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AGRICULTURAL CREDIT IN COSTA RICA:
DIAGNOSIS AND RECOMMENDATIONS

By

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A PLAN B PAPER

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Dedicated to
My wife Maria T., my children, Carla M.,
Gerardo J. and Sergio, and my mother,
Mrs. Eida

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CHAPTER 1

INTRODUCTION

1.1 Introduction

Although credit can be directed with sufficient facility toward some economic activities, the same cannot be said about agriculture, first because there are thousands of clients and secondly, most of them do not meet the requirements for obtaining a loan. Moreover, they do not know how to utilize credit and frequently, they do not accept the general conditions that the credit institutions establish. Unfamiliarity with the sources of funds is another problem.

Therefore, if credit does not accompany other complementary services, like technical assistance for example, the farmers present low modernization indexes, and productivity levels are not very different in relation to those who do not use credit.

Given the special characteristics of the agricultural¹ activity in Costa Rica (low level of technology, low yield, etc.), credit is required more than in the remaining economic activities. However, there are no reliable statistics on the

¹This term includes the credit toward agriculture and livestock.

amount of credit that agriculture requires. This amount depends upon credit conditions, alternatives and opportunities. On the contrary, the diverse sources of finance utilized for the farmers are well known, as well as the conditions of each of them. However, it is possible to assure that two-thirds of the total credit comes from the state credit institutions.²

1.2 Purpose of Paper

Given the importance that agricultural credit has for the Costa Rican economy and its role in the country's development, it is necessary to examine the agricultural credit situation with emphasis on the last eight years. For this reason the method of analysis employed in this study is descriptive and diagnostic.

1.3 Objectives

The specific objectives of the paper can be summarized as follows:

- 1) To determine the principal factors that have been affecting credit policy and their significance.
- 2) To suggest, in light of the principal events, modifications of the present agricultural credit policy.

²Gonzalez-Vega, Claudio. "Small Farmer Credit in Costa Rica: The Juntas Rurales". AID, Spring Review of Small Farmer Credit, Vol. II, February 1973.

- 3) To review existing literature in order to know which solutions have been considered in other countries.
- 4) To identify and describe the major sources of credit.
- 5) To describe the nature and dimensions of the Agricultural Sector.

1.4 Organization of the Paper

To accomplish the objectives, the written material is arranged in the following way: Chapter I explains the relevance of credit in agriculture, the purpose and objectives of this study.

Chapter II includes general information about the country and discusses the agricultural sector in some detail for the period 1970 to 1977.

Chapter III describes the different sources and services of agricultural credit, in order to analyze the amounts of credit given for products.

Chapter IV is concerned with the volume of money and credit in the economy and under what terms they are available.³

Chapter V analyzes and evaluates the norms, methods and policies in making loans.

Chapter VI contains the summary and conclusions and recommendations for establishing a new or revised credit policy.

³Nelson, G. Aaron et al. "Agricultural Finance", Iowa State University, Iowa 1973, p. 292.

CHAPTER II

THE AGRICULTURAL SECTOR

2.1 General Information of the Country⁴

Costa Rica occupies the southern part of Central America, where it is bounded on the north by Nicaragua, the southeast by Panama, the east by the Atlantic Ocean (Caribbean Sea) and the west by the Pacific Ocean. The total area is 50,900 square kilometers and its population is about 2.1 million (official estimate of June 30, 1977).⁵ The national capital is San Jose, which is also the capital of the province of the same name. The monetary unit is the colon. The free exchange rate is ¢8.60 to the dollar for purchase and ¢8.54 to sell.

The altitude of San Jose is about 1,160 meters (3,820 feet) above sea level. A mountainous country, Costa Rica ranges from sea level to peaks as high as 13,000 feet.

⁴Instituto Costarricense de Turismo. "General Information". Casa Grafica Ltda. San Jose, Costa Rica, 1977, page 1-2.

⁵Banco Central de Costa Rica. "Cifras de Cuentas Nacionales de Costa Rica. Serie 1957-1976. Estimacion 1977. San Jose, Costa Rica, Junio, 1978, page 24.

Costa Rica has an equable climate the year round, without seasonal variations; in general, the climate is determined by the altitude above sea level. The higher one goes, the cooler the climate. In general, temperatures are fairly constant both day and night. Along both coastlines the climate is one of tropical heat without being suffocating. It is temperate in the Central Valley, where the temperature seldom varies from a maximum of 80 degrees F. to a minimum of 65 degrees at night. Colder temperatures will, of course, be felt in the high mountain ranges.

There are two seasons: dry and rainy. The dry season normally runs from December through April, when the rains begin. During the dry season there is virtually no rain in the Pacific slopes, but the farmlands maintain their traditional green tones. In the rainy season there are generally cloud-bursts in the afternoon, with the mornings brilliant with sunshine. Along the Atlantic Coast the heavy rains normally coincide with the dry season on the Pacific, although the Atlantic side generally has heavier overall rainfall.

Costa Rica is readily accessible by air, land and sea. Visitors from North America, the rest of the Central American countries and Panama may travel by the InterAmerican Highway. Auto travelers from South America still face the problem of the Isthmus of Darien, in southern Panama, where the highway has not been completed. Costa Rica has a total of approximately 22,530 kilometers (about 14,000 miles) of highways, which connect all seven of its provinces.

Two railroad lines unite San Jose, with the Atlantic port of Limon and the Pacific Port of Puntarenas. These ports, together with Golfito (also on the Pacific) are the chief ports of export and import in the country. There are also many local airports throughout the country, in addition to the international airport of Juan Santamaria, 10 miles from San Jose, which handles both international and national flights.

Costa Rica has always been proud of the high literacy rate. Public grammar and high school education is free; there are also many private schools, five universities level centers and numerous educational institutions specialized in vocational and technical training.

Costa Rica has become famous in the history of the Americas as a country without an army, where the solid base of a democratic people has been forged in an atmosphere of peace and tranquility, with permanent respect for republican institutions.

2.2 Economic Importance

Since 1966, Costa Rica's real Gross Domestic Product (GDP) has grown at an average annual rate of 6.4 percent, including the comparatively stagnant years of 1974 and 1975 when the GDP grew at only 5.5 and 2.1 percent, respectively.^{6,7} During

⁶Banco Central de Costa Rica. "Cifras de Cuentas Nacionales de Costa Rica. Serie 1957-1976. Estimacion 1977". San Jose, Costa Rica, Junio, 1978.

⁷Agency for International Development. "An Assessment

these 12 years of relatively rapid economic growth, as is shown in Table 2.1, the agricultural sector was a leading sector, even though its direct share of GDP fell from 23 percent in 1966 to 20 percent in 1975 and 1976, and 22 percent in 1977. This was accompanied by the increased importance of industry, manufacturing and mining, commerce, and general government sectors.

As stated in Table 2.1, real economic growth slowed in the two years following the 1973-1974 international monetary and energy crisis. However, figures for 1976 and 1977 show an appreciable recovery, with the real GDP growth at 5.5 and 7.7 percent during 1976 and 1977, respectively. The agricultural sector has traditionally been and continues to be, the single most important sector in the Costa Rican economy, because it accounts for nearly one-fourth of GDP; three-fifths of total export earnings; and two-fifths of total employment. Furthermore, it has provided a significant share of investment resources and raw materials necessary for the country's industrial expansion. It is interesting to note that between 1965 and 1975, Costa Rica had the fastest growing agricultural sector in Latin America, in total and per capita terms.⁸

Most of this expansion has been in export commodities such as coffee, bananas, sugar, and beef, until recent years

of the Agricultural Sector in Costa Rica." United States, AID Mission to Costa Rica, San Jose, Costa Rica, Feb.1977, page 1.

⁸Banco Interamericano de Desarrollo (BID) et al. "Desarrollo Agropecuario y Rural de Costa Rica, Anexos tecnicos." San Jose, Costa Rica, Marzo-Junio, 1975, page 2.

TABLE 2.1

GROSS DOMESTIC PRODUCT, BY SECTOR OF ORIGIN
(Millions of Colones, Market Prices)

Item	1966	1967	1968	1969	1970	1971	1972	1973	1974	1975	1976	1977*
Agriculture	994.1	1,065.6	1,178.4	1,302.9	1,469.3	1,443.4	1,601.6	1,962.9	2,522.4	3,417.8	4,212.9	5,839.9
Industry ¹	730.9	781.2	897.3	1,004.5	1,192.2	1,325.0	1,507.1	1,903.3	2,677.9	3,427.3	4,072.1	5,123.7
Electricity, Gas & Water	64.4	70.4	83.0	94.3	109.8	127.8	147.0	160.3	205.9	303.7	409.6	533.8
Construction	184.9	204.3	228.1	245.6	277.4	343.3	423.8	507.1	692.6	868.9	1,193.4	1,462.8
Commerce	879.4	918.2	1,011.0	1,116.3	1,371.3	1,502.0	1,651.3	2,054.5	2,754.7	3,203.6	3,832.2	4,865.6
Transport & Storage	179.7	197.8	218.6	250.5	274.2	316.0	362.0	435.6	590.7	788.6	954.7	1,110.3
Banking & Insurance	165.9	187.2	204.4	236.9	302.7	321.0	404.5	508.5	635.3	816.6	1,040.8	1,307.9
Dwellings	391.7	425.8	444.0	467.6	498.7	524.9	553.4	626.5	784.8	1,123.8	1,371.1	1,675.5
General Government	494.8	498.1	541.9	614.5	693.2	813.6	998.0	1,196.6	1,576.4	2,083.7	2,682.2	3,222.2
Other	242.6	255.4	273.1	302.6	335.7	375.2	420.1	495.9	626.7	770.6	906.6	1,130.9
Adjustments	-	29.9	46.9	19.6	-	44.8	146.1	311.2	148.3	-	-	-
TOTAL	4,288.4	4,633.9	5,126.7	5,655.3	6,524.5	7,137.0	8,215.8	10,162.4	13,215.7	16,804.6	20,675.6	26,272.6
Real GDP (1966 Prices)	4,288.4	4,530.7	4,914.6	5,184.5	5,573.5	5,951.3	6,438.0	6,934.3	7,318.8	7,472.5	7,884.8	8,495.1
Percent Increase	-	5.6	8.5	5.5	7.5	6.8	8.2	7.7	5.5	2.1	5.5	7.7

¹Manufacturing & Mining

*Estimated

SOURCE: Banco Central de Costa Rica. "Cifras de Cuentas Nacionales de Costa Rica, Serie 1957-1976. Estimacion 1977. San Jose, Costa Rica, Junio, 1978, pages 12-13.

when extraordinary increases occurred in the production of basic grains (rice, beans, maize, and sorghum). In both the export and foodgrain sectors, increased production has been due to expanded acreage and augmented yields, with increased prices playing an important role in the expansion of area in production and in the adoption of new technology.⁹

The composition of agricultural exports has diversified somewhat during recent years. While coffee and bananas are still the leading crops, sugar and meat have become increasingly important; they increased from less than 10 percent of total exports in 1965 to 16 percent in 1975. However, while both products have since 1975 diminished their shares in the foreign market, they have played an important role in shielding the economy from price fluctuations for traditional agricultural export commodities, even though the overall economy does remain highly dependent on external market forces.¹⁰ (See Table 2.2)

TABLE 2.2
EXPORTS-FOB-BY SECTOR OF ORIGIN
(Millions of Dollars)

Item	1965	1970	1971	1972	1973	1974	1975	1976	1977
<u>TOTAL EXPORTS</u>	111.8	231.2	225.4	280.9	344.5	440.3	487.7	592.9	828.1
<u>Agricultural Goods</u>	86.9	169.9	158.1	206.9	243.2	287.6	317.2	374.7	546.3
Coffee	46.6	73.1	59.3	77.8	94.0	124.8	97.0	153.9	319.2
Banana	28.3	66.8	63.9	82.8	90.7	98.3	134.6	148.7	150.3
Sugar	4.6	10.1	12.9	13.1	21.5	24.4	48.2	24.7	15.6
Meat	5.2	18.0	20.5	30.2	32.6	34.2	32.1	40.5	44.1
Cocoa	2.2	1.9	1.5	3.0	4.4	5.9	5.3	6.9	17.1
Manufactured Goods & Miscellaneous	24.9	61.3	67.3	74.0	101.3	152.7	152.7	218.2	281.8
SOURCE: Central Bank of Costa Rica									

⁹ Ibid., p. 2.

