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NATIONALIZATION OF FOREIGN–OWNED TEA PLANTATIONS[1].

A Memorandum by
The Hon. Philip Gunawardena
Minister of Agriculture and Food

The total acreage under tea in Ceylon is 550,000 acres. The area is distributed between Estates and Small-holdings of various sizes as follows :–

		Number	Area
(i)	Estates over 1,000 acres in extent	77	105,706 acres
(ii)	Estates between 500 and 1,000 acres in extent	263	180,039 ,,
(iii)	Estates between 250 and 500 acres in extent	314	116,009 ,,
(iv)	Estates between 100 and 250 acres in extent	254	43,642 ,,
(v)	Estates between 50 and 100 acres in extent	246	16,147 ,,
(vi)	Estates and Small-holdings under 50 acres in extent	89,883	103,571 ,,
	Total	91,037	565,114 acres

It will be seen from the above figures that the bulk of Ceylon's tea is grown on large estates and that small estates and small-holdings play a relatively minor role in the Island's tea industry. Only 19% of Ceylon's tea is grown on individual holdings less than 100 acres in extent, as compared with nearly 50% of Ceylon's rubber and over 80% of Ceylon's coconut grown on small-holdings and small estates under 100 acres in extent.

1. An official document.

Ceylon's tea area can be divided, **on the basis of ownership,** into four main categories :-

	Number	Acreage	Percentage on Total Acreage
(i) Tea estates owned by Sterling Companies (i.e. companies registered in the U.K.)	233	172,709	30.56%
(ii) Tea estates owned by non-Ceylonse individuals	319	87,530	15.50%
(iii) Tea estates owned by Rupee Companies (i.e. Companies registered in Ceylon)	128	82,742	14.64%
(iv) Tea Estates and Small-holdings owned by Ceylonese individuals	90,357	222,133	39.30%
Total	91,037	565,114	100 %

The detailed break-up of each of these four categories, according to the size of the Estates and Small-holdings concerned and the Revenue District in which they are situated, is given in **Tables I to IV** annexed to this Memorandum.

The Government's election p r o g r a m m e stated that "foreign-owned" tea estates would be nationalised. It is presumed that the "foreign-owned" estates referred to are the estates falling into categories (i) and (ii) above, i.e. the Estates owned by Sterling Tea Companies and Estates exclusively owned by non-Ceylonese individuals. The estates falling into the third category, i.e. estates owned by Ceylon-registered Rupee Companies, are owned partly by Ceylonese and partly by foreign nationals. The Registrar of Companies has stated that figures giving the exact distribution of shares in these Companies betw~en Ceylonese and non-Ceylonese are not readily available, but it is well known that these shares have been steadily passing into Ceylonese hands in recent years and it is likely that, in a few years' time, these Rupee Companies would have passed exclusively into Ceylonese ownership. It is not necessary, therefore, to include the estates owned by these Companies in the present scheme of nationalization.

There are 552 tea estates in Ceylon which are exclusively foreign-owned. These estates cover an area of a little over 260,000 acres or just under half the total tea acreage in the Island. 233 of the foreign-owned estates covering approximately two-thirds of the total area belong to Sterling Companies while the balance 319 estates covering the other one-third of the area belong to foreign individuals.

The Company-owned estates are owned by 67 Sterling Companies, of which 38 are Companies which own only tea plantations while the other 29 Companies own rubber plantations as well. Full information is available regarding the yields, costs of production, profits, etc. of the tea estates owned by these Companies, as this information is published in the Annual Reports and Balance Sheets circulated to the shareholders of the Companies. The latest available information regarding each of these 67 Companies is summarised in Tables V and VI annexed. Table V deals with those Companies whose interests are solely in tea, while Table VI deals with those Companies which have interests in both rubber and tea. The following information is given in these Tables regarding each Company :-

(a) Total cultivated acreage and the acreage under tea in Ceylon. (A few of the Companies marked with an asterisk also have tea interests in India);

(b) The par value as well as the present value of each of the Company's shares as well as the total value at par and at present prices, of all the Company's issued shares;

(c) The total Reserves of the Company, including Capital Reserves;

(d) The "liquid assets" of the Company, i.e. the cash and investments and all other items which can be readily realised, excluding the provision for Taxation and Provident Fund Reserves;

(e) The average yield per acre of the tea estates belonging to the Company; and

(f) the capitalisation per acre of the estates belonging to the Company, calculated both on the basis of the par value of the shares and on the basis of present prices of the shares.

Even a cursory glance at the figures given in Tables V and VI reveals –

(a) that the average yield per acre of the tea estates owned by the Sterling Tea Companies is very high. All except 15 of the 67 Companies have an average yield of over 750 lbs. per acre. The majority of the Companies have average yields in the 800-1,000 lb. range and a few of the Companies even have yields of over 1,000 lbs. per acre. Considering that practically all the tea on these estates is over 50 years old and some of it nearly a century old, and that the tea consists not of specially-selected high-yielding clones but of tea propagated from ordinary tea-seed, the high average yield per acre is an index of the extremely efficient manner in which these foreign-owned tea estates have been managed and maintained. These are undoubtedly the finest and most valuable tea properties in the Island;

(b) that the capital invested in these Companies is relatively small. In the case of only 23 of the 67 Companies does the invested capital exceed Rsl 1,000 (£. 75) per cultivated acre;

(c) that the profits made by these Companies have been extremely handsome. 56 of the 67 Companies have paid out more than 100% of the issued capital in dividends over the last 10 years alone, and in a few cases the total dividends paid out during this period exceed 300% of the issued capital. I doubt whether there are many Companies whose shares are quoted on the London Stock Exchange which pay such consistently high dividends as these Sterling Tea Companies. The investors in these Companies have been repaid their capital several times over since the Companies were first established.

In drawing up a Scheme for the nationalization of foreign-owned tea plantations, the first and probably the most important question to be considered is the **basis on which compensation should be paid** to the owners of these plantations.

