their savings. But there are some exceptional cases where the cooperative serves as an intermediary for obtaining additional credit for a members. This subject will be discussed more extensively later. The member pays the (cooperative) fund interest on the credit he receives. The rate of interest will be lower than that at other, commercial financial institutions, for this is part of the service the cooperative provides to its members. The interest rate is calculated according to a simple formula: the total interest paid on the loans granted by the fund must cover the total amount of interest paid to members on their savings as well as the fund's total operating cost. Clearly, the more efficiently the fund is managed, the smaller the difference between the interest charged on loans and the interest paid to members on their savings - a factor which also encourages members to save more.

2.3 **The Differential Between Saving and Credit**

Let us take an example where the banks pay interest of 7% on savings, while the interest charged on loans is 15%. On the basis of this 8% differential, therefore, the cooperative must cover its entire operating expenses, plus a certain reserve for unforeseen circumstances. It also follows that these operating expenses must be much lower than the 8% differential, in order to ensure that the interest paid on members' savings will be higher than that available elsewhere and that the interest on loans granted to them will be lower. A common misunderstanding among cooperative members is that the cooperative should earn profits in the course of the year in order to pay interest to members. Making profits is not the objective of the cooperative, which is actually intended to be a system that exclusively serves its members. Theoretically, it could be said that the ideal cooperative is one which ends the year with zero profits or surplus. This means that it would have served its members in the best possible manner, by collecting the minimum amount necessary to cover its operating costs while enabling members to obtain the maximum service from it.

2.4 **The Surplus**

Although a cooperative does not make profits, it is reason able and desirable for it to run up surpluses. Surpluses are created in the cooperative because the world we live in is full of uncertainties. To protect itself against these uncertainties, the cooperative must marginally in crease the amount collected to cover its annual expenses. The surplus created as a result will be used to implement the fourth principle of cooperation (including division among members). The surplus will be distributed among members in proportion to the size of the loans they have taken out, and not in accordance with the amount of their savings accumulated in the cooperative.

2.5 **The Interest on Share Capital**

The interest paid on share capital must also be considered. Every member joining the cooperative must acquire only one share unit. According to the third principle of cooperation, a limited amount of interest may be paid on members' shares. This is a very misleading approach. Share capital in a cooperative should be remunerated in any form or way.

2.6 **Safeguarding the Real Value of Member's Savings**

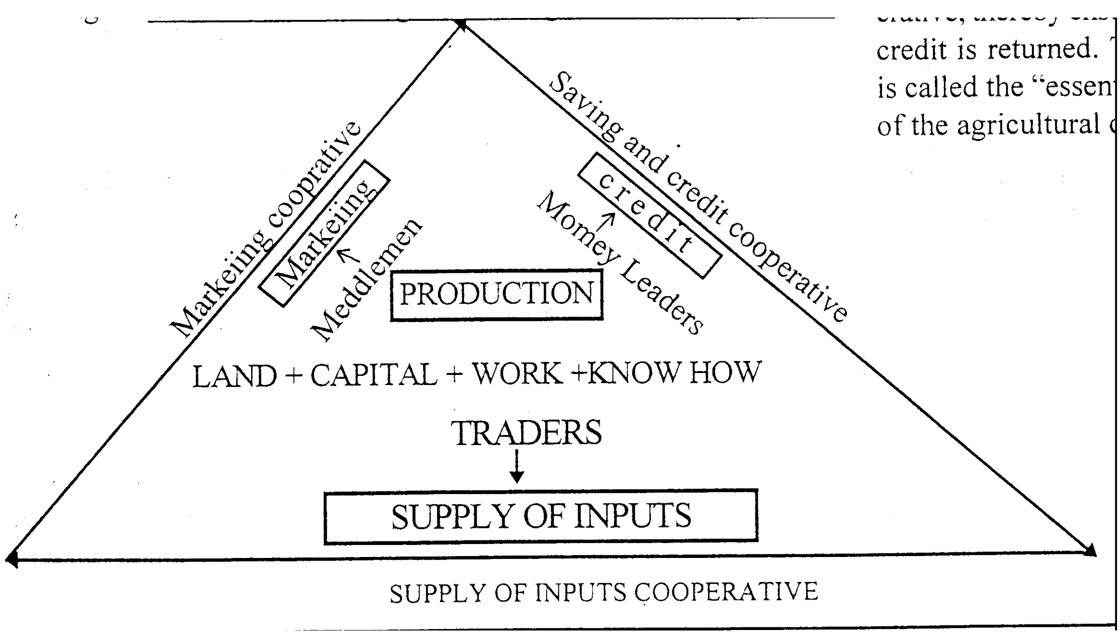
An important objective of credit and saving cooperatives is to safeguard the value of member's savings in real terms. As previously mentioned, credit and saving cooperatives have to pay their members interest at rates higher than those paid by commercial financial institutions. But this is not the whole story.

