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AGRICULTURAL FINANCIAL POLICIES IN BRAZIL AND THE US – A COMPARISON

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1.0 INTRODUCTION

Frequent inquires have been made from international trade circles concerning the high level of support and protectionism which some countries have devoted to their agricultural sectors. As examples, we can cite tariff barriers (of which the world average is about 40 %, reaching 1000% in some cases), non-tariff barriers (which many times are more complex and restrictive than tariff barriers), anti-dumping and similar measures, fiscal renunciations and, more specifically, subsidies to production or direct payments to producers.

As a consequence, countries efficient in producing some agricultural products endowed with comparative advantages are constantly and greatly harmed by the lack of access to the world market. This distortion limits by itself the total volume of transactions of these products and, ultimately, enhances prices in the market as a whole.

Because of that, and depending on the economic wealth of each country, the achievement, maintenance, and amplifying of new markets, as well as the agricultural production for the internal supply, has occurred: either in a sustainable way, without depending on the channeling of a high index of economic subventions, or under governmental support through subsidies devoted to the sector.

To derive the relevance of these questions to developing countries such as Brazil, suffice it to point out that agribusiness is responsible for a considerable percentage of its GDP and exports. In 2000, primary agriculture accounted for 10.10% of Brazil's GDP and around 23% of total labor force. The contribution of the whole agribusiness sector is estimated at around 27% of the GDP, corresponding to 27% of total labor force. In the case of foreign trade, agriculture accounts for about 36% of exports.

This scenario of external competition and protection measures toward internal markets has given direction to policies by which governments support their agriculture sectors.

Keeping in mind the importance of these questions, this essay has as its objective to identify the most important policies toward agricultural sector currently conducted by both Brazil and the United States, the major agricultural producers in the Americas. In order to clarify the reasons for these policies, the present analysis starts by describing the main facts that exerted, in both countries, great influence in their formulation.

2.0 THE BRAZILIAN AGRICULTURAL POLICY

2.1 THE RECENT HISTORY

In the middle of the 1990s, a considerable portion of the Brazilian farmers was greatly encumbered with debt to the financial system and, consequently, had their payment capacity compromised. This situation was a result of: 1) successive crops in which the internal and external market prices of agricultural products were not compensatory; 2) the simultaneous availability of great volumes of products in the internal market in reason of the opening of the economy undertaken by the government from 1990 onwards; 3) successive crop failures resulting from long periods of drought, and 4) high financial charges on rural loans.

On account of the high level of inflation in that period, the financial charges on agricultural loans were composed of both a fixed interest rate and an index of monetary correction, resulting in a final interest rate incompatible with the income of the sector.

In reaction to this scenario of delinquent indebtedness, the financing institutions adopted a more conservative policy in granting new agricultural loans, becoming much more selective than before and requiring collateral not previously demanded.

In consequence of all the factors previously mentioned, intensive negotiations between the farmers' representatives in the National Congress

and the federal government resulted in the prorogation and decrease of the interest rates on loans contracted until June 1995. Under this change, the federal government provided the conditions to enable the banks to extend the debts for up to 10 years, observing the limit of R$ 200 thousands for each beneficiary, with a new interest rate of 3% per annum, plus the annual percentage variation on the minimum prices[1] of any of 5 products chosen by the farmers.

In respect of values above R$ 200 thousands, the federal government adopted a scheme that allowed an extension of these debits for 20 years, and, according to the size of the holding of the producer, the establishment of the financial charges on these extensions of 6%, 7% or 8% per annum, plus the annual percentage variation on IGP[2] (which estimation to 2001 is about 9.11 %). In this case, there was no form of subvention from the government.

The two previously described systems of extending agricultural loans observed as a general principle the revival of the producers' debt repayment capacity and the grant of more favorable conditions to the small farmers (those with debts of up to R$ 200 thousands).

It is important to emphasize that, in the case of extending debts of up to R$ 200 thousands, the participation of the federal government was essential for the implementation of the measures, since it covered for the financial

[1] Minimum Price: Established annually by the government
[2] IGP= Índice Geral de Preços (General Index of Prices), used as a measure of the inflation rate.

institutions the costs of obtaining the money lent used in those loans and the estimated additional administrative costs related to the maintenance of these loans during the 10-year extension period.

With the profile of their debts extended and under more favorable financial conditions, the producers were able to have access to new loans.

In parallel to these arrangements, from 1995 onwards the interest rates on general agricultural loans ceased to be indexed to a price index and came to be totally pre-fixed, as shown below:

Crop Year*	Non Familiar Producer % a.a. (1)	Familiar Producer % a.a. (2)	IPCA % a.a. (3)
1994/1995	60.08	30.54	33.03
1995/1996	16.00	16.00	15.51
1996/1997	12.00	9.00	7.26
1997/1998	9.50	6.50	4.40
1998/1999	8.75	5.75	4.17
1999/2000	8.75	5.75	6.09
2000/2001	8.75	5.75	6.30
2001/2002	8.75	4.00	5.65 **

? From Jul of a year to Jun of the following year

? Estimate

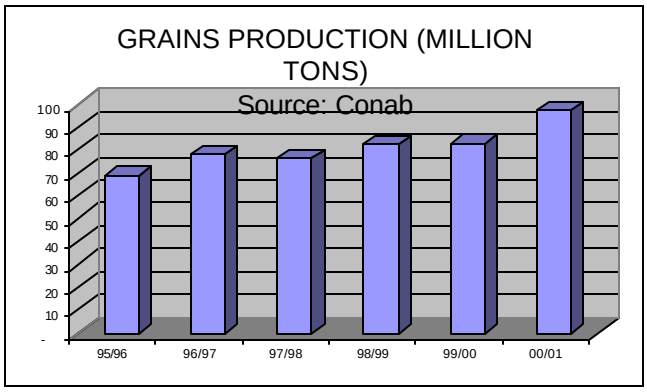
(1) Operation and investment loans

(2) Operation Loans

(3) IPCA= Consumer Price Index (Indice de Preços ao Consumidor), official inflation index.

