

THE RECENT CHANGES IN RURAL CREDIT MARKET IN RELATION TO PADDY CULTIVATION IN SRI LANKA: FINDINGS OF A FIELD SURVEY

By

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Abstract

The majority of smallholder farmers in Sri Lanka depend on credit to invest in paddy farming which they obtain from three different sources: institutional; semi-institutional and non-institutional. This article examines the recent changes in the credit market for paddy cultivation with special focus on changes in sources of credit and the implications of those changes on smallholder paddy farmer cultivation and income.

The data analysed in this article is derived from a recent study analysing the contribution of micro-credit systems in four locations selected in Anuradhapura District; two from Rajangana major irrigation scheme and the other two from village tank schemes located adjacent to those.

According to the analysis the emerging trends in the rural credit market are; the growing importance of service loans from non-institutional sources such as tractor owners relative to cash loans from institutional sources and money lenders; the emergence of semi-institutional sources like death donation societies as well as pawn brokers as major suppliers of credit. Service loans in the nature of services of tractors have become important due to the rapidly changing cultivating technology and the high cost and the scarcity of labour, and the changing socio-economic systems and values. The emergence and expansion of early mentioned semi-institutional sources is a result of the government and NGOs encouragement and interventions.

The emerging situation in fact has increased the farmers' accessibility to credit at a relatively less transaction cost. But, the level of benefits they accrue is determined by a number of such factors as the location set-up of the area (whether more open or inward), infrastructure facilities (accessible roads) and the number of credit suppliers available etc. To make the farmers in less developed areas accessible to these facilities government intervention by ways of infrastructure development and promotion of credit suppliers is of pivotal significance.

1. Introduction

At present, obtaining credit for paddy farming in Sri Lanka has become an unavoidable phenomenon, consequent upon two major factors - the high cost of production of paddy (Vidanapathirana, 2003, p. 28) and the inability of the majority of the paddy farmers to bear such costs. Application of modern techniques inclusive of inputs such as improved varieties of seeds, chemical fertilizers, weedicides and pesticides, and

the advanced practices such as transplanting, weeding and deep ploughing, and also the purchasing or hiring in of mechanical implements such as tractors, weeders and sprayers make a heavy dent into the finances of the farmers. The reasons that discourage the Sri Lankan paddy farmers from bearing these expenses are low productivity and low income (Dunham & *et. al.* 1997. p5, 25) they derive due to the uneconomic and small size of their paddy lands (according to the 1982 Agricultural Census, about 65 percent of the farmers are cultivating lands, less than 2 acres in extent), high risks associated with drought and floods, complex land tenure systems and price fluctuations of paddy and the high production cost. These smallholder farmers lack funds for investments in the next season once the loan commitments of the current season are settled.

Farmers obtain credit from various sources which can be divided into three major categories as institutional (formal), semi-institutional (semi-formal) and non-institutional (informal). The institutional sources are the banks and financial institutions governed by the financial rules and regulations of the Central Bank of Sri Lanka and subject to its continuous supervision. The semi-formal sources are the agencies established or encouraged by the government institutions or Non Government Organizations involved in savings mobilization and credit facilities. These are free from direct control of the Central Bank rules and regulations, yet operate within a legal and institutional framework. The community organizations involved in savings mobilization and supply of credit also belong to this category, which are known as micro credit institutions. The concept of 'micro-credit' refers to small scale financial services for the promotion of self-employment and income. Normally the micro-credit institutions are involved in social intermediations such as the promotion of small groups and supply of marketing facilities, in addition to their financial intermediations which include savings mobilization and supply of credit (Ledgerwood, 1998, p.1). The private money lenders and others such as friends and relatives who lend money to the farmers could be categorized as non-institutional sources, where most of the credit transactions are done on an oral basis.

2. Objectives

The main objective of this article is to examine the recent changes in the rural credit market in relation to paddy cultivation in Sri Lanka with special focus on changes in sources of credit, the reasons for those changes, and the implications of such changes on smallholder paddy farmers.

