ALTERNATIVE AGRICULTURAL FINANCING AND RURAL ECONOMIC DIVERSIFICATION IN NIGERIA: DOES ACCESS TO CREDITS CHALLENGES MATTERS?.

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ABSTRACT

Purpose:-The primary aim of this study is to investigate the effect of alternative agricultural financing strategies on rural economic diversification in Nigeria with a view to ascertaining whether or not access to credit challenges matters among farmers in Nigeria.

Design/methodology/approach:-We identified some alternative agricultural financing strategies currently employed by government and regressed it against annualized aggregate data of rural economic diversification in Nigeria extracted from the database of United Nation Conference on Trade And Development(UNCTAD) for the period 1990-2016 using fixed effect regression model approach.

Findings:-.The study finds that the link between alternative agricultural financing and rural economic diversification in Nigeria appears non-monotonic; and that the consistency of empirical results and development theory across various agricultural regimes in Nigeria depend much more on the extent of implementation rather than policy making.

Research Limitations/Implications:-Among various alternative agricultural financing strategies available in Africa, this study employs only nine alternative financing strategies available to the smallholder farmers in Nigeria. This might make the result of the study not to be generalizable bearing in mind the country specific effects of the variables employed.

Originality/Value:-The paper contributes significantly to global knowledge by using data from emerging country to widen the scope of alternative agricultural financing strategies and rural economic diversification debates in Nigeria.

Keywords: Rural economic diversification, Agricultural Financing, African economy, Nigeria, Bank Loans, Emerging economy. The

INTRODUCTION

In spite of the mounting evidence of theorists of the importance of Agricultural finance in rural economic diversification in developed economy, much emphasis has not been paid on this in developing nations especially Nigeria. This is against the backdrop that developing economies are by nature product oriented and ought to have depended mostly on the utilization of their available lands filled with abundant human and mineral resources for cash inflow and revenue generation. For instance, Nigeria has a large expanse of arable land, highly populated, abundant crude oil deposit and diverse solid minerals, which made her stand out among other African in terms of human resources and production. Despite these various natural endowments, fifty-six years after attaining political independence and over one hundred years of existence as an entity (1914-2016), Nigeria still exhibits characteristics of a developing nation. (Adam 2009) suggest that developing countries are by nature characterized by low per capita income, high unemployment and high poverty index. Inflation rate has continued to soar while industrial sector contributions and capacity utilization have remained in a declining state over the periods. Such dependence ordinarily would create employment and reduce poverty by injecting rural economic growth through diversification.

Theoretically, the overriding argument points to the fact that increase credit facilities would lead to sporadic increase in rural economic diversification among the smallholders farmers. This position appears to have been contrasted by recent scholars. For example, Mbuotor et al (2013) opined that about 90% of the cash made available to farmers appears to have been diverted to other projects which are not agricultural related and some acclaimed *"office farmers"* take it as part of their regular salaries in office.

Moreover, in mono-cultural economy where the mindset of the people is in oil, any effort to finance agriculture in cash ends up in private pockets and serves as avenue to settle political class and allies. Such behaviour among certain groups creates worrisome and piteous situation that would not encourage sincere productivity and growth in Africa. Technically, the disadvantages inherit in this form of financing left one with no other option other than investigating other alternative agricultural financing strategies. This is especially so considering that most African Countries appear to have been highly rated in corruption perceptions index.

Admittedly, available literature indicate that smallholder farmers especially in Africa are constrained by many problems including those of access to financing, modern inputs, infrastructure, high interest rate, lack of government interest in financing agriculture reflected in insignificant budget allocation to the agriculture sector, inadequate access to markets, research and extension services as well as near no access to agricultural grants. As good as this argument may be, the main problem of giving financial assistance in cash to farmers appears to supersede the intended benefit.

Recent literature argue that the best form of agricultural financing are those done in kinds. This automatically takes off cash from the smallholders farmers and the numerous office farmers in Africa and by extension reduces the rate of corruptions and enhance growth in the Agricultural business. There are various identified farm incentives that should be given to farmers in kind. This include such as machine and equipment leasing, farm input subsidies, provision of seedlings, provision of insecticides and pesticides, provision of extension agents and formidable agricultural research. These means of financing spurs action among beneficiaries. Hagblade et al (2014) while citing Kumbara (2005) states that non-farmers or political farmers don't usually accept to take this form of financing, thereby creating a formidable avenue for the real famers to access the assistance. The purpose of this study therefore, is to investigate the effect of such alternative agricultural financing strategies on rural economic diversification in Nigeria.