From these figures, we derive that the real interest rates on agricultural loans have remained at low levels since 1995, especially for the familiar producers, which have been benefited with negative final rates in the last 3 years.

To summarize, from 1995 to 2000, the government concentrated its efforts in finding a solution to the debts owed by producers which were jeopardizing part of the financial institutions and adopted a gradual decrease in the interest rates charged by the rural credit system.



The measures previously mentioned had an important contribution to the growth of grains production as shown here.

As already seen, in some cases these arrangements were undertaken with the government's financial involvement and, in the other cases, the government only had administrative participation without any kind of financial support.

It is necessary to clarify that these policies have been carried out within the possibilities of the inflation control and economic stabilization plan, initiated by the government in the middle of 1994.

2.2 THE BRAZILIAN RURAL CREDIT SYSTEM

In Brazil, rural credit is provided by credit cooperatives and by the commercial banks, participants in the National Rural Credit System[3] (NRCS). The rules and conditions to be observed regarding loans are established by the National Monetary Council[4] (NMC) - a body connected to the Finance Ministry - and the application of these rules and conditions is examined by the Central Bank.

These definitions have as their origin proposals from the Agriculture Ministry, which is in charge of the policies devoted to commercial agriculture, and from the Agrarian Developing Ministry, that responds for the policies applicable to the family farming units and to agrarian reform.

Under the official system of rural credit, the main origins of resources to the rural loans are:

a) Obligatory Resources (compulsory funds): the financial institutions that receive cash deposits are alternatively obligated to: 1) deposit into the Central Bank, during a period of 6 months, without any kind of remuneration, the amount equivalent to 25% of the money average received from the public as cash accounts during the previous semester; 2) pay to the Central Bank a fine of 20% of that amount with them being free to use the money in any proposal, and 3) lend that amount to

[3] NRCS: Sistema Nacional de Crédito Rural/SNCR
[4] NMC: Conselho Monetário Nacional/CMN

the farmers at the interest rate established by the National Monetary Council, presently 8.75% per annum[5];

b) Resources from the Constitutional Development Funds[6]/CDF (North, Northeast and Center-West regions): these funds have guaranteed in the federal constitution a certain percentage of some taxes collected from the public, that could be applied in loan programs to the productive sectors from the North, Northeast and Center-West regions of the country, among them the rural sector. Basically, these funds provide investment loans;

c) Resources from the Rural Savings Accounts: at the beginning of the 1990s, as a result of the scarcity of sources of finance for the rural sector and on the condition that they apply a previously determined percentage of the savings in loans to the farmers at an interest rate to be negotiated, some banks were allowed to operate with saving accounts. This percentage is presently fixed at 40%[7] and represents approximately about R$ 8,0 billion;

d) Equalized Resources: to be subsequently explained;

e) Resources from the Foment Programs: these programs have the federal budget as its source of finance and are devoted specially to foment investments in the rural areas. Currently, as a result of the strategy of

[5] Source: Rural Credit Manual – Central Bank (Manual de Crédito Rural – Banco Central do Brasil)
[6] CDF: Fundo Constitucional de Desenvolvimento/FC

prioritizing operating with equalized funds, the amount of resources allocated to this proposal has been negligible;

f) Other Resources: any other resources applied in rural loans at an interest rate resulting from negotiation between the financing institution and the borrower.

At the moment, the principal sources of finance throughout the agricultural sector have been, in descending order of quantity, those originating from the deposit accounts into the banks (sub-paragraph "a") and those equalized (sub-paragraph "d").

It is important to point out that the use of the resources from the compulsory funds, the biggest loan source of rural credit, does not imply any encumbrance to the public accounts referred to as economic subventions or subsidies.

On the other hand, the use of the second biggest loan source to the rural sector, the equalized resources, involves considerable government expenses as economic subvention (interest rate equalization), making a deep incursion on public funds.

Those resources mentioned before are channeled to crop loans, commercial loans and investment loans, while each one, depending on the different kinds of products, is capped at certain amount established by the NMC. The

[7] MCR

first one is devoted to cover the overall costs of planting, managing and harvesting (operating costs). Currently, it is payable in up to 5 monthly installments after harvesting.