The basis on which compensation is paid in schemes of land nationalization has varied widely from country to country. At one extreme, we have the Communist State in which the right to the extensive private ownership of agricultural land is not recognised and the bigger landlords are therefore paid no compensation whatever when their properties are taken over by the State. In the great programme of land reform which has been carried out in China in the recent years, for instance, the lands belonging to the bigger landlords were expropriated without compensation. At the other extreme, we have the practice adopted in countries with out-and-out capitalist economies (e.g. the United States) where a private landowner whose land is taken over by the State is paid full compensation calculated on the basis of the price which his land would fetch if it were offered for sale by a willing seller in a completely free market. It is strange but true that the Ceylon Government's Land Acquisition Act (No. 9 of 1950) has adopted this out-moded concept of the basis on which compensation should be paid for lands acquired by the State—a concept which has been rejected in all progressive countries including many non-Communist countries like India. Section 41 of the Ceylon Land Acquisition Act, which embodies this out-moded principle, reads as follows :–

"For the purposes of this Act, the market value of a land in respect of which a notice under Section 7 has been published shall............be the amount which the land might be expected to have realised if sold by a willing seller in the open market as a separate entity on the date of publication of that notice in the Gazette."

If compensation is paid on this basis, it will be necessary to pay prices as high as **Rs. 3,000 or Rs. 5,000 per acre** for most of the foreign-owned tea estates in Ceylon. Considering the extremely advantageous terms on which these lands were originally made available to foreign investors and the handsome profits which they have reaped from these plantations ever since, it is clearly neither necessary nor desirable to pay compensation on this lavish scale. On the other hand, it would be unwise to expropriate the lands without the payment of any compensation at all, as this could lead to undesirable international complications. The United Kingdom could, for instance, retaliate by seizing a part of Ceylon's sterling balances in London in order to make payments to the investors whose lands are expropriatd. The problem, therefore, is to find some formula for the payment of compensation which steers a middle course between the two extremes of outright expropriation on the one hand and the payment of the so-called "free market value" on the other.

In this connection, it is useful to examine the basis on which compensation was paid by the Indian Government under its various Land Reform Laws, by the Government of Burma under its Land Nationalization Laws and by the British Labour Government, which carried out an extensive programme of industrial nationalization in the years immediately after the last World War.

The importance of the Land reform measures, which India has undertaken in the 10 years since she achieved independence is not always fully appreciated outside that country. In this short period, and particularly in the years between 1948 and 1953, the various State Governments of India have enacted a whole series of laws for the abolition of zamindaris and other landlords who held various intermediary rights between the Government and the peasant cultivator. Assam, Bengal, Bihar, Orissa, the U. P., Madhya Pradesh, Kashmir,

Madras and Mysore are among the States which have so far passed Zamindari Abolition Acts. The basis on which compensation was paid to the zamindaris whose lands were taken over varied from State to State. As a general rule, however (except in Kashmir where no compensation was paid), the compensation was based on the average "net income" (i.e. the income after deduction of land-taxes, etc.) which the zamindar derived from the land. **The total compensation paid was a multiple of the net income** calculated according to a scheldule contained in each Act. The multiplying factor used for the purpose decreased as the net income increased. For example, under the Bihar Land Reform Act of 1950, the compensation payable is 20 times the net income where the income is less than Rs. 500 a year, 19 times the net income when it is between Rs. 500 and Rs. 1,250 a year, and so on, until when the net income is over Rs. 100,000 a year, the compensation payable to the landlord is only three times the net income. **The important point to note is that the compensation paid to landlords in India is not the "free market value" of the land,** in the sense in which this term is used in the Ceylon Land Acquisition Act. The Indian Government has resolutely set its face against the payment of compensation on this basis. As the compensation paid was not based on the free-market-value of the land, the zamindaris and other landlords contested the validity of these Land Reform Laws in the Indian High Courts on the grounds that the laws were contrary to Article 31 of the Indian Constitution which stated that no property should be acquired without the payment of full compensation. Some of these objections were upheld by the Courts and the **Government of India found it necessary to amend the Indian Constitution in 1951 to make it quite clear that the principle of paying full compensation for property acquired by the State did not extend to the acquisition of estates.** The new Article 31 A of the Indian Constitution reads as follows :–

"31 A. Notwithstanding anything in the foregoing provisions of this Part, no law providing for the acquisition by the State of any estate or of any rights therein or for the extinguishment or modification of any such rights shall be deemed to be void on the ground that it is inconsistent with or abridges any of the rights conferred by any of the provisions of this Part."

The Burmese Government, like the Indian Government, carried out a very extensive land reform programme shortly after Burma achieved independence. In Burma, the problem was rather more complicated than in India because the majority of the bigger landlords were not nationals of Burma. About a quarter of the total area of cultivated land in Burma (about 3 million acres out of a total of 12 million acres) was owned by alien landlords belonging to the Chetty community of South India. Because of a very large element of foreign ownership, the problem in Burma was rather similar to that of the tea industry in Ceylon. Under the Burmese Government's Land Nationalisation Acts of 1948, non-cultivators were prohibited from owning agricultural land and even persons who directly engaged in cultivation were limited to a maximum of 50 acres each. The maximum compensation to be paid to dispossessed landlords was set at 12 times the land tax currently paid, subject to a maximum of Rs. 60 per acre. As in case of the Indian land reform laws, this compensation was only a small fraction of the "free market value" of the land, which, on a very conservative estimate, was about 300 to 400 rupees per acre at the time.

