

## **Agrarian Transition and Livelihoods of the Rural Poor: Agricultural Credit Market**



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## **Executive Summary**

Agricultural credit is crucial for realizing the potential gain from agriculture as a profitable activity. Ensuring access to credit to small farmers who are operating at the subsistence level is a substantive issue. Small farmers in Bangladesh do not have sufficient assets to carry on with their production expenditure. They depend on agricultural credit from institutional and non-institutional sources to meet the various expenses of agricultural productivity.

In Bangladesh, the institutional sources of credit include the various banks, NGOs and other private institutions. Non-institutional credit includes the informal sources of credit, such as the local moneylenders, friends and relatives. There are various inefficiencies in the institutional sources regarding interest rate and other conditionalities. There is no insurance facility available to the farmers who are vulnerable to natural disasters. As there is not sufficient institutional credit available to the farmers, small and marginal farmers in the rural areas of Bangladesh depend on the non-institutional sources of credit to a large extent. Farmers prefer to take loan from the informal sources as it requires less formality. But the problem of this source is that the interest rate is quite high. In the process of repaying the loan, farmers lose their output and sometimes even have to sell their small holdings and become landless.

Another factor that leads to the distress of small and marginal farmers of Bangladesh is the reform initiated by the Structural Adjustment Programme (SAP). Bangladesh had to comply with the SAP as per the direction of the World Bank and IMF, for which the poor farmers had to lose the support they had previously been receiving from the government. The IFIs have been prescribing to reduce support to the agricultural sector. Increasing production cost due to diffusion of improved technology in agriculture on one hand and decreasing support on the other have led to the livelihood distress of the poor farmers in the rural areas of Bangladesh. The prescription of the IMF to reduce money flow in the economy would reduce the credit flow to the agricultural sector and thereby make the small peasants more vulnerable to internal and external shocks. It is feared that the various prescriptions of the IFIs would drive the poor farmers towards indebtedness and obstruct them from attaining sovereignty.

Indebtedness of peasants in Bangladesh has long been a phenomenon caused by shortage of cash funds. Alternative credit system is required for providing peasants with necessary funds. Unless the farmers get secured access to the sources of credit, they will not be able to invest in land and as such sustainable development in agriculture will not be possible. Therefore, intervention is needed from the state as well as from the private sector. But proper implementation of the adopted policies needs to be seriously monitored. It is necessary for the state and different organizations to carry on with their initiatives for increasing farmers' access to institutional credit. It is indispensable to construct a strong institutional base which would be able to provide farmers with sufficient credit facilities as and when necessary.

## **Section 01**

### **1.1 Introduction**

Increasing food production and attaining food security in Bangladesh require timely and adequate supply of agricultural inputs including agricultural credit. The farmers in the rural areas require financial support from institutional and non-institutional sources to meet the expenses of various agricultural activities. They also need support to recover losses due to failure of crops as a result of natural calamities (floods, droughts, cyclones, tidal bores or river erosion) and damage due to insect pests and diseases. With very low level of income it is difficult for them to accumulate capital for meeting the production expenditure. As such, a large number of farmers in rural Bangladesh are dependent on credit. For accumulation of capital for various productive activities as well as for sustaining livelihood, the poor farmers seek credit provided by institutional and non-institutional sources.

The credit is provided from two sources, formal and informal. Formal sources of credit are the government organizations, private financial institutions and NGOs. Among the informal sources are the traditional moneylenders (mahajans, beparis, and rich farmers) or friends and relatives. Farmers are faced with various problems in taking loans from the formal sources. Different conditions to be fulfilled for taking loans are difficult for the farmers. NGOs are important source of credit for the poor farmers. Problem in taking credit from the NGOs is the installment to be paid by the recipients. Often it becomes difficult for the poor farmers to pay the installment in due time and he may have to lend from another source to repay it and falls in high debt. Farmers prefer to take loans from the informal sector as it requires less formality. But the problem of this source is that the rate of interest is exorbitant and farmers lose all their produced output and sometimes even have to sell the small piece of land they own and become landless.

Components of livelihood of farmers in the rural area of Bangladesh are social, financial, physical, human and political assets. The financial assets include cash money, credit facilities, sellable livestock and readily sellable valuable assets. Livelihood assets include access to financial resources, the lack of which may lead to livelihood distress. In the rural areas, with their low level of income farmers rarely have cash money and other types of assets. As such, they have to depend on credit to a large extent.

Considering credit as a crucial factor in ascertaining sustainable development of the agricultural sector, it is necessary to find ways in which farmers' access to credit can be ensured. The aim of this study is to identify the various inefficiencies prevailing in the different sources of credit and suggests policy measures to overcome the problems thereby making credit more accessible to the rural poor farmers.

### **1.2 Objective of the study**

- Assessing the role of credit in the livelihoods of poor and marginalized farmers and in the generalized agrarian crisis. Reviewing the distribution of access to credit as well as the extent of availability of savings and investments in the rural sector.
- Exploring trends in the capital market, examining the strengths and weaknesses of the current set up, and assessing the opportunities for, and challenges to, change in this sector.

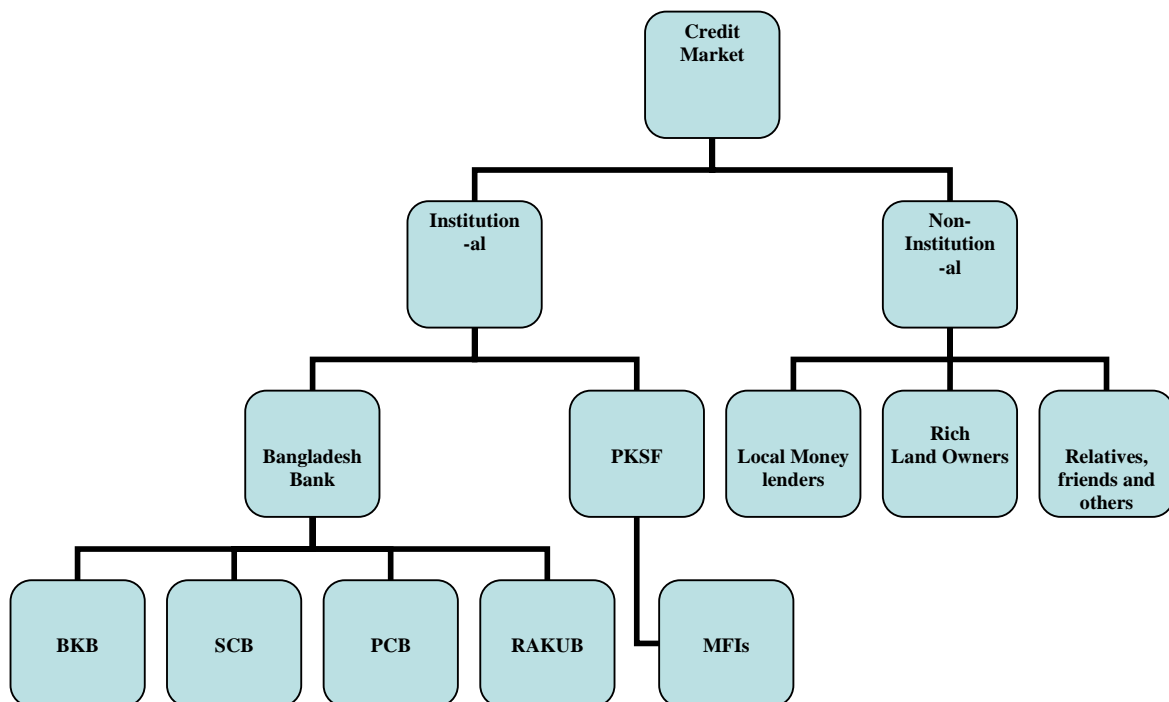
- Examining the effects of national policies and IFI directed policies on the agricultural credit market and considering the related advocacy agendas.
- Weighing the options: state directed loans, private lending etc. Finding out what farmers prefer and possibilities for improving the capital market within the current fiscal and political environment.