Commercial loans have two kinds of beneficiaries:

- **Farmers: that can take commercial credits by offering their products, stored in accredited warehouses, as collateral. Thus, they amplify the period to sell their production, and, consequently, the chances of obtaining a better price; and**

- **Processors of some eligible agricultural products: the access to these kind of loans is by and large limited to 50 per cent of their production capacity. Taking this type of loan, the processors are obligated to meet to farmers at least the minimum price set by the government.**

In turn, as its name already indicates, investment loans give producers long term support to investments like small agro industries, barns, machinery, equipment etc related to rural production. The state owned Brazilian Bank for Economic and Social Development (BNDES) centralizes resources devoted to these kind of loans, repassing the disposal funds to other banks to be effectively applied.

It is important to realize that, in reason of lack of funds, only in the recent years investment loans has resumed its availability.

2.3 GOVERNMENT SUPPORT

Beyond issues connected to plant care regulation, agricultural zoning etc, government support for the sector is noted under three main aspects: 1 – support to research; 2 – support to credit; and 3 – support to commercialization of agricultural products.

2.3.1 SUPPORT TO RESEARCH

Private entities engaged in agricultural research in Brazil are few. Among them, the most representative are those that deal with agricultural pesticides and feeds, which, in the majority of cases, carry out basic studies in their countries of origin.

Filling this gap, there is a network of public institutions consisting of federal and state universities and public research enterprises, such as Embrapa[8].

Although without adequate financial means, this official research network has been responsible for great advances, as follows: the development of technologies that enabled the transformation of the Brazilian savannas into productive lands (which today is responsible for the majority of grain production); the development of biological control techniques largely applied to the Soya bean, corn, rice and other kinds of cultivation,

decreasing production costs and allowing a considerable economy in imports of pesticides; genetic improvement of various plants affording advantages in productivity, quality and resistance to adverse conditions; etc. According to Embrapa data, in 2000 all these advances occasioned R$ 5,250 millions in economic impacts.

2.3.2 SUPPORT TO CREDIT

In consequence of growing budget restrictions, from 1995 onwards the Brazilian government has changed considerably its way of supporting rural credit. Instead of repassing large sums of money to the banks to permit loans to the farmers, gradually it has increased the use of the interest rate equalization system (a kind of economic subvention), through which it becomes viable for the financial institutions to grant loans to the rural producers at the interest rate established by the National Monetary Council, using funds collected from savers.

In order to avoid loss in this kind of operation, the government pays to the banks, monthly, the difference between the cost of using money belonging to savers, including the administrative and tributary costs of the loans, and the interest rate charged on the rural loans (presently of 8.75% per annum, in the case of commercial agriculture, and 4% per annum, in the case of loans to family units). It is worth mentioning that the financial risk of operations incurred through this system is assumed by the banks.

[8] Embrapa: Agriculture Brazilian Survey Enterprise.

An implicit advantage of this system is to provide loans to the farmers based on money collected from the market and at the risk of the financial institutions, avoiding pressures for governmental waivers if the loans were made based on government funds.

The average leverage of rural loans for each monetary unit spent with payments of interest rate equalization range from 1:5 to 1:10, depending, entirely, on the loan and the costs considered.

Bearing in mind the progressive process existing in Brazil toward fiscal adjustment and stabilization of the economy, the consequence of which is also reflected in the level of interest rates prevailing in the economy as a whole, probably the tendency is, on the medium term, an increase in the average leverage ratio achieved by this system.

Without the government support for agricultural credit few are the agricultural activities that could support the current high level of basic interest rates of the economy of about 19 % a.a..

Although the governmental support represents an important contribution to financing farmers, it has been far from attending the whole demand. To cover this lack of resources the private sector finances part of the production, either through consumers firms advancing payments to the future harvesting or through suppliers delivering inputs to future payments. A greater part of the commodities production has been financed in this way,

yet these were based on high interest rates or heavy depreciated expectation of future prices.

THE AGRARIAN REFORM

In order to enhance and give more rhythm and effectiveness to the activities within the ambit of agrarian reform policies, from 1996 onwards important adjustments have occurred in agrarian legislation, that have resulted, for example, in:

a) a faster cadence of arrangements toward expropriation, avoiding excessive sums in financial indemnification (reparation) to the land owners;
b) the establishment of high taxes on unproductive lands; and
c) new ways to access land, etc.

In relation to the last paragraph, two ways exist for landless laborers to gain access to new lands. Firstly, the traditional one: the government expropriates unproductive properties, divides them into parcels and develops a settlement providing the basic infrastructure. In the second way, the government provides, up to a certain limit, discounted loans to the landless laborer or to a group of them to buy a portion of land. Under such an arrangement, the beneficiary can buy some land at his own volition, at the price considered fair by him. This system avoids the long process of expropriation.

Adopting this sort of procedures, agrarian reform is expedited. Over the last 6 years, more families have been settled than the total settled in all the previous years put together.

Once settled, the new landowners become beneficiaries of the PRONAF[9], a program devoted to family units.

POLICY DEVOTED TO AGRICULTURISTS IN FAMILY UNITS

In order to pay special attention to small producers based on family units (regardless of being sharecroppers, squatters, renters, settlers or owners) there is a program called PRONAF that has the strategy of gradually including such producers in the commercial agriculture (it is a market oriented program), through financial assistance (investments and crop loans).

Adopting the annual family gross income as a parameter, the program classifies its beneficiaries into 4 groups, each one under different conditions and loan limits. In general, the interest rate charged on the loans under PRONAF program ranges from 1% per annum to 4% per annum.