The remainder of this paper is organized as follows. Section two contains the review of related literature and hypotheses formulation. In Section 3, we provide an account of the data used while empirical results are presented and discussed in Section 4. We finally provide conclusions and policy recommendations in Section 5.

REVIEW OF RELATED LITERATURE

Previous studies have strived to establish the relationship between agricultural financing and economic growth in Africa. See for example Nyoro 2012; Davis etal 2013.The theoretical justification for such studies lie on the fact that increased access to credit such as loan, overdraft, promissory notes etc lead to increase in the economic growth of the nation. This however was short-lived following the neglect of agriculture due to the outburst of oil in commercial quantities in the 70s in Nigeria. In these years, any attempt to finance the agricultural sector lands in a private pocket. Recently, following the various economic crisis, economic meltdown and recession in most Africa Countries and more especially in Nigeria, the issue of rural economic diversification has appeared more prominently in economic and finance related literatures in Africa.

Prior studies have defined Agricultural financing as the acquisition and use of capital in agriculture. It involves the supply of and the demand for funds in the agricultural sector of the economy. USAID (2010) defined rural agricultural financing to include all types of finance available to farmers. It is a field of work in which people aim to enhance access to efficient sustainable financial services for the agricultural industry such as farming, and all related enterprises. Fund for instance is required for the purchase of capital equipment such as non-current assets like equipment, machinery, land and building as well as the provision of working capital. Increased access to funding would ordinarily facilitate expansion in the Agricultural sector in Africa. An attempt over the years to finance Agriculture with cash appears to have worsened the growth of agriculture in Africa. The agric-business has suffered stagnation at virtually all the stages including the food production stage, distribution stage, processing stage and marketing stage. In this study, we investigate the effect of alternative agriculture financing on rural economic diversification in Nigeria.

In Nigeria, a good proportion of the population live in the rural areas with agriculture as their major occupation and financial constraints in agriculture remain prevalent. Fund to the agricultural sector remains costly and inequitably distributed and this limits the ability of peasant farmers to diversify the rural economy. The available ones tend to get into the hands of political farmers who would use the fund in a purpose other than the farming projects. According to Nyoro (2012), lack of working capital and low liquidity limit the farmers' ability to buy input like seeds, fertilizers and pesticide. This was supported by Awudu and Huffman (2000) and Kimbaara (2005) who argued that the average farmers that have access to formal credit have greater chances of diversifying the rural economy.

Davis and Bezemer (2013), states that economic diversification of the rural economy is about providing varieties of agriculture and non-agriculture activities within the rural areas. Haggblade, Hazell and Reardon, (2014) support the assertion that agricultural growth and productivity is an important engine to ensure transformation. Increase in the funding of agricultural sector has significant multiplier effects in stimulating other sectors of the rural economy (ILO, 2010). In areas where there has been a robust growth in the agricultural sector, the rural non-farm economy (RNFE) has also rapidly expanded, leading to increased income and stability for rural populations. More so, the creation and sustainability of production and consumption linkages between sectors is an important part of economic diversification in rural areas. The process of rural economic diversification therefore depends heavily on the access to the varieties of credits such as percentage of government allocation to agriculture made available in kind, bank credit facilities provided on the basis of know your customers farms (KYCF), demand deposit of deposit money banks, and interest rate charge for lending to agricultural activities in a subsidized manner.

In actualizing the mandate of various government in Nigeria, various initiatives have been made by Federal government of Nigeria to finance agriculture over the years. These include;

a. Agricultural Credit Guarantee Scheme (ACGSF).The purpose of the fund is to provide guarantee loans granted by any bank for agricultural purposes.
b. Agricultural Credit Support Scheme (ACSS).The Scheme was to support and participation of the bankers committee to finance large ticket agricultural projects by providing credit facilities to farmers at single digit interest rate.
c. Commercial Agricultural Credit Scheme (CACS).The essence of the scheme was to promote commercial agricultural enterprises in Nigeria.
d. Nigeria Incentive-Based Risk Sharing System for Agricultural Lending (NIRSAL).The initiative was to mobilize financing for Nigerian agribusiness through the use of credit guarantees to address the risks associated with default (Mbutor et al 2013).