## Section 02

### 2.1 Sources of Credit

In Bangladesh farmers are provided credit from two sources, formal and informal. Formal sources of credit include all the institutional sources including Bangladesh Bank, Palli Karma Shahayak Foundation, Bangladesh Krishi Bank, Rajshahi Krishi Unnayan bank, state owned commercial banks (SCBs), private financial institutions including private commercial banks (PCBs) and NGOs. Among the informal sources are the traditional moneylenders (mahajans, beparis, rich farmers), rich landowners or friends and relatives. Figure 1 represents the various sources of credit.

Figure 1: Credit Network



#### 2.1.1 Contribution of Commercial and Specialized Banks to the Credit Market

During the first half of the current fiscal year (July 2008-June 2009) agricultural credit disbursement in Bangladesh grew by 7.69 percent.<sup>1</sup> Realizing the role of credit in the sustainable development of the agricultural sector, government of Bangladesh, after the

<sup>1</sup> 'Bangladesh Agriculture credit disbursement grows 7.69 pct in July-December last year' Retrieved on January 18<sup>th</sup>, 2009 , <http://www.individual.com>

independence attempted to reinforce the national economy by mobilizing more resources as agricultural credit to meet the increasing demand of the farmers. Specialized banks like the Bangladesh Krishi Bank (BKB), Rajshahi Krishi Unnayan Bank (RAKUB), Bangladesh Cooperative Bank, four commercial banks (Sonali Bank, Janata Bank, Agrani Bank and Rupali Bank) and the Bangladesh Rural Development Board (BRDB) were used to meet the needs of farmers. In the area of agricultural credit, these institutions are still the dominant players. In the annual disbursement of agricultural credit, the highest share was of BKB. During the fiscal year 2008, 53.45 percent of the total disbursement was done by BKB. The share of State Commercial Banks (SCB) was 22.15 percent.<sup>2</sup> Actual disbursement of BKB and RAKUB during the year 2008 was 32.96 and 7.65 billion taka respectively. Farmers are provided with short, medium and long-term credit by these institutions. For example, with the purpose of financing production, processing, warehousing and marketing of agriculture and agro-based industrial products, BKB offers short, medium, and long-term loans. Loan terms are determined by the purpose for which it is given, the gestation period, and income generating capacity. Short-term loans by the bank are generally provided for seasonal agricultural production activities. The medium-term loans are sanctioned for acquisition of farm machinery, different types of pumps, agricultural equipments, livestock, dairy, poultry, and transportation facilities for agricultural produces. Long-term loans are advanced for capital expenditures including purchase of tractors, tube wells, establishment of agro-based industries, investment in horticulture, forestry, fisheries etc. Amortization period for short-term loans of BKB is 18 months, for medium-term loans up to 5 years and for long-term loans over 5 years.

Table 1: Agricultural credit performance by lenders- FY 2008 (billion taka)

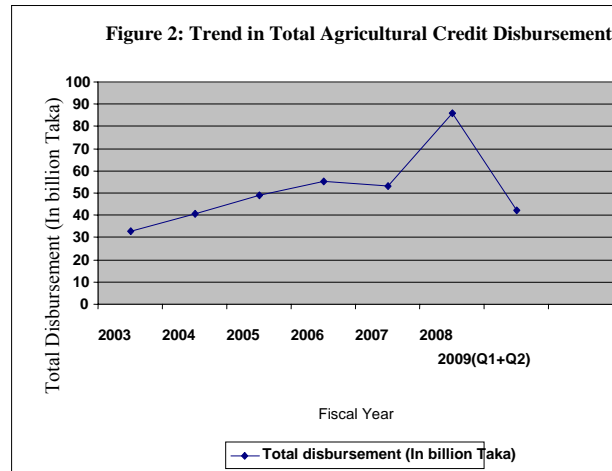
Lender	Disbursement target	Actual Disbursement	Recovery	Overdue	Outstanding	Overdue percentage of outstanding
SCBs	18	13.66	15.09	26.33	49.57	53.12
BKB	36.5	32.96	13.16	21.06	73.34	28.71
RAKUB	8	7.65	8.45	7.75	25.58	30.3
BRDB	7.11	7.35	6.97	2.47	9.16	26.97
BSBL	0.14	0.05	0.08	0.76	0.84	90.48
Sub Total	69.75	61.67	43.75	58.37	158.49	36.83
Foreign banks	3.69	8.54	8.02	0	3.01	0
PCBs	9.65	15.6	8.27	0.5	16.73	2.99
Sub Total	13.34	24.14	16.29	0.5	19.74	2.52
Grand Total	83.09	85.81	60.04	58.87	178.23	33.03

Source: Bangladesh Bank, Annual Report, 2008

Agricultural credit is disbursed for various purposes (Annex II). There have occurred ups and downs in the trend of agricultural credit disbursement. There was an upward trend in the disbursement of agricultural credit from the year 2003 to the year 2006. During fiscal year 2006 total disbursement was Tk. 55 billion, but there was a shrink in the volume in 2007, the figure came down to Tk. 52.9 billion marking a negative growth in the total disbursement of

<sup>2</sup> Bangladesh Bank, Annual Report, 2008

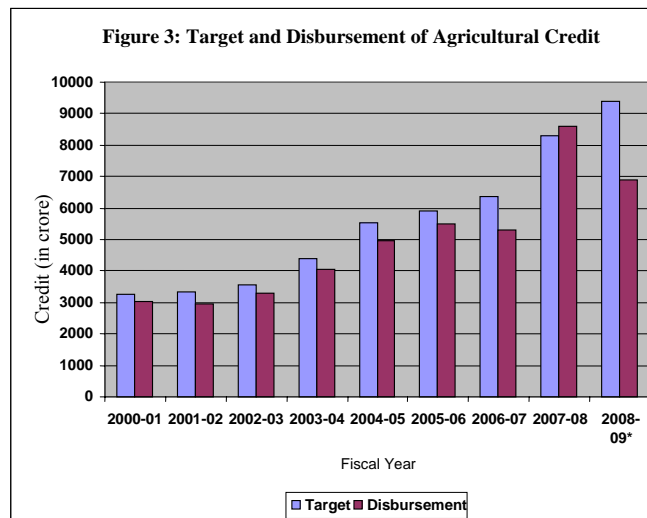
agricultural credit. During the year 2008, there has been a sharp rise in the disbursement. Total disbursement has stood at Tk.42.3 billion during the first two quarters of the current fiscal year. Figure 2 depicts the trend in the disbursement of agricultural credit.