As soon as their annual family gross income is enhanced, the beneficiaries are classified in a superior group, losing, progressively, the right to discounts in new loans, and, as a compensation for it, winning an additional loan limit, under the same interest rate.

Surpassing the limit of annual family gross income of the fourth group, the producers, in theory, must be financed by the normal rural credit, paying a bigger interest rate (8.75 % per annum), but having the right to larger loans.

PRONAF depends on equalizable resources, resources from the Constitutional Development Funds and, to a lesser extent, resources from the federal budget that are repassed to the banks to permit loans to beneficiaries of the first group (the weak ones).

Finally, the extent of the range of PRONAF must be pointed out. Recognizing the non-agricultural activities as a substantial complementary source of income to small farmers, the program also provides investment loans devoted to workmanship, agricultural tourism, small agro-industries etc.

2.3.3 SUPPORT TO COMMERCIALIZATION

The support given by the Brazilian government to the commercialization of rural products only comprises basic products such as rice, beans, corn, wheat, and cotton and it has the strategy of guaranteeing a minimum income to producers and promoting the commercialization of their crops.

[9] Pronaf: the National Programme to Strengthen Family Farming

To help producers' decision on what they should cultivate in the next crop, the government, before each planting period, issues the minimum prices of the staples previously mentioned that will serve as parameters for governmental support.

According to this, when the market prices of agricultural products are below or presents the prospective of falling below the previously established minimum price in some parts of the country, the government, depending on the availability of central funds, adopts one of the following procedures:

a) offering, at public auctions, bonuses to merchants that assume the compromise of acquiring those products by paying to producers the reference price fixed by the government (that can be either the minimum official price or the price fixed in an option contract). In addition, the merchant assumes the obligation of selling the acquired products in regions with supply difficulties (previously indicated by the government);

b) selling to the producers, at public actions, option contracts which give to them the right of selling to the government certain quantities of their crops at prices and dates previously established; and

c) emptying the market through direct acquisitions of the products from producers by its public agency National Food Supply Company (CONAB),

and paying to the farmers the relevant minimum price established before the crops were planted.

Regarding the procedures mentioned in sub-paragraph "a", this is a system called Subsidy Auction Programme – PEP, whose objective is to stimulate private initiative in buying agricultural products at the fixed minimum prices and selling them in places previously indicated by the government. In this way, the government guarantees to farmers the receipt of at least the fixed minimum prices for their produce and avoids the formation of public stocks of agricultural products, which implies high storage costs. To summarize, it works as an intervention at the margin.

Relative to option contracts, they ensure security of prices for farmers. Through them, the government enables the farmers to transfer part of their sales from periods of high supply to periods of low supply (generally, the contracts are launched at the beginning of a harvest and are due at the time of the next harvest).

If on the due dates of those contracts, the market prices are below the prices established by them, the government has the alternative of trying to exonerate itself from the obligation of buying the products by the payment of a bonus to either someone that has an interest in assuming that obligation or the owners of the contracts, if they so desire. Frequently, these bonuses are equivalent to the difference between the market prices and the prices of the contracts, plus the premium paid for their acquisition.

Finally, it must be emphasized that both the minimum prices and the prices of option contracts are generally below the average market and future prospective prices, respectively.

3.0 AMERICAN AGRICULTURAL POLICY

3.1 THE RECENT HISTORY

From the 1960's onwards, a gradual shift was made in some American programs devoted to the rural sector, especially those devoted to export crops. As an example, we can mention that instead of stimulating market prices through production controls and purchases, the American government began to support farm income with direct cash payments.

In the 1970's the costs of farm policies were temporarily hidden behind the inflation; at the same time, markets tightened as crop exports soared. Also, expecting inflation to continue, the Congress increased the nominal price-supported level. As a result, through that time unprecedented growth and prosperity was experienced by the agricultural sector.

During this period, many agricultural lenders relied on inflated expectations for future incomes and considering the current high value of agricultural assets, especially farm real estate, rapidly increased the volume of loans and applied lending practices that were contrary to safe and sound lending principles.

Yet, when tight monetary policies were embraced in the 1980's --soaring interest rates--, exports and market prices fell and farm program expenditures rose sharply, even with extensive supply controls reimposed. By 1983 this problem had become widespread all over the country and was followed by a collapse of the agricultural real estate market.

In consequence, total agricultural loan volume declined and loan losses soared. Because of that, in this time period many lenders left the marketplace. This trend was reversed only in the 1990's.

To face this scenario, important farm policy debates took place in 1985, having as an outcome a decrease in the price-support levels, offset by even larger direct cash payments.

Between 1985 and 1993, an effort was made by the Uruguay Round of General Agreement on Tariffs and Trade (GATT) to bring about greater farm policy reform. But the terms of the final Agreement on Agriculture did not go beyond reforms that had already been undertaken unilaterally by the American government before the negotiations had begun.

Up to 1996, some programs carried out by the American government, such as deficiency payment and contract acreage, generated distortion in the market of agricultural products and created uneconomic incentives for supply expansion.

Deficiency payments consisted of a direct government payment made to farmers who participated in wheat, feed grains, rice or cotton programs. The payment rate was based on the difference between the target price and the higher of the price support loan rate or the national average market price during a specified period of time.

Through contract acreage the American government used to implement supply control of some agricultural products, especially those devoted to exports, by paying farmers to keep a portion of their lands idle.