¹⁰ Ibid., p. 2.

2.3 Agricultural Land

Costa Rica's land area is about 5.1 million hectares (12.6 million acres) of which about 3.1 million hectares (7.7 million acres) are in crops and grazing; 1.8 million, or 35.1% of the total land, is occupied by forest; and the remaining 3.6% are swamps and paramos, as shown in Table 2.3.

Between the 1955 Census and the 1973 Census, the area of the country under production increased by 1.3 million hectares, with over 500,000 of the increment in pastures. Thus, the rapidly expanding livestock industry has led the agricultural development taking place in Costa Rica. But in recent years shortages of basic grains and fiber, specially cotton, have

TABLE 2.3

LAND USE AND VEGETATION COVER
Area in Km²

<u>Item</u>	<u>Total</u>	<u>Percent</u>
Crops and Grazing	31,225	61.3
Swamps and Paramos	1,832	3.6
Forest:	<u>17,843</u>	<u>35.1</u>
2nd growth	1,688	3.3
Overmature forest	2,304	4.5
Cutover old growth forest	3,729	7.3
Virgin forest	<u>10,122</u>	<u>19.9</u>
TOTAL	50,900	100.0

SOURCES: 1) Tosi, J. "Los Recursos Forestales de Costa Rica." CCT. 1974
 2) Direccion General de Estadistica y Censos. "Censo Agropecuario de 1973". Costa Rica, 1974.

brought about high incentive prices, causing pasture lands to be diverted to crops. This pattern has been evident in the North Pacific area, especially in the province of Guanacaste.

Livestock, bananas, palm oil, and cocoa are spearheading the development of the Atlantic lowlands where there are poor prospects for basic grains other than rice. The central highlands lead, and have further potential in coffee, fruits, vegetables, and dairying, while topography limits the potential of satisfying additional basic grain requirements from this area. Overall, land availability and the productive potential of the land is not a constraint in Costa Rica.

2.4 Land Tenure¹¹

Costa Rica is still largely a rural economy. According to the 1973 Census, 59.4% of the population is rural. The 3,122,456 hectares in farms is divided into 76,998 farm units. A high degree of land concentration is demonstrated by the fact that 57.6% of the farms average less than 10 hectares each and represent only 4.0% of arable area. On the other hand, farms of over 100 hectares represent 7.3% of the total number of land holdings but cover 67.0% of the total land area available for agriculture (See Table 2.4).

It is noteworthy that a substantial medium farmer group has emerged; farms of 10 to 200 hectares represent 38.9% of the farm units and cover 41.5% of the farm area.

¹¹Agency for International Development. "An Assessment of the Agricultural Sector in Costa Rica." United States, AID Mission to Costa Rica. San Jose, Costa Rica, Feb. 1977, p. 18.

TABLE 2.4

DISTRIBUTION OF TOTAL NUMBER OF HOLDINGS
AND TOTAL LAND AREA OF VARIOUS-SIZED HOLDINGS
- 1963 and 1973 -

Size (Hectare) ¹	Number	%	Area	%
<u>1963</u>	64,621	100.0	2,668,076.8	100.0
Less than 1	3,661	5.7	2,759.0	0.1
1-10	30,377	47.0	125,448.9	4.7
10-20	9,161	14.1	135,026.4	5.1
20-100	17,197	26.6	741,009.5	27.8
100-200	2,237	3.5	308,161.5	11.6
200-1000	1,746	2.7	666,364.7	25.0
1000-2500	183	0.3	258,445.3	9.6
2500 or more	59	0.1	430,861.6	16.1
<u>1973</u>	76,998	100.0	3,122,456.1	100.0
Less than 1	14,413	18.7	6,185.8	0.2
1-10	29,925	38.9	117,666.7	3.8
10-20	8,777	11.4	122,781.3	3.9
20-100	18,237	23.7	783,632.1	25.1
100-200	2,922	3.8	391,733.1	12.5
200-1000	2,424	3.1	915,778.8	29.3
1000-2500	220	0.3	320,924.1	10.3
2500 or more	80	0.1	463,754.2	14.9

¹One hectare = 2,47104 acres

SOURCE: Censos Agropecuarios 1963 y 1973.

Over 90% of the farms in Costa Rica are owner operated. Trends in land use can be seen by comparing 1963 and 1973 census data. The area in farms has grown by 454,380 hectares and the number of farms has increased by 12,377. The majority of the new farms are less than 1 hectare. The number of these small farms has grown by 10,752. Land concentration has increased somewhat in farms from 200 to 1,000 hectares. At the same time land area in 10 to 20 hectare farms has decreased.

Land use patterns have changed rather drastically since 1955 when agriculture was utilizing 26% of the total land area as compared to 1973 when 40% of the land area was in use. Between 1955 and 1973 the addition of 1,285,106 hectares to the agricultural land base showed an increment of only .4% in cultivated crops and 4% in permanent crops in comparison with a 51% increase in pastures and 44% in uncultivated lands. In 1973, 76% of the area in production (not including uncultivated lands) was in pastures, compared with 10% in permanent crops and 14% in cultivated crops.

CHAPTER III
AGRICULTURAL CREDIT SOURCES
AND SERVICES

3.1 Institutional Credit

In Costa Rica the National Banking System is the predominant source of credit for agriculture.¹² The banking system consists of a central bank and four commercial banks, all of which are autonomous institutions of the government of Costa Rica. Until 1948 three of the commercial banks were privately owned. The fourth bank, the Banco Nacional, has always been a government institution, and the other three were nationalized in 1948. Although there are other financial institutions, only the government's four commercial banks are permitted to accept demand deposits.

The Central Bank of Costa Rica was created on January 28, 1950, by Law #1130, and has the usual functions and objectives of a central bank, that is, to control money and credit in order to promote production, economic development, financial stability, and a satisfactory balance of payments.

The Central Bank is headed by a Board of Directors and is organized into eight divisions. One of them is the Division of Economic Studies which has as its chief objectives the

¹²The term agriculture includes both crops and livestock.

investigation of different events related to the process and situation of the country's general economy, and the provision of information about those changes which have occurred. Within this division, the Department of Credit Development has the primary function of carrying out efficient agricultural projects in accordance with sound agricultural, economic, and financial practices.

The General Audit of Banks operates within the Central Bank and exerts vigilance and fiscalization of all divisions and departments of this bank over the rest of the banks, including agencies and branch offices and over any other entities that the laws place under its control.

The commercial banks are: The Banco Nacional; The Banco de Costa Rica; The Banco Anglo-Costarricense, and The Banco Credito Agricola de Cartago and all are regulated by Law #1644 which went into effect, on September 26, 1953. Each of the four commercial banks has two departments, a commercial department and a mortgage department, through which they carry out their credit functions. The Banco Nacional also has a Department of Rural Credit with the function of lending exclusively to small farmers.

The commercial departments are much larger and completely dominate the mortgage departments in lending for agriculture. They operate principally with large corporations, and make short to medium term loans for investment and operation. The mortgage departments work independently of the commercial departments except for those limitations of administrative character that

their organic laws establish. They use finance resources from various sources: capital and reserves; emission and sale of mortgage bonds; external lines of credit, and other sources that the law indicates. Their loans are medium and long term with the objectives of acquiring agricultural or cattle farms, carrying animal husbandry, and building houses, installations, or plants.

The Rural Credit Department of the Banco Nacional promotes agricultural credit and the betterment of the social-economic conditions of small farmers. Among other objectives there are: the promotion of an equitable system of land distribution and the gradual improvement of its exploitation through regional plans of parceling and settling. One additional function is to organize a system of technical help for small farmers, promoting for that purpose the cooperation of diverse national and international institutions specialized in such activities.

The Rural Credit Department, in order to achieve its programs, coordinates the ministries and other governmental institutions specialized in the execution of different functions or services, which must participate in the formation and sound development of rural communities. In order to accomplish these objectives, there are Rural Credit Offices (Juntas Rurales). Each of them has a local board of directors integrated by three people that, together with the delegates, play an important role in allocating credit. For the execution of technical functions such as appraisals, inspections, and advice to customers, the

commercial bank designates the delegate, who must be an agronomist, in order to control, watch over and administer the Rural Credit Offices.

The Rural Credit Offices make loans for the following: agricultural and cattle provisions; fixed assets; machinery and tools; and any other resources that increase the rural sector and serve to expand agriculture. The terms of credit limitation, the interest rates, and the length of loans are established by the General Board of Directors of each commercial bank. The operations effected by the Rural Credit Offices are exempted from the payment of fiscal stamps or letterhead paper fees. The same applies for the certifications emitted by the Public Register or the inscription of constitution, endorsement, and cancellation of mortgages and contracts of pledge conferred to those offices.

The four commercial banks have regional offices. Each of them has a manager who is expected to "live in" and become knowledgeable about his local area and who usually has a background in agronomy. In addition to the manager, most regional offices have a local board of directors which consists of three prominent local citizens (very similar in operation to the Rural Credit Department of the Banco Nacional). Both the manager and the local board of directors can approve small loans, but larger loans must be approved by the central office.

The central offices of the four banks previously mentioned, are in San Jose, the capital of the nation, except for

Banco Nacional. INFOCOOP is the government institution primarily responsible for promoting the cooperative movement in Costa Rica through credit and technical assistance. The major sources of funds for this institution are capital and reserves that come mainly from government contributions, a percentage of bank profits and the tax on soft drinks, and foreign credit. However, in spite of its relative importance, INFOCOOP is not a significant source of institutional credit for agriculture.¹⁵

3.2 Other Sources of Agricultural Credit

There are some other sources of agricultural credit in the country. Among them are the following: about 52 private financiers,¹⁶ predominantly located in San Jose, and frequently pertaining to foreign banks; individuals; general stores (pulperias) cooperatives and business firms. Perhaps the most important of all of them are the commercial firms that import agricultural machinery and equipment (dealers); manufacturing firms and retailers of fertilizer, insecticide, fungicide and other farm inputs. These companies finance the purchasing of machinery and agricultural implements through credits of short, intermediate and long terms. For these loans, the procedure required is quick and opportune and the resources come from foreign countries, rediscounting of documents in the National Banking System, shares,

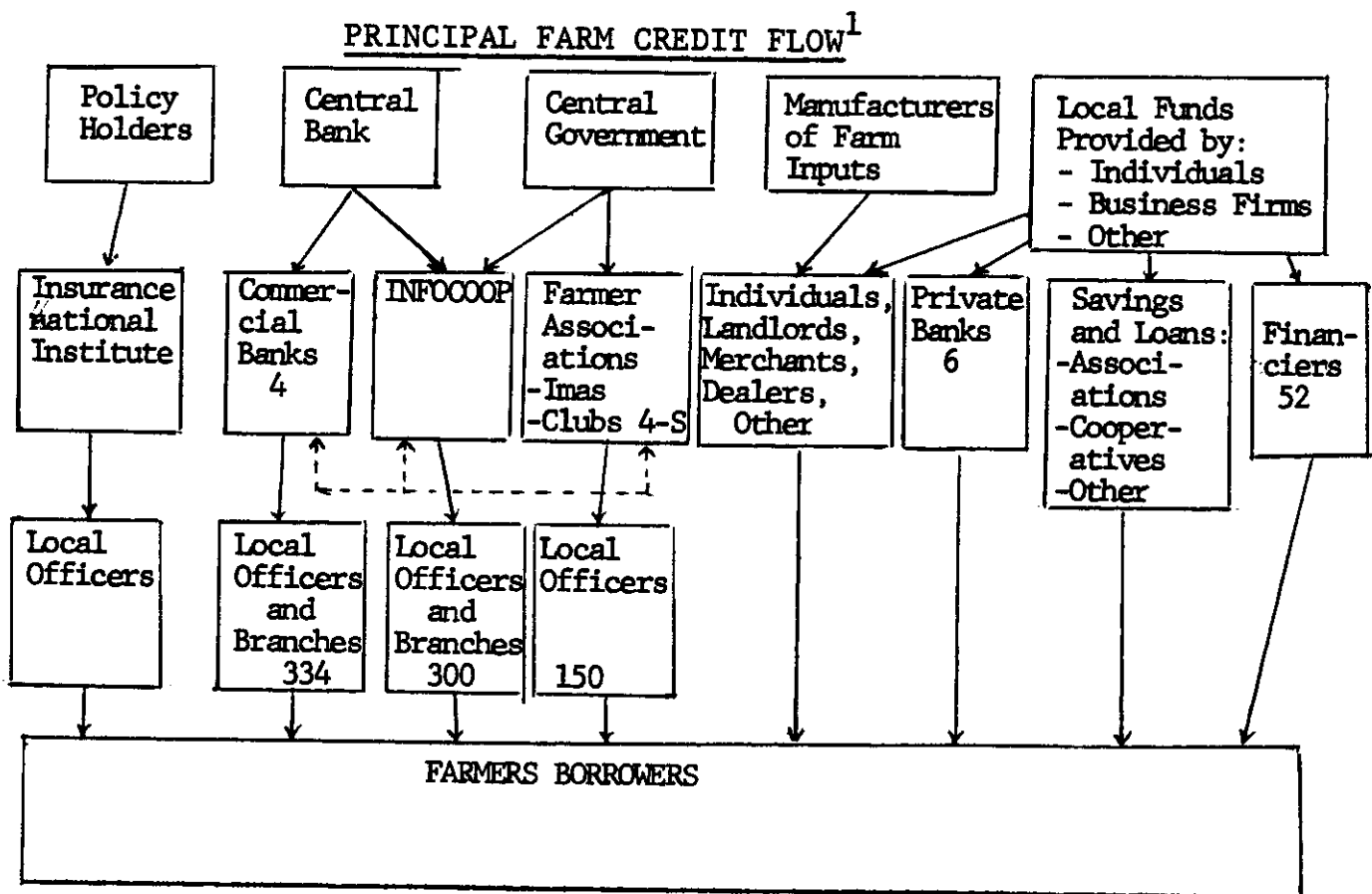
¹⁵Banco InterAmericano de Desarrollo (BID) et al. Desarrollo. . . , op. cit., Costa Rica, 1975, p. 19.