Source: Bangladesh Bank Quarterly Update, Dec, 2008

There has been a gap in the amount of credit targeted and disbursed during the previous years. In the FY08, the actual disbursement was Tk. 61.67 billion against the target of Tk. 69.75 billion. This was 16.51 percent higher than the disbursement of Tk. 52.93 billion in the FY07. <sup>2</sup> During the FY08, non-achievement of the target was due to low disbursement in crops, purchase and installation of irrigation equipments, livestock and fisheries. Whereas the target of disbursement in crop loan was 44.8 percent, the actual disbursement was only 40 percent. On the other hand, in case of marketing of agricultural goods, poverty alleviation and other agricultural activities, the disbursement exceeded the target.<sup>5</sup>

Figure 3 represents the difference in the volume of credit targeted and disbursed throughout the fiscal years from 2000 to 2007-08 (till March). As we can see from the figure, there has always remained a considerable amount of gap in the actual disbursement and targeted amount of distribution of credit.



Source: Bangladesh Economic Review, Ministry of Finance, 2008



If we observe the trend in agricultural credit target disbursement and actual disbursement, there will be seen a difference in both according to the purpose of credit disbursement. There has also remained a difference in the target attainment, which has been 93.28 percent in 2006 against 89.51 percent in 2005. In 2007 it was 83.34, which increased to 88.42 in FY 2008.<sup>3</sup> During the various years, there has been short of disbursement from the target due to shortage in the disbursement in crop loans, installation and purchase of irrigation equipments, fisheries, livestock and other agricultural sectors.

Inadequate institutional credit for the farmers has been due to the insufficient number of state commercial banks in the remote rural areas. 63 percent of state-owned bank's branches were located in rural areas till 1980 and between 1980 and 1990, in the rural areas, 73 percent of the newly opened branches were set up. However the percentage of the rural branches of the Nationalized Commercial Banks has reduced to 61 percent in 1998. So a large number of rural poor people have lost their access to institutional credit.<sup>4</sup> The relevant statistics of Bangladesh Bank shows the insignificant number of commercial banks which hamper the flow of credit to the agricultural sector.

### **2.1.2 Credit Programmes of Bangladesh Bank**

Some agricultural credit programmes have been under the supervision of Bangladesh Bank financed by donors, which include the Marginal and Small Farm Systems Crop Intensification Project (MSFSCIP), Shrimp Culture Financing Scheme, Shashya Gudam Rin Prokalpa (SHOGORIP) and 'Expansion of Urea Deep Placement Technology in 80 upazillas of Bangladesh during Boro 2008'. A total of Tk.0.74 billion was disbursed and Tk.0.44 billion was recovered during fiscal year 2008 under the various programmes.<sup>5</sup> Another important project is Northwest Crop Diversification Project, for which ADB provided fund to RAKUB. It had credit component of TK. 1.2 billion for financing production and providing marketing facilities of high value crops in 16 northwestern districts. Farmers and agro-based enterprises were to be distributed from the fund through NGOs.

In order to extend farm loan coverage for more rural people and revamp the rural economy, the central bank of Bangladesh adopted a credit policy on 14<sup>th</sup> July, 2009. The credit policy aims at ensuring disbursement of agricultural credit at a transparent manner and checking all the irregularities prevailing within the system. For the fiscal year 2009-10, the central bank has fixed the target of disbursing Tk. 11,512.30 crore as farm loan. Out of the total, Tk. 8453 crore is targeted to be disbursed by six government banks including Bangladesh Krishi Bank and Rajshahi Krishi Unnayan Bank. Tk. 2594.40 crore is to be disbursed by 29 private banks and Tk. 464.90 crore to be disbursed by 10 foreign banks.<sup>5</sup> There has not been given any clear announcement on the interest rate of the agricultural loan to be disbursed through NGOs. The initiative of the Bangladesh Bank to make it mandatory for all local commercial banks to give farm loan has induced the foreign banks, especially the Hongkong and Shanghai Banking Corporation (HSBC), Standard Chartered and Citi Bank N.A to invest in farm loan, even though they had not been interested in it due to global financial crisis. Both

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<sup>3</sup> Bangladesh Bank Annual Report (2006, 2007 and 2008)

<sup>4</sup> Titumir R. A. M, et al, 2006, Undercutting Small Farmers, *Rice Trade in Bangladesh and WTO Negotiations*, Unnayan Onneshan, Dhaka

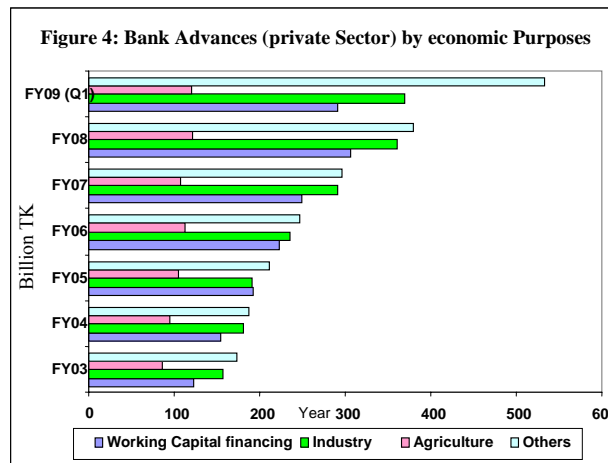
<sup>5</sup> New Age, 2009. 'Farm loan policy announced: Disbursement target set at Tk. 11,512.30 crore'.

the banks HSBC and Standard Chartered have the target to disburse Tk. 150 crore and Tk 172 crore as farm loan during the fiscal year 2009-10.<sup>5</sup>

### 2.1.3 Role of Private Commercial Banks in the Credit Market

For the past few years the private commercial banks have not played significant role in the credit market for the agricultural sector. The contribution of private sector domestic and foreign banks remained insignificant in the previous years, even though there is an upward trend in the volume of other loans disbursed by these banks. During the fiscal year 2005-06, contribution of the private banks to the agricultural credit market was only Tk. 3.34 billion, which was only 6 percent of the total credit disbursed to the sector by the NCBs and specialized banks. In 2006-07, lending to the agricultural sector increased to Tk. 11.17 billion, but it still remained modest compared to agricultural loan of Tk. 52.93 billion disbursed by NCBs and specialized lenders. In 2007-08, disbursement was of Taka 24.14 billion, which is only around 28.13 percent of the total agricultural loan disbursed in the fiscal year 2008.

As is seen from the table 2, there are a very few private banks in the rural areas and no branches of foreign banks are there at all. There are 49 branches of nine foreign banks concentrated in the urban areas which disburse credit to big industries and other non-productive sectors. These banks provide credit for consumption purposes as well.