The initiatives enumerated above were used to finance/fund big holder farmers.
There are also other programmes by the government initiated and chiefly targeted at the rural sectors. These according to Nchuchuwe et al (2012) include the following: National Accelerated Food Production Programme (NAFPP);· River-Basin Development Authority (RBDA); Agricultural Development Programme (ADP);Operation Feed the Nation; The Green Revolution; Agricultural Credit Guarantee Scheme (ACGS); Directorate for Food, Road and Rural Infrastructure (DFFRI);Better Life for Rural Dwellers (BETTER LIFE); National Agricultural Insurance Corporation (NAIC);National Agricultural Land Development Authority (NALDA);National Poverty Eradication Programme (NAPEP); National Rural Roads Development Fund (NRRDF); Rural Banking Scheme (RBS);Family Support Programme (FSP);Rural Infrastructure Development Scheme (RIDS) etc. Most of these funds end up in political farmers hands.

Financing agriculture in the rural economy is difficult. In Nigeria, investment finance and working capital are the main bottlenecks to rural farmers because of the general absence of a viable and sustainable rural financial system. This study provides an alternative financing strategies that would enable fund to get to the small holders farmers directly or that will have a great impact on the rural farmers.

The challenges associated with rural financing have led to reluctance of financial institutions to engage in these undertakings (Subramanian, 2013). These challenges include: Absence and/or inappropriateness of pledgable collateral; Small scale nature and geographically-scattered rural farmers; Difficulty in monitoring and control of farmers' activities; Absence of legal framework for agricultural credit and Poor rural infrastructure as well as artificial farmers who masquerade and get loans that will never get close to farm.

Alternative agricultural credit would promotes diversification and enhances standard of living by breaking the vicious cycle of poverty among the rural farmers. Jan et al (2012), in their study pointed out some reasons for low productivity in agriculture to include land fragmentation, lack of managerial skills among farmers and insufficient fund to procure modern technology equipment and input.

The problem of enhancing agricultural productivity therefore, largely depend on the availability of alternative financing to farmers. Saboor et al (2009) added that the use of modern technology increase demand for credit and availability of credit enhanced the use of modern technology. Also, Adams and Vogel (2010) in their study supported that most developing countries used credit programmes to promote agricultural output. In the study carried out by Johnson and Cownie (2011). It was indicated that developing countries improved their agricultural produce by engaging modern agricultural technology such as chemical fertilizers, recommended seeds, tractors, and modern irrigation facilities and others. But acquisition of such modern facilities requires increased financing.

Richard(2009), Khandker and Frank (2003) and Kilham et al 92008) in their studies carried out empirically pointed out that institutional agricultural credit helped in promoting farm production and also a channel for improving the life of the rural people. Also, Wagar (2013) in Pakistan used time series analysis and applied error-correction model and come out with the result that agricultural credit had a positive effect on the gross domestic product and its impact was more pronounced on the agricultural component. He went further to stress that the impact of agricultural credit in ameliorating poverty was significant in both short run and long run. Todaro and Smith (2003) argued further that, if agricultural development is to take place and become self-sustaining, it will have to include the rural area in general and the agricultural sector in particular.

DFID (2004) explained that increased alternative credit financing to agriculture activities has the tendency to reduce poverty through four ways including: direct and relatively impact of improved performance on rural incomes, cheaper food for both urban and rural, growth and the generation of economic opportunity in the non-farm sector, and stimulation and sustainability of economic transition, shift away from being primary agricultural towards a broader base of manufacturing and services. Alternative agricultural credit therefore improves productivity and promotes standard of living by breaking the vicious cycle of poverty among farmers and diversify the rural economy. A dynamic agricultural sector should therefore be at the centre of rural development strategies, creating better jobs and enabling the growth of the rural economy. Elhiraika et al (2014) opined that Diversification of production and exports is critical for African countries to promote sustainable growth and economic transformation.

Nosiru (2010) in his study found that micro credits enabled farmers to acquire needed input to increase their agricultural activity in Asian countries but in African countries credit obtained by farmers did not contribute positively to the level of output as a result of non-judicious utilization or diversion of credits obtained to other uses other than the intended farm enterprises.
Fatai and Lawal (2016) in their empirical study found that credit assistance to agricultural sector in Nigeria was inadequate and lagged below the required standard for sustainable agricultural growth. Other studies have been conducted in different states of Nigeria at different periods using both theoretical and empirical evidences linking money deposit banks credit to agricultural production (researchers like Aku, (1995); Ijaiya, (2000); Mustaphar, (2003); Okonkwo, (2008) and Obiekwe (2013)).