Most countries suffer from inflation, and the annual rate of inflation is usually higher than the rate of interest, which credit cooperatives pay to members on their savings. As a result, the real value of members' savings is eroded. Most people are unaware of this and lose money every year. In some countries, savers receive interest of 10% per annul, while the prevailing rate of inflation may be as high as 50% or even 100% annually. In such a case, therefore, it is not difficult to calculate how much members are losing on their savings. A savings fund run by those who are unaware of this problem is effectively failing to carry out one of its most important goals - maintaining the value of its members' savings.

2.7 **A Credit Channel for Productive Purposes**

Thus brings us to another task of the credit cooperative. As it is built on the principles of mutual aid and responsibility, the cooperative effectively acts as a guarantor for its member's loans. An individual requiring a loan, which is usually for productive purpose, will find it very difficult to negotiate with a bank. He will often receive a negative reply and even if his loan application is approved, he will have to produce a large number of guarantors and fulfill numerous conditions aimed at assuring the bank that the loan will be repaid. The credit cooperative, by representing a large number of savers and having considerable financial resources at its disposal, provides a safe and convenient channel for the transfer of credit to productive members. The cooperative ensures that loans to members are repaid by centralizing the marketing f members' products or produce under its own auspices. This is an essential prerequisite for cooperatives, particularly for rural, agricultural cooperatives. The granting of credit to a member effectively creates a closed loop within the cooperative. The credit granted is intended for investment, which is meant for production. The resulting produce is marketed by the cooperative, thereby ensuring that the credit is returned. This process is called the "essential triangle" of the agricultural cooperative

Fig. 1. The Essential Triangle of the Agricultural Cooperative



In most agricultural cooperatives throughout the world, this closed "essential triangle" does not exist. The absence of the essential triangle is one of the main reasons why these cooperatives fail.

2.8 **The Situation in Israel: A Case Study**

In Israel today, credit and saving cooperatives exist only in the kibbutz and Moshav (collective and cooperative settlements) sectors, and the cooperative organizations owned by them. The kibbutz and the Moshav are multi-purpose cooperatives'. One of their principal functions is to enable members to save. Naturally, interest is paid on their savings. The Moshav benefits from its members' savings by obtaining more readily available and cheaper credit than that available from the banks. The member, for his part, receives interest on his savings that is higher than the rate paid by banks on saving accounts. An additional function of the Moshav is to extend credit. The Moshav is, in fact, a credit cooperative which provides the sole source of credit needed by its members, both as producers and consumers: The long term credit provided is intended for various agricultural investment projects. Short term credit is seasonal, and designated for the financing of production in the current season.

The Moshav is obliged to market its member's entire output. The Moshav obtains the credit it requires from a number of sources, which are listed here according to their cost.

It is generally accepted that the cooperative cheapest source of credit is its members' savings. After that come various financial institutions, most of which are cooperative bodies belonging to the farmers themselves, such as marketing, supply and purchasing organizations as well as financial funds. After these are commercial banks and other financial corporations, such as insurance companies, whose credit is regarded as the most expensive available.

3. **Further Discussion of the Credit and Saving Cooperative.**

Up till now, we have been trying to describe the credit and saving cooperative as it should be, according to a largely theoretical model which is almost non-existent in practice. In this chapter, will try to examine various relevant problems further and see how they can be solved.

3.1. **Problems in Understanding the Nature of the Credit and Saving Cooperative.**

In most of the world's credit and saving cooperatives, members are not paid interest on their savings. In our study, which involved questioning members of cooperatives from throughout the Third World, a number of typical answers were obtained (2) and included the following:

- This is what we were taught by those who brought us into the cooperative.
- Interest is paid in the form of a dividend at the end of the cooperative's financial year.
- A dividend is paid on member's share capital, which in practice forms the cooperative's accumulated savings. What many cooperatives call Shares are practically very long term unwithdrawable fixed deposits.