Source: Bangladesh Bank Quarterly Update, Dec, 2008

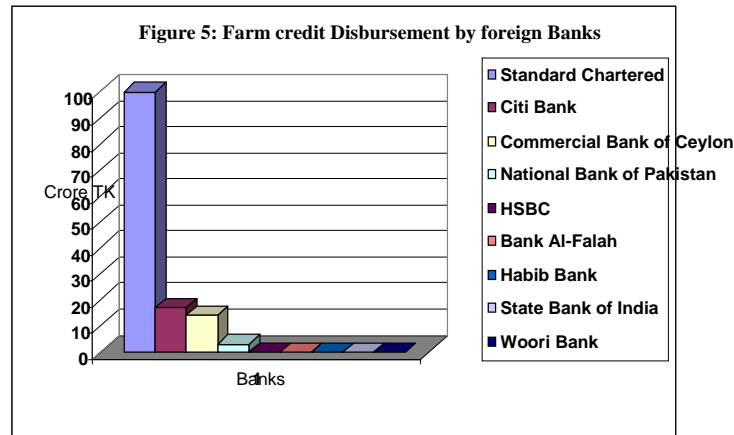
Bangladesh bank issued a circular on September 2008 and made it mandatory for all local commercial banks to disburse credit to the agricultural sector

Table 2: Banks in rural and urban areas

Banks	Number	Branches	
		Urban	Rural
State-owned	4	1238	2146
Specialized	5	155	1203
Private	30	1295	490
Foreign	9	49	0

Source: Bangladesh Bank

According to the circular of the central bank, all banks are to keep a certain portion of their loan portfolio for disbursing as loan to the agricultural sector. It has been announced in the circular that banks that do not have branches in the rural areas are to channel credit through non-government (NGO) linkage and in collaboration with other banks. Despite the order of the central bank,



Source: Daily Star, January 2009

in the first half of the current fiscal year no farm credit was provided by five foreign commercial banks including Hong Kong and Shanghai Banking Corporation (HSBC)<sup>6</sup>. Others that have not disbursed any farm credit during this period are Bank Al-Falah, Habib Bank, State Bank of India and Woori Bank. If we look at the overall agro-loan scenario, it will be seen that in the first half of the current fiscal year (July-Dec), Tk 4200 crore has been distributed against the total target of Tk 9400 crore.<sup>7</sup>

#### 2.1.4 NGOs - Alternative Source of Credit for Rural Poor

The government of Bangladesh has some limitations in trying to bring about sustained development especially in the fields of poverty alleviation and social delivery services. It recognizes the complementary role of NGOs in these areas. This recognition prompted the government to take several measures for promoting relations between the government organizations (GOs) and NGOs. NGOs have been acting as important source of credit for the rural poor farmers. According to the field based observation, most of the people in the villages tend to borrow from the NGOs as they are easily available to them. Certain big NGOs like ASA and BRAC have been undertaking income-generating activities for the rural poor which are an effective alternative to rural works programmes of the government. ASA has a number of multidimensional products which are small loan (female), small loan (male), agribusiness loan etc. The cumulative disbursement of loan upto Dec 2007 was Tk. 249809 million.<sup>8</sup> It advances loan to husbands of its female members who are small and marginal farmers. The loans help the poor farmers to save themselves from paying high interest to the moneylenders. BRAC has also adopted different measures regarding the agricultural development in the rural area. After the cyclone Sidr in 2007, the responsibility of

<sup>6</sup> The Daily Star, 2009. 'BB warns 5 foreign banks on zero farm lending', Retrieved on 22<sup>nd</sup> January, 2009,

<sup>7</sup> The Daily Star, 2009. 'Foreign banks flout farm loan rule', Retrieved on 18<sup>th</sup> January, 2009,

<sup>8</sup> ASA website, www.asa.org.bd

agricultural rehabilitation in some districts of the coastal area has been given to BRAC. BRAC undertook measures like supply of irrigation materials free of cost. For encouraging the cultivation of high yielding rice varieties and crop diversification different programs have also been adopted. BRAC also provides financial support to the people who do not have access to institutional financial services of savings and credit. “ Unnoti” is a special microfinance development programme for marginal farmers initiated by BRAC.<sup>9</sup>

### **2.1.5 Informal Credit System**

Informal sources of credit have been playing a dominant role in providing financial support to the poorest section of the rural community. In remote rural areas of Bangladesh the informal sources of credit in the past had been the moneylenders, goldsmiths and merchants who were popular among the low-income group regarding their availability and access to the people.

The goldsmiths, absentee landlords and merchants also have been sources of finance to the poor rural people. The merchants, who were few in number, collected paddy and supply rice or grocery items. Their transaction with the backward areas was mostly through two types of subordinate traders: paddy collecting traders and village grocery stores. The money lending merchants make dhaner upore loans [cash to be repaid in paddy] to their subordinate paddy traders prior to the cultivation season. These cash loans were lent at higher rate to peasants. Money lending merchants also make cash loans and give rice and other commodities on credit to village grocery stores.

Based on field level observation it can be said that local moneylenders called the mahajans are most prominent among the rural community. In times of acute financial crisis, they are the local financial support the rural people resort to. The attitude of people in the rural community has changed in terms of their dependency on the informal sector for credit. They now resort to the formal institutions during financial crisis. But the situation prevailing in the formal sector is such that the farmers are in the end forced to borrow from the local mahajans. In rural areas these days many NGOs have branches which disburse credit to the rural poor farmers. But the rate of interest is high in these NGOs and the repayment system is such that the farmers are always under pressure and as such at a certain period of time the farmers have to borrow from the local mahajans to repay the loans of the NGOs, thus becoming tangled in the credit knot.

## **2.2 IFI Policies and Impact on Livelihood of Farmers**

After the Green Revolution, farmers found the wonder seeds for Boro and Aman which gave them three times more yield than before. IRRI became the name for high yielding rice. The international donors played dubious role after the Green Revolution. They funded the research centers for invention of HYV seeds and supported development of irrigation and supply of agricultural credit for the diffusion of improved technology in agriculture. But a lot of input was needed for the wonder rice, which led to the requirement of agricultural subsidy. Thus the increasing volume of subsidy became a burden for the government budget. From then on the donor agencies namely the World Bank and the USAID have been suggesting cuts in the agricultural support and privatization of the agricultural input market. Fertilizer distribution infrastructure of Bangladesh Agricultural Development Corporation (BADC) was dismantled which had previously been given the monopoly for importing and marketing

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<sup>9</sup> BRAC Annual Report 2007, [www.brac.net](http://www.brac.net)

inputs. Private sector was then allowed to import agricultural equipments and distribute agricultural inputs. Green Revolution had led to the rapid downwards trend in the food price. This also had led the donor agencies to take position against agricultural support in research and irrigation. From then on agricultural sector has become a dirty world to the international financial institutions including World Bank, IMF and Asian Development Bank.

Since the IMF entered the country with promises of economic recovery, the farmers have become victims of their policies which led to deepen economic crisis. All over the developing countries, the policies of World Bank and IMF not only failed to address the persistent poverty but led to slower economic growth and increasing inequality. There are a huge number of projects in Bangladesh supported by the WB. But these projects have led to landlessness, unemployment and marginalization of people. IMF has long been prescribing the central bank of Bangladesh to reduce money supply. This prescription would tend to reduce money flow in the economy and as a consequence reduce credit flow to all sectors of the economy. Agricultural sector is the one that will be severely affected if the credit flow is reduced as the small and marginal farmers in this sector are largely dependent on the credit market. Likewise various policies of the institutions tend to have negative impact on the poor farmers of the country. The various projects of IMF and WB have escalated poverty, led to livelihood crisis and depleted natural resources of the country.

The impacts of the WB and IMF policies drive the poor farmers into indebtedness and obstruct the farmers in Bangladesh from attaining autarky. It is therefore, necessary for the government to refrain from the suggested policies of the international financial institutions in supporting the agricultural sector. Investing and supporting the rural poor farmers is necessary for attaining the MDG goals of poverty reduction.