3. Methodology

This article is based on the information of a recent study, conducted by the Hector Kobbekaduwa Agrarian Research and Training Institute in Sri Lanka, about the contribution of micro-credit systems in the smallholder farming sector¹. The referenced study was conducted covering both major and minor irrigated areas selected from the Anuaradhapura district in the North Central Province. Accordingly, four study locations were selected; two from the Right Bank of Rajangana Major Settlement Scheme (tract 5 from the head end and tract 12 from the tail end) and two from minor irrigated locations in the Kekirawa Agrarian Services Centre area (Medawewa-Aliyawetunawewa and Keeriyagaswewa Grama Niladhari Divisions). Three study methods were applied to gather data: (i) a questionnaire survey of the farm families involved in paddy cultivation (The survey covered 160 sample families randomly and equally selected from each location). (ii) the Rapid Rural Appraisal conducted to obtain information about micro-credit institutions in the study locations (iii) a literature review on the previous studies, articles and papers on credit.

¹ This study was conducted by the author (See the reference list for details)

4. Capital for Cultivation of Paddy

According to the findings of the sample survey, a great majority of the paddy farmers depend on credit, a factor more apparent in paddy farming. It was observed that paddy farming generated only little surplus, leaving a significant proportion of the farmers with little savings for reinvestment (except one farmer, the rest depended on credit partially or fully for paddy cultivation). For instance, some 61 percent of the sample partially and the remainder entirely depended on credit, for financing paddy cultivation. In the small tank areas, the farmers often found cash for cultivation through sale of cattle. Whereas, in major irrigated locations it came from employments and other sources such as petty trades. As much as 85 percent of the sample households indicated that they obtained cash loans or material loans by way of agricultural inputs for paddy cultivation. Meanwhile, 52 percent of the farmers had mortgaged their gold jewellery. However, mortgaging of land was quite uncommon amongst the sample farmers, and the degree to which it differed from area to area is examined in the latter part of this article.

5. Different Types of Credit

In the farmers' terminology 'credit' refers to borrowings in cash to be paid later in cash or kind with or without interest. They do not consider non-cash borrowings as credit. But, the reality was that in the study locations, borrowings in kind and service are so common, that the farmers are accustomed to obtain various inputs such as fertilizer and chemicals from boutiques to be paid back later in kind or cash. The services of the tractor owners are also obtained by the farmers to prepare their lands or for threshing on an agreement to pay back after harvesting. Harvesting done by the labourers are also on the same basis. Although the farmers do not identify the above transactions as credit, those have to be considered as credit because such borrowings have to be paid back in cash or kind. The early studies on credit in the country have not mentioned these service loans except the loans obtained in kind. Perhaps, those studies might have put them into the category of 'other loans'. But, in the study areas, service loans are so popular not to be ignored. Elsewhere in this article, further details about service loans are discussed. It is stressed here that credit obtained in cash, in kind or as services are taken into account as three types of credit.

Considering the credit obtained for cultivation of paddy in the study area for the cultivation period of 2000/2001 *maha* and 2001 *yala*, it is observed that credit obtained as services, especially for the preparation of lands, have been more prominent than the credit obtained in cash and kind. According to table 1 as much as 52 percent of the loans have been service (farm power) loans, the prominence of which can be seen both in smaller as well as larger irrigation schemes. Of all the loans obtained, 27 percent were material loans while the other 21 percent were the financial loans. Even according to table 2, 32 percent of the loans have been service (farm power) loans, which again amounted to 40 percent under small irrigation systems. The material loans in the study area represented 24 percent, while it was 44 percent for financial loans.

The above statistics indicate that in the rural credit market in relation to paddy cultivation in Sri Lanka, obtaining of services on a loan basis, especially farm power has become a prominent feature. There are a number of reasons for large scale operationalisation of the rural credit market to supply farm power on credit basis. One of the major reasons has been the increasing availability of tractors and other farm machinery which created a competition among their owners to provide services even on credit basis. This is a direct result of the liberal economic as well as other government policies followed during last three decades. In addition to the import

possibilities that prevailed without constraints under the free market economy, the other policies which helped the expansion of the tractor fleet were the government's incentives for farm mechanization (budget speeches in 1997 and 1998), the duty concessions for imported farm machinery and concessional loans for purchase of machinery and equipment.

The drastic increase in the labour cost compared with the cost of the services provided by the owners of farm machinery has been another important reason for the expansion of service loans. With the shortage of labour due to the outflow to the Middle East (Dunham & *et. el.* opsit, p14) and to the other sectors and the younger generation leaving agriculture in view of hard working conditions (Ranaweera, 1998) and low profitability (Dunham & *et. el.* opsit, p 5 & 25) and the supposedly lower social status, the farmers are compelled to obtain services from the tractor owners who provided their services on a credit basis. It is a convenient credit source compared with the bank loans where the farmers have to obtain cash credit to pay for these services.