The basis on which compensation was paid by the Labour Government in the United Kingdom under the various Nationalization Acts which it passed between 1945 and 1950 also deserves careful consideration. These Acts deserve special attention because the tea estates to be nationalized in Ceylon are almost entirely British-owned, and if the basis on which compensation for these estates is computed follows the pattern which was adopted under the British Nationalization Laws, then, neither the investors concerned nor the British Government can have any serious cause for complaint. The principal industries nationalized by the British Government between 1945 and 1950 were the Coal Industy, the Electricity Industry, the Transport Industry (Rail and Road Transport), the Gas Industry and the Iron and Steel Industry. Except in the case of the Coal Industry (where in view of the its extreme complexity a special Arbitration Tribunal determined the compensation payable), the compensation in the case of all the other industries was determined on the basis of the "Stock Exchange Valuation," i.e. on an assessment of the Stock Exchange value of the shares of all the Companies in that industry on a particular date. This method of assessing compensation has the advantage of simplicity—share prices are easily and readily ascertainable and are not open to dispute. It also appears to be a full and fair method of paying compensation. But the "Stock Exchange Valuation" method of paying compensation was bitterly attacked by the Conservative Opposition in Parliament, by the Press, the City of London, by the Stock Exchange and by other representatives of financial interests. The arguments used in the debates in Parliament have been summarised by Professor Gilbert Walker in an article on "Compensation in Nationalized Industries" in the following terms :-

"Government speakers had argued, quite rightly, that the prices reached on the Stock Exchange are accepted as a fair basis of exchange by those private investors who sell to other private investors, but they had gone on to draw the much less certain conclusion that there was no reason why these prices should not be considered equally fair and reasonable when private investors as a whole are required to sell their entire holdings to a public corporation. The Opposition were able to point out, with no hope, however, of convincing the Government, that the prices of shares quoted on the Stock Exchange relate only to those possibly small parcels of securities which happen to be thrown on the market on the days chosen for purposes of the valuation. These prices certainly do not represent the value of all the assets being acquired by the public corporation. When all the shares in an undertaking are purchased by one buyer at one time, as under authority of the nationalization Acts, that buyer acquires not only the ownership of the undertaking but also the **control**; and a quantity of shares giving the controlling interest is almost invariably sold at a price considerably above the quotation on the market for any individual and relatively small parcels changing hands in the course of an ordinary day's business."

Although, as stated above, vested interests bitterly opposed the calculation of compensation on the basis of Stock Exchange prices, independent observers consider it a fair basis for paying compensation. For example, Professor W. A. Robson, Professor of Public Administration in the University of London and an acknowledged authority on the problems of nationalized industry, has expressed the view that :–

"Despite the theoretical objection, there is little reason to believe that substantial injustice has occurred to legitimate expectations in any of these industries in which Stock Exchange quotations prevailed. Most of the fuss has been political."

I suggest that compensation for the nationalized tea estates should be paid on the basis of Stock Exchange Quotations. The share prices to be used for the purposes of this calculation would be the price on the last recorded transaction before a certain "appointed date" to be set in the Nationalization Act, which could, for instance, be the date on which the policy of nationalizing foreign-owned estates is officially accepted and announced by the Government. **The actual cash compensation to be paid to each nationalized company would be the value of all the issued shares calculated on the above basis, less the value of the cash investments and other realisable liquid assets belonging to the Company as shown in the last Balance Sheet published by the Company before the "appointed date".**

On this basis, the cash compensation payable in respect of the 38 Sterling Tea Companies listed in Table V (i.e. the Companies which own only Tea Plantations) would be £. 9,426.964 (the present market value of the shares) **minus** £. 3,464,500 (the value of the liquid assets of the Company), i.e. £.5,962, 464 or roughly Rs. 80,000,000. As these Companies own 86,076 acres of tea, the **average cash compensation payable in respect of the tea estates owned by these Companies will be approximately Rs. 925/– per acre, or between one-third and one-fourth of the present free-market-value as defined in the land Acquisition Act (Rs. 3,000-Rs. 3,500 per acre).**

In the case of tea estates owned by private individuals and those belonging to Companies which own rubber plantations as well as tea plantations, the compensation payable per acre could be based on the compensation payable per acre on the above formula for the nearest tea estates belonging to a Company owning tea plantations **alone,** with a proportionate adjustment on the basis ot the comparative yields per acre of the two estates. E.g. if it is proposed to acquire a tea estate belonging to a private indidual with an average yield of 700 lbs. per acre per year, and the nearest company-owned estate has an average yield of 800 lbs. per acre per year, and, if on the basis of the above formula, the compensation payable in respect of the company estate is Rs 910/– per acre, the compensation payable in respect of the privately-owned estate would be 7/8ths of Rs. 910/– per acre. The yield per acre for the purpose of this calculation would have to be worked out on the basis of the average yield for a period of (say) 3 years before the "appointed date". The average yields of the foreign owned tea estates owned by private individuals in each district do not differ very substantially from the average yields of foreign-owned Company estates, and we would not therefore be far wrong in assuming for the purposes of this Memorandum that **the average compensation payable for all foreign-owned tea estates in Ceylon would be in the region of Rs. 925/– per acre. In other words, the total compensation payable in respect of all the foreign-owned tea in Ceylon (260,000 acres) will be in the region of Rs. 240 million.**

National Tea Plantations Corporation.

How are the nationalised tea estates to be managed after they have been acquired by the Government? Management by a regular Government Department would clearly be inappropriate. The experience of the Land Commissioner's Department in the management of the handful of rubber and tea estates hitherto acquired by Government, has not been a happy one. Management by a Government Department would involve detailed Treasury control over expenditure and control by the Public Service Commission over the appointment, dismissal and disciplinary control of the staff. It is clearly not possible to run a commercial undertaking efficiently subject to these controls. The best procedure would be to set up a public Corporation to manage the nationalized estates. This Corporation, which might be called the "National Tea Plantations Corporation", would be responsible for exercising those supervisory functions which are now exercised in respect of foreign-owned tea estates by the Colombo "Agency Houses" which represent the Sterling Tea Companies and other foreign owners of these estates. Among the principal functions of these Agency Houses are :–

(i) the approval of the annual Estimates of Income and Expenditure of each estate, which includes the approval of the annual planting and manurial programme, the ani-blister-blight programme etc.;

(ii) the appointment, dismissal and disciplinary control of the top managerial staff and the approval of salaries and other conditions of service of the rest of the staff ;

(iii) purchase of all major items of estate supplies (fertilizer etc.) and placing of all major estate contracts ;

(iv) arrangements with Produce Brokers for the sale of the estate produce ;

and (v) over-all management of the finances and accounts of the Estate.

The supervisory function which are now performed by the Colombo Agency Houses would be taken over by the proposed new Corporation, while the day-to-day management of estate affairs would, as at present, be left in the hands of the Superintendent on the spot.

TABLE I.