## **Section 03**

### **3.1 Preference of farmers**

It has been seen from the field level observation that farmers in the rural areas now prefer to borrow from institutional sources, mostly from NGOs. In times of crisis, farmers resort to the local branches of NGOs as they find it more accessible. Farmers prefer NGOs as sources of credit because of the following reasons

- Some NGOs have branches in the remote rural areas, for which farmers have easy access to these institutions for getting credit. As has been observed in the field visit, the availability of credit to farmers in the rural areas has become possible due to the existence of branches of NGOs like ASHA, BRAC, Grameen Bank etc in remote rural areas.
- Even though the NGOs charge high interest, still the farmers do not have to undergo the formalities required to take loan from banks. Banks have failed to fulfill the demand of the poor farmers due to three main reasons. Firstly, the banks require collateral, which farmers find difficult to provide. Secondly, the process of fulfilling their application forms is too cumbersome for the illiterate poor farmers. Thirdly, the process of getting loan requires much time. As a result, when they get the credit, their purpose of taking loan may not be fulfilled.
- NGOs require less time to deliver credit to farmers than the banks. As such, farmers can get loans from NGOs whenever they require.

- Interest rate of NGOs is less compared to the local moneylenders. Therefore the poor farmers prioritize the NGOs as their first option of taking loan.

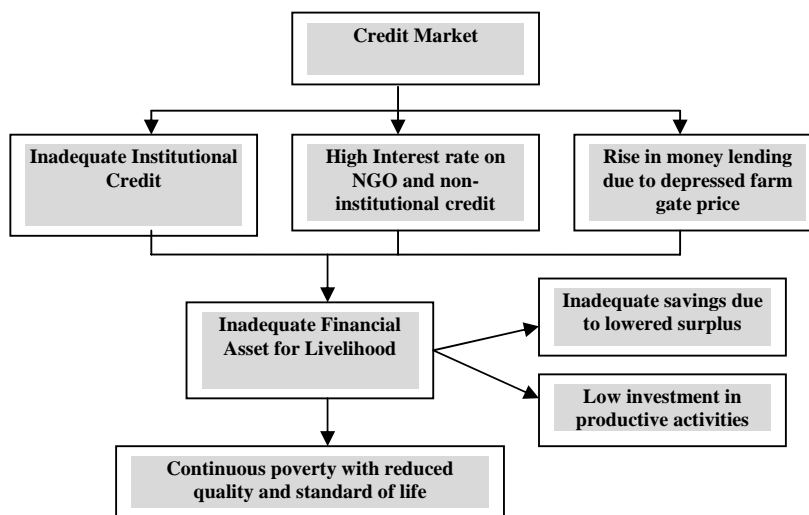
Farmer’s preference among the different sources of credit differs. The various sources of credit have their own strengths and weaknesses. We will analyze some of the concerning issues of the different sources of credit available to the farmers that have differential impact on their livelihood.

### 3.2 Concerning Issues of Credit Market and their Impact on the Livelihood of the Farmers

There has occurred inadequacy in the loan provided to the farmers from the institutional sectors. As has been seen in our previous discussion, lack of banks in the rural areas and low disbursement of credit to the agricultural sector by the private commercial banks have led to the inadequacy of finance in the credit market for the small and marginal farmers in the rural areas. Even though the NGOs and the non-institutional sources of credit require high interest rate, farmers are forced to take loans from these sources as they have very negligible amount of financial assets to serve as collateral. Depressed farm gate price that the farmers get for their products also lead to their insignificant assets.

Farmers in the rural areas have very low savings due to low level of surplus they get from production. And from the field level observation it has been seen that whatever they save is not spent on productive purposes in most cases. As such, they depend on the credit market to a large extent. The low level of savings and investment of farmers contribute to the lack of access to financial assets, which in turn leads to chronic poverty and deprivation. Figure 6 represents the impact of credit market inefficiencies on the livelihood of the poor farmers.

Figure 6: Impact of Inefficiencies of Credit Market on Farmers’ Livelihood



Realizing the necessity of credit in the agricultural sector and livelihood of the poor farmers, different governments at different times in Bangladesh have attempted to undertake various measures in providing credit to the agricultural sector. The different specialized banks along with state commercial banks have tried to meet the need of the poor farmers. But there were certain shortcoming within the system for which the public sector has been unable to meet the requirement of the poor farmers. This necessitated private sector intervention. NGOs and private commercial banks have thus come up with initiatives in providing loan to the farmers. But there are certain inadequacies within the private sector too. The concerning issues in the credit market are discussed below.

### **3.2.1 Conditions, Interest Rate and System of Repayment**

Certain conditions have to be fulfilled to obtain institutional credit. Among these the most important one is collateral. The farmer who applies for loan needs to mortgage some of his asset against the loan. Necessary documents need to be shown and submitted with the application for getting the loan. There are long procedures in the fulfillment of all formalities. Small and marginal farmers find these procedures very complex. These banks provide loan for different purposes. The different types of loans provided by the government banks and other institutions help the farmers to develop their farming techniques. Bangladesh Krishi Bank [BKB] provides loan in different categories, such as for buying power tiller, improving irrigation system etc.<sup>10</sup> From field level observation it has been found that farmers regard the collateral issue as the major problem in taking loan from the banks. Most of the farmers in the rural areas are illiterate and so it becomes difficult for them to understand the various conditions of bank loans to be fulfilled. Many farmers have complained about this difficulty during the field visit.

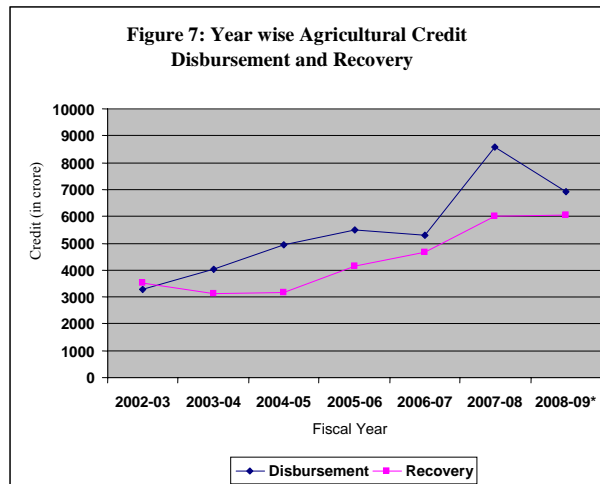
### **3.2.2 Low Recovery rate**

As we have seen before, in the volume of target and disbursement of agricultural credit, there always remained a gap. Similarly a gap also remained in case of disbursement and recovery, which is a concerning issue for the banks providing agricultural credit. Figure 7 shows the difference in the disbursement and recovery of credit that has prevailed in the credit market for the past few years.

From the figure it is seen that during some periods over the past few years, there has remained significant gap in the disbursement and recovery of agricultural loans. Acute shortage of resources of state commercial banks has occurred due to low recovery rate, which has obstructed the recycling of resources by the banks for the agricultural sector.

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<sup>10</sup> Hossain Mahbub, Rahman I Rushidan, 2003, Bangladesher Krishi O Gramin Unnayan,



Source: Bangladesh Economic Review, 2009  
\*Till March, 2009

Recovery drives of the banks to ensure repayment of agricultural loans were not carried out properly in the past. Moreover, recovery rate of agricultural loans were low because of inadequate dissemination of information. During the fiscal year 2008, different measures were introduced as recovery drive including negotiations, persuasion through various types of fairs, demand notice etc for stuck-up loans. The decrease in the recovery position is caused by natural calamities to a large extent. The recovery drives are not matched with the harvesting seasons, which might have improved the condition to some extent.

