Since agriculture is mainstay of the rural Malaysian economy, its role in poverty alleviation programmes has been very significant. According to Population & Housing Census of Malaysia (2000), 38 per cent of population lives in rural areas, and 36 per cent of the work force in rural areas depends on agriculture for income and employment.

The new areas of land reclaimed by various government agencies over the decades have been provided to poor to help them get out of the poverty trap. In the process of settlement, considerable amount of financial as well as human resources have been spent, and yet the programme has suffered from many shortcomings.

This chapter, therefore, attempts to study rationale for new settlement programmes, role of various institutions in developing new lands, successes as well as new challenges before the development planners. In addition, role of micro-finance as a strategy in helping rural poor to initiate their own income generating programmes is also analysed in this chapter.

Malaysia covers an area of 127,330 square miles, of which 60 per cent is covered by Sabah and Sarawak. Peninsular Malaysia, with 40 per cent of the land and 84 per cent of the population, contains bulk of Malaysia's cultivated land. Of the 9.6 million acres of land under permanent cultivation in 1975, 7.6 million acres were in Peninsular Malaysia and the remaining 2 million acres in Sabah and Sarawak provinces. It is primarily due to this reason that most of the agricultural and rural development activities have been concentrated in the Peninsular Malaysia.

Importance of Agriculture in Poverty Alleviation Programmes

The problem of poverty was originally a rural phenomenon as it was found to be deeply entrenched in the agriculture sector since almost all types of poor were dependent on agriculture for income and employment. Later on, with the mushrooming of urbanisation, urban poverty came to exist along side rural poverty. But the incidence of rural poverty has always been very high compared to urban poverty. For example in 1976, incidence of rural poverty was 50.9 per cent as compared with that of 18.7 per cent in urban areas. Similarly, compared to urban poverty, rate of reduction of rural poverty has been slower. Viewed from this perspective, poverty alleviation policies and programmes have thus remained rural-oriented and agriculture-centric.

Agricultural development over the years has been central to rural poverty alleviation planning. For instance, about 87 per cent of the poor households of Malaysia were rural and nearly 70 per cent of all the poor were employed in the agriculture sector in 1975\(^3\). Policies and programmes for the alleviation of poverty have, therefore, been biased largely towards agricultural growth. Much of the progress made in development of agriculture sector was the result of existing government programmes to help the rural poor mainly through extensive irrigation schemes for rice farmers, the large new land settlement schemes for landless labourers, and a substantial support programme for replanting to replace old and low-yielding rubber trees with high-yielding varieties\(^4\).

Thus, it was premised that development of agriculture would lead to development of rural areas but development of agriculture requires improvement in efficiency, productivity and competitiveness of farming community. All this was to be accomplished by the far-sighted policy of the government to train farmers with modern farming skills rather than giving them welfare-oriented grants. This would avoid their perpetual dependence on the state.

**New Land Settlement Schemes as Strategy for Poverty Alleviation**

One of the important aims of the agricultural development programme has been to accelerate improvement in the use of existing agricultural

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3 Ibid., p.223.
4 Ibid.
land resources. The improvement of yields through irrigation, replanting and better inputs and farming practices, it was considered, would contribute significantly to the attainment of goal of higher incomes of rural poor. In fact, a large number of persons in rural areas are either landless or unable to earn adequate income as labourers or own or cultivate adequate land to earn income that lift them above the poverty line. Underemployment and small size of holdings have been attributed as important causes of poverty in all the rural development schemes. Thus, either rural poor find employment opportunities in other sectors of the economy or reorganise their holdings or cut more trees to clear land for cultivation. The new land settlement programme is an attempt to clear more lands for cultivation.

Since 1960s, the Malaysian government has implemented various development schemes for rural poverty alleviation. Land development together with settlement schemes and in situ development have been the major components of these programmes. The land settlement was basically a programme that emphasised the opening of new lands for agricultural development and settlement schemes. And the in situ development programme concentrated on improving the level of infrastructure of the existing farm lands and villages. In fact, the in situ development programmes have substantially improved the quality of life in rural areas which have benefited everybody including poor. For example, 97 per cent of rural households have access to paved roads, 76 per cent have piped water in their houses, 80 per cent have access to electricity and 94 per cent have access to at least one primary school according to a
study of the World Bank's website (2003).5

Although both the programmes - new land settlement and in situ development - emphasised on the development of rural areas but new land settlement programme especially focussed on alleviation of rural poverty.

**Rationale for New Land Settlements**

In the post-independence Malaysia, policy-makers and planners were attracted by the prospect of exploiting vast areas of virgin land still covered by tropical rain forests. In the process, they devised novel strategies to utilise these large tracts of unalienated forest lands by distributing it among poor in order to help them to improve their income and come out of the poverty trap.

The aims and objectives in implementing new land development and settlement schemes varied from time to time, reflecting the government's responsiveness to changing situations and needs. For instance in 1957, the main objective was to satisfy the pressing demand of additional land for cultivation. However, between 1961 and 1970, most of the programmes were primarily aimed at raising the productivity of the rural low-income groups in agricultural sector. Under the NEP (1971-90) era, new land settlement objectives were tied up to the national

policy which stressed on poverty alleviation by raising income levels together with the process of re-structuring Malaysian society by correcting ethnic economic imbalances. However, the main thrust of the new land settlement programme has been to provide income opportunities to poor farmers by helping them to grow mainly cash crops for export - rubber, palm oil and, later, cocoa - rather than subsistence crops.

