AGRICULTURAL CREDIT AND CAPITAL FORMATION

Dorris D. Brown*

The overall theme of this 16th IAAE Conference is Decisionmaking in Agriculture. Three of the five papers presented in this section deal with models for capital formation. One paper is concerned with the cost and use of agricultural credit, one is concerned with the distribution of savings from group-type farming. This gives us discussion possibilities covering a wide range and broad scope of theory and practical agricultural credit and capital formation problems.

Love, in his paper, states that the purpose of providing agricultural credit is to increase production; and, hence, capital formation. Burger, Levi and Deaton discuss models that measure the impact of capital formation in agriculture. Burger and Love would have the flow of capital directed toward the elimination of subsistence farming. Deaton contends that peasant societies have a special characteristic of ceremonial and ritual expenditures that represent an important form of capital formation that should be added to the typical two-sector growth model. Levi gives such a revised model additional support by adding non-cash labor investment to the system.

Dr. Burger's paper states that the sources of investment capital include: (a) "forced" and voluntary savings in agriculture; (b) transfers from other indigenous sectors; and (c) transfers from external sources. She pleads for national investment policies that would abolish subsistence farming, direct agricultural investment capital to activities that increase capital formation and capital-labor productivity, and stimulate industrial development. Subsidy techniques would be used only when capital costs per unit of output are increasing and net income rates are decreasing. She includes a residual factor in her model to account for the effect of incremental investments on existing resources.

Levi proposes that unpaid family labor inputs used to improve productivity of land and other resources represent important sources of capital formation influencing agricultural development. Therefore, the enhanced productivity and capitalization of resources receiving family labor result in total investment greater than total cash savings. He suggests that unpaid family labor inputs represent foregone non-labor values with relatively low opportunity and social costs. Family labor investment is said to be greater on small farms than on large farms. Levi does not specify whether the skill of the managerial input has a similar effect. I would content that it does, particularly on the larger farms.

The Deaton paper, consistent with Veblen's theory of the leisure class, suggests that ceremonial and ritual expenditures of peasant

*International Bank for Reconstruction and Development, Washington, D.C.

societies should be considered as a capital formation phenomenon. He does not differentiate between ritual expenditures that are consumed in the short-run from longer run investment type ritual expenditures. He supports investment in the rural artisan sector because of its low opportunity input cast. He also suggests that investment in the commercial agricultural sector and modern industrial sector have only a minor impact on solving problems of unemployment. He would direct investment to approving and participating peasant societies.

Given a national policy to provide institutional finance to subsistence farmers, Mr. Love leads us through some of the practical problems of establishing viable self-supporting agricultural credit institutions for small holders. He provides criteria for measuring success of the institution and of evaluating viability of each loan application. Decision-makers must consider the factors he has stated.

The Hombrados paper provides an interesting case study regarding distribution of profits between contributors of land and labor in cooperative farming institutions. He has made an important contribution to our concern for capital formation and the contrast in returns to labor as compared to returns to capital-labor productivity in the other four papers. He does not inform us which system results in optimum capital formation and productivity.

For purposes of discussion the following issues are suggested:

1. Does the typical two-sector development model need further specification? If so, are the parameters suggested appropriate?

2. Which stimulates capital formation and investment most with small farmers:

   (a) Increasing the rate of return to capital productivity and, hence to capital and management;
   (b) Increasing returns to labor and labor productivity;
   (c) Investment in family labor activities;
   (d) Investment in ritual activities; or
   (e) Some combination of the above.

3. The relevance of changing capital-output ratios on capital formation, investment and agricultural development.

4. Given the situation of high risk, low rate of return and high cost of delivering investment capital to subsistence agriculture; what is the "best" socio-economic use of scarce capital resources? How can the small farmer problem be solved?

5. What is the role of agricultural credit institutions in capital formation? How can they be used more effectively?