### 3.2.3 Insurance

In Bangladesh there is no insurance for farmers against natural calamities like flood, draught etc. Every year farmers face huge losses for the natural calamities. In many countries, there is crop insurance that acts as incentive to farmers for using capital intensive technology in production.

In Bangladesh crop insurance was experimentally practiced by ‘Sadharan Bima Corporation’, but the project failed as the return from the premium was much low compared to the compensation payment to farmers.

Shadharan Bima Corporation has been working only as re-insurer of private insurance companies and thereby earning profit. The corporation could have contributed in the development of the agricultural sector if it would have used a percentage of the profit earned from there as crop insurance. In 1994, under the Ministry of Trade and Commerce, a committee was established to evaluate the profitability of crop insurance in Bangladesh. According to the Committee, there are various problems in implementing the crop insurance scheme here. Bangladesh is a highly disaster-prone country, for which bankers in our country avoid to deliver credit to the agricultural sector as they fear to lose their money. Cyclone Sidr in 2007 caused damage worth of \$1.7 billion. The damage was mostly in the agricultural sector. Experts believe that if there was the practice of crop insurance it would have provided a sort of guarantee to the private commercial banks.



### 3.2.3 High Rate of Interest on NGO Credit

According to the findings from the field visit, farmers in rural areas have to pay high interest rate for the loans they borrow from the NGOs. Another problem associated with the NGO credit is that these loans are provided for short period which is not suitable for agriculture. Agricultural loans should be advanced to the farmers for adequate time so that the farmers can invest at the beginning of any crop season and repay the loan after they get the harvest and can sell their product at proper price. Small and marginal farmers in the rural areas take loans from the NGOs and due to their failure afterwards to repay the loan, they are bound to take credit from another NGO, which causes chronic indebtedness of the poor farmers to the NGOs. In some cases, they have to sell out their valuable possessions for repaying the loans. Such a case is briefed in Box 1, which represents the situation of the poor farmers in the rural areas.

Box 1  
**Tangled in the knot of debt**

Md. Jasim of Srimantopur in Comilla is a landless farmer who usually does sharecropping and during off-season works as daily labour. For buying seeds and other inputs at the beginning of Boro season, he borrowed Tk 1000 from a local NGO for which he had to pay a weekly installment of TK.60. He was to repay the loan within five months. During that period he got sick and instead of saving for repaying the loan, after meeting family expenses, he was burdened with expenditure on treatment and medicine. When it was time for repaying the loan, he had no other way but to borrow from another NGO for repaying his previous debt.

Source: Case studies in Comilla and Tangail.

### 3.2.4 Barrier to Economic Freedom

The money lenders have interest to keep poor peasants in poverty as it ensures their continuous benefit from the lending. The money lenders have similar interest in restricting technological development because that may allow the peasants to have economic freedom. The interest rate charged by the moneylenders is very high and farmers have to pay double the amount to the mahajans in the end. In this case also the farmers are under pressure for the repayment and in some cases they are forced to sell all their possession including their dwelling. Box 2 represents a case study in which a small farmer is bound to go to the local moneylenders as a last resort as she is unable to get the required loan from the institutional sources. Similar incidents are common in the remote rural areas.

Box 2  
**Mahajan- The last resort**

Asma Khatun of Delduar in the district of Tangail produces vegetables. She took loan from a local NGO. According to Asma, she could not go to banks as she had no landed property which is usually required for taking loan from banks. Asma said, 'Interest rate was very high for me. Paying installments had become difficult for me, so for repaying my loan I had to borrow again from a mahajan (local money lender) in my area.' Asma during that time was unable to repay the mahajan for which she had to sacrifice her yield, which the mahajan took away. According to Asma, there are many people like her in her village who go to the mahajans as last resort of loan.

Source: Case studies in Comilla and Tangail.

### 3.2.5 Petty Contribution of Cooperatives

Role of cooperatives in the agricultural sector is very insignificant. From field level observation it has been seen that local cooperatives have limitation in managing credit as they are not specialized in credit activities. Moreover, there is a lack of resource which leads to incapability of the cooperatives to function. In Bangladesh there are some cooperatives in some rural areas which are very insignificant in number and their functions are also very poor. Box 3 shows the deplorable situation of such a cooperative that has been detected during field survey.

**Box 3**  
**Cooperative in Comilla**

Abdul Kuddus, Moktar Hosssain, Md. Jasim and some other farmers in the village of Srimantapur in the district of Comilla have formed a cooperative from their small savings. During severe financial crisis of any of their fellow mates they provide loan from the fund. Even though they think it is very useful in times of emergency requirements, due to financial hardship it has become difficult for them to continue the operation of this cooperative

Source: Case studies in Comilla and Tangail.

Inadequacies prevailing in the institutional and non-institutional sources have led to insufficient supply of credit to the farmers. Small and marginal farmers face difficulty in getting access to finance. Lack of finance available for them leads to continuous poverty of the farmers with reduced quality and standard of life.

Therefore, the problems prevailing in the credit market need to be addressed for increasing their access to the financial assets for improving their livelihood.

## Section 04

### 4.1 Policy Recommendation

The present government has taken various measures for supporting farmers in the agricultural sector of the country. Fertilizer price has been reduced to a large extent thereby reducing the cost of production. The aim of the government is to give the farmers necessary support for the ongoing Boro season to achieve high yield.

The credit system in Bangladesh requires some changes for providing adequate loan to the poor peasants to have a sustainable development in the agricultural sector. Changes in the institutional sources of credit are required. As the small and marginal farmers are more dependent on the informal sources of credit changes can be brought in this sector as well and the two sources may be incorporated in a certain way which will ensure the flow of credit to the poor peasants. Some policy recommendations are made in this section. To achieve overall improvement of the agricultural finance system, the country must address the following development issues:

- 1) Through the continuous improvement of banking services and techniques, enhance capital market flexibility and adopt reforms toward a universal banking system which will cater to farm and non-farm credit
- 2) Effectively monitoring and developing evaluation system thereby improving management efficiency and development of cost-effective financial innovation
- 3) Strengthening supervised credit system.

#### *Policy Options regarding local Moneylenders*

As local informal moneylenders constitute a large part of the rural agricultural credit market, this sector cannot be totally discarded. What can be done is to bring changes in this sector to save the poor farmers from the exploitation of the moneylenders.

In different areas of Bangladesh there are a group of moneylenders who are the source of credit for the rural poor farmers during their financial crisis. If the farmers are unable to get credit from the institutional sources or are tangled up in the knot of high interest of the institutions, they go to the moneylenders as the last resort. There is a tendency among the borrowers to default loans taken from one lender and switch to another lender. Strong community network is necessary for avoiding such hazard. An association of moneylenders can be formed under village cooperative. If a borrower defaults the loan of one moneylender, the information about the borrower's default action should be spread throughout the lending community and precautionary measures can be taken against that.

Precautionary measures can be taken before lending to any loan applicant. For example, the lender can employ the applicant in his farm for sometime or he may purchase crops from the borrower for a certain period. These dealings with the applicant may give the lender information regarding the alertness, honesty and repayment ability. The lender may begin giving loan to the peasants with small 'testing loans'. Transaction with the applicant peasant can give the lender idea about the applicant's transaction capability and reveal his characteristics. Since farmers in rural areas rely on the local moneylenders for credit, the sector can be used as a channel to transfer loan from the government or other institutional sources.