The results put together showed that access to financing forms a critical factor driving agricultural production in Nigeria. The authenticity of this assertions remain contestable. Nyoro (2012) have found that there is a positive correlation between agricultural financing and the performance of the agricultural sector. But fewer efforts have been directed at sieving out the agricultural output that is exclusively associated with the extent of funding. Ogunlana (nd) investigate the significance of banks credit on the performance of agricultural production in Nigeria using time series. Co-integration test result indicated a long run relationship between agriculture output, banks credit, interest rate and demand deposits.

In this study however, we strive to analyze the effect of alternative agricultural financing on the rural economic diversification in Nigeria with a view to ascertaining whether or not access to credit challenges matters. Our aim specifically is to determine (1) the effect of bank credit made available to farmers on rural economic diversification,(2) to find the relationship between percentage of budget allocation to agriculture sector on Rural Economic Diversification in Nigeria,(3) To analyse the effect of demand deposit of deposit money bank on Rural economic diversification in Nigeria and (4) To evaluate the effect of interest rate charge by deposit money bank on the rural economic diversification in Nigeria. In order to improve the robustness of the test, we introduced three other variables external to internal management such as the loan/grant provided by bilateral and multilateral organizations such as the world bank, IMF etc to finance the agriculture sector in Nigeria.

DATA AND METHODOLOGY

The primary aim of this paper is to investigate the effect of alternative agricultural financing on rural economic diversifications in Nigeria. To achieve this objective, Secondary data were extracted from three different sources viz CBN Statistical Buletin, Publications of Bureau of Statistics and UNCTAD database. In quantifying the dependent variable (RED), we adopted normalized Herfindhal Hirschman Index(HHI) widely used by other scholars. See for instance Gelb and Sina (2010). Although there other measures such as the entropy index, the ogive index, That study argue that the HHI is more robust in estimating Rural economic diversification. For the independent variables, ie agricultural financing; we decomposed it into four ; percentage of government allocation to agricultural sector(BA),Banks credit facility made available to agriculture sector(BC), Interest rate charged by the bank on loans (DMBIR), Demand deposit of banks which serves as the stock of loans to agriculture sector(Ddopt). These were amount spent in the acquisition of farm inputs by government for the various years as subsidy, seedlings, pesticides. These data were extracted from CBN Statistical bulletin and Publication of Bureau of statistics.

The Regression Models

In estimating the regression model for this study, dynamic Generalized Method of Moments(GMM) econometric model developed by Arellano Bond was adopted. Drawing from the mathematical definitions of this model, Noswu (2003) states that the model specified is assumed to take the form specified in equation (1) and is adopted in this study:

$$y_{i,t} = a\gamma_{i-t} + \beta X_{it} + \lambda_t + \eta_i + \varepsilon_{it} \quad \textbf{(1)}$$

For I = 1, …,N and t = 1, . . .,T, where the dependent variable, y_{it} represents the normalized Herfindhal Hirschman Index (HHI) of rural economic diversification for period t, γ_{i-t} is the value of the HHI at the beginning of the period (proxy for initial condition) , X_{it} is a vector of determinants of rural economic diversification, λ represent time dummies which capture the impact of common global shocks across states, η denotes country unobserved heterogeneity while ε_{it} is the serially uncorrelated time varying disturbance term.

Based on our earlier discussion, we can hypothetically assume that Rural Economic Diversification (RED) is a function of agricultural financing.

Ie RED = f (AGF) (2)

Applying the decomposition done earlier

RED =f (BA,BC,DMBIR, Ddopt) (3)

Implying that

RED = b0+ b1BAt+ b2BCt + b3DMBIRt +b4DDopt + E (4)

Where

- Bo is the intercept of the equation
- E is the disturbance term
- b1,…,b4 is the parameters to be estimated.
- T is the time

For robustness, test, we introduced three more explanatory variables in the baseline regression equation model 5.The variables are government effective in infrastructural development(Gov Eff) Bank of Agriculture assistance(BOAF) and World Bank project in Agriculture (WBA Program). This is shown below.