Table 1: The Percentages of the Number of Credit Obtained by the Sample Families during 2000/2001 *maha* – 2001 *yala*, under Different Types of Credit

Credit Types	Major Irrigations	Minor Irrigations	Total %
Financial loans directly obtained	14	11	13
Financial loans obtained by mortgaging of gold	04	07	05
Financial loans obtained by mortgaging of lands	01	01	01
Financial loans obtained by mortgaging of other goods	01	-	01
Material loans	27	27	27
Service (farm power) loans	51	54	52
Total	100	100	100

Source: Chandrasiri (2005), Rural Credit for Small Farming Sector: Achievements, Failures and Future Prospects

Table 2: The Percentages of the Value of Credit Obtained, by the Sample Families during 2000/2001 *maha*, 2001 *yala*, under Different Types of Credit

Credit Types	Minor Irrigations	Major Irrigations	Total %
Financial loans obtained directly	28	29	28
Financial loans obtained by mortgaging of gold	07	09	08
Financial loans obtained by mortgaging of lands	09	03	07
Financial loans obtained by mortgaging of other goods	02	10	01
Material loans	26	19	24
Service (farm power) loans	29	40	32
Total	100	100	100

Source: Chandrasiri (2005), Rural Credit for Small Farming Sector: Achievements, Failures and Future Prospects

The results of the referenced survey reveal that mortgaging of gold jewellery and lands also prevail, though on a small scale in the rural sector as a mode of borrowing money. During the concerned two cultivation periods, *ie. maha* and *yala* credit obtained in these ways amounted to 5 percent and 1 percent respectively (refer table 1).

Meanwhile amount wise it is 8 percent and 7 percent respectively (refer table 2). Since the recent past, these credit systems have expanded on a large scale, requiring a detailed review.

The observations of this study revealed that credit obtained by mortgaging gold jewellery was not only for cultivation of paddy, but also for other purposes (even to cover the expenses in gaining foreign jobs)-a practice gaining ground among the rural people during the last few years. In addition to the private money lenders, the other sources of credit for this purpose are the government and the private banks and other institutions involved in mortgaging. As mentioned earlier, spread of private banks, financial institutions and pawn brokers due to the liberal economic policies (Central Bank of Sri Lanka, 1998, p. 211), these have paved the path for the emergence of the observed situation. The other reason for the preference to mortgage gold has been that it is the easiest way to find money quickly especially for the poor who have no collaterals requested by the banking and other financial institutions. Hence, the survey observations also revealed that rural farmers tended to purchase gold jewellery with the purpose of pawning. Increasing tendency on the part of the state banks to pursue the pawning to business more vigorously deviating from the traditional cultivation loans, led to an expansion of the loans through pawning. The withdrawal of credit guarantees and re-financing facilities given by the government to the banks for their cultivation loans also contributed to this situation.

Another change in the rural credit market has been the mortgaging paddy fields to obtain loans under new terms and conditions. In the established system of mortgaging, the lender had the access to cultivate the plot of land in question until the borrower redeems the mortgage fully along with the interest. Under the emerging form, the credit taker or the land owner is allowed to continue the cultivation of land, whilst the lender is entitled to obtain a rent on the land, according to a pre-agreed rent in which the borrower supplies a portion of paddy harvest from the land mortgaged. This is continued until the total amount of the loan is paid back. The normal rate of lending is one bushel of paddy per cultivation season for each Rs.1,000 borrowed.

The new form of land mortgaging seems to have been adopted to fall in line with the values of the rural society and the prevailing state of the paddy farming as well. The farmers in the study areas are of the view that usually the mortgagers did not like to reveal that they had mortgaged their lands, because it would imply their insolvency. Under the old system, maintaining secrecy over the mortgage was out of the question and hence the new system seems to be in line with the borrowers' aspirations and the social ethics. There is another plausible explanation for the newly emerging system. For the instance, paddy cultivation has lost its attraction due to reduced profitability (Vidanapathirana, U., 2004, opsit, P. 28). So the lenders are not likely to be interested in taking a risk by involving in cultivation of those lands as they did under the old land mortgaging system. Hence, the new mortgage system appears to have come into existence not only as a way of finding capital to suit the existing values, but also to adapt to the emerging situation in the paddy sector.