¹⁶Banco Central de Costa Rica. "Oficinas Bancarias y Otras Instituciones Sujetas a la Fiscalizacion de la Auditoria General de Bancos." San Jose, Costa Rica, Dec.31, 1978.

and so forth. Figure 3.1 shows the flow of credit among the most important farm credit institutions in Costa Rica.

Information is not available for determining just how significant these sources are within the total agricultural credit. However, an indicator of its quantitative importance is the fact that in the well-populated areas of the country commercial firms have been established. Moreover, district representatives of these firms travel to less accessible regions in order to extend their companies' business contacts and insure distributors for their products.

FIGURE 3-1



¹An adaptation from the book: Wilcox, W. Walter et al. "Economies of American Agriculture." Englewood Cliffs, New Jersey, 1974, p. 384.

3.3 Geographical Distribution of the National Banking System

The existence of a sufficient number of bank offices throughout the country is one of the basic necessities for establishing a convenient service of agricultural credit. Costa Rica has 334 unit banks of different categories. This large number of regional offices, especially relative to other Central American nations, indicates that banking services are very widespread and that few farms or individuals are isolated by distance from these services.

As shown in Table 3.1, the relative importance of each bank is also noted by the number of regional offices, especially since they disburse more credit for agriculture than the central departments. On December 31, 1978 the Banco Nacional had a total of 225 regional offices, including branches (Sucursales); Agencies (Agencias); Bonded General Warehouses; Auxiliary Cashier's Boxes; Rural Credit Offices; and so on, in comparison with the Banco de Costa Rica which had 58, the Banco Anglo at 35, and The Banco Credito Agricola at 16.

With the purpose that the National Banking System can offer competent services, and the bank's customers can make adequate use of those services, the Central Bank is responsible for maintaining a convenient geographical and institutional distribution of new offices. For determining the establishment of a new bank office any place in the country, the Central Bank considers as its principal factors of evaluation the following: the number of inhabitants, total volume of production, social-economic characteristics, and geographical features of the region.

TABLE 3.1

NATIONAL BANKING SYSTEM
GEOGRAPHICAL DISTRIBUTION OF SERVICES
BY PROVINCE

Province	Banco Nacional	Banco de C.R.	Banco Anglo	Banco Credito Agricola	Total
<u>Costa Rica</u>					
Central Office Depart- ments	4	2	2	3	11
Financial Sections	1	15	1	5	22
Branches	13	14	9	4	40
Agencies	30	15	14	1	60
Urban Agencies	1	7	8	1	17
Auxiliary Cashier's Boxes	76	5	-	1	82
Bonded General Warehouses	11	-	1	1	13
Auxiliary Bonded General Warehouses	1	-	-	-	1
Rural Credit Offices	72	-	-	-	72
Auxiliary Rural Credit Offices	16	-	-	-	16
TOTAL	225	58	35	16	334
<u>San Jose</u>					
Central Office Depart- ments	4	2	2	-	8
Financial Sections	1	2	1	1	5
Branches	1	1	1	1	4
Agencies	6	11	3	1	21
Urban Agencies	1	7	8	-	16
Auxiliary Cashier's Boxes	31	1	-	-	32
Bonded General Warehouses	2	-	1	-	3
Auxiliary Bonded General Warehouses	1	-	-	-	1
Rural Credit Offices	11	-	-	-	11
Auxiliary Rural Credit Offices	5	-	-	-	5
TOTAL	63	24	16	3	106

TABLE 3.1 (Continued. . .)

Province	Banco Nacional	Banco de C.R.	Banco Anglo	Banco Credito Agricola	Total
<u>Alajuela</u>					
Branches	4	4	1	-	9
Financial Sections	-	4	-	-	4
Agencies	6	1	3	-	10
Auxiliary Cashier's Boxes	15	1	-	-	16
Bonded General Warehouses	2	-	-	-	2
Rural Credit Offices	22	-	-	-	22
Auxiliary Rural Credit Offices	1	-	-	-	1
	50	10	4	-	64
<u>Cartago</u>					
Central Offices Departments -	-	-	-	3	3
Branches	2	2	1	2	7
Financial Sections	-	2	-	3	5
Urban Agencies	-	-	-	1	1
Auxiliary Cashier's Boxes	8	-	-	1	9
Bonded General Warehouses	2	-	-	1	3
Rural Credit Offices	6	-	-	-	6
Auxiliary Rural Credit Offices	2	-	-	-	2
TOTAL	20	4	1	11	36
<u>Heredia</u>					
Branches	1	1	1	-	3
Financial Sections	-	1	-	-	1
Agencies	2	1	1	-	4
Auxiliary Cashier's Boxes	4	-	-	-	4
Bonded General Warehouses	1	-	-	-	1
Rural Credit Offices	2	-	-	-	2
TOTAL	10	3	2	-	15

TABLE 3.1 (Continued. . .)

Province	Banco Nacional	Banco de C.R.	Banco Anglo	Banco Credito Agricola	Total
<u>Guanacaste</u>					
Branches	3	3	2	1	9
Financial Sections	-	3	-	1	4
Agencies	6	-	3	-	9
Auxiliary Cashier's Boxes	5	1	-	-	6
Bonded General Warehouses	2	-	-	-	2
Rural Credit Offices	13	-	-	-	13
Auxiliary Rural Credit Offices	1	-	-	-	1
TOTAL	30	7	5	2	44
<u>Puntarenas</u>					
Branches	1	2	2	-	5
Financial Sections	-	2	-	-	2
Agencies	7	2	4	-	13
Auxiliary Cashier's Boxes	10	-	-	-	10
Bonded General Warehouses	1	-	-	-	1
Rural Credit Offices	14	-	-	-	14
Auxiliary Rural Credit Offices	4	-	-	-	4
TOTAL	37	6	6	-	49
<u>Limon</u>					
Branches	1	1	1	-	3
Financial Sections	-	1	-	-	1
Agencies	3	-	-	-	3
Auxiliary Cashier's Boxes	3	2	-	-	5
Bonded General Warehouses	1	-	-	-	1
Rural Credit Offices	4	-	-	-	4
Auxiliary Rural Credit Offices	3	-	-	-	3
TOTAL	15	4	1	-	20

SOURCE: Banco Central de Costa Rica. "Oficinas Bancarias y otras Instituciones Sujetas a la Fiscalizacion de la Auditoria General de Bancos. Costa Rica, Dic.31, 1978, pp. 1-3.

3.4 Allocation of Credit By Activities

Table 3.2 shows how credit from the National Banking System has been distributed among the principal sectors of the Costa Rican economy. During 1965 the credit outstanding at the end of the year for Agriculture was 434.1 million colones while in 1977 the amount was 1,590.7 million colones. On the other hand, Livestock and Industry in 1965 showed figures of 203.6 and 205.1 million colones, respectively, increasing to 1,647.5 and 1,900.4 million in 1977. During those thirteen years Livestock and Industry increased more rapidly than any other activities, while credit for crops decreased in 1972 and its growth rate in most individual years has almost always been well below the average for total credit.

Over the period 1965-77, the growth rate of credit for Livestock was slightly above average, but not high enough to bring the growth rate for crops and Livestock together up to average. Credit for Industry grew more rapidly than total credit, while the growth of credit for other purposes varied greatly from year to year. From 1965 through 1977 credit for Agriculture increased 266%, that is, at an average rate of 20% per year; however, during the same period, Industry obtained a total increment of 826% for an average per year of 64%.

Table 3.3 presents the percentages of credit outstanding at end of each year, and here once again, the declining share of crops in the total credit may be observed. In the same thirteen years, Agriculture decreased by 60%, while Industry increased by 51%. Nevertheless, although agriculture is losing importance in

TABLE 3.2
 NATIONAL BANKING SYSTEM¹
 AMOUNT OF CREDIT OUTSTANDING AT END OF
 YEAR, BY ACTIVITY, 1965-1977
 - Millions of Colones -

Item	1965	1966	1967	1968	1969	1970	1971
Agriculture	434.1	446.2	450.1	460.9	474.3	560.7	622.0
Livestock	203.6	218.6	251.6	285.2	330.7	386.7	528.5
Industry	205.1	198.4	232.1	247.2	271.9	325.3	374.2
Electricity	6.4	6.9	29.2	28.6	6.3	5.3	4.5
Commerce	56.6	51.6	40.5	36.8	32.3	40.9	108.2
Service	62.0	62.0	66.8	60.0	65.3	84.9	118.1
Dwelling	101.5	104.1	118.6	125.8	133.4	150.3	183.5
Personal Credit	55.2	54.6	58.8	61.1	59.2	60.8	149.0
No Classified Credit	46.6	45.9	30.8	28.0	29.5	26.7	26.7
TOTAL	1,171.1	1,188.3	1,278.8	1,333.6	1,402.9	1,641.6	2,114.7

Item	1972	1973	1974	1975	1976	1977
Agriculture	620.5	620.7	798.4	1,161.5	1,475.9	1,590.7
Livestock	632.2	817.9	1,054.2	1,200.4	1,408.3	1,647.5
Industry	434.7	586.6	974.4	1,324.9	1,560.9	1,900.4
Electricity	5.2	4.1	2.5	3.3	2.3	2.1
Commerce	136.1	111.9	228.6	335.0	375.2	408.0
Service	149.2	144.0	220.9	340.8	447.7	625.4
Dwelling	206.9	232.2	275.3	467.3	597.5	784.7
Personal Credit	178.2	175.4	216.2	280.9	298.8	304.5
No Classified Credit	26.8	15.7	39.9	45.8*	36.0	40.5
TOTAL	2,389.8	2,708.5	3,810.4	5,159.9	6,202.6	7,303.8

¹Excluded Central Bank of Costa Rica

*Include a credit for ₡12.6 outside the country.

SOURCE: Banco Central de Costa Rica. "Credito y Cuentas Monetarias, 1977."