Theseanswersindicateanunderlyinginabilitytounderstandthenat ureofthecreditandsavingcooperativeandthemannerinwhichitfun ctions.

3.1.1. **An Imported Product**

The concept of the credit and savings cooperative has been exported to most countries of the world. The same model for the cooperative has been applied in every country, in the same manner in which it successfully operated in the country from which it was imported. Whether it has been imported to Germany, France, Canada or the United States, the model has been copied from that existing in the country where it was invented.

As a result, the manner in which the cooperative system is applied is quite divorced from local realities. Nor does it take into ac count the traditional methods of granting credit which exist in most countries, and no attempt is made to accommodate these methods. There are definitely cases where productive cooperative activity could have been developed on the basis of local models of traditional credit disbursement (3). Even in Israel, imported cooperative systems, such as consumer cooperatives, credit and saving cooperatives and housing cooperatives, no longer exist. They have failed and vanished from the scene, precisely because they did not answer the needs of the local population

3.1.2. **Interest on Savings at the End of the Working Year**

In most credit and saving cooperatives, the accepted manner of paying interest on savings is as follows: At the end of the working year, the cooperative calculates its total income, which de rives partly from interest on loans granted to members, and partly from the cooperative's deposits in banks

or centralized credit organizations. The cooperative's operating costs are then deducted from this income. In most cooperatives, no distinction at all is made between direct operating costs and indirect operating costs or financing costs. The residual income, which in many cases is mistakenly deducted as a surplus, is used for a number of purposes: - member's education and professional training
- transfer to centralized cooperative organizations
- investment in the cooperative
- reserve funds

The remainder is allocated to members as interest on the balance of their savings in the cooperative.

This state of affairs highlights several key problems:

1. The cooperative's annual income is not large. If the cooperative were to loan all its financial resources to the members, then its total annual income would increase. It is quite obvious that the amount the cooperative would obtain in interest on its deposits (in banks or else where) would be lower than the total amount it would receive as interest on loans granted to its members. This, in fact, is the nature and purpose of the cooperative - to serve its members. Granting the maximum amount of loan credit to members, but only against suitable guarantees, will have the effect of increasing the cooperative's total income. This situation will enable higher interest to be given on members' savings, while allowing lower interest to be paid on loans granted to members. The effect of all this will be better service to the member.
2. Allocating interest payments to the member only at the year end, after all expenses have been defrayed, does not provide the management of cooperatives with any incentive to reduce their annual operating costs. In any case, the manager of the. cooperative knows that his expenses will al ways be paid. He

often finds him self in a situation where operating costs are. unjustifiably, high, adversely affecting service to the members. This problem, together with a proposal for solving it, will be discussed later on

3. Most countries suffer from inflation. As a result, their credit and saving institutions are in tended not only to provide loans, but also to protect savings as much as possible from the effects of inflation. In most credit and saving cooperatives, the member repays his loans in monthly installments, which include part of the principal as well as monthly interest on the outstanding balance of the loan. This situation leads to a net inflow of cash to the cooperative. In most cases, these surplus amounts are deposited at various financial institutions, such as banks or cooperative credit organizations, until they are once again granted as loans. The interest received on these sums is low, and always less than the annual rate of inflation in the country in question. This stratagem, which is operated by most cooperative managers, leads to an erosion in the value of their members' income and savings.

4. There is confusion between liquid savings and fixed deposits. One of the most common reasons given for why members do not receive interest on their savings is that there are difficulties in calculating this form of interest, because members are able to withdraw money from the cooperative at any time. This is a very serious mistake. If a member wishes to keep his money in a current account, he obviously cannot be paid interest on it. Yet there should be a hard and fast rule that a member must close his money for a pre arranged period, usually the same length of time for which members are granted loans. The member will only be paid interest on this type of deposit. This type of arrangement would en courage

members to keep their money for longer periods of time, thereby enabling the cooperative to conduct a more rational loan policy. Members needing all or part of their money urgently will be able to receive it at negative interest or draw money, on which they will pay interest, from an emergency fund.