New land settlement programmes were also meant to introduce changes in the rural areas by improving the economic and social well being of the rural people including poor. The prime economic objectives have been to increase the income level through the utilisation of land under productive agricultural use with the people's own effort and resourcefulness. The social objectives were to ensure that the poor people develop and form a viable, cohesive as well as progressive community. Although the economic objectives of the programme could be achieved through technical and material change but there is a need for corresponding change in attitudes, thoughts, values, beliefs and behaviour of the poor which can be brought through social change. To paraphrase, integrated development of the poor has been the overall objective of new land settlement programmes. During 1990s, a new approach viz., regional development was initiated for settlement programmes. As a result, the settler's house, schools, road system, community hall, shophouse,

market place, agency's office and other social amenities have been organised in such a way that they encouraged integrated development of the area as well as greater interaction among settlers. Such arrangements facilitated the process of change.

Although land settlement as understood presently has been essentially a post-independence phenomenon; irrigation schemes involving the opening and development of new land had begun at the end of the nineteenth century. This study, however, only examines the settlement programmes as implemented after independence. Another objective of new land settlement schemes was the need to fully utilise the potential of unused land throughout the country. This factor, though important but not so widely proclaimed, was indeed one of the major considerations behind the creation of Federal Land Development Authority (FELDA) in 1956. It was envisaged that FELDA would be able to assist those states having inadequate staff and funds to process their backlog of land applications. Through FELDA, loans and other assistance were channelled from the federal government to the various state governments. However, after 1960, both federal and the state governments set up a number of other agencies to carry out land development and settlement projects as the process became more complicated.

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7 Ibid., p.31.
Land settlement schemes have been implemented in several stages. Initially, the lands were developed by the agency i.e., from clearing jungle to crop planting. In many schemes, apart from a wooden house, other basic facilities such as road, water supply, schools, clinic and community hall were also provided. Subsequently, upon completion of these facilities and services, settlers from various states were selected to settle in the scheme area. In other words, availability of basic facilities helped the poor to lessen their poverty burden considerably.

Each poor settler family has been allotted a house and land holding ranging from 3.2 to 4.9 hectares planted with either rubber or palm oil trees. The settlers continued the cultivation and development with the assistance of development agency. They also received RM150 per month as minimum credit during pre-harvest period as production normally starts from the fourth or fifth year of plantation. All credits including the development cost incurred have to be paid back to the agency and this was done through deduction from their income earned during the production stage. In a sense, land settlement programmes for poor have not been free of cost. These programmes inculcated a sense of entrepreneurship skill among poor to enable them to self-sustain the programme in the long run.

9 Abdullah, n.6, p.30.
10 Ibid.
11 Ibid.
12 Ibid.
Settler selection requirements were that an applicant should be between 21 and 45 years of age, married - preferably with children - and physically fit. Prospective settler must be landless, but have an agricultural background. The eligibility to fulfil these elementary conditions only qualified rural poor to participate in the new land settlement schemes.

Settlers normally worked in teams to maintain and harvest the crop from a group of holdings. Thus, the settler's earnings were a function of both his team's efforts and the productivity of his own plot. Settlers were obliged to use a portion of their earnings to pay back a 15-year loan covering the cost of establishing the project. When the loans were fully paid off, they were given title to the land. However, after 1985, the conditions for land titles changed and the new settlers have been reduced to being just labourers in FELDA's new schemes. In fact, since 1991, FELDA has ceased to be an active land settlement agency and focussed its attention and expertise on the on-going problems such as replacement of crops with better quality seeds, emergence of second generation unwilling to work on the farm.

New land settlement programmes implemented by various public sector agencies such as FELDA, Rubber Industries Smallholders Development Authority (RISDA), Federal Land Consolidation and

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14 Abdullah, n.6, p.30.

15 Ibid.
Rehabilitation Authority (FELCRA) and State Land Development Agencies, besides expanding rural economy and providing new employment opportunities, have contributed significantly towards improving living standards and reducing rural poverty in the country. By 1990, FELDA alone has developed 49.7 per cent of the total 353,300 hectares, of which 88.3 per cent were planted with oil palm, 5.9 per cent with rubber and 1.3 per cent with cocoa. Other agencies developed the remaining 177,551 hectares. Under this programme, 26,100 families were resettled.

**Challenges**

As the availability of new land was becoming more scarce in Peninsular Malaysia and also for environmental reasons, the pace of new land settlement started declining there in the late-1980s. The new land settlement projects thereafter started gathering momentum in Sabah and, to a lesser extent, Sarawak. The country’s new development policy which emphasised on industrialisation and other urban based activities for achieving rapid economic growth, served as disincentive to prospective poor young settlers due to availability of remunerative employment in urban areas. Thus, with the exodus of young in search of better employment opportunities outside the agriculture, the land settlement schemes have been left with an ageing population of workers. In 1990, one-thirds of farm household

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16 Ibid.
17 Ibid.
18 Abdullah, n.6, p.29.
heads were more than 55 years old and two-thirds were more than 46 years\textsuperscript{19}. Between 1980 and 1995, 20 per cent of the country’s rural population migrated to the cities and by 1995, 55 per cent of the country’s population was classified as urban. Most of this migration was driven by the availability of higher-paying employment opportunities outside the agriculture sector\textsuperscript{20}.

In fact, non-availability of workers in rural areas has been a limiting factor to the expansion of land settlement schemes. The continuous decline in the size of the agricultural work force - reflecting a natural progression of the development process - has resulted in a sectoral labour shortage. Due to this shortage, about 300,000 hectares of rubber holdings have remained untapped and 30,000 hectares of oil palm could not be fully harvested according to the National Agricultural Policy 1998 or NAP3. The share of agricultural employment in Malaysia’s total work force declined from 26 per cent in 1990 to 18 percent in 1995\textsuperscript{21}.

Owing to prevailing problems under the new land settlement programmes, various alternatives have been contemplated by the government to alleviate residual of rural poverty. Among these are: i) shifting the strategy of expanding new land hectarage to \textit{in situ} land development (existing alienated land) to increase productivity; ii) introducing

\textsuperscript{19} FAO, n.13, p.171.
\textsuperscript{20} Ibid., p.170.
\textsuperscript{21} Ibid.
integrated farming activities such as livestock, aquaculture and food crop production in oil palm and rubber plantations; and iii) increasing participation of the poor groups in agro-based and other downstream processing activities.