TABLE 3.3

NATIONAL BANKING SYSTEM¹
PERCENTAGE OF CREDIT OUTSTANDING AT END
OF YEAR, BY ACTIVITY, 1965-1977

Item	1965	1966	1967	1968	1969	1970	1971
Agriculture	37.07	37.55	35.20	34.56	33.81	34.16	29.41
Livestock	17.39	18.40	19.67	21.39	23.57	23.56	24.99
Industry	17.51	16.70	18.15	18.54	19.38	19.82	17.70
Electricity	0.55	0.58	2.28	2.14	0.45	0.32	0.21
Commerce	4.83	4.34	3.17	2.76	2.30	2.49	5.12
Service	5.29	5.22	5.22	4.50	4.66	5.17	5.58
Dwelling	8.67	8.76	9.30	9.43	9.51	9.15	8.68
Personal Credit	4.71	4.59	4.60	4.58	4.22	3.70	7.05
No Classified Credit	3.98	3.86	2.41	2.10	2.10	1.63	1.26
TOTAL	100.00	100.00	100.00	100.00	100.00	100.00	100.00

Item	1972	1973	1974	1975	1976	1977
Agriculture	25.96	22.92	20.95	22.51	23.79	21.78
Livestock	26.45	30.20	27.67	23.26	22.70	22.56
Industry	18.19	21.66	25.57	25.68	25.17	26.02
Electricity	0.22	0.15	0.65	0.06	0.04	0.03
Commerce	5.70	4.13	5.99	6.49	6.05	5.59
Service	6.24	5.32	5.79	6.61	7.22	8.56
Dwelling	8.66	8.57	7.22	9.06	9.63	10.74
Personal Credit	7.46	6.47	5.67	5.44	4.82	4.17
No Classified Credit	1.12	0.58	1.05	0.89	0.58	0.55
TOTAL	100.00	100.00	100.00	100.00	100.00	100.00

¹Excluded the Central Bank of Costa Rica.

SOURCE: Banco Central de Costa Rica. Credito y Cuentas Monetarias, 1977.

the distribution of credit, during the last five years the increasing share for Livestock was sufficient to prevent the combined shares of Crops and Livestock from declining. The declining credit share for crops was accompanied by a decline in the share of crops in terms of the gross domestic product since the mid-1960's.¹⁷

3.5 Distribution By Products of Agricultural Bank Credits

The funds that the National Banking System has for attending the demand of agricultural credit comes from two sources: 1) domestic resources, and 2) foreign resources.

Funds from domestic resources originate in the following principal concepts: demand deposits; time deposits; interests on loans; bonds outstanding; capital and reserves; reimbursement of loans; commission for banking services; government deposits; and rediscount of documents.

With respect to foreign resources, the main sources of money are the loans made directly by the commercial banks and by the Central Bank with international financial institutions.

In relation to Table 3.4, the loans for crops represented 38.5% of the total amount financed in 1977; whereas the credit for beef cattle and poultry attained 34.4%. Even though the structure of agricultural credit has favored crops in relative numbers and in absolute quantities, the participation of crops in the total amount of credit gradually lost importance; in 1970, it was at 75.7%, in 1971, at 58.8%, and in 1973, at

¹²Banco Interamericano de Desarrollo (BID) et al. Desarrollo. . . , op. cit., Costa Rica, 1975, p. 8.

TABLE 3.4
NATIONAL BANKING SYSTEM
DISTRIBUTION BY PRODUCTS OF AMOUNT OF CREDIT
DISBURSED FOR AGRICULTURE, 1970-1977
(Thousands of Colones)

Product	1970	1971	1972	1973	1974	1975	1976	1977
Permanent Crops	516,239	519,049	494,259	560,322	727,284	706,612	644,324	440,772
Coffee	470,508	461,504	454,102	528,678	649,862	591,147	582,941	316,442
Bananas	14,809	25,885	4,631	2,779	29,447	951	7,052	12,069
Cocoa	1,638	1,464	1,039	2,042	2,101	7,808	8,747	7,054
Sugar Cane	27,763	27,917	31,901	25,195	43,384	102,757	37,031	94,899
Guineo Cuadrado	27	51	63	92	96	65	15	101
Platano	1,361	1,703	2,049	1,282	1,806	3,019	6,919	7,844
Pineapple	37	246	335	254	588	865	1,621	2,363
Raicilla	-	279	139	-	-	-	-	-
ANNUAL CROPS	36,810	56,963	63,778	66,775	134,288	370,115	390,633	394,540
Cotton	2,567	3,000	1,844	3,154	5,720	5,950	13,367	63,858
Rice	23,852	39,806	43,122	43,858	74,662	244,534	244,899	211,114
Corn	2,413	6,319	8,889	6,317	12,298	38,359	40,893	38,876
Beans	1,759	1,761	1,529	1,217	8,011	16,444	11,307	11,070
Sorghum	88	453	991	1,808	8,520	25,403	32,317	28,181
Tobacco	3,115	1,317	3,674	5,724	16,744	18,551	17,999	16,036
Potatoes	3,016	4,277	3,729	4,698	8,333	14,785	26,716	25,405
VEGETABLES	1,400	1,890	2,293	2,072	3,081	4,616	5,957	5,439
Onions	595	540	652	790	2,110	3,404	1,530	1,450
Tomatoes	696	1,116	1,641	1,282	971	1,213	3,969	3,989
Other	109	234	-	-	-	-	458	-
LIVESTOCK, POULTRY & FISHING	177,910	312,150	308,528	457,369	523,055	449,795	521,661	640,053
Beef Cattle	163,377	268,007	267,243	428,488	475,768	390,384	424,343	491,581
Dairy Cattle	11,660	36,519	32,725	20,803	33,929	48,866	75,537	125,407
Hogs	639	2,798	3,866	2,538	2,888	4,335	7,103	9,217
Poultry	2,234	4,427	4,694	5,540	10,470	6,210	14,427	13,166
Fishing	-	399	-	-	-	-	254	682
SUBTOTAL	732,359	890,052	868,858	1,086,958	1,387,708	1,531,138	1,562,575	1,480,804
OTHER PRODUCTS	-	75,563	81,937	76,225	137,502	285,571	362,370	377,994
TOTAL	732,359	965,615	950,795	1,163,183	1,525,210	1,816,710	1,924,945	1,858,798

SOURCE: Ministerio de Agricultura y Ganaderia, "Boletín Estadístico Agropecuario."

TABLE 3.5
NATIONAL BANKING SYSTEM
DISTRIBUTION BY PRODUCTS OF PERCENTAGE OF CREDIT
DISBURSED FOR AGRICULTURE, 1970-1977

Product	1970	1971	1972	1973	1974	1975	1976	1977
<u>PERMANENT CROPS</u>	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Coffee	91.0	89.0	91.9	94.4	89.4	83.7	90.5	71.8
Bananas	2.9	5.0	0.9	0.5	4.0	0.1	1.0	2.7
Cocoa	0.3	0.3	0.2	0.4	0.3	1.1	1.4	1.6
Sugar Cane	5.4	5.4	6.5	4.5	6.0	14.5	5.7	21.5
Guineo Cuadrado	-	-	-	-	-	-	-	-
Platano	0.3	0.3	0.4	0.2	0.2	0.4	1.1	1.8
Pineapple	-	-	0.1	-	-	0.1	0.3	0.6
Raicilla	-	-	-	-	-	-	-	-
<u>ANNUAL CROPS</u>	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Cotton	7.0	5.3	2.9	4.7	4.2	1.6	3.4	16.2
Rice	64.8	69.9	67.6	65.7	54.7	66.1	63.0	53.5
Corn	6.6	11.1	13.9	9.5	8.0	10.4	11.0	9.9
Beans	4.8	3.1	2.4	1.8	5.9	4.4	3.0	2.8
Sorghum	0.2	0.8	1.6	2.7	6.2	6.9	8.3	2.1
Tobacco	8.5	2.4	5.8	8.6	12.3	5.0	4.6	4.1
Potatoes	8.2	7.5	5.8	7.0	6.1	4.0	6.7	6.4
<u>VEGETABLES</u>	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Onions	42.4	28.6	28.4	38.1	68.5	73.7	25.7	26.7
Tomatoes	49.7	59.1	71.6	61.9	31.5	26.3	66.6	73.3
Other	7.8	12.4	-	-	-	-	7.7	-
<u>LIVESTOCK-POULTRY & FISHING</u>	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Beef Cattle	91.8	85.9	86.6	93.7	90.0	86.8	81.3	76.8
Dairy Cattle	6.6	11.7	10.6	4.5	6.5	10.9	14.3	19.6
Hogs	0.3	0.9	1.3	0.6	0.5	1.0	1.4	1.4
Poultry	1.3	1.4	1.5	1.2	2.0	1.3	2.8	2.1
Fishing	-	0.1	-	-	-	-	-	-

SOURCE: Ministerio de Agricultura y Ganaderia. "Boletín Estadístico Agropecuario."

54.0%, whereas in 1977, it was only 38.5%.

During 1977, the commercial banks made 44,567 loans (see Table 3.6) in the amount of 1,858,798 thousand colones, against 51,306 operations and 1,924,945 thousand colones the previous year. Comparing annual variations, credits for crops went down by 19.2 percent in 1977, while loans for cattle augmented by 23.4 percent in the same year. The decrease in crops may be explained as a result of the downward trend observed in coffee credit in the last three years as a consequence of the higher coffee prices prevailing in the world market, an effect of the imbalance between supply and demand of the product.

Table 3.4 reveals the strong upward trend in beef cattle loans, which are parallel to an increment of cattle production, as a result of the increasing demand for animal products, especially for beef cattle.

This panorama turns even more critical for agriculture, when the amount of loans disbursed for financing the coffee crop and the beef cattle are excluded. Proceedings in this manner, during 1970 both products obtained 86% of the total credit; in 1973; 83%; in 1974, 74%; and in 1977, the percentage was only 43%. As can be noted, coffee and beef cattle have been taking a big share of the credit, leaving only a small amount for distribution among the remaining agricultural activities. Except for uncommon variants, the structure cited has been maintained for a number of years.

With regard to the preceding comments, it is left to be seen that a change must occur in the present policy. Primarily, the quantity of credit disbursed in those two activities must be restricted such that additional amounts of credit may be made available for other crops or products that are less consolidated and that, as such, have received little financial help to date owing to the manner in which institutions have been allocating credit.

With respect to the permanent crops, the most significant change occurred in the financing of the coffee crops, which experienced a decrease of $\text{Q}266.4$ million colones from 1976 to 1977. But, even though this happened, the product has continued to conserve a high share in its group, as high as 72% (see Table 3.5). As noted, the dominance of coffee continues to occupy a place of privilege within agricultural credit.

On the other hand, in comparison with the aforementioned years, sugar cane experienced a rise of 156.3%, having a share of 21.5% in the total amount of credit disbursed for permanent crops. However, such important crops as bananas and cocoa which generate a large percentage of the foreign resources for exports, account for less than one percent of the total credit disbursed.

In relation to the annual crops, with the exception of cotton which increased by $\text{Q}50.5$ million colones in 1977, all the other products registered decreases. Table 3.4 also shows that over the same period rice accounts for the higher share in obtaining more than 50% of the credit for the group under consideration. While beans, which have a great importance in the

diet of the Costa Rican people, only account for 2.8% (see Table 3.5) of the annual crops and for less than one-half percent of the total credit disbursed.

In general, the products which are most favored in the allocation of bank credit also tend to be the products which are most important in value of output, but the distribution of credit is much more concentrated than the distribution of output.¹⁸

The relative stability in the allocation of credit suggests the highly conservative nature of the banking system, that is, the same crops receive a significant share of credit year after year. To some extent this allocation of credit reflects the relative returns of the various products in Costa Rica, but it also reflects the fact that loans for these traditional products are less risky and less costly for banks to administer.

Table 3.6 shows that the distribution of the number of bank loans disbursed for the various agricultural products are presenting a reduction, which could indicate either that the commercial banks do not try to gain new customers or that the number of farm owners is lower every year because of expansion in farm size. This tendency is very harmful since small farmers have contributed to the creation of the kind of social, economic, and political stability that Costa Rica presently enjoys. Moreover, the situation is rapidly

¹⁸Banco Interamericano de Desarrollo (BID) et al. Desarrollo. . . , op. cit., Costa Rica, 1975, p. 9.