5. In most countries it is or was standard practice to charge interest of 1% a month on the outstanding balance on loans. This is a practice taken from the developed Western nations, but does not take into account the conditions prevailing in the country where the cooperative is located. In countries where the monthly, an not annual, rate of inflation may reach 5-10%, a loan at 1% monthly interest is nothing but a gift and a highly tempting prospect. The relative ease with which such a loan can be ob trained from a credit cooperative will impair the member's ability to make rational financial judgements. The formula, which needs to be applied here, is one, which takes as a basic assumption the service the cooperative provides to the member. This formula states that the member should pay interest on loans he receives from the cooperative at a rate lower than that payable on any alter native source of credit, while the cooperative should pay the member higher interest on his savings than that available elsewhere.

6. Expenses such as members' education and training, investments in the cooperative and re serve funds are extremely important for every cooperative. These expenses cannot be financed from the proceeds of the cooperative's surplus (4), whether they are for the member's economic or social welfare. The burden for financing them should therefore be shared equally among the members.

3.1.3. **Share Capital in the Credit and Saving Cooperative**

The concept of cooperative share capital is far from understood in countries where there are credit and saving cooperatives. Many of their members are unable to distinguish between share capital, and savings and deposits. This confusion is increased by the fact that a member can buy a number of shares, leading him to think that share capital, savings and deposits are one and the same thing. Misconceptions such as these are very common.

First of all, it should be explained that share capital is not a clearly defined concept (5). Share capital is effectively a ticket for entering the cooperative. Paying it in full allows the prospective member to become a member equal to all the others. Secondly, share capital represents the member's relative portion in the total investment necessary to establish the cooperative. (It should be remembered that the money necessary for running the cooperative must be considered as part of its operating expenses, and not part of its share capital.) The credit and saving cooperative usually has a very large number of members. The amount of in vestment required for establishing such a cooperative relative to other enterprises is very low. If we take the total number of members and divide them into the total investment required, then we will have the amount of share capital per member. Usually, the amount in question is relatively, very low. This fact, it should be noted, e makes it easy for a large number of members to join the cooperative. The most important criterion for joining a cooperative is the size of the member's savings, and not the size or number of his shares. In practice, there is no need for a member to buy more than one share. When the cooperative

needs to invest capital, then the size of the member's share must be increased and the difference financed out of his own pocket.
The member's remuneration on his share is the interest paid on it. This interest, it should be noted, is part of the cooperative's indirect operating expenses and is definitely not the same as the interest paid on the members' savings. Avoiding this common mistake will help the vast majority of cooperatives operate and serve their members more fairly.

3.2 **The Surplus in the Credit and Saving Cooperative**

How is the surplus reimbursed to the member of a credit and saving cooperative and from where is it actually derived? The credit cooperative is, in fact, a cooperative which functions on the bass of the differential between its credit and saving operations. The cooperative's income is the interest it receives on the credit it allocates to members, while its outgoing are:
- interest payments on members' savings
- direct and indirect operating expenses.

The cooperative's management is guided by a single criterion: that the rate of interest members pay for credit should be lower than the rate offered by the banks, and that the rate of interest payable to members on their savings should be higher than that available at the banks.

In order to increase its revenues (which consist of interest payments levied on credit allocations), the cooperative must try to grant the maximum possible amount of credit to its members. Theoretically speaking, an efficient cooperative is one which initially grants its members credit allocations equal in value to their total savings, in order to maximize its long term receipts. The aim of such a policy is to offer members as

high an interest rate as possible on their savings, while apportioning a certain amount of money to cover the cooperative's operating costs. This indicates that two principles are at work. - encouraging members to save by offering higher interest rates than the commercial banks
- granting members the maxi mum possible amounts of credit, providing that all the necessary guarantees are supplied.

These two rules can help us understand the system by which a credit cooperative functions. (The credit cooperative's principle of operation, in fact, stems from the difference between the two rates of interest, on loans and savings.) For example, an interest rate of 7% is offered on savings and members are charged 12% interest on their credit allocations. The 5% differential between the revenues on credit allocations, and the expenses incurred in paying interest to savers constitutes the basic capital used for operating the cooperative.

The problem we are faced with here consists of determining the source of the credit and saving cooperative's surplus. It would appear that the surplus is to be found in the 5% differential which covers the cooperative's operating expenses. How ever, if the cooperative is run efficiently, it should be possible to re duce its operating expenses, to some 4%, for example, in which case there would be a surplus of 1 %.

Who receives the surplus accrued? According to the fourth principle of cooperation "the surplus resulting from the operations of a cooperative should be reimbursed... amongst members proportionately to the business transactions they have undertaken with the (cooperative) society".