Another challenge in new land settlement programme is the involvement of several departments in the implementation of a project. For example, the Department of Forestry looks into the exploitation of timber before the land is released for settlement purposes. The Bureau of Soils, Land and Mines oversees the alienation of the land, and the Department of Agriculture recommends the crops to be grown. To get a new settlement started, there must exist sufficient cooperation and coordination so that the project can be launched efficiently within the minimum time. Land settlement must be more than just the simple process of putting people on any unoccupied piece of land which is capable of being cultivated by settlers using only unsophisticated farm implements. Because many, if not all, of the settlement agencies do not possess the needed personnel and jurisdiction, they have to depend or call upon the services and good offices of other departments. At times, when it becomes extremely difficult to do so, even the initiation of a settlement scheme is beset with all sorts of difficulties22.

During 1960s and mid-1970s, Malaysia has seen a proliferation of agencies engaged in land settlement programmes. This explained the

22 Bahrin, n.8, p.102.
importance of land settlement as an instrument of national development policy in general and rural poverty alleviation in particular. Malaysia has had a large number of land development projects. Many of these projects have been implemented independently of one another and, until recently, they were not coordinated properly resulting into duplication of work as well as wastage of scarce resources which otherwise were important for poverty alleviation programmes. In 1971, the federal government set up Land Development Coordination Committee with the aim of streamlining and dovetailing all the efforts of land development in the country. The benefits that could have been derived from such a committee were, however, vague and limited. The committee was subsequently dissolved in 1973 and the Ministry of Land Development was created. It may be emphasised here that this Ministry has been responsible only for the various resettlement projects organised and administered by the federal government. Those planned and implemented by the state governments remained outside the Ministry’s jurisdiction. In addition, the government has implemented five regional development projects for poverty alleviation where the development of land resources into agricultural holdings played a dominant role. Although much of the land development has been carried out by existing implementing agencies, yet a share has also been taken by private companies under the aegis of government policy of privatisation. The extensive regional development projects—Jengka, Kesedar, Ketengah, Dara, and Johor Tenggara—are being administered by autonomous corporations.

23 Ibid.
Given the current circumstances, land settlement schemes have no longer been the source of economic growth. Nevertheless, importance of the programme in bringing about a change into planned rural areas [as well as reducing poverty] will continue to attract attention of the policy-makers.

**Poverty among Smallholders**

The agricultural sector of Malaysia comprises three types of landholdings: smallholders, estates, and new settlement schemes. The smallholder sector, which houses majority of rural poor, encompasses about 60 per cent of the agricultural land in Peninsular Malaysia and a somewhat small percentage in Sabah and Sarawak. The largest groups of smallholders are those engaged in the production of rubber, paddy and coconuts and these groups witnessed largest incidence of poverty to the tune of 39.2 per cent, 58.3 per cent and 31.3 per cent respectively (1995). The smallholder sector also continues to experience problems of low productivity and uneconomic size of holdings.

About 30 per cent of the total acreage is in the estates, which has increasingly been planted with oil palm, though rubber is still important. Because oil palm requires considerably less labour per acre than rubber,

24 Abdullah, n.6, p.29.

employment on the estates has fallen as land formerly planted with rubber has been replanted with oil palm. The estates now account for less than a third of total employment in these two crops in Peninsular Malaysia but incidence of poverty among the estate workers still accounted for 39 per cent in 1995. Last but not the least, the new settlement schemes, in which large number of individual poor settlers work under a common management, constitute about 10 per cent of the agricultural acreage of Peninsular Malaysia and produce mostly palm oil and rubber.

One of the important reasons for continuing poverty among rubber smallholders is traditional methods of plantation and low yielding varieties of trees. There is a need to replant rubber trees aged more than 25 years with much higher clones gain compared to the older clones. From 1952 to 2003, a total of 1,489,508 hectares of land have been replanted with 1,068,346 hectares of rubber, 284,341 hectares of oil palm and 136,821 hectares of other crops. It has been estimated that 20,000 hectares of rubber trees will be replanted every year with new clones. The government has set up a special fund to assist the smallholders in the replanting activities. This strategy would surely help to alleviate poverty among smallholders at a faster rate.

**Role of State Agricultural Institutions in Poverty Alleviation**

The need to evolve mechanisms for monitoring and implementing


27 Ibid., pp.37-38.
land and rural development programmes at national level was recognised immediately after the independence. The government created federal institutions with the objective to help state government as well as implement federal government policies and programmes in new land settlement schemes. Three important apex level institutions which came into existence for land settlement programmes were: FELDA in 1956, FELCRA in 1966 and RISDA in 1973. The aims of each institution were basically to encourage the production of export crops, settle unused land with poor rural households and form efficient production units by uniting smallholders. In 1973, the Ministry of Land Development was also set up to effectively coordinate the activities among various land development agencies. These institutional arrangements were made in the context of the New Economic Policy (1971) wherein the state played a pro-active role to help Bumiputra to get out of the poverty trap. A glance at the results of these institutions convinces us that they played an important role in poverty alleviation.