#### *Institutional Reforms:*

Institutional sources are the major sources of credit for the rural people. There is the need to bring certain changes in these institutions while advancing loan to the poor farmers.

- Banks and other institutions providing agricultural loans should evaluate farmers seeking loans, select projects worthy of investment. Products of high demand should be given the priority while giving out loans.
- It is necessary for the institutions to monitor the use of the loan provided by them. Regular monitoring may maximize the efficiency of the loan. A monitoring agency can be built up to carry on with the operation. The agency can give advice to the farmers regarding the efficient use of the loans. It has been observed that landless farmers spend loan for consumption

expenditure. They are not able to use the loans in any development activity which generates additional income for them.

- Transparent management is necessary to raise large funds and manage the fund thereby ensuring efficient use of them. In the context of our country, this may be difficult as most of the poor peasants are illiterate. An association of literate farmers can be built with the help of NGOs who are working in the education sector. This association can help the illiterate farmers to keep an account book of their loan management.
- Simplification of procedure of institutional credit is necessary. Banks require documents and procedures for taking loans from the institutions are very cumbersome. As such farmers avoid taking loan from these institutions and fall under the grip of local moneylenders.
- Farmers can be given incentives to invest the loans they get on productive purposes. For example, if they can show a good return from their investment after taking the first loan, they may be given the next loan on a low interest rate.
- A strong insurance company can be established under Bangladesh Krishi Bank, to ensure that farmers get insurance facilities. Areas which are vulnerable to flood and drought can be targeted for crop insurance.

#### *Policy for Credit through Agricultural Co- operative*

Agricultural cooperatives can be used as a channel to transfer credit to the poor farmers. As in Korea, village cooperatives play important role and contribute largely to the development of agricultural sector. These cooperatives provide self-help between farmers through creating mutual credit with surplus money from the farmers.<sup>11</sup>

Reforms should be taken in this sector to make it an efficient instrument in delivering credit to the small and marginal farmers. The credit that Bangladesh Krishi Bank sanctions for distribution and the loans that the private organizations wish to advance to the farmers may be transferred to them through the cooperatives. Recently this issue has been raised. Funds for the cooperatives can be created from the disbursed credit from BKB and NGOs and farmers then would be able to take loan from the fund.

The cooperatives can be created by and for the farmers. In Bangladesh, existing cooperatives can be developed and can create funds for poor farmers which will save them from the exploitation of the moneylenders and avoid the cumbersome procedures of taking credit from institutional sources, at the same time induce the farmers to save.

Along with the main function of channeling credit to the poor farmers the cooperatives can take following measures:

- Collect deposit from members to develop their savings habit.

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<sup>11</sup> 'Farm credit issues in Asia', Available from: <http://www.ffc.agnet.org>  
Accessed on 1<sup>st</sup> March,2009

- Collect fund from Bangladesh Krishi Bank, NGOs and other institutions which intend to provide credit for the small and marginal farmers.
- The cooperative should have full information on its clients' need and characteristics
- It should have the provision of soft loan for small and marginal farmers.
- There should be an insurance scheme, the main objective of which will be to protect farmers against crop losses suffered on account of natural calamities.
- The cooperative should arrange training programmes for small and marginalized farmers

The cooperative may be a good channel of loan to the small and marginal farmers as it will consist of farmers who are a part of the farming community and are well informed of the needs and characteristics of other farmers in their community.

The cooperative may have two divisions. One may be farmer service cooperative that may deal with the supply of inputs and marketing issues and the other may be Primary Agricultural cooperative that will deal with only credit transfer. It should be mentioned here that cooperatives should not expand their activities beyond financial intermediation unless they can develop strong managerial and institutional capabilities. The cooperatives can be regarded as channel for advancing credit to the farmers due to the following reasons:

- It would lower the risk of default. The fund of the cooperatives would be created from the disbursed loan of BKB and NGOs. As member of the cooperatives, the farmers would be handling the fund and as such they would be more aware of their responsibility to repay the loan.
- If credit from the BKB, NGOs and other institutions are used to create resources to be distributed through the cooperatives, it would ensure easy and timely availability of loan for the farmers.
- Farmers would be free from paying high interests as in case of other institutional and non-institutional sources.

### *Introduce Crop Insurance*

Most of the developed countries have different types of schemes on crop insurance. Countries like India, Pakistan and Srilanka also have such schemes. In Pakistan there is a crop insurance scheme that offers farmers life insurance coverage.<sup>12</sup>

Lack of any crop insurance has become an obstacle for the farmers in getting loans from banks, as the institutions do not intend to deliver credit to the small and marginal farmers who are most vulnerable to natural disasters. The Insurance scheme will not only provide farmers financial security but will give the banks a sort of guarantee. In Bangladesh it is very necessary to introduce crop insurance to provide support to farmers against natural calamities like flood, drought etc. The crop insurance scheme may also give incentive to the farmers in

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<sup>12</sup> Rahman. S, 2009. 'Crop Insurance can boost farm credit: say bankers on eve of budget'. The Daily Star, June 3<sup>rd</sup>, 2009

using capital intensive technology in production. During the adaptation of any crop insurance scheme the following issues should be looked into;

- The people for whom the programmes are meant should be able to understand it.
- Government must provide necessary resources to sustain any insurance scheme.
- There should be scopes for research, which is indispensable for developing adequate insurance models for particularly low income country like ours. Projects can be adopted at pilot level and repeated expert level recommendation is required.
- Trained and dedicated manpower is necessary for running and sustaining any programme efficiently. Serious effort should be given to build up a critical mass of manpower for efficiently carrying on any such scheme.

Based on the above discussion, different policy measures are suggested to improve the agricultural credit market in the policy matrix below. Related advocacy agendas are also given in the following section which may be taken into consideration by the policymakers.

## Policy Matrix and Advocacy Agenda

Sector	Problems	Solutions	Policy Measures
Informal Sector	<ul style="list-style-type: none"> <li>▪ High Interest rate</li> <li>▪ Loan Default</li> </ul>	<ul style="list-style-type: none"> <li>▪ Precautionary measures to reduce default</li> </ul>	<ul style="list-style-type: none"> <li>▪ The sector can be used as an intermediary to transfer government credit to farmers.</li> </ul>
Institutional Source [Government]	<ul style="list-style-type: none"> <li>▪ High Interest Rate</li> <li>▪ Requires Collateral</li> <li>▪ Complex Procedure</li> <li>▪ Concentrated with rural elite</li> <li>▪ Needs to be subsidized for giving loan on low interest rate</li> <li>▪ Operation in rural areas is costly.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Evaluate projects while giving loan</li> <li>▪ Regular monitoring</li> <li>▪ Open branches in remote areas</li> <li>▪ Simplification of procedures</li> </ul>	<ul style="list-style-type: none"> <li>▪ Monitoring Agency for regular monitoring use of loans</li> <li>▪ New schemes as incentives to farmers to use loan in productive activities</li> <li>▪ Credit from banks and NGOs can be transferred to the farmers through farmers' cooperatives.</li> </ul>
Institutional Source [Private]	<ul style="list-style-type: none"> <li>▪ Not sufficient enough</li> <li>▪ Lacks long term sustainability</li> <li>▪ Do not reach the poorest of the poor</li> </ul>	<ul style="list-style-type: none"> <li>▪ Assistance from government in opening branches in rural area</li> <li>▪ Keep long term vision while providing credit</li> <li>▪ Should have the aim to reach the poorest section of peasants.</li> </ul>	<ul style="list-style-type: none"> <li>▪ Institutions interested in providing credit can advance loan through local cooperatives</li> <li>▪ May collect fund from foreign donors to open up small branches in remote rural areas to provide credit to the marginal farmers</li> </ul>

On the basis of above mentioned policy measures, some specific advocacy agenda are set below.