Two incidentals here can help us understand the question of the surplus:

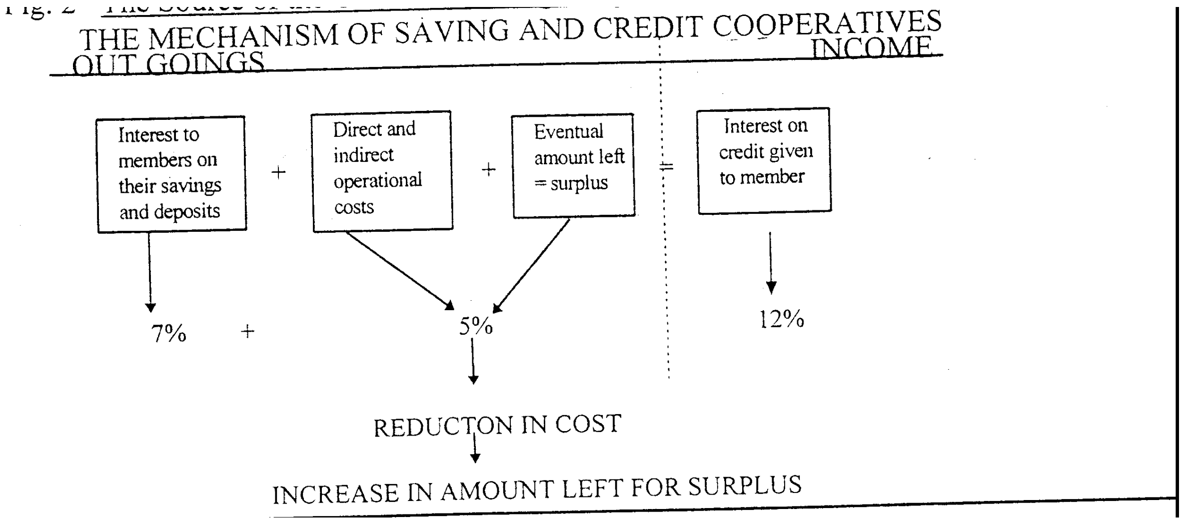
- the surplus resulting from the g operations of a cooperative
- the payment proportional to a member's transactions with the cooperative society.

In credit cooperatives, the income-generating operations are the credit transfers. The interest obtained from these should cover interest payments to savers, as well as operating expenses. Any remaining sum is a surplus - so we see that the surplus goes to those who have obtained credit from the cooperative.

We must now consider how the surplus will apportioned among the members in accordance with the above-mentioned principle.

Each individual's share of the surplus will be proportional to the amount of credit he has received from the cooperative. This concept should prove that savings in operating costs lead to a reduction in the interest rates charged in members' credit allocations.

Fig 2. **<u>The Source of Credit and Saving Cooperative's Surplus</u>**



3.3- **The Remuneration of the Manager**

There is another problem to consider: the method for remunerating the manager of the cooperative. In order to provide the manager with the necessary motivation for his task, he must be paid a reasonable salary reflecting his success in running the cooperative efficiently. The manager needs to earn an amount which is sufficiently high, and above traditionally accepted wage scales, and which will induce him to pro duce satisfactory results on be half of the members.

How can this be done? The answer is to pay the manger a percentage of the cooperative's revenue, that is, a percentage

of the interest charges on members' credit transactions.
What are the resulting practical implications for the cooperative?
1.By receiving a percentage of the interest payments charged on credit transactions, the manager should be motivated to increase the total amount of credit granted to the members.
2. The sum he receives is totally dependent on the amount of money saved by the members, as the cooperative cannot grant credit in excess of its overall receipts from members' savings.
3. The manager is aware that ca any increase in his salary is dependent on the members' receiving an increased amount of credit which, in turn, depends on their saving an increased amount of money.
4. The manager, as a result, will do everything in his power to encourage members to save, in order to increase the level of credit available.
5. Members will have an incentive to save if the interest rate accrued in so doing is favorable, if the manager is efficient and if the manager does his utmost to reduce the cooperative's operating expenses.
6. The manager is paid a salary commensurate with his performance. So theoretically, if he is highly remunerated he will be less inclined to indulge in any form of financial abuse.