A total of 249,300 hectares of new land was developed by public sector agencies, representing 60 per cent of the target set for land development under the Fourth Malaysia Plan (FMP). Of the total, FELDA developed 104,200 hectares, FELCRA 27,500 hectares, RISDA 9,700 hectares and the State government agencies 107,900 hectares. In terms of cropping pattern, 37 per cent of the area was cultivated with rubber, 54 per cent

28 FAO, n.13, p.166.
29 http://www.pmo.gov.my/RancanganWeb/Rancangan.nsf/
with oil palm, 5.7 per cent with coconut and cocoa and 3.3 per cent with
paddy, sugarcane and coffee\textsuperscript{30}. A total of 15,800 families have been resettled
in various FELDA land schemes while FELCRA resettled 1,840 families in
its schemes, increasing the total number of settlers in FELDA and FELCRA
schemes to 79,900 and 14,200 families, respectively\textsuperscript{31}. A total of RM3,618
million was allocated for land and regional development under the FMP, of
which 62.2 per cent had been expended. The average cost to resettle a
family in FELDA schemes increased from RM37,500 in 1980 to RM51,200 in
1983, due to the remoteness of schemes, increased cost of labour and
general cost increases\textsuperscript{32}.

Not only this, even the efforts of private sector did not lag behind. For
instance, a total of 53,900 hectares of new land was developed by the
private sector, of which 31,300 hectares were planted with oil palm\textsuperscript{33}. This
achievement represented 42 per cent of the FMP target of 128,400 hectares.
The major public sector agencies involved in joint-venture projects with
the private sector were the Pahang Tenggara Regional Development
Authority (DARA), the Johor Tenggara Regional Development Authority
(KEJORA), the Trengganu Tengah Regional Development Authority
(KETENGAH), the South Kelantan Regional Development Authority
(KESEDAR), and the Food Industries of Malaysia (FIMA).

\textsuperscript{30} Ibid.
\textsuperscript{31} Ibid.
\textsuperscript{32} Ibid.
\textsuperscript{33} Ibid.
Land and regional development programmes include new land development, *in-situ* development and land consolidation and rehabilitation. As of 2003, a total of 891,986 hectares of new land have been developed by FELCRA and 137,000 hectares have been developed by the Regional Development Authorities (RDAs)\(^{34}\). As for the *in-situ* development, a total of 1,830,150 hectares of land has been developed benefiting 318,310 participants. As of 2003, FELDA has successfully developed 811,140 hectares of new areas. A total of 667,899 hectares were planted with palm oil, 136,732 hectares with rubber, 4,663 hectares with sugar cane and the balance of 1,846 hectares with other crops\(^{35}\). A typical village covers an area of 42,173 hectares.

**Challenges before Agricultural Institutions**

The frequent departmental changes and the many agencies busy resettling people independently seriously compromised the realisation of national goals. In most instances, the limited number of qualified personnel has to be spread thinly amongst the various organisations, thus impairing the effectiveness of their collective contributions. Since many of these organisations worked independently of each other, unhealthy rivalry has often been created - a development which cannot be advantageous to the nation as a whole. There is a need for interdepartmental cooperation in fulfilling the varied tasks of land settlement which remains fundamental

\(^{34}\) Salleh, n.26, p.37.

\(^{35}\) Ibid.
to the success of the programme\textsuperscript{36}. 

A rationalisation of the functions and responsibilities of various government agencies needs to be undertaken to reduce overlapping of functions and increase the efficiency in using resources. In order for public sector agencies to be more effective in providing advisory and technical services to the target groups, they should be encouraged to work more closely with the relevant organisations representing Bumiputra entrepreneurs and businesses and develop these organisations as an important vehicle for complementing government efforts. The objective will be to enable these organisations play more active role in the development of Bumiputra businesses. Following is a brief description of the functions, problems and challenges of the federal agricultural institutions.

\textbf{Federal Land Development Authority (FELDA)}

When the idea of structured land settlement was first introduced in Peninsular Malaysia in 1956, the government created FELDA, whose main function was giving advice and loans to local authorities directly engaged in land settlement. At the first instance, FELDA had, on its own, established Bilut Valley Land Scheme in Pahang. However, when its overall performance was found to be unsatisfactory, the government abolished all the local development boards and entrusted FELDA with the responsibility

\footnotesize{\textsuperscript{36} Bahrin, n.8, p.106.}
of developing and settling areas of over 1,619 hectares. At the same time, the government felt that the efforts of FELDA alone would not be sufficient to meet the growing demand for land. It, therefore, encouraged and also provided federal loans and grants to various state governments to open up land on their own as well as establish other federal level land development agencies specialising in specific areas.

Federal Land Consolidation and Rehabilitation Authority (FELCRA)

It was launched in 1966 with the task of developing rural sector and assisting the community in contributing towards national economic development, while at the same time helping in improving standard of living of rural poor. However over the years, with dwindling availability of new land for settlement, objectives and activities of FELCRA underwent a change. Beginning 1st September 1997, FELCRA was corporatised and changed its name to FELCRA Berhad. Accordingly, its status also changed from being a Government body to fully owned and incorporated enterprise of the Ministry of Finance. The change to a corporate entity has enabled FELCRA Berhad to restructure its business operations in the light of new objectives. Backed by the experience it gained in estate management and its core activities, FELCRA Berhad diversified the scope of its activities by

37 Ibid.
38 Ibid.
39 For details on FELCRA objectives, activities, etc., see paper circulated on 'Federal Land Consolidation and Rehabilitation Authority' in the International Training Course on Localising the Anti-Poverty Agenda: The Malaysian Experience, Kuala Lumpur, 22 September - 12 October, 2003.
focussing on overseas markets. FELCRA Berhad has been keen in becoming a strong and successful conglomerate, while being committed to a dynamic and profitable rural sector in its balanced operational strategy which provides for profitable ventures and social obligation programmes.

The evolving objectives of FELCRA Berhad also brought about changes in its functions, which among others, included: rehabilitation of unsuccessful state managed schemes; the consolidation of unused government land fringing villages for the purpose of providing additional land to small farmers to enable them to possess economic size land holdings; youth land development programme to develop unused marginal government land to be provided to unemployed rural youths; and in situ development projects.