TEA ESTATES IN CEYLON OWNED BY STERLING COMPANIES CLASSIFIED ACCORDING TO REVENUE DISTRICTS.

Name of district	No of Estates	Total Acreage under Tea	Estates under 50 acres in extent		Estates 50 acres and above but below 100 acres		Estates 100 acres and above but below 250 acres		Estates 250 acres and above but below 500 acres		Estates 500 acres and above but below 1000 acres		Estates 1000 acres and over	
			No.	Acreage	No.	Acreage	No.	acreage	No.	Acreage	No.	Acreage	No.	Acreage
Colombo	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Kalutara	2	1,602	—	—	—	—	—	—	1	601	—	—	1	1,001
Galle	1	768	—	—	—	—	—	—	—	—	1	768	—	—
Matara	1	406	—	—	—	—	—	—	1	406	—	—	—	—
Hambantota	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Kandy	75	51,953	—	—	—	—	3	559	26	10,640	32	22,959	14	17,795
Matale	6	3,772	—	—	—	—	1	232	—	—	4	2,495	1	1,045
Nuwara Eliya	82	56,467	—	—	—	—	7	1,417	25	9,534	36	26,930	14	18,586
Kurunegala	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Ratnapura	24	20,694	—	—	—	—	2	444	5	2,220	9	6,462	8	11,568
Kegalle	9	6,696	—	—	—	—	—	—	2	821	5	3,550	2	2,325
Badulla	33	30,351	—	—	—	—	1	127	8	3,020	12	8,290	12	18,914
TOTAL	233	172,709	—	—	—	—	14	2,779	68	27,242	99	71,454	52	71,234

TABLE II

TEA ESTATES IN CEYLON OWNED BY NON–CEYLONESE CLASSIFIED ACCORDING TO REVENUE DISTRICTS.

Name of District	No. of Estates	Total Acreage under Tea	Estates under 50 acres in extent		Estates 50 acres and above but below 100 acres		Estates 100 acres and above but below 250 acres		Estates 250 acres and above but below 500 acres		Estates 500 acres and above but below 1000 acres		Estates 1000 acres and over	
			No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage
Colombo	1	33	1	33	—	—	—	—	—	—	—	—	—	—
Kalutara	1	11	1	11	—	—	—	—	—	—	—	—	—	—
Galle	8	754	5	132	2	108	—	—	—	—	1	514	—	—
Matara	2	483	—	—	1	76	—	—	1	407	—	—	—	—
Hambantota	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Kandy	138	35,799	38	955	23	1,561	21	3,460	30	11,147	24	16,473	2	2,203
Matale	12	3,040	2	60	1	62	2	429	6	1,899	1	590	—	—
Nuwara Eliya	44	14,762	12	359	2	165	7	1,298	10	3,534	12	8,213	1	1,193
Kurunegala	1	86	—	—	1	86	—	—	—	—	—	—	—	—
Ratnapura	10	2,868	3	94	1	69	1	159	2	592	3	1,954	—	—
Kegalle	11	4,205	2	59	—	—	—	—	7	2,784	2	1,362	—	—
Badulla	91	25,489	32	709	8	543	11	1,794	24	8,903	10	5,956	6	7,584
TOTAL	319	87,530	96	2,412	39	2,670	42	7,140	80	29,266	53	35,062	9	10,980

TABLE III

TEA ESTATES IN CEYLON OWNED BY RUPEE COMPANIES CLASSIFIED ACCORDING TO REVENUE DISTRICTS.

Name of District	No of Estates	Total Acreage under Tea	Estates under 50 acres in extent		Estates 50 acres and above but below 100 acres		Estates 100 acres and above but below 250 acres		Estates 250 acres and above but below 500 acres		Estates 500 acres and above but below 1000 acres		Estates 1000 acres and over	
			No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage	No	Acreage
Colombo	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Kalutara	3	1,840	—	—	—	—	—	—	1	395	2	1,445	—	—
Galle	3	1,894	—	—	—	—	—	—	1	473	2	1,421	—	—
Matara	1	494	—	—	—	—	—	—	1	494	—	—	—	—
Hambantota	—	—	—	—	—	—	—	—	—	—	—	—	—	—
Kandy	33	20,790	—	—	—	—	—	—	15	5,677	15	10,390	3	4,723
Matale	6	4,599	—	—	—	—	—	—	1	419	3	1,871	2	2,309
Nuwara Eliya	31	16,586	—	—	—	—	6	1,229	13	4,997	9	6,274	3	4,086
Kurunegala	1	334	—	—	—	—	—	—	1	334	—	—	—	—
Ratnapura	19	13,966	—	—	—	—	1	153	4	1,390	11	7,558	3	4,865
Kegalle	5	2,864	—	—	—	—	—	—	2	690	3	2,174	—	—
Badulla	26	19,375	—	—	—	—	1	175	5	1,878	16	11,095	4	6,227
TOTAL	128	82,742	—	—	—	—	8	1,557	44	16,747	61	42,228	15	22,210

TABLE IV

TEA ESTATES AND SMALL—HOLDINGS IN CEYLON OWNED BY CEYLONESE, CLASSIFIED ACCORDING TO REVENUE DISTRICTS

Name of District	No. of Estates and small holdings	Total Acreage under tea	Estates and Small-holdings under 50 acres in extent		Estates 50 acres and above but below 100 acres		Estates 100 acres and above but below 250 acres		Estates 250 acres and above but below 500 acres		Estates 50 acres and above but below 1000 acres		Estates 1000 acres and over	
			No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage	No.	Acreage
Colombo	420	845	413	345	—	—	1	148	1	352	—	—	—	—
Kalutara	6,734	7,558	6,720	2,712	3	262	3	517	3	776	5	3,291	—	—
Galle	8,718	20,612	8,655	10,760	30	2,055	21	3,331	9	2,877	3	1,589	—	—
Matara	3,149	22,009	3,070	8,654	37	2,580	29	4,320	7	2,965	6	3,490	—	—
Hambantota	1	22	1	22	—	—	—	—	—	—	—	—	—	—
Kandy	41,159	79,863	10,982	42,320	57	4,073	62	10,229	41	14,787	16	7,172	1	1,282
Matale	1,463	9,001	1,433	2,081	7	503	11	2,069	12	4,348	—	—	—	—
Nuwara Eliya	7,162	19 002	7,135	6,850	2	449	3	2,153	16	5,107	6	4,463	—	—
Kurunegala	131	611	129	171	—	—	1	119	1	321	—	—	—	—
Ratnapura	5,291	26,984	5,213	8,819	24	1,685	35	5,443	13	4,136	6	6,901	—	—
Kegalle	10,376	17,099	10,340	8,905	12	878	10	1,636	12	4,537	2	1,143	—	—
Badulla	5,753	18,507	5,691	9,520	35	992	14	2,201	7	2,548	6	3,246	—	—
TOTAL	90,337	222,133	89,787	101,159	207	13,477	190	32,166	122	42,754	50	31,295	1	1,282

