
Analysis of Farm Credit Disbursed by State Banks in Ampara District, Sri Lanka

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Abstract

Credit is the precursor for investment and modernization of production, whilst also helping to create rural employment opportunities. The objective of the study is to analyze credit disbursed by state banks for rural development, the rate of defaults by borrowers and factors affecting loan repayments. Seventy five respondents who had obtained loans from the Bank of Ceylon and Peoples Bank were randomly selected from the Ninthavur DS area in the Ampara district. They were interviewed using a pre-tested structured questionnaire. Majority of the borrowers were small-scale farmers (92%), while the rest were involved in other occupations. Credit obtained was used for investment purpose (56%) and for cultivation purposes (38.7%). Almost 34.67% of borrowers from the banks were loan defaulters, who differed from non-defaulters in terms of lower age, educational levels and farm income. It was also found that defaulters had a significantly higher amount of indebtedness compared to non-defaulters. A regression analysis showed that amount of outstanding loans was significantly affected by the amount of loan granted, crop yields, other indebtedness and annual income. State banks should improve their services to clients to access credit easily and look for the socio-economic characteristics that significantly influence loan repayment by borrowers before granting loans to farmers to reduce the incidence of loan delinquencies or credit risk.

Key words: farm credit, agriculture, state banks, borrowers, repayment.

Introduction

Credit disbursed by bank to the agricultural sector on the increase of rural income and gross cover in the agricultural and related sectors, will be felt on condition if credit resources are used for renovation and modernization of fixed assets used in agriculture. Efficient use of credit resources promotes the development of agriculture and alternative rural entrepreneurship, increase rural population living standards and accelerates rural economic growth (www.cbsl.gov.lk).

Agricultural lending involves giving out credit (in cash and kind) to small-scale farmers for the purpose of farming. There is no doubt about the crucial roles of credit in economic development. Agricultural household models suggest that farm credit is not only necessitated by the limitations of self-finance, but also by uncertainty pertaining to the level of output and the time lag between inputs and output.

Banks have limited amount of funds to grant credit to rural population according to their capital requirement, security value and their indebtedness. Farmers have limited capital and resources and have to make choices

about how this credit should be utilized. Some farmers may not be used these credit mainly for agricultural purpose and they are utilizing that for any other purposes. The amount of loan disbursed to the agricultural sector has recently increased in Sri Lanka. Farmers and rural entrepreneurs increasingly use credit to develop their economic activities. Bank loans have ensured or promoted the development of farms, the owners of which have been able to use credit efficiently but in general the relatively small amount of credit has not significantly influenced the development of the rural sector. There are state banks in Sri Lanka and rural communities/farmers can obtain credit from those banks under several schemes for several purposes. This research is based on the state banks disbursing credit to rural people in the Nintavur DS area of Ampara District.

Materials and Methods

The study involved the selection of respondents who had taken credit from State banks (Peoples Bank and Bank of Ceylon) in Nintavur DS. Using a sampling frame consisting of borrowers from the two state banks, seventy five respondents were randomly selected from the Ninthavur DS area in the Ampara

district. They were interviewed using a pre-tested structured questionnaire. The selected respondents were later segregated into two groups- loan defaulters and non-defaulters for further analysis. Most of the information pertaining to this study was collected from primary and secondary sources. Analysis consisted of summarizing the data collected and a linear regression was done to identify factors affecting loan repayments by defaulters.

For defaulted borrowers the model specified used was as follows;

$$Y = f(X_1, X_2, X_3, X_4, X_5, \dots, X_n)$$

Where: Y = Dependent Variable. (respondent's outstanding amount of bank loan to repay).

$X_1, X_2, X_3, X_4, X_5, \dots, X_n$ = Independent variables.

Results and Discussion

Majority of the borrowers were small-scale farmers (92%). Credit obtained was used for investment purpose (56%) and for cultivation purposes (38.7%). The results showed that about 34.67% of borrowers were loan defaulters, which was higher (36.3%) among borrowers of Bank of Ceylon. The loan defaulters varied from non-defaulters in terms of age, educational levels and farm income received. Land ownership was higher among non-defaulters (85.7%), while leased land use was 34.6% among defaulters.

The amount of credit granted was reported to be insufficient for about 26.7% of the borrowers, who cited high cost of production as the major reason. The major uses of the loan taken by borrowers were for cultivation (38.7%), investment (56%) and consumption (5.3%).

About 54.7% of borrowers faced problems in accessing credit and 29.3% of borrowers dissatisfied with the services provided by the state banks, stating that there were delays in loan disbursement (27.3%), high interest rates (22.7%), security requirements (40.9%) and legal procedures (9.1%). In a comparative study of formal and informal loans in the Kurunegala District, Gunawardena (1981) found that loan transaction costs for borrowers from banks were considerably higher than for customers of moneylenders and traders, but also that formal lenders fail to provide sufficient services.

The results of a linear regression found that crop yield, amount of loan granted, other indebtedness and total annual farm income significantly affected loan repayments (outstanding loan balances).

Balogun and Alimi (1988) identified the major causes of loan default as loan shortages, delay in time of loan delivery, poor supervision, and non profitability of farm enterprises. Also Hoque (2004); Gupta (1990); and Sinkey and Greenwalt (1991) found that loan default occurs when borrowers are not able and/or willing to repay loans.

The study found that most of the loans taken were used for cultivation and investment purposes. The presence of loan defaulters was a common feature among the state banks analysed. It was observed that there were variations in socio-economic traits between loan defaulters and non-defaulters. Insufficiency of credit provided by state banks was cited by borrowers, thus not meeting the needs for production activities. Access to credit was another issue reported and dissatisfaction with services provided by state banks

Table 1: Results of Regression Analysis- Factors affecting loan repayments

Variables	Coefficients		t value
	B	Std. Error	
Constant	-7160.75	13111.26	-0.54
Crop Yield-Paddy (Kg/acre)	11.19	3.11	3.61***
Amount of Loan taken (Rs/Borrower)	0.50	0.09	5.21***
Other Indebtedness (Rs/Borrower)	-0.32	0.12	-2.73***
Annual Farm Income (Rs/Borrower)	0.16	0.07	2.36**
Dependent Variable: Outstanding loan balance (Rs/Borrower)			

****, ** Significant at 1% & 5% level respectively

was due to delays in loans, high interest rates, security needs and legal issues. Repayments of loans were affected by the crop yield, amount of loan granted, earlier indebtedness and annual farm income.

State banks should improve their services to clients to access credit easily and look for the socio-economic characteristics that significantly influence loan repayment by borrowers before granting loans to farmers to reduce the incidence of loan delinquencies or credit risk.

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