**Rubber Industry Smallholders Development Authority (RISDA)**

Prior to the establishment of RISDA, Rubber Industry (Replanting) Board existed from 1952 to 1972 whose main functions were to administer the Rubber Industry Replanting Fund (RIRF), to manage and implement schemes under RIRF Ordinance 1952 and plan and implement innovations for smallholder sector. In view of the changing requirements, the Board was abolished and in its place, the government set up RISDA with wider role to play in the development of rubber industry. The main functions assigned to RISDA were: to implement agricultural innovations, implement replanting and new planting for smallholders, modernise the smallholder sector, cooperate with other agencies and obtain and maintain all necessary statistics relating to the development of smallholder sector. However, in
2003, RISDA Act was amended, once again, to meet changing responsibilities.

The total area planted under rubber by smallholders was 1,115,800 hectares and by estates it was 153,300 hectares. Similarly, production of rubber under smallholders was 503,654 metric tonnes and under estates it was 84,813 metric tonnes. Out of the total replanted area of about 1,445,636 hectares from 1952 to 2002, about 1,031,075 hectares was in rubber alone which constituted 72 per cent. Despite such an impressive achievement, RISDA is still beset with a number of problems. The main problem encountered by the authority is low level of income which is forcing smallholders to look for alternate remunerative employment. As a result, the sector is facing labour shortages. Similarly, level of adoption of new technology is very low due to illiteracy and lack of awareness about opportunities, resulting into lower yield. Lastly, the size of holdings require reorganisation to make them more efficient and profitable.

Thus, having discussed the role of agricultural institutions in land settlement programme in Malaysia, we now focus on an innovative institutional mechanism i.e., availability of micro-finance to rural poor to alleviate their poverty.

41 Ibid., p.33.
42 Ibid., p.38.
Micro-finance and Rural Poverty Alleviation

Micro-finance, in a preliminary sense, refers to giving small loans to poor and/or hard core poor at subsidised interest rate. However, over the years, micro-finance has assumed much more broader meaning with a provision of services ranging from delivery of credit, acceptance of savings, insurance to money transfer to poor and low income households and their micro-enterprises. Quite often, the term 'micro-credit' and 'micro-finance' are used interchangeably but they represent the provisions of different and distinct levels of financial services. Micro-finance is the provision of a broad range of financial services to low-income micro-enterprises and poor households. The range of financial services usually includes acceptance of savings and provision of loans. Other products might also include like insurance, leasing and money transfers. However, 'micro-credit' emphasises on the provision of credit to low income households, usually in the form of small loans for micro-enterprises and other income generating activities.

Those who provide micro-finance services generally fall into three sectors: formal, semi-formal and informal. The formal sector is characterised by a high level of regulation and supervision that provides some level of recourse to borrowers and savers. Organisations falling in this sector include banks (commercial, rural, savings, postal, cooperative), development banks (state-owned or private), finance companies, building societies and credit unions, pension funds and insurance companies. Organisations within the semi-formal sector may not be formally regulated but are often licensed and supervised by some form of official government agency. This sector
might include savings and credit cooperatives, credit unions, employee savings funds, village banks, registered self-help groups, and non-government organisations (NGOs). The informal sector is generally characterised by the absence of any form of regulation and supervision. Rotating savings and credit associations, non-registered self-help groups, commercial money lenders, traders and shopkeepers, friends and relatives may be included in this group.

Models of Micro-finance

Among the proliferation of micro-finance institutions (MFIs) in developing and even some developed countries, a number of distinguished models have emerged. The *Grameen Bank* model, first experimented in Bangladesh, has been applied in many countries in a wide variety of settings. The *Grameen* model requires careful targeting of the poor through means tests, usually with a focus on women and intensive field work by staff to motivate and supervise the borrowing groups. Groups normally consist of five members, who guarantee each other's loans. The Amanah Ikhtiar Malaysia (AIM) model is somewhat based on *Grameen* type.

The *Village Bank* is a widely replicated model, found mainly in Latin

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43 Robyn Cornford, "Microcredit,' 'microfinance' or 'access to financial services' What do Pacific people need?", (Brisbane : The Foundation for Development Cooperation), www.fdc.org.au
America and Africa, but with substantially less total outreach than the many *Grameen* Bank replications\(^44\).

Somewhat less structured than village banks (and a good deal less than *Grameen* banks) are *Credit Unions* (CUs). These are democratic, non-profit financial cooperatives owned and controlled by their members\(^45\).

A fourth model, based on ‘self-help’ groups (SHGs), is somewhat similar to the village bank concept, although less structured. Most prominent in India, SHGs have around 20 members who should be relatively homogeneous in terms of income. Their primary principle is the lending of members’ savings but SHGs also seek external funding to supplement internal resources.

In a quite different category from the four models discussed above, each of which has strong voluntary elements involving the action of NGOs or community-based entities, is ‘*rural financial systems approach*’. As practised in Indonesia, this model exhibits a diversity of regulated financial institutions providing rural financial services. These range from a national-

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\(^{44}\) Under Village Bank, a typical implementing agency establishes individual village banks having 30 to 50 members and provides capital (called the ‘external account’) for lending to individual members. Individual loans are repaid at weekly intervals over 16 weeks, at which time the village bank returns the principal with interest to the implementing agency.

\(^{45}\) CUs mobilise savings, provide loans for productive and provident purposes and have membership which are based on some common bond. The membership of CUs is likely to be more heterogeneous than that of *Grameen* banks, although various CUs differ in the extent to which they include poorer and low income households.
level institution with substantial outreach and extensive networks to small, local institutions occupying particular market niches.

**Rationale for Micro-finance**

A rationale for micro-finance is built up on the following aims:

- Integrating agricultural and rural development with downstream processing of farm products and encouraging village industries and rural entrepreneurship to generate additional sources of income; and

- Since the poor are largely engaged in agriculture, micro-finance enables them to diversify and they are encouraged to be involved in modern farm and non-farm or off-farm activities.