STERLING COMPA

	NAME OF COMPANY	Total Cultivated Acreage	Acreage under Tea in Ceylon	Par Value per Share
				£. s.d.
1.	Adams Peak Tea Estates Ltd.	1,034	1,034	1. 0. 0
2.	Amblamana Tea Estates Ltd.	989	989	2. 0
3.	Battalgalla Estate Co. Ltd.	591	591	1. 0. 0
4.	Bogawantalawa District Tea Co, Ltd.	2,648	2,648	1. 0. 0
5.	Ceylon Amalgamated Tea & Rubber Estates Ltd.	2,568	1,987	1. 0
6.	Ceylon & Indian Planters' Association Ltd.	2,046	2,046	1. 0. 0
7.	Craig Tea Estates Ltd.	766	766	1. 0. 0
8.	Craighead Tea Co. Ltd.	906	906	1. 0. 0
9.	Deltenna (Ceylon) Tea Estates Ltd.	911	911	5. 0 Pr 2. 0 Or
10.	Demodera Tea Co. Ltd.	2,752	2,752	10. 0. 0 Pr 1. 0. 0 Or
11.	Dickwella Tea Co. Ltd.	930	930	1. 0. 0
12.	Dimbula Valley (Ceylon) Tea Co. Ltd.	2 867	2,867	5. 0. 0 Pr 1. 0. 0 Or
13.	Duckwari Tea & Rubber Estates Ltd.	1,295	1,176	1. 0. 0 Pr 2. 0 Or
14.	Estates & Agency Co. Ltd	4,939	1,668	1. 0. 0 Pr 5. 0 Or
15.	Galaha Ceylon Tea Estates & Agency Co. Ltd.	3,236	3,236	4. 0
16.	Glentaffe Tea Estates Ltd.	480	480	2. 6
17.	Hanipha (Ceylon) Tea & Rubber Co. Ltd.	1,517	1,517	1. 0. 0
18.	Highfields Ceylon Ltd.	3,889	3,889	1. 0. 0
19.	Highland Tea Co. of Ceylon Ltd.	1,709	1,709	5. 0
20.	Hunasgiriya Tea Co. Ltd.	877	877	1. 0. 0
21.	Kintyre Tea Estates Co. Ltd.	504	504	1. 0. 0
22.	Lanka Plantations Co. Ltd.	2,740	2,740	1. 0. 0
23.	Lethenty Tea Estates Association Ltd.	975	975	5. 0
24.	Mayfield (Dimbula) Tea Co. of Ceylon Ltd.	1,598	1,481	1. 0. 0
25.	Mooloya Estates Ltd.	1,235	1,235	1 0. 0
26.	Namunukula Tea Estates Co. Ltd.	1,403	1,403	5. 0
27.	New Dimbula Co. Ltd.	3,653	3,653	1. 0. 0
28.	Nuwara Eliya Tea Estates Co. Ltd.	7,278	7,278	1. 0. 0
29.	Ouvah Ceylon Estates Ltd.	3,615	3,615	1. 0. 0
30.	Peacock & Nilambe (Cey.) Tea & Rubber Estates Ltd	1,765	1,765	2. 0
31.	Pundaloya Tea Co. of Ceylon Ltd.	1,894	1,894	1. 0. 0
32.	Ragalla Tea Estates Ltd.	1,183	1,183	1. 0. 0
33.	Rangalla Consolidated Ltd.	2,385	2,385	10. 0
34.	Scottish Ceylon Tea Co. Ltd.	3,169	3,169	5. 0 Or 1. 0. 0 Pre
35.	Scottish Tea & Lands Co. of Ceylon Ltd.	7,260	7,260	1. 0. 0
36.	South Wanarajah Tea Estates Ltd.	1,518	1,518	2. 0
37.	Spring Valley Ceylon Estates Ltd.	1,994	1,994	1. 0. 0
38.	Standard Tea Co. of Ceylon Ltd.	4,957	4,957	1. 0. 0
	TOTAL	86,076	81,968	

* Present value of shares refer to values in 1957.

TABLE V

STERLING COMPANIES WITH TEA INTERESTS

(SOLELY TEA)