- Bangladesh Bank has kept the provision for banks that do not have branches in the rural areas to advance loan through NGOs. But the fact is that already interest rate of NGO loans are high. If the banks channel their credit through NGOs the interest rate will increase more and create pressure on the poor farmers. The banks and NGOs through conciliation should fix a minimal interest rate for the farmers.

- Banks make delay in disbursement of loan to the farmers for which they cannot invest it at the right time. Institutions should keep this in view while advancing loan.

Regarding the findings from the field based observation, the following measures may be adopted in the rural areas, thereby making the poor farmers' access to credit easier.

- NGOs providing loan to the farmers in rural areas require the farmers to pay installments every week which is a heavy burden for the farmers. Such stringent rules of frequent payment of installments should be changed.
- Banks in advancing loan to the farmers demand documents and include cumbersome procedure in loan advancement. The procedures should be changed and simplified.
- Banks while advancing credit require deposit to be kept by farmers. This system should be changed as farmers in financial crisis are not in a position to arrange the money for the deposit.

#### **4.2 Concluding Remarks**

Recognizing the importance of availability of cheap institutional credit for the development of livelihood of the small and marginal farmers, government of Bangladesh has increased the amount of credit disbursement. Bangladesh Bank has also been undertaking policies to make credit more accessible to the poor farmers. It is necessary for the institutions to carry on with their initiatives thereby constructing a strong institutional base for disbursing credit for the rural poor. At the same time they have to find out the loopholes that obstruct the smooth flow of loan to the farmers. According to the National Agricultural Policy adopted in 1999 several measures were planned to be undertaken for the development of credit structure of the economy, but there has not been any monitoring to observe whether the measures have properly been implemented. In the new draft of the policy adopted in 2008 there is no mention of the issue of agricultural credit. The new government after coming to power has adopted policies for the development of the agricultural sector including reduction in fuel and fertilizer price. Whatever policies are adopted there should be proper implementation of the policies and monitoring of the measures adopted. At the same time there should be willingness and initiatives from private sector to invest in agriculture. Incentives should be given from the government level to the private sector. It is indispensable for the government to carry on with the efforts for sustainable development of the agricultural sector thereby improving livelihood of the rural poor.



## **Annex I**

### *Selection of study area*

The study has been conducted in three areas predominant in agriculture representing small and marginal farmers of the country. The areas are Kopakhi in Delduar upazila under the districts of Tangail and Srimantopur in Chandina upazila under the district of Comilla.

In the area of Delduar upazila in Tangail, about 81 percent of farm households consist of marginal and small farm households. There are 10.13 percent of the farmers in the area are landless. The major crop of the area is the different varieties of rice including IRRI, Boro and Aman. In the area of Chandina upazila in Comilla, 52.61 percent of the farm households are small and marginal farmers. 23 percent farmers are landless. This area is also predominantly agricultural.

### *Method of data collection*

The study is explanatory in nature. It comprises of both qualitative and quantitative data and information. In order to achieve the objectives of the study, data have been collected from both primary and secondary sources. Primary data have been collected through field visits which are mostly qualitative. Secondary data are obtained from reports, journals, research papers, newspapers and books. Information on relevant issues is collected from websites available on the internet.

Relevant information on the concerned issue has been collected through questionnaire survey. A structured questionnaire has been developed for the purpose. Information regarding the sources and use of credit, conditions and interest charged for undertaking loans, problems in taking loans from different sources, preference of farmers among different sources and their views regarding the necessary changes in the credit market has been collected. Primary data and information collected through questionnaire have been summarized and analyzed for the purpose of the study. Focus group discussions with farmers and officials of NGOs and government officials have been carried out.

### *Method of data processing*

Qualitative data collected through questionnaire have been analyzed to identify the important aspects of the credit market in Bangladesh. Information collected through interviews of individual small farmers has been incorporated in the paper as case studies. The case studies given in the paper reveal the problems and views of poor and marginal farmers in the rural areas of Bangladesh. There are some special cases and some cases that reveal the problems prevailing generally in the rural areas. Secondary data are analyzed for understanding the trend in the volume of credit disbursement by government and different lenders.

## Annex II: Trend in agricultural credit

Institution	FY03	FY04	FY05	FY06	FY07	FY 08	FY 09		
							Q1	Q2	Q3
Program /target( July-June)	35.6	43.8	55.4	55.4	63.5	83.1	93.8	93.8	93.8
Total disbursement( In billion Taka)	32.7	40.7	48.9	55	52.9	85.8	15	27.3	26.8
Crop	16.8	18.4	20.9	22.3	22.9	25.8	3.6	10.8	10.1
Irrigation	0	0.1	0	0.1	0.1	0.1	0	0.2	0.3
Agricultural equipment	0.1	0.2	0.2	0.2	0.3	0.4	0.1	0.2	0.3
Live-stock	1.5	2.5	2.8	2.8	2.7	4.5	1.3	1	1.3
Fisheries	0.6	1.2	1.3	2.2	2.4	3.9	0.6	1.2	1.5
Grain storage and marketing	3.1	4.2	5.6	7.6	0.5	1.4	0.4	0.3	1.0
Poverty alleviation	7.7	10.2	11.5	14	11.9	22.6	3.4	4.8	5.6
Others	2.9	3.9	6.6	8.7	12.2	27	5.5	8.9	6.6
Total recovery( In billion Taka)	35.2	31.4	31.3	41.2	46.8	60	13.3	17.3	30.0
Total overdue	65.2	62.6	57.8	66.5	66.4	58.9	62.6	64.1	62.5
Outstanding(( In billion Taka)	119.1	127.1	140.3	161.8	145.8	178.2	175.9	185	187.3
Overdue as percentage outstanding	54.7	49.3	41.2	41.1	45.5	33	35.6	34.7	33.3
Growth in percent <sup>1</sup>									
Total disbursement	10.8	24.5	20.1	12.4	-3.7	62.2	24	0.6	12.2
Total recovery	8	-10.8	-0.3	31.6	13.5	28.4	1.7	-3.8	123.5

Source: Bangladesh Bank, Quarterly Update, May, 2009,

<sup>1</sup> Quarterly growth rate refers growth over the same quarter of the previous year

## Annex III

### Questionnaire for Survey

1. Do you take loan?

Yes  No

2. Where do you take credit from?

Bank  NGO  Local Moneylenders  Others

3. Which source do you prefer?

Bank  NGO  Local Moneylenders

4. Why do you prefer this source?

5. How do you use the credit?

Agricultural purpose  household purpose  Others

6. What problems do you face while taking loans from banks?

7. What problems do you face while taking loans from NGOs?

8. If you have taken loan from local moneylenders, what problems have you faced?

9. Do you save? If yes, how do you use your savings?

10. Is there any cooperative in your village?

Yes  No

11. If yes, how do the cooperatives help you?

12. What changes should be brought in the agricultural credit market, according to your view?

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