After a long debate about the way the American agricultural policy should take, the Federal Agriculture Improvement and Reform (FAIR) Act was signed into law in April, 1996, changing the current policies, intending to reduce the distorting effects of the traditional farm support, and establishing the correspondents expenses for the fiscal years of 1996-2002. Its measures included a range of fields: commodities, credit, conservation, rural development, trade and nutrition.

First, it removed the link between income support payments and farm prices and eliminated acreage contracts and supply control. Thus, producers became more independent in making market orientated decisions on what

to plant and not "government orientated decisions", as previously. Besides other objectives, this measure was intended to improve U.S. competitiveness in world markets.

Under its flexibility contracts the FAIR Act also sought to increase budget discipline and to move closer to the elusive goal of budget certainty, replacing the open-ended deficiency payment entitlements from the 1989 and 1990 farms bills with an explicit cap on most farm support expenditures.

In order to insulate farm policy from an automatic growth of intrusive support, the FAIR Act also capped nominal loan rates at low levels, for the American pattern avoiding market-distorting price-supported levels.

3.2 THE AMERICAN RURAL CREDIT SYSTEM

The American Farm Credit System (System) is a network of borrower-owned lending institutions and related services organizations specialized in providing credit and related services to farmers, ranchers, and producers.

The System is composed of the following lending institutions:

- **six Farm Credit Banks that provide loan funds to Production Credit Associations (PCAs), which provide short- and intermediate-term loans; Agricultural Credit Associations (ACA), which make short-, intermediate-**

and long-term loans; and Federal Land Credit Association (FLCA), which make long-term loans;

- **one Agricultural Credit Bank (ACB), with the authority of a Farm Credit Bank and makes loans of all kinds to agricultural, aquatic, an public utility cooperatives and is authorized to finance U.S. agricultural exports and provide international banking services for farmer-owned cooperatives.**

All System banks and associations are governed by boards of directors elected by the stockholders who are farmer-borrowers of each institution. Besides, Federal law requires that at least one board member has to be elected from outside of the System by the other directors. Unlike commercial banks, System institutions do not take deposits.

These institutions are regulated by the Farm Credit Administration (FCA), an independent agency in the executive branch which has as its major functions conducting examinations of all System institutions; enforcing safe and sound banking practice, Federal Statutes, and FCA regulations; developing regulations and policies; interpreting the laws applicable to the System and identifying risks faced by the institutions and taking corrective actions.

The loans provided by the System may be made to support the processing and also the marketing activities of the borrowers.

In order to facilitate obtaining money from the market, the System banks formed an entity named Federal Farm Credit Banks Funding Corporation (Funding Corporation), also examined and regulated by FCA, that markets the securities the banks sell in the Nation's capital market to raise loan funds. The Funding Corporation, through a group of securities dealers and dealer's banks that covers the entire country, offers these securities, chiefly bonds and discount notes.

It is important to stress that, through this system, the farm credit institutions obtain the majority of their loan funds and that it works as a market orientated activity, without government intervention or subvention.

The specific interest rates charged by the System institutions are not determined by FCA. Specifically, it is in charge of making sure that System institutions price their loans at levels that are consistent with safe and sound banking practice.

The effective interest rates on loans is computed based on the stated rate to show the effect of loan origination fees and stock purchases required of the borrower at the time their loans are made.

The interest rates can be fixed or variable. In the last case, the lending institution has to advise borrowers of the amount and frequency by which the interest rate can be adjusted during the term of the loans and the factors that can determine adjustments, such as the costs of the funds, operating expenses, and provisions for loan losses.

Until 1987, the System institutions accounted for the largest single source of funding for agriculture. However, since then commercial banks have become the leader in agricultural lending. To have an idea it is suffice to say that nowadays System institutions present a farm debt market share of about 26% and the commercial banks of around 41%. The remaining 33% are attended by other money sources as Farm Service Agency (discussed in the next topic and that represents about 5% of total loans), life insurance companies (6% of the total loans amount), and input suppliers and integrators (that accounts for 22%).

3.3 GOVERNMENT SUPPORT

3.3.1 SUPPORT TO RESEARCH

The American government provides financial support to several private universities all over the country. These resources are supposed to be used in the development of techniques connected to the crops grown in the region around of each university, especially those related to water and soil conservation.

3.3.2 SUPPORT TO CREDIT

From the already mentioned we can derive that loans devoted to American farmers (procedures of crops and investments) are in the majority of the

cases commercial credits, provided by either System institutions or any other financial institutions without any kind of government subsidies.

Yet, in order to help farmers who are temporarily unable to obtain private, commercial credit, the American government's Farm Service Agency (FSA)[10] makes use of two loan programs:

a) GUARANTEED LOANS

Under the Guaranteed Loan Program FSA guarantees some kinds of loans -- for up to 95 percent of its principal amount, depending on the risk involved in the loan-- made by conventional agricultural lenders.

These loans only can be made either to purchase farmland, construct or repair buildings and other fixtures, develop farmland to promote soil and water conservation and to refinance debt (farm ownership loans), or to purchase items needed for a successful farm operation, including livestock, farm equipment, feed, seed, fuel, farm chemicals, repairs, insurance, etc (operating loans).