TABLE 3.6
 NATIONAL BANKING SYSTEM
 DISTRIBUTION BY PRODUCTS OF NUMBER OF LOANS
 DISBURSED FOR AGRICULTURE, 1970-1977

Product	1970	1971	1972	1973	1974	1975	1976	1977
<u>Permanent Crops</u>	3,282	4,173	3,329	3,321	3,756	3,834	4,008	3,269
Coffee	2,212	2,693	1,984	1,949	2,236	1,877	2,042	1,558
Bananas	69	62	59	30	34	40	81	138
Cocoa	110	152	51	71	99	105	236	238
Sugar Cane	695	755	851	966	1,061	1,402	950	556
Guineo Cuadrado	6	6	7	14	7	4	2	8
Platano	153	442	344	238	255	324	590	638
Pineapple	37	33	25	53	64	82	107	133
Raicilla	-	30	8	-	-	-	-	-
<u>ANNUAL CROPS</u>	5,008	7,489	8,526	7,433	12,794	21,770	18,728	14,129
Cotton	25	26	23	33	24	23	62	214
Rice	1,233	2,221	3,103	2,390	2,768	5,147	4,443	2,261
Corn	1,051	2,837	3,029	2,498	3,566	8,265	7,340	6,138
Beans	1,841	1,353	903	717	3,604	4,963	3,467	2,815
Sorghum	4	20	41	82	171	370	390	359
Tobacco	394	469	958	1,174	1,965	2,038	1,743	1,349
Potatoes	460	563	469	539	696	964	1,283	993
<u>VEGETABLES</u>	383	496	539	415	524	568	711	573
Onions	161	149	161	143	158	148	181	151
Tomatoes	195	300	378	272	366	420	520	422
Other	27	47	-	-	-	-	10	-
<u>LIVESTOCK, POULTRY & FISHING</u>	11,899	18,129	16,633	18,756	20,090	17,686	18,453	18,465
Beef Cattle	9,815	13,065	11,937	15,621	16,513	13,607	12,992	13,119
Dairy Cattle	1,775	4,353	3,603	2,363	3,269	3,365	4,337	4,337
Hogs	105	345	639	369	308	307	481	524
Poultry	204	350	454	403	-	-	627	464
Fishing	-	16	-	-	-	-	16	21
<u>SUBTOTAL</u>	20,572	30,287	29,027	29,925	37,164	43,858	41,900	34,436
Other Products	-	2,892	3,881	4,220	6,063	8,696	9,406	8,131
<u>TOTAL</u>	20,572	33,179	32,908	34,145	43,227	52,554	51,306	44,567

SOURCE: Ministerio de Agricultura y Ganaderia. "Boletín Estadístico Agropecuario."

becoming more complicated owing to foreign investors. This causes a rapid increase in the price of land making it difficult if not impossible, for nationals to compete. This is especially true in view of the monetary exchange rate which almost always favors foreign investors.

If the preceding issues can be proved, the government should immediately take the appropriate actions, to the end that the sale of land to foreign investors will be prohibited.

CHAPTER IV

MONETARY AND CREDIT POLICIES

4.1 Monetary Policy

4.1.1 Introduction:

Monetary policy is concerned with the volume of money and credit in the economy and the conditions under which they are appropriated. By regulating the supply of funds and the terms under which they are made available, the government can influence the level of economic activity. The economic pattern can also be modified by measures that affect the supply of funds for selected sectors of the economy.²⁰

As previously indicated, the Central Bank of Costa Rica constitutes the primary monetary regulatory authority in the nation; and through its power, entrusted to it by law, exerts very significant influence on commercial banks and on the supply of credit. Its policies also affect other lenders, such as merchants, dealers, private banks, insurance companies, and so on.

²⁰Nelson, G. Aaron et al. "Agricultural Finance." Iowa State University, Ames, Iowa, 1973, p. 292.

In Chapter 3 the basic function of the Central Bank was introduced, yet it is important to amplify its objectives. Basically this institution uses its broad powers to foster growth at high levels of employment, maintaining a stable "colon" in the domestic economy and overall balance in the international payments. This means that the Central Bank has a responsibility to the nation's economy as a whole, not to any one segment alone. It means that the system should develop and maintain a national monetary policy supported by financial machinery as needed to provide an economic climate in which private enterprise will develop, grow, and prosper. To facilitate achieving this objective, authorities should take action to help counteract both inflationary and deflationary movements. As was written in a publication by the Board of Governors of the U.S. Federal Reserve System:²¹

"In a dynamic and growing economy, enough credit and money is that amount which will help to maintain high and steadily rising levels of production, employment, incomes, and consumption, and to foster a stable value for the dollar. When credit, including bank credit, becomes excessively hard to get and costs too much, factories and stores may curtail operations and lay off employees. Smaller payrolls mean hardships for workers, who curtail their purchases; merchants feel the decline in trade and reduce their orders for goods. Manufacturers in turn find it necessary to lay off more workers. A serious depression, unemployment, and distress may follow. When credit is excessively abundant and cheap, the reverse of these developments - an inflationary boom - may develop. An increase in the volume and flow of money resulting from

²¹The Board of Governors is a governmental agency in Washington, D.C., consisting of seven men appointed for 14-year terms by the president of the United States, with the advice and consent of the Senate.

an increase in the supply and availability of credit, coupled with a lowering of its costs, cannot in itself add to the country's output. If consumers have or can borrow so much money that they try to buy more goods than can be produced by plants running at capacity, this spending only bids up prices and makes the same amount of goods cost more. If merchants and others try to increase their stock so as to profit by the rise in prices, they bid up prices further. Manufacturers may try to expand their plants in order to produce more. If so, they bid up interest rates, wages, and the prices of materials. In the end they raise their own costs."²²

While such a large part of the Central Bank's primary function depends upon regulating the supply of credit, commercial banks of the nation play an important role in undertaking the distribution of that credit. This is because commercial banks are the financial institutions through which credit can be created, so it is through them that the credit supply of the nation is controlled.

There are a number of means that the Central Bank can use to control credit expansion but two controls are particularly relevant in Costa Rica. The Central Bank: 1) maintains a "tope"²³ system in an attempt to control the supply of credit, and 2) sets rates of interest and other terms of lending by the commercial banks. Other active methods of control are: 3) adjusting reserve requirements of commercial banks, 4) open market operations, 5) changing the Central Bank rediscounting rate and lending operations to commercial banks.

²²Nelson, E. Aaron et al. "Agriculture Finance". Iowa State University, Ames, Iowa, pp. 293-294.

²³This means maximum limit of money that commercial banks can lend by activity.

4.1.2 The "Tope" System

In the face of substantial demand for bank credit at low cost, the Central Bank historically used a "tope" system to control the expansion and allocation of credit. Under this system, overall limits for credit were established, as well as limits for each bank and for most types of activities. In the late 1960's the system was strictly administered, that is, relatively little credit expansion was permitted, and the commercial banks were forced to adhere closely to the prescribed limits. However, the "tope" system has been modified several times in an attempt to make it more flexible. So in March 1971 the Central Bank changed the traditional system of "topes" for another one based on maximum and minimum percentages. This indicated how commercial banks would have to maintain a structured credit system in relation to the various types of activities. The level controls in this system did not function directly as in the tope system; but in an indirect manner, utilizing other instruments of monetary policy such as interest rate, rediscounting, open market operations, and reserve requirements.

During 1972 the Central Bank maintained the percentage structure of credit but established quantitative and qualitative limits of credit per term. Thus the credit was distributed during the year in accordance with the seasonality of the demand, which permitted adjusting the credit policy to the economic conditions prevailing at that time. In addition, it was necessary to introduce other modifications for the purpose of adapting the

system to the operative needs of the commercial banks, procuring simultaneously the standardization of the program being executed. Unfortunately, the system did not attain the final objectives and was abandoned in 1973 for the old practice of setting specific limits (topes).

However, upon the reactivation of the former "tope" system more emphasis was placed on reducing the credit expansion rate in those activities which were less important. Therefore, from 1973 to 1977, with rare exceptions, the principal instrument of monetary regulation has been the tope system, while other tools such as reserve requirements, rediscounting rates, and interest rates have not been employed aggressively, pursuing almost the same policy as the preceding years.

4.1.3 Interest Rate Controls

As previously mentioned, one of the most important characteristics of the Costa Rican banking system is that interest rates are controlled by the Central Bank. Rates of interest on time and savings deposits in domestic currency generally range from 6 to 14 percent depending on the period of the deposit, but on savings deposits denominated in dollars, the rate is 3 percent. Obviously, these interest rates are well below the rate of inflation, which implies a negative rate of return in real terms for deposit holders. On the other hand, no interest is paid on demand deposits.

Until September 30, 1974, on bank lending for agriculture, rates of interest were 8 percent when the bank made loans from

its own resources. After this date, the Central Bank established a policy of differential system rates depending on the economic activity and type of borrower. Some of the interest rates were raised, yet the emphasis was placed on providing small farmers with the lowest possible interest rate. The rates in the new system are as follows:

1) Agriculture and Forestry

a) Coffee

i) Agricultural activities: Small Farmers	8 percent
Coffee Cooperatives	10 percent
Other	11 percent
ii) Loans not included in i): Small Farmers	8 percent
Coffee cooperatives	10 percent
Other	12 percent

b) Sugar Cane

i) Agricultural activities:	
Small Farmer	8 percent
Sugar cane cooperatives	6 percent
Other	10 percent
ii) Loans not included in i):	
Small Farmer	8 percent
Sugar cane cooperatives	6 percent
Other	12 percent

c) Basic Grains (Corn, Beans, and Sorghum),
Vegetables and Fruits

i) Agricultural activities	8 percent
ii) Loans not included in i):	
Small Farmer	8 percent

Other	12 percent
d) Rice	
i) Agricultural Activities:	
Small Farmer	8 percent
Other	10 percent
ii) Loans not included in i):	
Small Farmer	8 percent
Other	12 percent
e) Oilseeds (Soybean, Cotton, Peanuts, African Palm, etc.)	
i) Agricultural activities	8 percent
ii) Loans not included in i):	
Small Farmer	8 percent
Other	12 percent
f) Forestry and Other Agricultural Products	
i) Agricultural activities:	
Small Farmer	8 percent
Other	10 percent
ii) Loans not included in i):	
Small Farmer	8 percent
Other	12 percent
2. Livestock, Hunting and Fishing	
a) Beef Cattle	
i) Breeding and Raising	8 percent
ii) Fattening:	
Small Rancher	8 percent
Other	10 percent

iii) Loans not included in i) and ii):	
Small Rancher	8 percent
Other	12 percent
b) Dairy Production	
i) Breeding and Raising:	
Small Rancher	8 percent
Other	10 percent
ii) Loans not included in i):	
Small Rancher	8 percent
Other	12 percent
c) Loans Livestock not included in a) and b) and for Poultry, Hunting, and Fishing	
Small Business	8 percent
Other	10 percent

The foregoing rates operate for both annual crops and investment credit. When resources for lending are more costly, as in the case of some foreign loans, the commercial banks are permitted to charge a reasonable percentage over the cost of funds. For instance, credits from the second loan of the World Bank, were made for an interest rate of 8.5 percent plus a commission of 1 percent. Furthermore, the commercial banks that had contracted loans at fluctuating rates but made loans at fixed rates , would be able to make new credits from the payments

at higher fluctuating rates (2 points over the cost of funds) adjustable every six months, and only after their own contracts had been satisfied (payment of principal and interest).

In spite of the increase, rates of interest for bank lending continue to be negative in real terms implying a substantial subsidy for individuals who receive bank credit. Moreover, under these circumstances, interest rates are ineffective in distinguishing between productive and nonproductive investments, since those with negative or low real rates of return can be profitable for the borrower.

Likewise, the current pattern of interest rates is likely to have a negative effect on the decisions of bank officials. Although the government's commercial banks are not supposed to maximize profits, they are nonetheless influenced by profit considerations since the banking bureaucracy is concerned with the profitability of the operating divisions. Bank officials will tend to favor loans with lowest risk and administrative costs and with highest interest rates. This tends to discriminate against bank lending to small farmers, because such loans tend not only to be more risky with higher administrative costs, but also because the small farmers pay the lowest interest rate.²⁴

4.1.4 Rediscounting Rate Policy

The Central Bank can adjust the rediscount rates (the rate of interest at which the Central Bank rediscount commercial

²⁴Banco Interamericano de Desarrollo (BID) et al. Desarrollo. . . , op cit., Costa Rica, 1975, page 4.

banks' loans) as a means of influencing extension of credit to the public on the basis of acceptable government securities and other assets. Commercial banks may borrow from the Central Bank to a modest degree under usual conditions (and to a considerably greater degree in extreme circumstances). Also, nonmember banks, such as other financial institutions and non-financial business could borrow from, and rediscount securities with, the Central Bank to meet emergency conditions broader than the institution itself, that is, emergency conditions in the community or nation. When banks are borrowing, an increase in the rediscount rate increases their costs and thereby tends to discourage borrowing. But, more important, it serves as a warning that credit extension needs watching, and banks know that if such warnings are not heeded, the more positive and forceful tools of adjusting reserve requirements and open market operations may follow. Thus a major influence of adjusting the rediscount rate could be psychological, and as such it is a potent influence not only on commercial banks but on business generally.