It would be worthwhile to undertake a few case studies based on the Malaysian experience in micro-finance.

**Role of Micro-finance in Rural Poverty Alleviation in Malaysia: Case Studies**

Having discussed the meaning, various models and rationale of micro-finance in theoretical perspective, this part of the chapter now analyses the role of micro-finance in alleviating poverty from rural Malaysia.
Micro-finance is not new in Malaysia. Over the years, it has been operated by credit unions, cooperative banks and specialised credit windows of banks. Micro-finance services of financial credit range around RM 10,000 and mostly to finance small businesses, agricultural loans and loans for poverty reduction.

There are a number of NGOs engaged in micro-finance. These include Yayasan Usaha Maju operating in Sabah, Koperasi Kredit Rakyat in Selangor and the most widely known micro-finance institution is Amanah Ikhtiar Malaysia (AIM). Besides, Majlis Amanah Rakyat (MARA), council of trust to the Bumiputra and Credit Guarantee Corporation (CGC) are other institutions to introduce micro-finance services to run micro-enterprises.

Rural credit institutions like Agriculture Bank of Malaysia, Farmers' Organisation Authority, Federal Land Development Authority, and agro-based cooperative societies provide micro-finance in the agriculture sector. However, to understand properly the role of micro-finance in rural areas, two micro-finance institutions viz., Amanah Ikhtiar Malaysia (AIM) and Bank Pertanian Malaysia (BPM) have been discussed below in details.

**Case Study 1: Amanah Ikhtiar Malaysia (AIM)**

Amanah Ikhtiar Malaysia (AIM) or Endeavour Trust of Malaysia is a non-governmental organisation which was established on 17 September 1984. [http://www.banktani.tripod.com/](http://www.banktani.tripod.com/)
1987 to institutionalise an action research project of University Science Malaysia. The action research project titled “Project Ikhtiar” was carried out in the North-West of Selangor. It was sponsored by the Selangor State Government, Islamic Economic Development Foundation (YPEIM) and Asia-Pacific Development Centre (APDC).

The Objectives of AIM

- to give flexible loans to finance income generating activities to the poor households and eventually move them out of poverty trap. It is complementary to the Government’s objective of eradicating poverty amongst the poor households in Malaysia.

- to test whether poor community could get their family out of poverty through small and continuous loans for economic purposes. The Ikhtiar Loan Scheme is an innovative approach in eradicating poverty amongst the rural poor in Malaysia. It has a specialised delivery system focussed exclusively on the very poor, taking credit to their homes and villages with an approach based on self-development and regardless of race, religion or political belief.

- to create, out of the hardcore poor households, highly motivated individuals who are committed to earn an honest living and eventually move out of the poverty trap.

AIM is governed by its board of trustees which meet at least twice a
year and appoint from among themselves a Management Committee to be responsible for the day to day operations. The Management Committee, chaired by Managing Director, meets at least once every quarter.

The strategies pursued by AIM are to provide interest free loans to borrowers to undertake income generating projects. The loans are to be repaid on a weekly basis. Once fully paid, bigger loans are offered. The first loan is normally restricted to RM1,000 up to a maximum of RM4,000 for successive loan. Successful borrowers could apply for a much bigger loans of RM5,000 or even up to RM10,000\textsuperscript{47}.

Following the model of the \textit{Grameen} Bank, poor borrowers formed themselves into groups of five who, in turn, guarantee each other's loans. They undergo a one week compulsory training of one hour per day to understand their rights and obligations in order to ensure good repayment.

\textbf{Strategic Considerations of AIM}

\textit{Exclusive Focus on the Very Poor}: An exclusive focus on the very poor rural dweller is necessary in order to get the right target and achieve maximum impact, of course with limited amount of resources. AIM uses a special means test to identify the eligibility of poor with the help of field staff to determine all major sources of household income and its amount. It is a very important and rigorous task in order to prevent leakage to non-

\textsuperscript{47} Ibid.
poor households and to enable AIM to reach poorest of the poor to become a member.

In 1989, there were approximately 100,000 poor rural households in Peninsular Malaysia who lived at or below two-thirds of the poverty line income as defined by the Malaysian Government. To ensure the eligibility of the poor, AIM's field staff would check house structure, family profile, sources of income, assets and ownership of land by filling up the means test form. The households with 30 point house index and income of not more than US $114 per family or US $23 per capita can join AIM and get loan.

*Specialised Delivery System*: In order to deliver credit to the poor households in a mechanism that they understand and could participate and benefit from the loans, AIM applies requirement criteria to ensure that the poor have access to AIM credit programme. These requirements are: i) convenient loan conditions (no collateral, no guarantor, no legal threat or legal action); ii) credit is taken to the door step of very poor; iii) simple procedures, training and test; iv) formation of groups by potential members; v) collective responsibility; vi) small loans and weekly repayment; vii) loans for income generation; viii) close supervision; ix) availability of a subsequent loan; and x) open conduct of all businesses at the centre’s meeting.

Rigorous Practical Staff Training: All staff must have very good understanding of AIM's rules and procedures to enable them to motivate the very poor to join AIM.

Supportive National Policy Framework: AIM has been designed to be politically impartial. This has enabled it to extend loans to the very poor regardless of their political affiliation. This also facilitates very excellent collection of repayment without any political interference.

Even though AIM is not linked to any political party in the government, AIM as a programme which supplements the poverty alleviation efforts in Malaysia, has support of the national government. The State governments have also been supporting AIM with operational grants. The branches and regional offices of AIM, together with government agencies, have been organising programmes and workshops for the members and their families. This smart partnership has benefited many poor households in AIM's overall programmes.

Loan Schemes of AIM

AIM offers the following loan schemes to its members:

Ikhtiar Loan Scheme 1 (Skim Pembiayaan Ikhtiar 1 – SPI 1): It provides

loans to those poor households with average monthly income of not more than RM340 or two-thirds of national poverty line income. Initial loans are for a maximum of RM1,000, increasing gradually to RM2,000, RM3,000, RM4,000 and RM4,900. The loan repayment period is between 50 to 100 weeks.