To be eligible for guarantees, loans have to satisfy certain qualifying criteria and lenders must continue to be in charge of servicing the borrower`s account during the term of the loans. The maximum loan size that FCA can guarantee is U$ 731.000, amount adjusted annually based on inflation.

[10] FSA: Farm Credit Agency is an agency that belongs to the United States Department of Agriculture.

According to the rules of the program, if the borrower has caused FSA a loss by receiving debt forgiveness on more than 3 times or if he is delinquent on any Federal debt (beyond other qualifying features such as to have a satisfactory credit history, demonstrate repayment ability and provide sufficient security), the producer can not apply for these types of loans.

Payment terms and interest rates in guaranteed loans are negotiated between the lender and the borrower, of which the limit is equal to the rate charged the lender's average farm customer. Generally, repayments terms vary according to the type of loan made, the quantity and quality of the collateral securing the loan, and the producer's ability to repay. On the average, operating loans are repaid within 7 years and farm ownership loans cannot exceed 40 years.

To receive the FSA's guarantees, the loans must be adequately secured as a first lien on crops to be produced and on livestock and equipment purchased or refinanced. A lien also can be demanded on certain other chattel and real estate property. In the case of farm ownership loans, only real estate or a combination of real estate and chattel are accepted.

A special characteristic of guaranteed loans is that it represents assets that can be resold by the lenders to an interested party, such as an investor willing to make safe investments with a reasonable return (in this case the safety is represented by the government guarantee against default). Even

having sold the guarantee portion of the loan the original lender retains the loan servicing responsibilities.

In fact it works as a secondary market for FSA guaranteed loans. With the alternative of selling the guaranteed portion of loans in the secondary market, the lenders can: 1 - gain more liquidity on their assets (the funds can be freed for additional lending or investing activities); 2 - reduce their interest rate exposure; and 3 – offer the producer more flexible repayment terms, as well as fixed or reduced interest rates to improve cash flow.

It is important to remember that guaranteed loans enhance the banks lending capabilities, since the guarantee portion of the loan is generally not applied against a bank's lending limit.

b) DIRECT LOANS

Even when a producer is unable to qualify for a guaranteed loan, he can take a direct loan from FSA depending on whether he is eligible or not. Being eligible – having sufficient repayment capacity and enough collateral to fully secure the loans --, the producer receives direct loans from FSA, who also provides borrowers with supervision and credit counseling.

Different than guaranteed loans, direct loans do not have refinancing among their purposes. These are the three main types of direct loans available: Farm Ownership Loans, Operating, and Emergency Loans. Emergency loans cover production and physical losses in counties declared as disaster areas.

For the Ownership and Operating Loans, the maximum loan size is US 200,000 and for Emergency Loans is US 500,000. In each one the repayment term and interest rate vary according to the collateral securing the loan and the applicant's ability to repay.

Generally, operating direct loans are repaid within 7 years and the farm ownership loans terms cannot exceed 40 years. The interest rates for direct loans are periodically adjusted, based on the government's borrowing cost.

Similar to guaranteed loans, direct loans must be adequately secured: first lien on crops to be produced and on livestock and equipment purchased or refinanced with loan funds; beyond this, if it is necessary, lien on other chattel and real estate property or a combination of both.

Apart from the already mentioned, the American government reserves for beginning farmers who cannot qualify for conventional loans a portion of Direct loan funds. To them, three types of loans are available: Farm Ownership Loans, Operating Loans, and Downpayment Farm Ownership Loans.

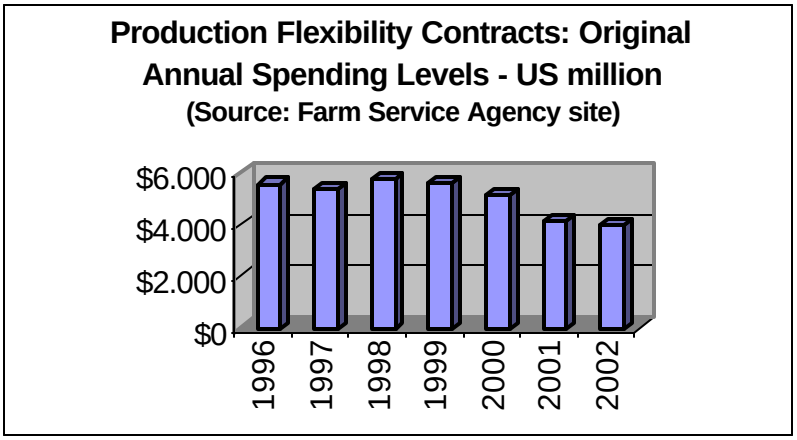
In the last case, the American government finances beginning farmers, under a 10 year-loan term and at a fixed interest rate of 4% a.a., up to 30 % of the purchase price of a farm or a ranch (that is limited to US$ 250,000). The applicant must make a downpayment of at least 10 % of the purchase price. A commercial lender or a private party may provide the

remaining balance. If the commercial lender is an eligible one, the government can guarantee up to a 95% of the loan.

3.3.3 SUPPORT TO PRICES

Based on the changes introduced by the 1996 Farm Act, the American government has carried out a renewed program to support prices of agricultural products.