3.3.1. **Internal and External Forms of Motivation**

The formula suggested here is an attempt to increase the manager's motivation by external factors (as a contrast to self-motivation), which will have the effect of encouraging him to alter his behavior and strive to improve the results of his work. Internal factors (connected with self-motivation), such as work achievement, a desire to be appreciated, a sense of responsibility and a desire to advance, all of which are recognized as influencing a person to increase his managerial skills and, in particular, achievements, are, transpires, almost totally insignificant in many countries. The economies of many developing countries are influenced by the economy of affection. This is a phenomenon, which prevents people from being influenced by the above-mentioned factors and leads those with various levels of responsibility to take actions to which do not benefit the organizations they manage (6). On the other hand, those factors which tend to encourage people to earn more money, in countries where wage levels are not sufficiently flexible to adequately recompense the manager, can lead to improved performance on the part of management. The cooperative, as with other wage systems in many countries, does not pay high salaries to- its managerial staff. Here, it is proposed that the cooperative's manager be paid according to his work performance. The better the result she obtains for the cooperative, the more highly he will be remumerated, while every member, of the cooperative will benefit as a result. This is a feasible and desirable method of solving the problems facing the cooperative and its manager wherever the economy of affection is prevalent.

3.3.2. **Members' Loan Guarantees**

There are very many cases of credit and saving cooperatives where a large number, of members fail to repay their loans. Obviously, a system, which is incapable of collecting money owed to it, is like a man sawing off the branch of a tree on which he is sitting- both are doomed to fall. Why is it so difficult to collect outstanding debts owed to the cooperative?
The answers are many and relate mainly to the fact that once a member decides not to repay, there is no way the cooperative can collect his debt. The cooperative is unable to locate the

debtor, who may often be quite unable to pay, so it is left empty-handed. This is what happens to cooperatives operating in countries where the economy of affection dominates, and hinders the operation of organizational mechanisms, which in other countries, work perfectly.

The most important advice for every cooperative, clearly, is to reinforce its system of loan guarantees and securities. A member needing a loan must offer sufficient guarantees to ensure that the cooperative will be able to collect the debt. Crucial as this requirement may be, members always find ways of avoiding it (7). But if we oblige the cooperative manager to observe this requirement, then we are introducing some of the principles of the economy of affection into our own system, thereby increasing the cooperative's ability to operate successfully.

The cooperative manager would, as previously mentioned, receive a percentage of its income, that is, a percentage of the interest the cooperative charges on loans granted to members. He would receive this payment only when the loan and the interest on it are repaid. If the loan is not repaid, then the manager will suffer a loss in income. By this process, we increase the manager's personal involvement and degree of motivation. He will realize that every loan issued by the cooperative must be accompanied by suitable guarantees and securities. What is more, as the manager’s income will be reduced if the loan SI§1 is not repaid, he will do all he can to ensure that this does not happen. Accordingly, he will use the methods available within the traditional framework of the society in which he lives. Nobody likes to lose his own money, so by looking after his own livelihood, the manager will also be safeguarding the cooperative's money, This method is likely to create a situation where the cooperative manager earns a very high salary. This situation works to the advantage of the cooperative's members, as the manager will have an interest in reducing its operating expenses, which will increase their own earnings. Another advantage of the method proposed here is that it will deter the manager from embezzling the cooperative's money, as such an act would be equivalent to slaughtering the proverbial hen that lays the golden eggs.

4. **The Credit and Saving Cooperative as a system for Financing Production**

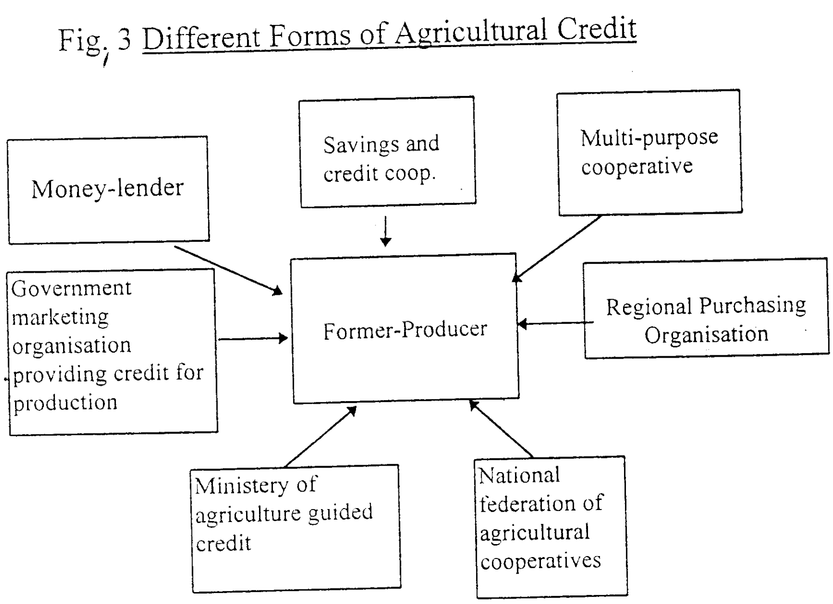
In the Third World, the credit cooperative very often refrains from granting credit, particularly when it is intended for productive purposes. We have already discussed this problem and the damage caused, whereby the cooperative will not allocate any of its financial resources as credit to members. Now, we will try to examine the more specific aspect of credit allocations for production in particular.