_Ikhtiar Loan Scheme 2 (Skim pembiayaan Ikhtiar 2 – SPI 2)_ : This scheme provides loans between RM5,000 to RM9,900 to borrowers who have good repayment record of previous two loans and having monthly income not exceeding RM600. The repayment period of the loan is between 50 to 150 weeks.

_Ikhtiar Loan Scheme 3 (Skim Pembiyaan Ikhtiar 3 – SPI 3)_ : This provides loans up to RM10,000 to borrowers with good track record with repayment for at least 2 times (SPI 1) or (SPI 2) and having a monthly income not exceeding RM1,000. The loan could be repaid up to a maximum period of 150 weeks.

**Performance and Achievements of AIM**

As of August 2003, AIM has an outstanding loans balance of about RM130 million. From its inception in 1987, the loan programmes have benefitted more than 120,000 members. The existing members now stand at about 89,000. Based on the figures of 150,000 (two-thirds) of poor
households targeted by AIM, it has successfully made an outreach of about 80 per cent in term of the number of poor households it targeted\textsuperscript{50}.

By August 1997, after a decade in operation, cumulative economic loan disbursement was US $16.98 million to 47,783 poor households in nine states\textsuperscript{51}. AIM’s repayment rate is 99.95 per cent signifying the fact that micro-credit has been bringing about considerable increases in households income which facilitates servicing of loans and making positive impact and changes in the lives of the poor. This also proves that the poor are bankable and have shown their creditworthiness by repaying their loans in full and on time.

A study conducted by Socio-Economic Research Unit (SERU) in 1991 on behalf of the Prime Minister’s Department, Government of Malaysia has confirmed that not only there is evidence of increase in income among members, the findings also showed evidence of positive changes in their self-development. Members had gained confidence, consciousness, responsiveness thereby helping them ensure a better future for their families. The overall positive findings by SERU, together with improvement in the quality of life, assets, savings and positive values clearly demonstrated the effectiveness of AIM’s approach in reducing poverty.

\textsuperscript{50} Ibid.

\textsuperscript{51} http://www.members.ozemail.com
**AIM’s Sources and Uses of Fund**

AIM’s operational costs are borne by borrowers through administrative charges levied on each loan. State governments also give some contribution for operational cost to fulfill their commitment and cooperate with AIM to operate in their respective states.

AIM has obtained its loan capital in the form of a grant from the national government through Islamic Economic Development Foundation (YPEIM). In 1996, national government allocated US $80 million as interest free loan to AIM through YPEIM to be disbursed to AIMS’ members within five years during the Seventh Malaysia Plan (1996-2000). The banks and other financial institutions also extended a soft loan to AIM to be lent to the poor. Their total amount was about US $11.2 million. In short, AIM gets support both from the government and private sector to realise its objective in reaching the poor in Malaysia.

By August 1994, AIM had some 6,100 Grameen groups in operation. Assuming that its procedures to identify the poor were both effective and consistently applied, this is quite impressive coverage of the target population, achieved in seven years. Total loans disbursed amounted to US $14.8 million and, reflecting the relative priorities accorded to savings and credit, total savings were US $1.8 million. Some

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52 Ibid.
28 per cent of lending was for agriculture, 46 per cent for trade, 15 per cent for animal husbandry and 10 per cent for other activities\textsuperscript{54}.

By 1998, however, AIM provided loans to 103,000 individuals and total disbursement went up to RM 328 million (US $86 million at the current exchange rate, considerably more if contemporary exchange rates are applied)\textsuperscript{55}. Some 80 per cent or more of all funds were loaned for economic activities, the remainder for 'social' purposes. AIM’s activities have been directed almost entirely to the alleviation of poverty particularly among poor Malays. AIM was set up with a charter ‘to disburse small loans on reasonable terms exclusively to the very poor households to finance additional income-generating activities’ but for all practical purposes, it has confined its attention to Bumiputras (principally Malays). This is evident from its outreach data rather than from its charter.

\textit{Challenges facing AIM}

Some 60 per cent of AIM’s operational costs between 1989 and 1995 were covered by the Malaysian government grant, while the state governments granted additional support of up to 40 per cent annually\textsuperscript{56}. In consequence, AIM had limited stimulus to strive for self-sufficiency in its early years. Loan capital was provided by central government grants,
supplemented by soft loans from Credit Guarantee Corporation (CGC) and some commercial banks, especially those with majority government shareholdings.

Among other factors, interest rate control may have played some part in keeping commercial banks out of micro-finance. Bank Negara, the central bank of Malaysia, restricted the spread between base and maximum lending rates in the commercial banking system to 4 per cent, less than that would be required to cover the extra costs associated with micro-finance lending. In the case of some loans guaranteed by CGC, the permissible spread was only 2 per cent, reinforcing this effect.

AIM has experienced an increase in defaults since the onset of the Asian Financial Crisis in 1997 with 154 loans in default at the end of March 1998, compared with 77 at the end of March 1997. Nevertheless, repayment rates were still very high, with the on-time repayment rate in March 1998 reported as 99.4 per cent. It was reported that there had been no significant change in operating costs, and while AIM has recently introduced a number of changes including higher interest rates and higher loan sizes, these, of course, predated the Asian Financial Crisis of 1997.

Even before the crisis, the Government was committed to support


58 Ibid.
AIM as an effective tool for poverty reduction. The crisis appeared to have increased this commitment. In March 1998, the Government announced that it would allocate an additional RM100 million to AIM, reflecting the need to protect more vulnerable groups from the adverse effects of Asian Financial Crisis59.