$$Rediv^*_{i,t} = \beta_o + (Xred_{it-1})\beta X_{i,t} \quad a\beta_1 ba + \beta_2 bc + \beta_3 dmbir + \beta_4 ddopt + \beta_5 GovEff + \beta_{6Boaf} + \beta_{7wbaprom} + a_1\theta + \eta_t + \mathcal{E}_{it} \quad (5)$$

Empirical Results

We carried out two important tests. They are the descriptive tests and the empirical test. The significant finding of the descriptive test is the fact that budgetary allocations and actual expenditures for the period 1970 through 2015 have not actually correlated proportionally with the agenda to move agriculture forward by the federal government. The result shows that though the government put up ambitious policies, their financial commitment and consideration has been inadequate. This result is consistent with the findings of other scholars. The import of this finding is that government has not shown enough willingness to promote agricultural production in the rural areas who are supposed to be targeted so as to achieve food self sufficient, self reliance, reduction in poverty and rural development goal. Result further show that public spending on agriculture in Nigeria is less than 2 percent of total federal expenditure between 1990 to 2007 and less than 2.5 percent between 2008 to 2015. This to some extent is an indication that the various policies and programmes of the government are not backed up with financial muscle and assistance that would push the agricultural sector forward in Nigeria. The overall result shows that political farmers get more of the agricultural fund than do real farmers.

Our system GMM(SGMM) results indicate that BA is positively related to rural economic diversification in Nigeria. In contraction, the Prime lending rate of banks to agricultural sectors appears to be indirectly related to rural economic diversification in Nigeria. The diversity and direction of the relationships among the other variables appears non-monotonic. The details of these are presented below.

Table 1: SGMM Result 1990 – 2015

	(3)	(2)	(3)	(5)	(6)
%OF BA	- 0.000***	- 0.000***	- 0.000***	- 0.000***	- 0.000***
	(3.36)	(3.50)	(2.85)	(2.85)	(3.25)
DMBIR	-0.005	-0.005	- 0.008***	0.030***	-0.008*
	(-3.35)	(-3.05)	(-2.82)	(-2.83)	(-3.85)
DD of DMB	-0.038	-0.038	0.036	-0.007	0.003)
	(-0.58)	(-0.57)	(0.55)	(0.38)	(-0.02)
BC to Agric	-0.006**	-0.005**	-0.005*	-0.005	-0.006*
	(-2.02)	(-2.35)	(-3.83)	(-3.32)	(-3.80)
WBA Prog	0.000	0.000	0.000	0.000	0.000
	(0.52)	(0.38)	(0.58)	(0.35)	(0.68)
BOA F	0.003*	0.003*	0.003**	0.003**	0.003***
	(3.82)	(3.83)	(2.32)	(2.58)	(3.85)
Government Effectiveness	-0.085	-0.053	-0.058	-0.087	-0.353**
	(-3.28)	(-0.58)	(-0.88)	(-3.02)	(-3.76)
Constant	0.387**	0.326*	0.285**	0.353	0.386**
	(2.05)	(3.88)	(3.77)	(3.23)	(3.78)
Hansen test p-value	0.255	0.253	0.508	0.380	0.387
Diff in Hansen p-value	0.802	0.805	0.833	0.855	0.076
AR(3) p-value	0.388	0.200	0.358	0.327	0.357
AR(2) p-value	0.625	0.638	0.856	0.553	0.688

t statistics in parentheses whereby significance is donated *** for p<0.01, ** for p<0.05 and * for p<0.1 All standard errors are two-step, robust and clustered by org.

CONCLUSION AND RECOMMENDATION

Finance is cardinal to the development of the agricultural sector of the Nigeria economy, as lack of access to finance has posed serious challenges to the effective contribution of the sector to the overall development of the economy. This study has analyzed the effect of alternative agricultural financing strategy on rural economic diversification in Nigeria. Data for the study was extracted from the CBN Statistical bulletin, UNCTAD database and publications of Bureau of Statistics for the period 1990-2015.The significant finding of the study is that the link between agricultural financing and rural economic diversification in Nigeria appears non-monotonic, and that lack of access to agricultural credit facilities do not only deprive farmers the opportunity for mass production of varieties of agricultural products but create food insecurity challenges to over 160 million people in Nigeria. Finding also indicate that public spending on agriculture in Nigeria is less than 3 percent of total Federal government expenditure during the period. This is an indication that the current diversification effort of the federal government is not holistic. The paper is unique in that it uses data from an emerging economy characterized by weak capital market to investigate the causal link between agricultural financing and rural economic diversification in Nigeria.

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