6. Sources of Credit and their Changes

In this article, the analysis of the sources of credit is two faceted: with and without service loans. This two-way analysis facilitates the identification of general and special changes that have emerged in the rural credit market in relation to paddy cultivation in the recent past. In the study area there are a large number of credit agencies belonging to institutional (formal), semi-institutional (semi-formal) and non-institutional (non-formal) categories. Of the source from which the sample families have obtained credit by type (cash, kind and services) the non-institutional sources

appear to be more prominent. As data in table 3 reveals, this prominence is manifest both by the number and the amount of loans. Accordingly, the number and the amount of loans obtained from non-institutional sources during the referenced period (2000/2001 *maha*, 2001 *yala*) are percentage-wise 76 and 62 respectively.

The major reason for preference of non-institutional sources of credit in the study areas has been the recent expansion of paddy traders (collectors) and the tractor owners, who provide cash loans and services on credit basis under more flexible and convenient terms. Accordingly, the number and the amount of credit obtained from the tractor owners and the paddy traders have been 25 percent and 19 percent respectively (see table 3 for details). The factors associated with the emergence of the paddy dealers in large numbers in rural areas have been very similar to those associated with the emergence of the tractor owners. The growth in the rural financial market, import facilities, duty concessions and concessionary loans for importing machinery and the vehicles and the infrastructure development including the construction of roads (Central Bank of Sri Lanka, 2000, p7) are some such factors. The traders who purchased or hired lorries using these facilities have been able to purchase paddy on a large scale. The new paddy millers too have followed suit.

A competition is emerging among the paddy collectors within and outside the study area to collect paddy from the study locations. As a strategy, the paddy collectors in the study locations give credit to the neighbouring farmers in advance with the idea of recovering the loan from the payments they have to make, when they purchase the harvest. A considerable number of paddy farmers depend on these loans which are easily obtainable without any transaction cost. As an obligation and for maintaining a good relationship, the loan taker farmers sell their produce to the same loan provider and let them recover the loan from the due payments.

With the increasing role of tractor owners and paddy collectors as credit suppliers for paddy cultivation, another change that has taken place in the rural credit market, is the diminishing role of the private money lenders who had occupied a prominent place in lending. For example, according to the 1996/97 Consumer Finance and Socio-Economic Survey of the Central Bank of Sri Lanka, the contribution of the private money lenders in the rural credit market has been 16 percent and 9 percent respectively regarding the number and the amount of loans given (Central Bank of Sri Lanka, 1996). In accordance with the findings of the present study, by the year 2001/02 their contribution had reduced to 0.4 percent and 0.6 percent respectively regarding the respective aspects. Even according to the data in table 4, which excludes service loans (loans obtained for preparation of lands), the role of private money lenders seems to have drastically dropped. Percentages of their contribution in terms of the number of loans and amounts are 0.8 and 0.9 respectively. This declining role is same in the case of other non-institutional sources of credit such as friends and relatives in the rural credit market. Increased availability of different and more convenient sources of credit (such as supply of services on credit basis) has accounted for this change.

According to data in table 3, the semi-institutional sources are the second most important sources of credit in the study areas accounting for as much as 18 percent in number and 23 percent in amount of credit disbursed during the referenced period. As mentioned earlier, when the credit disbursement is estimated without considering service loans, the percentage of credit provided by semi-institutional sources goes up. Table 4, prepared on that basis reveals that 38 percent of the loans and 30 percent of the amount disbursed are from semi-institutional sources. This increase has registered a drop in the contribution of non-institutional sources. For example,

their contribution has declined from 76 percent to 50 percent regarding the number of loans and from 62 percent to 49 percent regarding the amount disbursed.