NAME OF COMPANY	Total Cultivated Acreage	Acreage under Tea in Ceylon	Par Value per Share	Par Value of Shares (Total)	Present Value per Share	Present value of Shares (Total)	Capitalisation per cultivated acre at par value of shares	Capitalisation per cultivated acre at present value of Shares	Yield per Acre (Tea)	Total Dividend last 10 years (as percentage) of par value of Shares	Total Reserves	Liquid Assets
			£. s.d.	£.	s.d.	£.	£.	£.	lb.		£.	£.
1. Adams Peak Tea Estates Ltd.	1,034	1,034	1. 0. 0	90,000	17/6	78,750	87	76	949	101 .5	55,000	53,500
2. Amblamana Tea Estates Ltd.	989	989	2. 0	75,300	2/-	75,300	76	76	904	113	48,000	45,500
3. Battalgalla Estate Co. Ltd.	591	591	1. 0. 0	45,000	36/4½	81,844	76	138	752	136.5	44,731	26,000
4. Bogawantalawa District Tea Co, Ltd.	2,648	2,648	1. 0. 0	335 000	26/9	488,062	84	169	980	161.5	93,500	98,000
5. Ceylon Amalgamated Tea & Rubber Estates Ltd.	2,568	1,987	1. 0	232,640	-/10	193,867	90	76	742	52	25,000	90,000
6. Ceylon & Indian Planters' Association Ltd.	2,046	2,046	1. 0. 0	163,600	17/3	141,105	80	69	799	164.5	32,236	46,000
7. Craig Tea Estates Ltd.	766	766	1. 0. 0	50,000	37/	92,500	65	120	928	136	74,116	47,500
8. Craighead Tea Co. Ltd.	906	906	1. 0. 0	116,030	22/6	130,534	119	144	964	111	42,000	93,000
9. Deltenna (Ceylon) Tea Estates Ltd.	911	911	5. 0 Pref. 2. 0 Ord.	64,000	3/6	90,375	71	99	814	139.5	33,000	34,500
10. Demodera Tea Co. Ltd.	2,752	2,752	10. 0. 0 Pref. 1. 0. 0 Ord.	200,000	26/6	258,500	73	94	848	236.5	300,292	123,500
11. Dickwella Tea Co. Ltd.	930	930	1. 0. 0	70,000	29/7	103,542	75	111	982	142	72,369	63,500
12. Dimbula Valley (Ceylon) Tea Co. Ltd.	2 867	2,867	5. 0. 0 Pref. 1. 0. 0 Ord	247,088	34/3	378,192	86	132	843	135	105,390	237,000
13. Duckwari Tea & Rubber Estates Ltd.	1,295	1,176	1. 0. 0 Pref. 2. 0 Ord.	76,000	4/6	141,000	59	109	864	390	25,000	50,000
14. Estates & Agency Co. Ltd	4,939	1,668	1. 0. 0 Pref. 5. 0 Ord.	600,000	5/4½	637,500	121	129	928	134	1,122,500	176,500
15. Galaha Ceylon Tea Estates & Agency Co. Ltd.	3,236	3,236	4. 0	175,200	5/3	229,950	54	71	831	184.5	294,308	139,000
16. Glentaffe Tea Estates Ltd.	480	480	2. 6	23,375	1/11¾	18,505	48	38	741	98.5	17,293	22,500
17. Hanipha (Ceylon) Tea & Rubber Co. Ltd.	1,517	1,517	1. 0. 0	100,000	19/3	96,250	65	63	669	121.5	82,000	73,500
18. Highfields Ceylon Ltd.	3,889	3,889	1. 0. 0	407,433	20/9	422,712	104	108	861	122	295,126	— —
19. Highland Tea Co. of Ceylon Ltd.	1,709	1,709	5. 0	143,500	4/9	136,325	83	80	892	129	92,276	34,500
20. Hunasgiriya Tea Co. Ltd.	877	877	1. 0. 0	60,333	19/9	59,578	61	67	674	91	47,548	64 500
21. Kintyre Tea Estates Co. Ltd.	504	504	1. 0. 0	47,877	36/3	86,777	94	172	874	157.5	57,795	42,000
22. Lanka Plantations Co. Ltd.	2,740	2,740	1. 0. 0	199,800	33/6	334,665	62	122	859	160.5	122,565	80,500
23, Lethenty Tea Estates Association Ltd.	975	975	5. 0	50,000	8/-	80,000	51	82	1,078	120	— —	48,000
24. Mayfield (Dimbula) Tea Co. of Ceylon Ltd.	1,598	1,481	1. 0. 0	94,300	25/6	120,233	38	75	750	188	65,000	67,500
25. Mooloya Estates Ltd.	1,235	1,235	1 0. 0	70,000	26/7	93,042	40	75	690	166.5	54,939	50,000
26. Namunukula Tea Estates Co. Ltd.	1,403	1,403	5. 0	140,800	7/9	218,240	100	155	872	205.5	82,000	64,000
27. New Dimbula Co. Ltd.	3,653	3,653	1. 0. 0	408,538	31/6	643,447	111	176	952	272.5	398,875	109,000
28. Nuwara Eliya Tea Estates Co. Ltd.	7,278	7,278	1. 0. 0	703,468	23/9	835,368	96	115	878	180.5	403,362	345,500
29. Ouvah Ceylon Estates Ltd.	3,615	3,615	1. 0. 0	435,000	26/6	576,375	120	159	877	188	153,512	183,500
30. Peacock & Nilambe (Cey.) Tea & Rubber Estates Ltd	1,765	1,765	2. 0	160,000	1/7½	130,000	70	73	806	111	72,022	96,000
31. Pundaloya Tea Co. of Ceylon Ltd.	1,894	1,894	1. 0. 0	132,000	24/6	161,700	52	85	792	163	78,000	109,500
32. Ragalla Tea Estates Ltd.	1,183	1,183	1. 0. 0	78 000	19/3	75,075	66	63	1,000	172.5	243,395	72,000
33. Rangalla Consolidated Ltd.	2,385	2,385	10. 0	154,810	14/6	224,474	65	94	569	150	54,000	70,500
34. Scottish Ceylon Tea Co. Ltd.	3,169	3,169	5. 0 Ord. 1. 0. 0 Pref.	126,628	7/-	173,679	40	55	752	302.5	184,238	109,000
35. Scottish Tea & Lands Co. of Ceylon Ltd.	7,260	7,260	1. 0. 0	450,000	39/9	894,375	62	123	755	201,5	339,568	186,500
36. South Wanarajah Tea Estates Ltd.	1,518	1,518	2. 0	77,291	6/-	231,875	50	152	745	156.6	100,856	65,500
37. Spring Valley Ceylon Estates Ltd.	1,994	1,994	1. 0. 0	225,000	25/-	281.250	105	141	944	144.5	130,050	93,000
38. Standard Tea Co. of Ceylon Ltd.	4,957	4,957	1. 0. 0	360,000	25/-	450,000	72	90	928	331	449,622	154,000
TOTAL	86,076	81,968		7,188,004		9,426,964					5,891,124	3,464,500

* Present value of shares refer to values in 1957.

TABLE VI.

STERLING COMPANIES WITH TEA INTERESTS.