Credit is the source of all stages of agricultural production. The cost of credit and its scarcity is a major thorn in the side of most of the world's farmers. In many Third World countries, cooperatives will just not grant their accumulated money as credit for financing production. In conversations with members of agricultural cooperatives in the Kivu region of Zaire (8), we heard the recurring complaint: "We save with our local credit cooperative. We have already accumulated considerable sums of money, but when we go and ask for credit to develop our cooperative, we are rejected on the grounds that this is part of the cooperative's regulations and that this is the law." This is an unhealthy situation. It is a distortion of the basic principle behind the credit and saving cooperative and forces farmers to take loans from the banks or moneylenders.

4.1 Different Forms of Credit for Agricultural Production

The following survey examines the various forms of credit available for agricultural production. We may begin by defining the different systems available for obtaining agricultural credit. The farmer plays a key role in our study. What are the sources of credit at his disposal?

Fig. 3: **Different forms of Agricultural Credit**



4.1.1 **Traditional Forms of Credit**

In traditional societies, fanners needing credit may often turn to moneylenders and middlemen. The interest charged on credit from them is generally very high.

4.1.2. **The Credit and Saving Cooperative**

If farmers organize themselves to form a credit and saving co operative, they will be able to obtain credit much more cheaply than with money-lenders. But this credit will be limited in volume by the size of the credit cooperative and its state of development.

4.1.3. **Multi- Purpose Cooperative**

The third source of credit is the Multi -purpose cooperative, of which the Moshav and kibbutz are examples. Credit and savings operations are among the most important functions of the motive and kibbutz, which, be cause of their diversified range of activities, have far greater resources than the single-purpose credit cooperative. They can also be involved in all aspects of credit allocation, including determining its volume and obtaining the necessary guarantees (9).

4.1.4. **The Regional Purchasing Organization and its Functions**

Although individual kibbutzim and Moshavim play a very important role in credit allocation, they are, however, unable to effectively satisfy the farmer's most pressing needs. Farmers know that their combined membership is not large enough to provide a turn over sufficient for the guarantees required by the banks providing credit. As a result, they have grouped themselves into regional purchasing organizations for obtaining the production inputs (10).

A. **Credit Supply**

Each regional purchasing organization is made up of between 15 and 20 Moshavim or kibbutzim. These collectives organize them selves in order to streamline the large number of procedures, which must be completed to obtain credit. This is how the collective farmers obtain the finance necessary for purchasing their production inputs, which are mainly feed stuffs for cattle and poultry. Buying these items re quires a great deal of working capital, which only a powerful body, such as the regional purchasing organization, can provide.

B. **Credit Regulation**

The secondary function of the regional purchasing organization is that of a credit regulation agency. We know that the cycle of agricultural production varies from one Moshav to another. There are seasons when the farmer invests money and uses all his available financial resources. And there are seasons when he sells his produce and is paid for it. During the latter seasons, the farmer is temporarily in surplus. This surplus generally occurs with all the Moshav farmers in the same season.

The regional purchasing organization will, as a result, use the surplus moneys by distributing them among the various member Moshavim that are still in the production stage and therefore need considerable credit allocations (11). The regional purchasing organization thereby frees the member Moshav from all the bureaucratic procedures involved in obtaining credit. All the Moshav has to do is pro vide the regional purchasing organization with guarantees of its members joint responsibility fo repaying the credit provided.