Adjustments in the rediscount rate may serve also as a signal of easier credit conditions. A reduction of the rates lowers the cost of commercial bank borrowing and, in turn, encourages commercial banks to make business loans. It also provides a psychological effect in that business may feel more inclined to undertake expansion plans if credit promises to be adequate and lower in cost.

So, while changes in the rediscount rates are directly effective on member banks, the effect is passed on indirectly to the economy in general through the effect on the general interest rate structure.²⁵

In Costa Rica, as in almost all nations, the Central Bank provides resources for the commercial banks through rediscounting and lending operations. The interest rates at which the Central Bank rediscounts commercial bank loans were as follows during 1977:

1) Rediscounts

- a) Loans up to 360 days in relation to foreign agricultural and industrial products. . . 6 percent.
- b) Loans up to 360 days for the production and storage of domestic agricultural, hunting, fishing, and industrial products and for price regulation by the National Production Council. . . 7 percent
- c) Loans up to 360 days for the production and distribution of electricity and other sources of energy and for the provision of public services. . . 7 percent. Loans up to 180 days for the marketing and storage of domestic goods . . . 8 percent
- d) Loans up to 180 days for the financing of cooperative of consumption . . . 10 percent
- e) Loans up to 180 days for marketing and storage operations not included in b) and c) . . . 14 percent

²⁵Nelson, G. Aaron et al. "Agricultural Finance." Iowa State University, Ames, Iowa, 1973, pp. 298-299.

Moreover, the Central Bank makes loans to the commercial banks at different interest rates such as:

2) Loans:

- a) Up to one year for financing operations with the Rural Credit Department and Credit Offices for Small Farmers . . . 4 percent
- b) Up to 90 days for financing to the commercial banks in operations under Article 62, numeral 4) of the Organic Law of the Central Bank . . . 10 percent
For financing the stabilization of prices of products of basic necessity by the National Production Council . . . 4 and 2 percent
- c) Up to 90 days for financial operations to the commercial banks in operations under article 62, numeral 3) of the Organic Law of the Central Bank . . . 10 percent
- d) With resources obtained from foreign loans²⁶.

Table 4.1 shows that the Central Bank during 1977 re-discounted documents from the commercial banks by an amount of 82.5 million colones. Although the rediscount policy pursued by the Central Bank seems to have lost importance in the last two years, this institution has not succeeded in limiting the expansion of credit. This situation is specially due to the fact that the loans to small farmers as well as the stabilization of prices have increased rapidly, specially because of the policy of subsidy interest rates.

²⁶This rate is established for the Central Bank according to each case.

The preceding situation is aggravated by the lack of compliance by the commercial banks with the tope system. The outstanding bank credit often exceeds the programmed amount of more than 10%.

TABLE 4.1

CENTRAL BANK OF COSTA RICA
AMOUNTS OUTSTANDING OF REDISCOUNTS
AND LOANS, 1970-1977

(Thousands of colones in monthly average per year)

Item	1970	1971	1972	1973	1974	1975	1976	1977
LOANS:								
- Small Farmers	68,820	91,299	148,798	202,570	262,326	356,757	381,188	414,748
- Stabilization of Prices	<u>11,778</u>	<u>24,502</u>	<u>43,838</u>	<u>46,668</u>	<u>126,715</u>	<u>293,321</u>	<u>465,577</u>	<u>625,464</u>
Total Loans	80,598	115,801	192,636	249,238	389,041	650,078	846,765	1,040,212
Rediscount	<u>51,176</u>	<u>150,623</u>	<u>107,851</u>	<u>118,997</u>	<u>238,330</u>	<u>474,339</u>	<u>178,364</u>	<u>82,519</u>
TOTAL	131,774	266,424	300,487	368,235	627,371	1,124,417	1,025,129	1,122,731

SOURCE: Banco Central de Costa Rica. "Estadísticas Economicas, 1970-1977". Costa Rica, 1978.

4.1.6 Reserve Requirements

The Central Bank has authority to change the reserve requirements of the commercial banks. This method constitutes a powerful tool in controlling bank credit due to the fact that the amounts of reserves a bank has, in relation to the required reserves, rules its potential loan quantity. When a bank has excess reserves, additional loans may be made. On the other hand, if a bank has a reserve deficiency, the bank must make up that deficit by borrowing, selling securities, reducing the volume of loans, obtaining more deposits without making loans, etc.

For instance, if the Central Bank would like to expand the amount of credit, a decrease in the legal reserve requirements would permit the banks to obtain an excess of money from the reserves for loans. On the contrary, if the Central Bank would like to limit the quantity of credit, it can do so by increasing the reserve requirements.

In Costa Rica the legal minimum requirements established by law that the commercial banks must maintain in the Central Bank as guarantee of their deposits are the following:

- 1) 20% of the total amount on demand and time deposits up to 30 days.
- 2) 10% of the total amount on demand and time deposits longer than 30 days.
- 3) Foreign loans are exempt from the reserve requirements.
- 4) Deposits in foreign and domestic currency must compute independently, but in both cases the reserve requirements must

be maintained in Costa Rican colones.

- 5) Starting on January 1, 1978, the reserve requirements were increased in the following way:
- a) In deposits up to 30 days, the reserves' requirements will increase by 1% per month, which will be accumulative and will start with 21% until reaching 30%.
 - b) In deposits longer than 30 days, the reserve requirements will be 0.5% per month, starting at 10.5% until reaching 15% on an accumulative base.

In spite of the above regulations the banks often failed to fulfill them when the amounts ranged from 46,000 colones to 63 million colones.²⁷ This, consequently, complicated the function of the Central Bank in regard to the supply of credit and money in the national economy.

4.1.6 Open Market Operations

This instrument of monetary policy refers to the buying and selling of securities by the Central Bank, specifically on the national financial market. The main objective of open market operations is to influence the reserves of commercial banks. If the Central Bank decides that an increase of credit is necessary in order to expand the economic activity, the institution buys securities. But on the other hand, if the facts indicate

²⁷ Banco Central de Costa Rica. "Memoria Anual-1977. Informe de la Auditoria General de Bancos." San Jose, Costa Rica, Nov. 1978, pp. 24-25.

that there are inflationary pressures in the economy, the Central Bank should sell securities and restrict the supply of money.

In practice reserve requirements and open market operations are two different but complementary tools of executing the same goal. Both methods affect the reserve as well as the loan capacity and investment policy of the commercial banks. In general, reserve requirements are not adjusted very often, while open market operations either adjust reserves every day or when seasonal variations in requirements are present.

Frequently, the Central Bank uses open market operations as a tool of monetary policy. For example, during 1977, given the high coffee prices on the international market, this institution decided to sell "Coffee Saving Bonds" on the national market as a means of limiting the excess of money in the economy. Fortunately, this measure was effective in realizing its objectives.²⁸ However, even though that policy was functional, the National Banking System also served as buyer of fiscal bonds which in effect once again incremented the amount of money in circulation, thus virtually negating the positive effect of limiting the expansion of credit. It also became one of the

²⁸ Banco Central de Costa Rica." Memoria Anual-1977. La Economia Nacional." San Jose, Costa Rica, pp. 25-26.

most important sources of money for the central government.

4.2. Credit Policy

The Central Bank must not only concentrate on maintaining the stability of money but must also promote adequate economic development, obtaining full utilization of the productive resources, necessary to maintain general economic equilibrium.

Other objectives of this institution are as follows:

- 1) To avoid the inactivity of production when it is caused by insufficient credit; 2) to promote the diversification of production toward those products which would enhance balance of payment.

In relation to the credit structure allocation (see part 3.4), the credit program of the Central Bank is generally divided into the following six groups:

- | | |
|----------|------------------------------|
| Group I | Preferred Loans: |
| | - Coffee Crops |
| | - Sugar Marketing |
| | - Basic Grains* |
| | - Other |
| Group II | Agroindustrial Activities |
| | Agricultural Sector: |
| | - Agriculture |
| | - Livestock |
| | - Economic Foster Programs* |
| | - Agricultural Small Farmers |

- Emergency the Dry Pacific Region*
- Emergency the Banana

Industrial Sector:

- Industry
- Economic Foster Programs*
- Raw Material Imports

Group III	Other Activities
Group IV	Financial Sections
Group V	Capitalization of Savings*
Group VI	Investment Assets

*This item is not subject to quantitative limits of credit.

In the Groups III, IV, and VI and in the item "Other" of the first group the commercial banks can freely allot the resources among different activities. On the other hand, the Central Bank has not established quantitative limits to programs with regard to: Basic Grains, Economic Foster Programs, Emergency Dry Pacific Region; and Capitalization of Savings. The Economic Foster Programs embrace diverse projects and special lines of credit which are considered very important for the national economy in relation to some basic objectives. So the projects in order to be selected, must meet these requisites:

- 1) To give origin to an increment in the GDP over the rate of increment previously estimated.
- 2) To not be included within the ordinary credit program.
- 3) To cover an important proportion of the project with foreign resources.

4) To be approved by the Central Bank for each case and for the credit amount not to be subjected to quantitative limits.

Table 3.2 shows the credit distribution by the National Banking System. Even though the system for accomplishing this allocation would not be considered best, it tried to favor preferred productive activities such as agricultural, livestock and industrial.

Although there exist many agencies in Costa Rica related to agriculture, there is not an agency which is specifically dedicated to establishing the volume and priorities of credit in the productive sectors. If the nation lacks a governmental office capable of preparing and evaluating projects in an economic and financial sense, the Central Bank will be forced to take the initiative in this area. Therefore, this institution will be impelled to employ the most convenient system for allocating credit, yet always taking into consideration the prevailing reality of the country at that time.

Table 4.2 shows that Costa Rica has expanded its money supply very quickly since 1970. This expansion of credit principally occurred in credit to central government and to the private sector. In the former, the increment was due to buying by the commercial banks of fiscal bonds and in the latter because these banks directly financed the development of many projects. Also, although a little less in the last two years, the rapid expansion of credit to official institutions can be observed. This fact was a result of a liberal policy of credit

TABLE 4.2

NATIONAL BANKING SYSTEM
TOTAL CREDIT, AMOUNTS OUTSTANDING AT END OF
YEAR, 1970-1977
(Millions of Colones)

Year	Total	To Central Government	To Official Institutions	To Private Sector
1970	2,022.7	343.8	37.8	1,641.1
1971	2,495.7	346.0	83.0	2,066.7
1972	2,877.9	472.8	92.2	2,312.9
1973	3,166.1	406.9	153.0	2,606.2
1974	4,662.6	572.1	342.9	3,747.6
1975	6,290.5	670.8	600.2	4,999.5
1976	7,856.8	884.5	919.4	6,052.9
1977	9,735.9	1,623.3	970.3	7,142.3

SOURCE: Banco Central de Costa Rica. "Credito y Cuentas Monetarias." San Jose, Costa Rica, Dic. 1978.

pursued by the Central Bank toward the National Production Council for the stabilization of prices in goods of basic consumption, and the granting of credit to CODESA (Costa Rican Development Corporation) in order to develop some specific programs.

CHAPTER V

NORMS, METHODS, AND POLICIES PURSUED BY THE COMMERCIAL BANKS FOR MAKING LOANS

Norms, methods, and policies that the commercial banks pursue for the granting of credit are established in the organic law of the National Banking System. Nevertheless, the board of directors of each bank, including the Central Bank, can create procedures for the purpose of regulating the banking operation in the most effective manner.

As part of their philosophy, government's commercial banks must evaluate the applications of credit with a criterion of absolute impartiality, adopting those systems that guarantee equal treatment in similar conditions.