(TEA CUM RUBBER)

	NAME OF COMPANY	Total Culti-vated Acreage	Acreage under Tea in Ceylon	Par Value per Share	Par Value of Shares (Total)	Present Value per Share	Present Value of Shares (Total)	Capitali-sation per cultivated acre at par value of Shares	Capitali-sation per cultivated acre at present value of Shares	Yield per Acre (Tea)	Total Dividend last 10 years (as percentage) of Par value of Shares	Total Reserves	Liquid Assets
				£. s.d.	£.	s.d.	£.	£.	£.	lb.		£.	£.
39.	Alliance Tea Co. of Ceylon Ltd.	2,395	1,750	1. 0. 0	150,00	23/9	173,125	62	74	808	104	71,803	108,000
40.	Anglo American Direct Tea Trading Co. Ltd.	19,116	5,486	1. 0. 0	1,162,370	30/6	1,772,614	34	92	806	192.5	2,370,938	1,769,000
41.	Anglo Ceylon & General Estates Co. Ltd.	22,323	7,604	5. 0	1,500,000	11/3	3,375,000	178	392	845	285	942,308	1,184,500
42.	Associated Tea Estates of Ceylon Ltd.	2,161	788	1. 0. 0	110,000	25/6	140,250	23	65	733	92	52,640	53,000
43.	Bandarapola Ceylon Co. Ltd.	1,654	749	5. 0	60,000	6/10½	82,500	36	50	701	99.5	59,000	46,000
44.	Caledonian (Ceylon) Tea & Rubber Estates Ltd	1,993	1,310	1. 0. 0 Pref. 2. 0 Ord.	132,000	2/3	144,500	66	72	756	165	64,816	48,500
45.	Carolina Tea Co. of Ceylon Ltd.	2,538	1,954	5. 0	128,700	5/6	141,570	33	55	785	117	100,317	83,000
46.	Central Province Ceylon Tea Co. Ltd.	5,169	4,978	1. 0· 0 Pref.	547,755	7/-	720,567	106	139	936	146	208,109	178,500
				5. 0 Ord.		3/3	146,250	25	41	1,137	230	41,000	60,000
47.	Ceylon Para Rubber Co. Ltd.	3,567	633	2. 0	90,000								
48.	Ceylon Proprietary Tea Estates Co. Ltd.	2,252	1,814	1. 0 0	146,127	25/6	186,311	53	82	808	146	87,013	44,000
49.	Ceylon Tea Plantations Co. Ltd.	15,930	9,465	1. 0. 0	572,120	43/3	1,237,209	25	77	798	267.5	515,400	458,000
50.	Consolidated Estates Co. Ltd.	6,417	4,930	10. 0. 0 Pref. 1. 0. 0 Ord.	341,500	27/9	458,718	53	71	690	176.5	389,896	136,500
51.	Consolidated Tea & Lands Co. Ltd.	33,617	4,135	1. 0. 0	2,600,000	25/3	3,282,500	35	97	840	168.5	3,388,526	2,635,000
52.	Deviturai Rubber & Tea Estates Co. Ltd.	2,530	1,177	1. 0. 0	187,269	10/9	100 657	74	39	882	79	84,953	42,500
53.	Doloswella Rubber & Tea Estates Ltd.	2,192	1,229	1. 0. 0	230,400	10/3	120,960	105	55	900	56.5	39,401	111,500
54.	East India & Ceylon Tea Co. Ltd.	3,288	2,689	1. 0. 0	225,000	27/6	309,375	38	94	769	135	164,933	133,500
55.	Eastern Produce & Estates Co. Ltd.	10,973	9,086	1. 0. 0	405,000	42/6	860,625	30	78	789	201.5	643,564	332,500
56.	Ederapola Tea Co. of Ceylon Ltd.	1,446	490	5. 0	60,000	4/1½	49,500	41	34	712	108.5	51,798	25,000
57.	General Ceylon Rubber & Tea Estates Ltd.	3,816	3,439	5. 0	122,520	15/9	385,938	32	101	663	199.5	269,504	125,000
58.	Imperial Ceylon Tea Estates Ltd.	2,108	1,839 *	1. 0. 0	112,000	41/9	233,800	53	110	918	160.5	166,028	132,000
59.	Lunuva (Ceylon) Tea & Rubber Estates Ltd.	14,823	11,242	1. 0. 0	853,781	24/.	1,024,537	57	69	814	157.5	1,063,316	614,000
60.	Mahawale Rubber & Tea Co. Ltd.	1,609	720	1. 0. 0	160,000	8/-	64,000	99	39	663	48	30,000	68,000
61.	Panawatte Tea & Rubber Estates Ltd.	4,907	536	1. 0. 0	209,966	13/9	144,351	42	29	651	102	141,056	94,000
62.	Pelmadulla Tea & Rubber Co. Ltd.	4,316	2,089	1. 0. 0	276,836	25/-	346,045	64	80	812	291	212,337	265,000
63.	Rajawella Produce Co. Ltd.	11,850	5,851	1. 0. 0 Pref. 10. 0 Ord.	450,000	17/-	625,000	38	52	712	127	213,982	132,500
64.	Rosehaugh (Ceylon) Tea Co. Ltd.	3,545	2,578	5· 0	200,000	5/7	223,333	56	63	695	95	97,909	78,500
65.	Tea Corporation Ltd.	2,659	2,062	5. 0	105,014	6/4	127,766	39	48	757	75	33,970	39,500
66.	United Planters' Co. of Ceylon Ltd.	6,723	5,933	1. 0. 0	512,120	27/-	691,362	76	103	771	166.5	758,090	177,000
67.	Yataderia Rubber & Tea Co. Ltd.	1,836	1,091	2. 0	140,007	-/11¼	66,461	76	36	666	65	37,000	37,000
	TOTAL	197,753	97,647		11,790,480		17,234,824					12,300,107	9,210,500

* Present value of shares refer to 1957.

BLE VI.

S WITH TEA INTERESTS.