As already mentioned, the 1996 Fair Act, the effects of which extend through 2002, removed the relation between income support payments and farm prices by providing a seven annual fixed but intended declining production flexibility contract payments (ranging from U$ 5.7 billion to U$ 4.0 billion through 2002, as shown in the graph).



From the total initial allocation (US$ 35,6 billion for the 1996-2002 period), 46.22% was destined to corn, 26.26% to wheat, 11.63% to upland cotton, 8.47% to rice, 5.11% to sorghum, 2.16% to barley, and 0.15% to oats.

Through this system, producers who had participated in the wheat, corn, sorghum, barley, oat, rice and cotton programs in any one of the 5 years prior to 1996, and that agreed in enrolling in a 7-year production flexibility contract payments, receive from the government, annually, direct payments regardless of the level of farm prices – different than what happened under the prior policy whereby deficiency payments were dependent on farm prices.

The amount received by farmers because of these contracts is equal to 85% of its contract acreage times its program yield for that commodity. The per-unit payment rate for each contract is determined annually by dividing the total annual contract payment level for each commodity by the total of all contract farm's program production.

It is important to emphasize that, although the 1996 Fair Act has allotted a fixed amount of funds for each of the 1996-2000 crops, after that year there were additional payments provided by following acts in 1999 and 2000, supplementing considerably the initial provisions. Following, is shown some supplemental provisions devoted to corn, sorghum, barley oats and wheat.

US Cents per Bushel

Production Flexibility Contracts – PFC	CORN	GRAIN SORGUM	BARLEY	OATS	WHEAT
Original Provisions to Payments Rates					
1996	25.1	32.3	33.2	3.3	0.87
1997	48.6	54.4	27.7	3.1	0.63

Production Flexibility Contracts – PFC	CORN	GRAIN SORGUM	BARLEY	OATS	WHEAT
1998	37.7	45.2	28.4	3.1	0.66
1999	36.3	43.5	27.1	3.0	0.64
2000	33.4	40.0	25.1	2.8	0.59
2001	26.0	30.0	18.0	2.0	0.47
2002	25.0	29.0	17.0	2.0	0.46
Supplemental Provisions					
1998					
1999	18.7	22.5	14.1	1.6	0.33
2000	36.3	43.5	27.1	3.0	0.64
	36.3	43.5	27.1	3.0	0.64
Total Provisions					
1996	25.1	32.3	33.2	3.3	0.87
1997	48.6	54.4	27.7	3.1	0.63
1998	56.4	67.7	42.5	4.7	0.99
1999	72.6	87.0	54.2	6.0	1.28
2000	69.7	83.5	52.2	5.8	1.23
2001 *	26.0	30.0	18.0	2.0	0.47
2002 *	25.0	29.0	17.0	2.0	0.46

*Estimate Source: Farm Service Agency site

Having described the most substantial inception of the 1996 Fair Act, regarding price support, it is time to report the major American government price support instrument, that provides operating capital to producers of wheat, feed grains, cotton, peanuts, tobacco, rice, oilseeds, and sugar processors: nonrecourse marketing assistance loans.

Through its Commodity Credit Corporation (CCC), a state owned and operated corporation, the American government handles all money transactions for agricultural price and income support (prior to 1996, CCC also was in charge of maintaining balanced, adequate supplies of agricultural commodities, and correspondent orderly distribution).

By and large, the producer can opt either to get a nonrecourse marketing assistance loan or to participate in the Loan Deficient Program.

In the first case, loan rates are based on a certain percentage (85% in general) of the simple average prices received by producers during the marketing years for the immediate 5 crops, excluding the highest and lowest price. The loan rates also vary among counties, considering where the product is stored and can be adjusted with premiums and discounts, according to the case, to reflect the quality factors of a given quantity placed under loan.

Producers can settle their outstanding loans either in cash until the end of the loan period (9 months in general) or on maturity, by forfeiting to CCC the commodity previously given as collateral.

The loan repayment rate is the lower of: 1) the applicable county loan rate, plus accrued interest and other charges; or 2) the announced loan repayment rate for the respective commodity, that is established based on the previous day's market prices.

If when the loan is repaid the announced loan repayment rate is lesser than the loan principal, the producers realize a marketing loan gain, expressed by the difference between the amount of the applicable loan rate and the announced loan repayment rate for the respective loan. See the following table:

Us Cents per Bushel

Soybean Marketing Loan/ LDP Examples	PRICE SCENARIO 1	2	3
1 – Loan rate	5.26	5.26	5.26
2 – Loan rate, plus accrued interest	5.35	5.35	5.35
3 – Announced loan repayment rate	6.00	5.30	5.00
4 – Loan repayment rate (lower of 2 or 3)	5.35	5.30	5.00
5 – Marketing Loan gain or LDP rate *	0.00	0.00	0.26

5 = 4 –- 1

Source: Farm Agency Service

Having opted for loan deficiency payments, producers receive payments equal to the amount by which the applicable county loan rate exceeds the announced loan repayment rate for the respective commodity times the quantity of product for which the LDP is requested and is otherwise eligible to be placed under loan.

The perception of both Loan Deficiency Payments and marketing loan gains, for all commodities, is annually limited to certain amounts (during the 2000-crop year, the sum of them were subject to up to US$ 75,000 per person). This limitation is separate from the general US$ 40,000 per person maximum for market transition payments (production flexibility contract payments).