Table 3: The Percentages of Number and Amount of Credit obtained by the Sample Farm Families during the period of 2000/2001 *maha* and 2001 *yala* for Cultivation of Paddy (including the loans obtained in cash, kind and services)

Way Obtained	Percentage According to number			Percentage According to amount		
	Major Irrigations	Small Irrigations	Total	Major Irrigations	Small Irrigations	Total
Institutional Loans	4.5	7.6	5.5	15.7	16.2	15.8
Peoples Bank	3.2	3.2	3.2	6.1	8.1	6.7
Bank of Ceylon	0.6	4.4	1.8	1.0	8.1	3.0
Seylan Bank	0.1	0.0	0.1	0.5	0.0	0.3
Hatton National Bank	0.1	0.0	0.1	7.2	0.0	5.2
Rajarata Development Bank	0.3	0.0	0.2	0.7	0.0	0.5
Private Mortgaging Institutions	0.1	0.0	0.1	0.2	0.0	0.1
Semi-Institutional Loans	18.7	16.7	18.1	24.9	16.7	22.6
Cooperative Rural Banks	1.2	0.3	0.9	1.3	0.5	1.1
SANASA	2.0	0.0	1.4	6.2	0.0	4.5
Samurdhi Bank	0.7	2.9	1.4	0.7	5.0	2.0
Death Donation Society	6.3	1.2	4.6	7.7	0.6	5.7
Ritico Society	0.0	1.2	0.4	0.0	1.4	0.4
Govi Jana bank/Yaya						
Demonstration programme	6.9	10.8	8.2	7.4	9.1	7.9
Farmers organization	1.6	0.3	1.2	1.4	0.1	1.1
Non-Institutional Loans	76.8	75.7	76.4	59.4	67.1	61.6
Private Money lender	0.4	0.3	0.4	0.5	0.9	0.6
Traders	21.5	13.7	18.9	22.7	10.4	19.2
Friends	12.4	3.5	9.5	7.0	4.9	6.4
Relatives	1.2	5.3	2.5	2.6	7.5	4.0
Paddy millers	0.7	0.3	0.6	0.7	0.2	0.5
Tractor owners	37.2	48.8	41.0	19.6	37.8	24.8
Villagers/land owners	3.5	3.8	3.6	6.3	5.4	6.0
Total	100	100	100	100	100	100

Source: Chandrasiri (2005), Rural Credit for Small Farming Sector: Achievements, Failures and Future Prospects.

A number of factors seem to influence the observed prominence of semi-institutional or micro-credit institutions as a way of obtaining credit for paddy cultivation. Firstly, the expansion of micro-credit systems including the Govi Jana Bank, the Samurdhi Bank and the SANASA in savings mobilization and credit as a result of various efforts taken by the government institutions and NGOs' to promote them. Secondly, the involvement of community organizations like the Death Donation Societies to provide credit for paddy cultivation, which was unusual in the past. According to table 3, out of all the credit disbursements, 5 percent in number and 6 percent in amount have been from Death Donation Societies. In table 4, the relevant figures are 10 percent and 8 percent respectively.

An increased involvement of the Death Donation Societies in the promotion of savings and credit can be seen in the locations selected from Rajangana Major Irrigation and Settlement Project. There were two Death Donation Societies engaged in welfare activities also, in each of the two study locations selected from the Rajangana Scheme. All of these societies are involved in providing credit. Meanwhile, some have operated specific loan schemes for paddy cultivation although the amount released is hardly adequate. For example, credit amounting to Rs.10,000 and Rs.5,000 could be obtained respectively for this purpose from channel 2 and channel 1 Death Donation Societies in track 12. During the reference period (from 2000/2002 *maha* - 2001 *yala*), the former society had disbursed Rs. 304,000 among 78 farmers for paddy cultivation. Further, the latter one had distributed Rs.310,000 among 62 farmers. This is an important trend in the history of agricultural credit in Sri Lanka.

According to the present study, the role played by the conventional banks in the rural credit market has grown less in significance eg. as revealed in table 3, only 6 percent in number and 16 percent in amount of the loans for paddy cultivation have been from these sources. But according to table 4, where the calculations exclude the service loans, the contribution of conventional banks goes up in importance. The major reason for the declining trend of institutional loans has been the farmers' tendency to increasingly depend on semi-institutional and non-institutional sources for their credit requirements mainly because of the flexibility in those institutions in granting credit in contrast to the tedious procedural process of the banking institutions. The reluctance on the part of the banks to grant loans especially for risky unattractive profit making ventures like small holder paddy farming has also discouraged the farmers. This tendency is more observable with the recent government policies such as withdrawal of credit guarantee and the re-finance facilities and writing off of defaulted loans compelling the banks to bear a part of the loss. So the banks are more inclined towards pawning loans rather than traditional cultivation loans. Even in instances where the bank grants loans, the amount is not quite enough for the small farmers to meet the increasing costs of cultivation.