On the other hand, the crisis has made it more difficult for AIM to attract concessional funds from the commercial banks. Prior to the crisis, AIM was negotiating a bank loan of RM20 million at an interest rate of 1 per cent. However, the banks withdrew from these negotiations because of stricter policies adopted as a result of the crisis60.

AIM still depends on support from the government and related agencies for funding. With a fixed administrative charge of 4 per cent, it does not cover its operating costs and could not be sustainable and self-dependent.

AIM should look back its fundamental principles because of the loss of direction. It seems to be focusing on the not-so-poor or non-poor and giving larger loans to better-off borrowers. With the management restructuring after the crisis, it is hoped that AIM will be succeeded by a period of stability and recovery.

59 Ibid.
60 Ibid.
As the number of poor households decreases, due to the efforts made at various level to reduce poverty, the outreach to new members becomes scarce. Potential expansion of growth would be in the states of Sabah and Sarawak which have shown a higher poverty level\textsuperscript{61}.

Citing 'blatant disregard of the fundamental *Grameen* principles', some critiques have drawn the attention to 'leakage [of loans] to the 'not-so-poor' and the 'non-poor'. It is vital for AIM to relay the message that its outreach are those poor who are at the bottom of the two-thirds of the national poverty line income as it has been discovered that due to relaxation on means testing, the less poor and the non-poor have got benefited to become [AIM's] members. Somewhere, screening of the very poor has been ineffective and disorderly and not-so-poor could stand to gain in the process.

To sum up, small loans on reasonable terms to the very poor for financing additional income generating activities can be an effective and efficient way to reduce extreme poverty as AIM has demonstrated in Malaysia. The approach has been well tested and could work well if the personnel are committed and understand its objectives. The government also should give its support but not interfere in its policy-making and day to day operations.

**Case Study 2 : Agricultural Bank of Malaysia (BPM) and Micro-finance**

Bank Pertanian Malaysia (BPM) or Agriculture Bank of Malaysia was

\textsuperscript{61} Ahmed, n.49.
established on 1 September 1969 by an Act of Parliament (No. 9/69) and it commenced its operations in 1970\(^{62}\). As a statutory body, the bank is responsible for organising, providing, supervising and coordinating credit facilities for agriculture sector in Malaysia. BPM's history is closely linked to the implementation of the MUDA Irrigation Project; a project to address the irrigation needs of the double cropping paddy areas in the states of Kedah and Perlis. The World Bank, sole financier of this project, in its early stage, had identified the inadequacy of short-term production credit for small and poor farmers as a constraint to the success of the project. Accordingly, a special credit scheme was formulated to overcome this problem. This resulted in the establishment of BPM as a development finance institution specialising in providing credit facilities for the agricultural sector especially to small and poor farmers.

BPM's objectives, as stated in the Bank Pertanian Malaysia Act 1969, are to:

- promote sound agricultural development in Malaysia or in any part thereof;

- coordinate and supervise the grant of credit from public funds for agricultural purposes by various persons and bodies of persons whether corporate or incorporated;

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\(^{62}\) For details on Agriculture Bank of Malaysia, visit http://www.bpm.com.my/
• provide loans, advances and other credit facilities for the development of agriculture including production and marketing; and

• mobilise savings with specific regard to agriculture sector and in furtherance of this objective, to accept savings and term deposits.

**Recent Micro-credit Schemes of BPM**

BPM has launched its Micro Credit Scheme (Pembiayaan Kredit Mikro) on 3 June 2003 after the announcement of the economic package by the Prime Minister on 21 May 2003. The scheme started with an initial capital injection of RM200 million from the government and will be increased to RM500 million when the fund for the scheme has been finally raised.  

The scheme has been offered to small entrepreneurs in agriculture related projects in production, processing and marketing. Loan size is up to a maximum of RM20,000 with an interest rate of 4 per cent per annum and loan period of not more than four years. Up to October 2003, RM188.6 million was disbursed to the borrowers with a loan balance of RM174.1 million. It is too early to measure the performance of the scheme, although the collection rate to date is about 92 per cent.

63 Ahmed, n.49.
64 Ibid.
65 Ibid.
Critical Issues for BPM

- The extension of loans with low interest rate (4 per cent) will become an issue if the fund is not supported by grant or soft loan from the government. If BPM has to outsource its funding from the market, the government should be willing to come out with the differential margin for BPM to extend loans with low interest rate.

- Implementation of micro-credit will put more burden on BPM in term of operational costs. The scheme will increase credit risks due to its relaxed condition of no collateral/guarantors.

To sum up, agricultural sector has played a very important role in rural poverty alleviation as almost all types of poor have been dependent, directly or indirectly, on agriculture for their livelihood. Under the farm sector, development of vast tracts of virgin land was devised as an income generating strategy to help rural poor. Utilisation of land increased agricultural production notably cash crops like palm oil and rubber which helped to earn foreign exchange. To achieve these objectives, institutional infrastructure in the form of development agencies like FELDA, FELCRA and RISDA was created. These agencies implemented various programmes specifically targeting rural poor.

To further supplement income of poor farmers and/or to help those who were left out of land settlement schemes, government provided, through various agencies, micro-finance to help them to start their own
enterprises. In this context, AIM and BPM played very crucial roles to disbursing funds to the target groups.

The two case studies are a pointer in the direction of giving agriculture sector a pivotal place in the national developmental efforts. However, the coverage of the poor and hard core poor has not been upto the expectation as the system somehow got manipulated to provide loans to not-so-poor or non-poor beneficiaries. This is not an exception in the case of Malaysia but seems to be a bane for many of the developing countries. The difference is only of degree and not of kind among several such countries. Second, agriculture sector showed a dismal performance in the second half of 1990s (1996-00) and majority of the poor and hard core poor are dependent on this sector. It thus becomes of utmost importance to provide a variety of inputs including micro-finance to poor people in Malaysia.