5.1 Types of Loans

The commercial banks can lend for the following:

- a) Current farm production cycle expenses such as land preparation, seed purchases, sowing, harvesting, and general assistance of farms. All of which are referred to as Avio Agricola (Agricultural Provisions).
- b) Development of livestock production. The loans can be made for: purchase of; steers for fattening, young cattle for raising, milk cattle; importation or purchases within the nation of

cattle for reproductive purposes (female or male); breeding, raising, and fattening of pigs; and other activities such as poultry, fishing, and apiculture.

c) Refaccionario Mobiliario (Intermediate term loan). This embraces the buying of machinery, tools, and other necessary implements for crops and livestock. Also, organization and promotion of enterprises are capable of being financed within this division.

d) Refaccionario Mobiliario (Long term credit).

This section comprises those permanent investments on the farm, which are made in order to obtain maximum agricultural production. Consequently, the following could be financed: investment related to the installation of equipment; construction of barns, storage rooms, sheds, fences, rural dwelling, etc.; sowing of permanent products; irrigation and drainage; preparation of farm maps; and legal expenses related to the deed.

5.2 Maximum Loan Ceiling

Credits must be in determined amounts in accordance with the objectives of each plan. There are loan limits by individual and private businesses, which vary in relation to the banking department that executes the credit operation.

The maximum loan limit of the commercial department is 15% of its capital and reserves. In cases of a special nature this limit can be extended to 25%, but the Central Bank must give the respective authorization for it.

In the Mortgage Department the loan ceiling for one person or farm may never exceed 5% of the capital and reserves of that department.

Rural Credit Offices and Credit Offices for Small Farmers provide loans up to ¢100.000 colones per person or farm unit.

5.3 Guarantees for Loans

All credits must have a real or fiduciary guarantee according to the policy pursued by each bank. Prior to the credit allowance, the guarantee must be appraised. The real guarantees are basically pledges and mortgages.

Except in some special cases, first mortgage must be given to the banks. Second or junior mortgage on the same property is only accepted if it is filed for within the same bank. The commercial banks do not accept as guarantee of loans either mortgages in partial rights of undivided farms, or properties in bond.

Co-signers, the most frequent type of guarantors, are acceptable for terms no longer than 3 years only if they possess strong credit and character references, and are economically capable of payment in the event of default. A co-signer plus a chattel mortgage is the most common form of guarantee for large crop, livestock, machinery and equipment loans.

Collateral is another type of guarantee but its use is limited in agricultural operations. In those rare instances,

it operates with bonds, stock certificates, accounts, etc.

The government point of view is to encourage the use of co-signers and reduce the importance of other means of guarantee in bank lending, giving more emphasis to the farmer's investment plan and the potential productivity of the project.

5.4 Investment Plans

Investment plans are the detailed use of funds stemming from the credit operation. The banks utilize special forms for that purpose, although at present there is no consistency among banks. Once the application for a loan has been made, if the credit is established, the law requires the annotation of a resume of the investment plan on the legal document of credit.

The commercial banks have the right of inspecting-auditing the investment plans. In the event that they are able to verify that the funds had been used for other objectives than those proposed in the original document; with no previous authorization, the banks can terminate the loan contract and demand that the outstanding debt be immediately liquidated.

As was mentioned in 5.1, the most important purpose of the funds is for crop and livestock production; secondly for purchases of intermediate goods; and finally for farm related real estate.

5.5 Delivery of Funds

The funds are administrated to the clients in partial or total payments according to the objectives of the plan. If credit is dispersed in payments each needs the approval of two different sections of the bank: 1) agricultural, and 2) appraisal. In order to accomplish this task, the bank inspectors visit the farms and verify whether the funds are being utilized for the specified purposes.

5.6 Loan Repayment Terms

Basically the terms of the farm credits made by the commercial banks are calculated according to the investment plan. Although it varies from one bank to another, generally, the granting of loans pursues the following framework:

Use	Term	Period of Grace
Annual Production Cycle	1 year	-
Production Cycle Greater than 1 year	from 1 year to 2 years	-
<u>Refaccionario Mobiliario</u> (Intermediate term loan)	5 years	1 year
<u>Refaccionario Inmobiliario</u> (Long term loan)	10 years	2 years
Purchase of Farms and Encumbrance cancellation	20 years	4 years

5.7 Loan Procedure

For the purpose of setting up a loan the commercial banks have developed their own special forms which are delivered to the applicant, who must fill it out by himself. However, some banks have employees available in their central offices who interview the potential borrower and assist in the completion of these forms. In addition, many branch offices and agencies actually have personnel specialized in preparing the application for the farmer. In the Rural Credit Offices a delegate and assistants can receive and process the loan application. Almost the same procedure is followed in the Credit Offices for Small Farmers.

In this first step the following general information is required: name, age, address, date, telephone number, commercial references, amount of credit, the use of the funds, kind of activity, and so forth.

Once the bank has accepted the application, it requires the following additional information: 1) balance sheet; 2) income statement; 3) financial projections; 4) projected profits; 5) detail of properties owned by the applicant and his guarantors; and 6) any other data that the bank considers necessary. In the Rural Credit Offices (Juntas Rurales) and Credit Offices for Small Farmers the loan application is shorter in data. Generally, these units must verify if all information given by the applicant is correct.

Up to this point, the credit file for each borrower is formed by the loan application and by the additional information above cited. In addition, in order to complete the credit file the following information is included: 1) a credit report about the past experience of the bank with the applicant and guarantors. (The credit record of the borrower obtained from other banks and private business are also very useful, however, this information is generally not obtainable); 2) a special statement about the investment plan; 3) a report concerning the general condition of the farm; 4) the experience and ability of the applicant as a farmer; 5) an appraisal of the properties given in guarantee.

As the credit file is formed, the employees of the respective office can evaluate and authorize the loan application, but only if the quantity of each loan is within the credit limit that the board of directors has set up. The amount of credit that an official can authorize depends on his position, the type of agency, and the bank in which the application was presented. The quantitative limit fluctuates between ¢5,000 colones and ¢40,000 colones, when Rural Credit Offices or Credit Offices for Small Farmers are involved. Credit operations exceeding the amounts previously indicated must be authorized by the central office of the bank.

Time between the presentation of the first document and the effective resolution of the credit varies according to different factors, some of which are the following:

1) prior credit experience by the bank with the client;
2) applicant's interest in the presentation of the basic information; 3) kind of guarantee offered; 4) faulty guarantees hampering the loan process; and 5) the availability of resources. An initial estimation of the time required for approving the loan application varies from two to sixty days, depending on the factors mentioned above.

CHAPTER VI

CONCLUSIONS AND RECOMMENDATIONS

The conclusions and recommendations of this paper could be summarized as follows:

1) Due to the lack of existing studies, statistical information, and the resources for obtaining them; there are many limitations in determining whether the institutional credit has been sufficient for satisfying the agricultural demand. Certain activities of the agricultural sector have received appropriate financing, however, others have not received adequate funding. Perhaps this shortage of funds in specific areas is often caused by lack of investment plans, insufficient technology, low prices, and so on. In a study such as this, it is almost impossible to establish whether the banking system was the main factor of development of certain activities or whether private investment was in effect the dynamic factor in expansion.

2) Even though it is not known whether the credit requirements have been satisfied in the agricultural sector, it is feasible to point out that the granting of loans toward different activities of this sector have received preferential treatment (see Table 3.4). For instance, the coffee crop and

livestock have obtained the biggest support from the National Banking System, whereas products like beans, sorghum, or banana have only received a small share in the total amount of credit disbursed for agriculture.

3) The Central Bank of Costa Rica is the responsible institution for monetary and credit policy. To fulfill these functions the Central Bank established topes (portfolio limits) for the commercial banks, that is, the maximum amount of money that each bank could lend for economic activity. After this allocation, each bank distributes the quantities assigned among the different agricultural activities.

The appropriation of funds to the diverse sections within these areas, however, is a complicated and cumbersome process. If the actual distribution of credit is to be effective, fair, and appropriate, it is absolutely necessary to create a new governmental office to assume the responsibility to assist the Central Bank in this function. Through it a national agricultural policy could be defined. Within its jurisdiction would lie the investment priorities in each sector or activity, the possible amounts of credit required supplied by the National Banking System, and so on.

If the creation of the suggested agency is postponed the Central Bank will have to take the initiative, and perhaps be more aggressive in indicating to the commercial banks the amounts of credit for activities or products.

The Central Bank has not obtained the desired success in controlling the expansion and allocation of credit,

especially due to the ineffective operation of the tope system, which has created administrative difficulties for the commercial banks. Nevertheless, this active method of monetary policy proves to be a good one, only needing the inclusion of some corrections in order to improve its operation. Such measures can be related to: a) the commercial banks must comply with the credit program set up by the Central Bank. In the event that they did not do so, the General Audit of Banks would proceed to use its legal powers for punishing the infractors of the law; b) the Central Bank must use both the tope system and the rediscounting policy for establishing a system of incentives, which tend to promote loans to: small farmers, new riskier crops, and new clients.

4) The Central Bank of Costa Rica first increased the interest rates on September 30, 1974 and subsequently on January 1, 1977. In spite of the increases, it is considered to remain below the cost of money on the market, and therefore rates continue functioning as a subsidy for those farmers that are receiving bank loans. Moreover, if these interest rates are smaller than the market rates, it will permit the diversion of funds from bank credit toward different objectives other than those indicated by the client in the original application and consequently will produce higher gains. Likewise, benefits derived from farm operation won't be reinvested readily. Common sense dictates that the farmer will utilize his own profits making investments in other activities that produce

higher profitability in comparison with the interest rate paid for those loans taken from the banks. In other words, the producer's decision will be to continue using the funds originated for the operation of its agricultural business, in investment of high yield outside the farm, and to continue financing its production with loans obtained at a low cost from the banking system.

Because of the negative real rates of interest bank employees have an incentive to promote the safest farm credits with the lowest administrative cost. Logically, this is very harmful for small farmers who pay loans at low interest rates yet embrace high bureaucratic cost, as well as to the promotion of new crops with a high level of risk.

Thus increasing the interest rates to the level of the cost of money on the market, will not only permit the commercial banks to lend in activities of high risk but to also improve the rates paid in time deposits. Perhaps this policy could also serve to establish passive interest rates in checking accounts. The capture of new private funds by this method could be utilized by the banks in financing riskier projects that produce high benefits but that so far have not received convenient credit help.

In addition, the augument in the rates of interest will permit the banks to generate additional profits, which could be used in some proportion in order to finance activities intimately related with agriculture which have not had

any support by the commercial banks. For example: research "in agricultural experiment stations to develop technologies, production practices and managerial skills that increase productivity of agricultural resources"²⁹; extension service "for colleges of agriculture and extension education that convey knowledge and research results to farmers;"³⁰ selection, preparation, evaluation and execution of investment projects. All are important and critical aspects of agricultural development which could be improved with more decisive participation on the part of the commercial banks.

The function of establishing the interest rates was given by law to the Central Bank. Since this system is a power tool of development through the allocation of credit, the Central Bank could analyze the alternative of setting up differential rates of interests in accordance with the area of production. In the past this has never been done. Yet the main purpose of this new kind of system would serve to stimulate the production in those regions potentially suitable for specific crops. Obviously, this method will tend to discourage non-productive types of sowing in areas of poor land or scarce ecological value.

²⁹Baker, C.B. "Economic Growth of the Agricultural Firm. 1. Introduction to Economic Growth of the Agricultural Firm." Washington State University, Pullman. Bul. 86, Feb. 1977, p. 6.

³⁰Ibid., p. 6.

5) Bank credit is essentially granted in order to finance agriculture and livestock. Both activities obtained almost half of the total bank loans. In relation to agricultural credit, the coffee crop and livestock shared the highest portion of credit, being as high as 82% in 1973 and 50% in 1977.

In the last two years (1976-1977), the high prices on the world market (due to the imbalance between supply and demand) produced a decrease in the credit to the coffee crop which was principally compensated by an increment for livestock. Due to the significance of both products, in particular the coffee crop, in relation to its contribution to the GDP, as well as the generating factor of foreign exchange and employment, the operative and credit facilities toward the coffee crop have stimulated and continue stimulating an economy based on a single crop, which receives all the support from a strong class of farmers that in defense of personal interest severely limit the allocation of resources in other important activities of the national economy.

Therefore, it is necessary to review the financing of the coffee crop (and livestock) for the purpose of releasing funds that can be granted to new products in the agricultural sector. This policy implicitly also stimulates the investment of farmers' benefits in his own business.