It works as a security against the volatility of the market prices.

4.0 A COMPARISON AND COMMENTS ON THE TRENDS

There are great differences between the policies toward the rural sector carried out by both the Brazilian and the American governments. One of them is that the former gives more emphasis on the credit and the latter on the support to commercialization.

Taking apart the enforced financing, the current structure of interest rates on the Brazilian economy prevents private banks from granting loans to the rural sector. As a consequence, nowadays it is worth much more to the financial institutions to prioritize activities that provide low risk and

considerable gains with high interest rates (as applying its availability's in public bonds, currently paying interest rates of about 19% per annum).

To counteract this economic state of affairs, the Brazilian government uses interest rate equalization as a mechanism, through state owned and cooperative banks, to increase the flow of funds to financing the rural sector. Probably in the next years this system will continue to exert an important role in the credit field. On the other hand, as the basic interest rates of the economy start to decrease, the necessary environment to a more effective participation of private banks in financing the rural sector will be naturally created.

Different from Brazil's case, and as an consequence of the further achieved macroeconomic stability, that includes low level of interest rates on the economy as a whole (currently on about 3.5% per annum), granting loans to the agricultural production is considered by the American private financial institutions an opportunity to make money.

Another difference between the countries in this matter is that in general the interest rates charged on agricultural loans are not fixed in the USA; it is variable based on the cost of the money. Although this rule is not good from the point of view of the borrowers, it provides security to the financial institutions diminishing the risk of dealing with this sector of the economy.

Regarding prices support, the American policy seems to have much more influence on market prices. This conclusion derives from the amount of

money annually spent in this field, which, depending on the product, can reach US$ 75,000 per producer. Beyond this, a considerable number of farmers receive up to US$ 40,000 per year as an offset for changes implemented in the 1996 Farm Act.

Similar to what happened in Brazil until 1996, the American producers can settle their outstanding marketing assistance loans by forfeiting to the government the commodity previously given as collateral. In general, this mechanism ends up inhibiting the private process of commercialization, hiding existing inefficiencies and promotes misallocation of resources, since producers are protected from prices regardless of the place of production.

A subtle difference between the American and Brazilian credit policies relies on the guarantee mechanism. That is, in the US, depending on the case, a private agricultural loan can count with government guarantees. In Brazil, law recently prohibited this hypothesis. Instead of guaranteeing loans, in a few cases the Brazilian government concedes credit direct to the beginning farmers.

A great amount of financial transfers from the government to farmers have occurred since the 1996 Fair Act, namely Production Flexibility Contracts. In fact, it has worked to the producers as an additional income out of farm production. Under this mechanism, the US government has annually transferred to farmers sums of money much greater than all the amount of credit and commercial subsidies put together spent by the Brazilian government.

Although some universities still receive supports from the government to develop agricultural research, private enterprises as producers of seeds and farm chemicals have been responsible for considerable technological advances.

Nowadays internal and external debates concerning the Free Trade Area of Americas (FTAA) and the next round under World Trade Organization (WTO) have taking place in the political and economical scenarios. The Brazilian government has stated that those debates must be held including all the aspects connected to agricultural subsidies and non-tariff barriers on agricultural trade.

In its turn, the US government is facing pleas from its farmers to increase the level of subsidies. Although the landmark Farm Act of 1996 had been weaning farmers from subsidies, annual supplementary funds have been passed driving the cost of farm programs to new peaks.

Besides, a new farm bill has been debated in the American Congress. The first proposals demonstrate a bias to increase the level of agricultural subsidies. This internal context makes the American free-trade agenda to be more difficult to keep.

Another point to be considered is that the success of the negotiations on a free trade area in Americas, that for Brazil must include agricultural issues,

will largely depend on the European countries decision make about their levels of rural subsidies.

5.0 SUGGESTIONS OF MEASURES TO BE IMPLEMENTED IN BRAZIL

Although restricted by law to the federal banks and cooperative banks (composed by credit cooperatives), it is appropriate to extend the interest rate equalization mechanism to the private banks.

By means of improving competitiveness among the financial institutions, a decrease in the administrative costs would be expected -- in some cases, those costs represent about 55% of the total expenditure with interest rate

equalization --, generating economies that would be reversed either for funding new agricultural government actions or for composing the efforts toward fiscal deficit control.

As the Brazilian economy becomes more stable (with lesser level of interest rates and diminished necessity for money from the market to refinance its debts), the National Monetary Counsel should authorize commercial banks to create investment funds with the specific intent of channeling money from the financial market to agroindustries, even if it implies some level of interest rate equalization.

This policy, beyond stimulating the internal increased value to agricultural products and enabling gains of external competitiveness, could result in a large range exploitation of processed commodities and non-commodities agricultural products market, either in the internal market or, also, in the international market.

In this regard, the Brazilian farmers already dominate the technology necessary for a low cost agricultural production of a variety of those products. Despite the satisfactory level of chicken, pork, and orange juice industries (that deal with final products that present higher aggregate value), the funnel seems to be concentrated in the post farm production phases of the other products. That is, there is a lack of basic infrastructure to develop internal and achieve external existing markets.

This state of affairs suggests the implementation of policies focused not only directly on farmers but also, and in some cases mainly, to the strength and exploitation of agricultural products processing market.

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