7. Implications of the Emerging Credit Market on the Smallholder Farmers

This section discusses the implications of the changes in the rural credit market on the smallholder paddy farmers. The implications arising out of the structural changes of the rural credit market with the expansion of the non-institutional sources and the consequent emergence of a new type of credit suppliers, as paddy collectors and tractor owners who provide their service on a credit basis and also the expansion of some other credit sources as mortgaging of gold and land come under review here.

The aforesaid structural changes have been an offshoot of liberal economic policies of the post 1977 period and some other state policies such as provision of concessionary loans to purchase farm equipment. for encouraging the smallholder farmers towards farm mechanization. These policies have provided a better environment for the emergence of a large number of varied financial and other institutions and also service suppliers and individuals (tractor owners and paddy purchasers, lorry owners etc.), even in rural areas, who provide credit competitively on a more flexible basis. This competitive environment with diverse sources of credit appears to have been advantageous for the poor farmers, in general, who have no collateral. For example under track 5, one of the study locations of the referenced credit study, there are many financial institutions including the Bank of Ceylon and the People's Bank within very close proximity to each other in addition to the micro-credit institutions within the location (see table 5 for details about micro-credit institutions within the study areas). So the paddy farmers at that study location have many sources of credit to which they can gain access depending on their choice.

Table 4: The percentages of Number and Amount of Credit obtained by the Sample Farm Families during the Period of 2000/2001 *maha* and 2001 *yala* (including the loans obtained in cash and kind only)

Way Obtained	Percentage According to number			Percentage According to amount		
	Major Irrigations	Small Irrigations	Total	Major Irrigations	Small Irrigations	Total
Institutional Loans	9.3	16.7	11.6	19.7	26.1	21.2
Peoples Bank	6.6	7.1	6.7	7.7	13.1	8.9
Bank of Ceylon	1.2	0.0	3.9	1.3	13.0	4.1
Seylan Bank	0.3	0.0	0.2	0.6	0.0	0.4
Hatton National Bank	0.3	0.0	0.2	9.0	0.0	6.9
Rajarata Development Bank	0.6	0.0	0.4	0.9	0.0	0.7
Private Mortgaging Institutions	0.3	0.0	0.2	0.2	0.0	0.2
Semi-Institutional Loans	38.9	36.5	38.2	31.2	26.9	30.2
Cooperative Rural Banks	2.4	0.6	1.8	1.7	0.8	1.5
SANASA	4.2	0.0	2.9	7.8	0.0	6.0
Samurdhi Bank	1.5	6.4	3.1	0.9	8.1	2.6
Death Donation Society	13.2	2.6	9.8	9.7	1.0	7.7
Ritico Society	0.0	2.6	0.8	0.0	2.2	0.5
Govi Jana bank/Yaya						
Demonstration programme	14.4	23.7	17.3	9.3	9.1	10.6
Farmers organization	3.3	0.6	2.4	1.8	0.1	1.4
Non-Institutional Loans	51.8	46.8	50.2	49.1	47.0	48.6
Private Money lender	0.9	0.6	0.8	0.7	1.5	0.9
Traders	43.4	30.1	39.2	28.5	16.7	25.7
Friends	6.0	4.5	5.5	8.8	8.0	8.6
Relatives	1.5	10.3	4.3	3.3	12.1	5.3
Villagers/land owners	0.0	1.3	0.4	7.9	8.7	8.1
Total	100	100	100	100	100	100

Source: Chandrasiri (2005), Rural Credit for Small Farming Sector: Achievements, Failures and Future Prospects

However, such facilities differ in track 12, the other study location in the same Irrigated Settlement Scheme. Unlike track 5, located at the head end of the scheme, Track 12 is located at the tail end, and also 8 miles away from the track 5. track 12 is located in an interior area and serviced with backward infrastructure facilities and no popular financial institutions are available within or nearby the area. Even the micro-credit institutions available are only a few compared with those in track 5, restricting the emergence of a competitive atmosphere. So the benefits of those to the poor leave much to be desired.