6) A big share of available credit for agriculture is lent to farmers that can offer acceptable guarantees, that is, to those who possess land or other means of transferable

wealth. Small farmers and peasants without land obtain little or any benefits from the low interest rates, or the low price of inputs, etc. Frequently, they are unable to make use of these advantages due to the lack of guarantees or complementary resources of production.

Thus it is necessary for the commercial banks to give special attention to the technical and financial evaluation of the investment plans, in relation to project capacity for generating income, rather than emphasizing the borrower's capacity to provide mortgages or other types of guarantee.

It is important to take into account that the guarantee given as security of loans can never increase the farmer's capacity for paying a credit. So the government's banks should also consider that many times the purposes of accepting a guarantee is to avoid the need for securing a loan from unscrupulous lenders who impose hard conditions with the inherent goal of dispossessing the farmers of their farms. The suggested policy is even more essential for those farmers who are not strong financially or have other creditors. Thus, in order to improve the present policy, the guarantee requirement must be the last step in the development of a credit plan.

In view of the present conditions the following changes should be made: a) credit must be granted to farmers not only because they applied but on the basis of need; b) in Costa Rica there are many small farmers, leaseholders, and others that do not have land for mortgaging or fiduciary guarantees to offer. For this reason, the granting of loans

must be realized in accordance with the technical capacity of the project in execution and the payment capacity of the overall farm activities.

If the commercial banks require some guarantees, these would basically be on the crops or on those investments in machinery, equipment, and the like, acquired with the credit. For the purpose of protecting the farmers' investment more and to facilitate the banks in recovering the loan in case of loss, the establishment of crop insurance is very convenient, especially for those basic products not yet covered and for all those regions of production, without an insurance program.

7) The commercial banks, in accordance with the philosophy that created them, must constitute institutions of development of traditional and nontraditional products. As is well known, by nature some agricultural activities embody a higher risk. For this reason the development of such products has not been achieved. If this risk is not shared between private business and the bank, these activities will continue showing a level of stagnation for a longer period of time. This shared interest could be the beginning of that development; and, of course, this could not only produce in the farmer a climate of confidence but could permit the banks to modify their reputation of being a purely mercantile bank.

Whether certain agricultural activities make possible credit recuperation or they are important from a social-economic

point of view, it is indifferent that the guarantees should not be real, that the administrative costs of certain types of credits should be very high, or that the number of small clients should be many.

8) It is the observation of many bank employees, that although bank functions have increased substantially, the number of bank officials and technicians has remained relatively stable. For this reason, they are dedicating almost all their time to routine work, which was previously executed by employees less qualified, having virtually abandoned their important fieldwork.

There is a feeling among many that the new professionals are academically less prepared and often, perhaps due to insecurity, avoid making decisions on accepting loan applications for larger sums. They choose to send the applications to the central offices which lengthens the time required for obtaining a loan. Unanticipated delays are particularly damaging to farmers since production depends on the biological cycle.

If the directors of commercial banks want credit to constitute a positive factor for development of agriculture, then it is necessary to provide simultaneously with loans, other complementary services such as technical assistance. To achieve this, the number of field experts and bank officials would need to be increased and their professional training improved. If the banks do not choose to follow this suggestion, they should at least contribute monetarily to other specialized

technical institutions, strengthening in this manner, their efforts to convey to the farmers the elemental techniques of production. It is obvious that improved agricultural techniques would in reality serve as a guarantee for repayment of credit since the farmers ability to pay depends on successful production.

9) At present each commercial bank has its own procedure for granting loans. For the convenience of all it is essential that the Central Bank intervene in order to standardize the norms and procedures among the banks. The establishment of general norms for the following would be very important:

a) Loan Procedure: repayment terms, period of grace, delivery of funds, maximum amounts of credit, guarantee policy, time resolution, form application, and so forth.

In view of the fact that the Central Bank's information on commercial bank lending for agriculture depends on reports from outside the banking system, it is imperative that the institution provide its own source for obtaining data concerning the following items:

b) Information Register: number of operations, size distribution of loans, farm size, credit disbursed by products and by regions, type of guarantee, land tenure, type of farmer, delinquency rates, etc.

The importance of the above information is obvious. Therefore, the Central Bank must establish immediately the

statistical system of data collection in the field of agricultural credit because of its significance in quantitative analysis and in the process of decision-making. "In addition the international lending institutions could use such information for the total agricultural portfolios of the commercial banks, rather than requiring overly detailed information for only the program which these institutions have financed."³¹

10) A factor to consider in the granting of credit is related to the property of capital. It is often argued that foreign businesses established in Costa Rica provide substantial help to the nation in two ways: offering new technology, and investment of foreign funds in productive activities. But what is really happening in relation to credit is creating and perpetuating negative results. Since commercial banks presently often finance the realization of foreign enterprises, and since foreign applicants generally have stronger financial backing, they create unfair competition to the national farmer. Thus national credit, in part, is going to foreigners in preference to local farmers. The situation is even more prejudicial when one realizes that not only are loans being granted from local resources but from international credit institutions whose resources were assigned specifically for the national farmer or other Costa Rican agricultural businesses.

³¹Banco Interamericano de Desarrollo (BID) et al. Desarrollo..., op. cit., p. 23.

For this reason the National Banking System should avoid the practice of lending to foreign enterprises. These businesses have not only competed for available credit but have promoted increasing costs of land, as well as the establishment of large estates. High costs of land favors foreign currency and reduces the number of Costa Ricans who could compete for it. The effect is obvious greater areas of land are owned by foreigners. If this situation is to be remedied, changes have to be made. Government action should prohibit the sale of land to foreign enterprises and private individuals, or at least to limit the purchase size and the kind of agricultural land involved in the legal transaction.

The main purpose of this paper is to detect and focus on agricultural credit problems and suggest recommendations. All issues mentioned will have to be analyzed deeper in posterior studies to determine what action the government should take.

11) There are many farmers that sow within their farm different products during the same crop year. If the farmer needs a loan from the commercial banks, the general practice is that the farmer applies independently for each crop. In order of this, it is only reasonable that the commercial banks try to make the loan in only one credit operation, financing all the activities that the farmer proposes to do in the same agricultural year. This suggestion clearly has advantages for both the farmer and the bank. For instance, time employed by

the farmer for obtaining credit would be reduced in only one operation. On the other hand, the bank could benefit because of a decrease in the number of operations, which would reduce the paper work, time involved, payment of legal fees for inscriptions, etc. Consequently, the administrative costs would be lower. The savings, for example, could be used for the development of loans for new small farmers.

If a commercial bank approves a loan, the total amount of credit would not have to be deposited in a checking account, because this practice induces the farmers to pay interest over quantities of money that he is not using yet. Instead the banks could provide the disbursements according to the accomplishment of each phase of the project and in accordance with the progress of the respective activity. Within this framework, it would also be useful to the farmers if the banks would be responsible for making the payments to the holders of any debts that would incur in the farm operation. Although these measures would appear to increase administrative costs, they would be compensated by the following benefits: a) avoid credit deviation, b) improve the credit function, especially for small farmers, c) keep the technician very close to the fieldwork, d) decrease the necessity for liens on loans and other legal proceedings, thus reducing cost.

12) A topic of relevant importance is related to the integrated function that the credit agents of the commercial

banks, the delegates of the National Production Council, and the agronomists of the Ministry of Agriculture and Livestock must carry out. Although, it is true that in certain small towns or villages they work effectively in teams, in other places this is not achieved and often farmers do not obtain any benefit from these groups.

Because they represent the responsible institutions of providing credit, marketing, and technical assistance, it is of vital importance to review and coordinate those teams of governmental employees, which constitute unquestionably a powerful instrument of development for the agricultural production.

13) If by some means the Central Bank is able to determine what products are important to develop from a social-economical point of view, the first step in seeking that expansion is to remove the limitations defined in the tope system for a certain number of years. In other words, the Central Bank would not establish the maximum amount of credit that each commercial bank could lend for that product. Nonetheless, past experience must be considered in order to avoid possible deviations of credit for both the farmers and the banks.

14) In Costa Rica most of the best agricultural land is utilized in sowing traditional products especially for exportation. As a result of this, there is a scarcity of basic products for the Costa Rican diet.

Since bank credit is not only an influential factor of development but also of diversification, the National Banking System would use this tool to obtain it. In other words, the banks will finance traditional products only if the borrower contracts to sow a reasonable percentage of his farm land with a product of national basic consumption. Additional incentives could be offered to those farmers that want to comply with the policy of diversification (e.g. special interest rates).

15) The comparison between the central vs. decentralized decision-making on credit is an important issue to be analyzed in Costa Rica's near future.

As was mentioned under recommendation 3) central decision-making on credit is concerned with the present function that the Central Bank has, that is, the procedure that this institution uses in setting up amounts of credit by activities. After this allocation, the commercial banks determine for whom and for what products the credit will be used.

Decentralized decision-making should include a much broader base. By this system the decision of how much to lend and for what products will begin to flow from the farmers themselves. They will communicate their decision of production to the bank agencies which could then send reports of financial needs directly to the Central Bank which will include all of them in the national credit program.

Of course, both methods have strengths and weaknesses some of which will be mentioned. For instance, in the Costa Rican environment the centralized method would help determine more quickly the amounts of money to lend. Nevertheless, this process produces many biases in determining the size of loans and the kind of products to be granted credit. Perhaps some of these problems could be dealt with, in part, through the suggestions indicated in number 3) of this chapter.

Even though the decentralized method could indicate more exactly than the first one how much money to lend and for what products, the system would require: much operation time because many farmers would have to be interviewed; administrative costs will increase; a modern information system through which data flows without delay would be necessary; the level of education of those informants would have to be adequate, they would have to understand the importance of reporting accurate data.

The Central Bank could evaluate the convenience of setting up the decentralized system in its process of allocation of credit, or at least this institution could take a survey of farmers in order to determine the amounts of credit that would be needed.

16) Together with the suggested data about credit that the Central Bank must maintain, there is in Costa Rica a substantial need for collecting new data and for improving many of the existing time series.

Logically, the quality and availability of data influence the preparation and implementation of new policies and programs. In view of these facts and in view of the fact that the cost for obtaining data is almost always very high, there is sufficient cause to expect that the cost of data collection should be shared among the seventy different agricultural public institutions in existence in the nation and the private enterprises. Therefore, especially the following government offices must strengthen their function as reliable collectors of data: Statistics and Census Bureau, Ministry of Agriculture and Livestock, National Production Council, PIADIC (Agricultural Informative Program of Central American Isthmus). These institutions must maintain data on the following items: cultivated area, total production, yield per hectare, average productivity for farm labor, costs of production, consumer prices, farm prices, prices of substitutes, importation, exportation, stocks, milk production per cow, meat yield per animal slaughtered, cattle stock, slaughter, average weight, percentage death losses, birth rates, cattle breeding records, farmer records, precipitation, temperature, wind, humidity, hours of sunlight per day. Figures concerning the following items are also important: international prices, world production, world consumption, population, and so forth.

17) The activities listed below would be promoted primarily for the following reasons: increasing the national production; substituting imports; and meeting domestic consumption requirements.

a) Basic Grains (especially beans and corn). Beans and corn are typical small farmer crops, grown under traditional techniques with low yields and profits. There is a concern for betterment because these products are very important for human consumption and production of concentrates.

b) Dairy Cattle. Costa Rica has extensive areas which are well-adapted to dairying. In some of these regions milk production is an established and efficient activity. Substantial imports, an expanding local market, and experienced group production characteristics make dairying a priority development activity.

c) Forestry. The large areas of the country still covered by virgin hardwood forests will be bare by the end of this century if current cutting rates continue. Deficient policies, pasture expansion, and poor public control contribute to the problem. Removal of the forest cover leads to soil erosion and to the destruction of watersheds which are indispensable for human consumption, agricultural purposes, and energy production. Much of the wood which is cut is wasted because of poor handling. Wood-based industries are an important sub-sector and could be developed further, but only in conjunction with rational forest management.

18) Finally, the National Banking System and especially the Central Bank of Costa Rica must strengthen research in this area of agricultural credit for the purpose of seeking convenient alternate solutions to the problems; and creating

a modern system of farm credit, adapting to the special Costa Rican system the most advanced operational techniques used in other countries.

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