C. **Rural Industrialization**

The third field of activity of the regional purchasing organization is rural industrial development. This refers to industries located in rural areas close to the member settlement
industries located in rural areas close to the member settlement
and which are mainly involved in processing or packing agricultural product. Examples of these industries are chicken and turkey slaughter-houses, packing plants for export consignments of fruit and flowers, processing centers for

cotton fibers and feed stuff production plants. Agricultural purchasing organizations are therefore secondary cooperatives, that is, cooperatives whose members are themselves cooperatives.

4.1.5. **National Federations**

The farmer has another credit source at the national level - the cooperative federations. Let us take the example of the Moshav Movement. The federation in this case has a department responsible for liaising with financial institutions to which it can turn for support. The Moshav Movement owns a bank (which is, of course cooperative bank) belonging to all the member Moshavim, and a Moshav fund, which consolidates the financial resources, provided by the Moshavim. The fund is reponsible for supplying credit to the member Moshavim when it is needed. It is also responsible for providing guarantees to the Moshavim when they apply for credit from various financial institutions. The guarantees for each credit allocation granted to a Moshav are as follows:
-25% of the guarantees must be provided by the Moshav's individual members. The Moshav provides the bank with a document confirming the decision of its general meeting to approve the loan, and another document containing the signatures of the members guaranteeing the loan.
-50% of the guarantees are provided by the regional purchasing organization.
-25% are provided by the Moshav Movement Fund.
The regional purchasing organization and the Moshav Movement, it should be noted, hold permanent joint guarantees of all their Moshav members. In addition, the Moshav Movement organizes its financial and economic institutions to provide an insurance service for all members of

the movement as well are served fund for elderly members. The movement also provides emergency credit to its member Moshavim (12).

4.1.6. **Guided Credit**

The Ministry of Agriculture plans the distribution of credit through its guided credit department. This department is responsible for allocating credit from governmental sources to credit applicants in the agricultural sector. It is also responsible for ensuring that the credit granted is properly used.

4.1.7. **Marketing Agencies**

Various governmental marketing agencies, mainly concerned with financing exports, provide another source of agricultural credit. These supply special credit allocations, which are invariably short-term but carry a relatively low rate of interest. The credit is granted to a farmer as soon as he signs a contract, via his Moshav, to export all of his production through the governmental agency. The credit granted is repaid in installments when the farmer begins to export his produce.

4.2 The Essential Triangle of Production (ETP)

Agriculture is of course based on production. But the farmer cannot produce if he does not have the necessary agricultural inputs. In order to acquire them, he needs finance, which he usually lacks. Consequently, he has to find a source of credit in order to buy the inputs he needs. Once he has done this, the farmer is able to start producing. Eventually, he will have to repay the credit, which has been granted. By marketing his

produce, he receives money, which he can use to repay his debts. These transactions are illustrated by a triangle whose sides represent credit, inputs and marketing. In short, the farmer obtains finance for purchasing the inputs necessary for production which, when it is sold, will provide the money, to repay the initial credit granted.
In a, traditional society, the farmer uses moneylenders and obtains credit at a very high cost. He buys his inputs from traders who charge high prices and impose stiff terms of payment. The farmer's production is purchased by middlemen who pay the lowest possible price for it. This situation, which is termed as traditional, is very widespread and always operates to the detriment of the farmer. It can, however, be changed by introducing into the previously described triangular relationship an additional element for the benefit of the farmer, namely, the cooperative.
The credit and saving cooperative provides the farmer with the credit which is essential for purchasing production inputs from a supply cooperative. This is the starting point of production. The sale of all the fanner's agricultural produce via the marketing cooperative enables him to repay the credit he has received, at the end of the farming season. Clearly therefore, the addition of the cooperative to the essential triangle of agriculture promotes agricultural and rural development (13).

In traditional farming societies, the triangle is always closed. The money-lender, the trader who sells farming inputs and the middleman who sells the agricultural produce - who may be a number of people or one and the same person - keep a tight grip on their money. When they provide credit for agricultural production, therefore, they do so with an eye to controlling the market, which ensures that they get their money back.
In cooperative systems through out the world, this

consideration is ignored. There is no need for the essential triangle of agriculture to be closed in order to as sure the success of the cooperative. But every cooperative sys tem involved in agricultural production must ensure that those providing credit will always be able to get their money back when produce is sold at the end of the farming season.

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