The institutions and suppliers of credit were fewer and the competition among those was lesser in the areas selected for this study representing the small tanks. The interior location, poor transport and other infrastructure facilities and comparatively weaker economic condition of the people who have water only for one season have brought about this situation. For example, Keeriyagaswewa is located 10 miles off Kekirawa town and only a very few credit suppliers are available there. To obtain credit from non-institutional sources, the farmers had to visit Ganewalpola town, 6 miles away from their village. So the benefits emerging from the expansion of non-institutional credit sources and the competition among them seem to have a bearing

Table 5: Micro-Credit Institutions in the Study Areas

Study Location	Micro-Credit Institutions
Rajanganaya: Track 5	i. Randenigama SANASA Society ii. SANASA Society in track 5 iii. Tissapura Farmer Organization iv. BOP 715/2, Lift Irrigation System Farmer Organization v. Tissapura Annoniyadara Sangamaya vi. Sadasarana Welfare Society vii. Rajanganaya Govijana Bankuwa viii. Rajanganaya 5th mile post Samurdhi Banku Sangamaya ix. Rural Bank of the Saliyapura Multi Purpose Co-operative Society
Rajanganaya: Track 12	i. SARVODAYA Society in track 12 ii. Farmer Organization in track 12 iii. Death Donation Society under Channel one in track 12 iv. Eksith Avamangalyadara Samithiya under channel Two in track 12 v. Angamuwa Samurdhi Banku Sangamaya
Kekirawa: Medawewa Aliyawetunawewa	i. Aliyawetunawewa Govi Sanvidanaya ii. Medawewa Govi Sanvidanaya iii. Eksath Subasadaka Sangamaya iv. Olombewa Samurdhi Banku Sangamaya v. Kekirawa Govijana Bankuwa
Kekirawa: Keeriyagaswewa	i. Ekamuthu Givisanvidanaya in Kaluebbe ii. Ganewalpola Samurdhi Banku Sangamaya iii. Manawa Sampath Prajamula Sanvidanaya of the Ritico Foundation

Source: Chandrasiri (2005), Rural Credit for Small Farming Sector: Achievements, Failures and Future Prospects

on the nature of the location (whether the area is isolated or not, availability of infrastructure facilities like roads and the economic condition of the people). This will be further examined under each credit system or source.

The paddy collectors as well as the tractor owners emerged as new business initiators under an environment of liberal economic and other policies of the government, competing when each other for their survival and providing some of the credit and services even without interest, and also sans any transaction cost. However, this seems to have favourably benefited the smallholding sector paddy farmers although their competition and effect differ depending on the area. For example, compared with other locations, the farmers in track 5 of the Rajangana Right Bank, where better infrastructure facilities and more paddy collectors are available with stiff competition among them to collect paddy and supply credit, the poor farmers receive more advantages in obtaining credit from them. From the paddy collectors' perspective, the objective of supplying interest-free credit is to obtain paddy from the loan takers. Another special feature of this system is that the credit suppliers do not force the creditors to sell their paddy to the farmer alone. The credit takers may sell the produce elsewhere and repay the loans. However, this does not happen usually

because the traders who advance the loans also pay the market price for the paddy. In addition, sale of the farmer's produce to another party would result in a breakdown of the close relationship between the two parties which again will create difficulties in obtaining credit for the ensuing season. This situation indicates that although more business ventures are initiated, the opportunities for viably pursuing them in the rural environment are limited. Other interesting observation is that rural markets still operate on personal trust than on legal obligations.

Concerning the same credit source (paddy collector lenders), its operation in some areas like track 12 as well as in areas under minor tanks where there are less facilities and small number of traders to collect paddy with no competition among them was some what different from what was explained earlier. In those places for the credit obtained from the paddy collectors/traders, the farmers had to pay an interest changing from 60 percent to 84 percent per year. In addition, the farmers had to agree to sell their produce to the paddy collectors who provided them credit. The price given for their produce was sometimes 25% lesser than the market price. So a comparison of the operation of this credit system in different areas makes it clear that it is unfavourable, to the farmers in areas with lesser facilities, in terms of interest, conditions and the price paid for their paddy. However, it is still beneficial to the farmers when compared with some other credit systems such as traditional money lenders who provide credit at an annual interest rate that varies from 60 percent to 180 percent.

Some of the similar conditions could be observed with the tractor owners who prepare paddy lands on a credit basis. The tractor owners who provide their services on loan basis under a competitive environment do not charge an interest or any other amount other than the charge of Rs.1,400 per acre. This is more prevalent in track 5 where there was a stiffer competition among the tractor owners to supply their service just in the same way the paddy collectors try to collect paddy. There the farmers gain more benefits as no interest is charged. The situation is the opposite in interior locations where such competition does not exist.

Normally, the cost of fuel is borne by the farmer under the above system, and is deducted from the tractor charge in track 5. But this does not happen in track 12 and in other locations selected for the study. In the areas under small tanks, in addition to the above charges, tractor owners insist on the payment of their charge in kind with paddy. As explained above, the replacement of the traditional money lenders in the rural credit market by the paddy collectors and the tractor owners has been a favourable change, so far as the smallholding sector paddy farmers are concerned. The paddy collectors and the tractor owners are fairer for the smallholder farmers than the traditional money lenders who were rather hard on them, by charging higher interest rates (changing from 60 percent to 180 percent per annum) and presenting unfair conditions.

Increasing popularity of pawning gold jewellery is another change in the rural credit market. The pawning (of gold jewellery) is done through state and private banks which expanded after 1977 and also individuals are involved as pawn brokers. As revealed by the present study, credit institutions charge an annual interest ranging from 30 percent to 36 percent, lesser than that of the private pawn brokers whose interest is above 84 percent. The farmers in track 5 under the Right Bank of the Rajangana Scheme who are near a town, patronize the banks there in pawning their gold jewellery at a low interest rate. But, the farmers in track 12 under the same scheme and small tank areas selected for the referenced study get their credit requirements by paying a higher interest for their mortgages. A considerable number of farmers in these study locations seek the services of banks for their credit on mortgages.

In instances of mortgaging of paddy lands under the new credit system observed in the study, one bushel of paddy per cultivation season for each Rs.1,000 obtained under mortgage agreement is given to the credit supplier. In Rajangana, two bushels of paddy for every Rs. 1,000 borrowed have to be given per year as the scheme has enough water to cultivate two seasons in an year. At the time the relevant data was collected, the farm gate price of one kg. of paddy was Rs. 12. Accordingly, the borrower pays an annual interest of about 48 percent, for the money borrowed, which is very high. The interest rate applied seems to differ from place to place. Especially in the interior areas with not enough sources to obtain credit, the amount paid as interest goes up to 1/3 of the harvest per season, per acre for borrowing Rs. 30,000 for an acre of paddy land. The amount of the loan changes according to the productivity of the paddy land. On the condition of paying a bushel of paddy for every Rs.1,000 obtained, 30 bushels per acre per season have to be paid for a loan of Rs. 30,000. But, on the condition of paying 1/3 of the harvest per acre per season amount goes up to about 33 bushels in the areas of Rajangana where the average production per acre is about 100 bushels or higher. Under this transaction, the farmer is the loser. His loss is more when the production goes up. So this system of mortgaging will discourage the farmer from increasing the yield on his land worsening his socio-economic standing.

8. Conclusion

In the recent past, a lot of changes have taken place in the rural credit market for paddy production. Among those changes, the major ones are; an increase in pawning gold jewellery, expansion of mortgaging paddy lands under a new system, the increase in the percentage of service loans in the rural credit market due to the increased involvement of the tractor owners to prepare paddy lands on credit, in a situation of shortage of labour, the paddy collectors becoming prominent among credit givers due to the fact that they give credit on relatively fairer terms and conditions, community organizations like the Death Donation Societies offering credit and a drop in the dominant role played by the traditional money lenders in the rural credit market. These changes have happened in an environment where the income of paddy farming is declining whereas necessary policy support and facilities for the emergence of various types of new credit supplying institutions and entrepreneurs have taken place under the liberal economic policies.

With the expansion of different sources of credit and the high completion among those to provide various services and credit, a favourable situation has dawned for the smallholding sector paddy farmers enabling them to obtain credit under more concessional terms, but these benefits are more enjoyed by the farmers in areas with more facilities, such as better infrastructures and more credit suppliers etc. The same sources of credit are operating with differing terms and conditions in the interior areas with fewer facilities, making the conditions less favourable for the borrower. Therefore, in order to increase the access to benefits of the liberal economy in the rural credit market for the farmers in the backward areas, the government could intervene through developing infrastructures and promoting more credit institutions.

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