M RUBBER)

Value Shares otal)	Present Value per Share	Present Value of Shares (Total)	Capitalisation per cultivated acre at par value of Shares	Capitalisation per cultivated acre at present value of Shares	Yield per Acre (Tea)	Total Dividend last 10 years (as percentage) of Par value of Shares	Total Reserves	Liquid Assets
£.	s.d.	£.	£.	£.	lb.		£.	£.
0,00	23/9	173,125	62	74	808	104	71,803	108,000
,370	30/6	1,772,614	34	92	806	192.5	2,370,938	1,769,000
,000	11/3	3,375,000	178	392	845	285	942,308	1,184,500
,000	25/6	140,250	23	65	733	92	52,640	53,000
,000	6/10½	82,500	36	50	701	99.5	59,000	46,000
,000	2/3	144,500	66	72	756	165	64,816	48,500
,700	5/6	141,570	33	55	785	117	100,317	83,000
,755	7/-	720,567	106	139	936	146	208,109	178,500
	3/3	146,250	25	41	1,137	230	41,000	60,000
,000								
,127	25/6	186,311	53	82	808	146	87,013	44,000
,120	43/3	1,237,209	25	77	798	267.5	515,400	458,000
,500	27/9	458,718	53	71	690	176.5	389,896	136,500
,000	25/3	3,282,500	35	97	840	168.5	3,388,526	2,635,000
,269	10/9	100 657	74	39	882	79	84,953	42,500
,400	10/3	120,960	105	55	900	56.5	39,401	111,500
,000	27/6	309,375	38	94	769	135	164,933	133,500
,000	42/6	860,625	30	78	789	201.5	643,564	332,500
,000	4/1½	49,500	41	34	712	108.5	51,798	25,000
,520	15/9	385,938	32	101	663	199.5	269,504	125,000
,000	41/9	233,800	53	110	918	160.5	166,028	132,000
,781	24/.	1,024,537	57	69	814	157.5	1,063,316	614,000
,000	8/-	64,000	99	39	663	48	30,000	68,000
,966	13/9	144,351	42	29	651	102	141,056	94,000
,836	25/-	346,045	64	80	812	291	212,337	265,000
,000	17/-	625,000	38	52	712	127	213,982	132,500
,000	5/7	223,333	56	63	695	95	97,909	78,500
,014	6/4	127,766	39	48	757	75	33,970	39,500
,120	27/-	691,362	76	103	771	166.5	758,090	177,000
,007	-/11¼	66,461	76	36	666	65	37,000	37,000
,480		17,234,824					12,300,107	9,210,500

RURAL INDEBTEDNESS IN CEYLON(1).

By

W. M. TILAKARATNA

Rural indebtendness is popularly believed to be an unmixed evil. Despite the fact that industry and commerce have expanded and are being run by the increasing use of credit, the debts of rural farmers have been traditionally frowned upon. At the outset it is necessary to make the point that there is nothing basically evil about rural indebtedness itself. As stated in a recent study, "If credit is essential to the conduct of progessive agriculture, in such agriculture as opposed to static subsistence farming, the amount of a farmer's debt at any particular time may be an indication of prosperity and efficiency rather than of poverty and financial difficulties. It is only debt which has ceased to be productive that is dangerous." (2) What has really given it a bad name is that shortage of credit and market imperfections resulting in high rates of interest have tended to make debts so uneconomic that the farmer, due to inability to repay out of income, has fallen into a state of chronic indebtedness in certain countries, notably in India. Such instances together with historical evidence of chronic indebtedness in some of the European peasantries have led to the belief that invariably there is a heavy burden of rural indebtedness in every underdeveloped country. This article will be devoted to examining the extent and nature of rural indebtedness in Ceylon.

The data available

There is little historical information about rural indebtedness in Ceylon. There were a series of village surveys conducted, under the supervision of the Economic Adviser to the Government, between 1936 and 1948. The purpose of

(1) The contents of this article form chapter III of a thesis entitled "Credit Problems of Small Farmers in Ceylon" accepted for the degree of Doctor of Philosphy of the University of London, December, 1957.

(2) F.A.O., **Agricultural Credit for small farmers,** p. 3.

these surveys was to collect data pertaining to the income, expenditure, property, debt and other social and economic conditions of the villages. The selection of the villages was on the basis of a stratified random sample. In each district a number of villages forming not less than one per cent. of the total were selected at random. Even if the question whether one per cent. of the villages provides an adequately representative sample of rural Ceylon is ignored, there are certain other grave defects in the data. First, only eleven out of the twenty districts were eventually surveyed before the whole scheme was abandoned in 1948. Secondly, the surveyes were conducted in different districts at different times during the period 1936 to 1948. The spread was far too wide especially in view of the fact that the period fell into three distinct economic phases, namely, the post-depression recovery upto 1939, the war-boom years between 1939 and 1945 and the postwar inflationary period after 1945. Doubtless all these varying economic conditions have had their repurcussions on the rural economy. The facts revealed by such widely spaced-out surveys would show widely differing results. There is no basis for aggregating the data of all the surveys and, consequently a selection has to be made. For the purposes of this article seven surveys conducted between 1936 and 1940 are selected.(1) The data are not used as a representative sample for the entire rural sector. They are used only as a rough indicator of the pre-war position not because they provide an adequate sample but because they are the only data available.

In 1950, the Department of Census and Statistics carried out a sample survey of the entire rural sector. The field work was carried out from October 1950 to April 1951. A stratified sample was used but the selection of villages was not done on a random basis. The selection of villages was entrusted to

(1) In all, eight surveys were conducted in the pre-war period but one of them pertaining to Kalutara District was in the nature of a pilot survey. **The Report on the Economic Survey of seven villages in the Rayigam Korale of Kalutara District** did not give as comprehensive data on indebtedness as the reports of subsequent surveys. Hence this particular survey is not selected. Those selected are the surveys of Chilaw, Galle, Hambantota, Kurunegala, Matale, Matara and Puttalam Districts.

Divisional Revenue Officers who had to select typical villages representing their respective divisions. There were 108 villages selected to represent the various Divisional Revenue Officers' divisions. The method of selection of villages may have introduced a certain amount of sampling bias because the officials may have wished either to exhibit their best villages or to reveal the worst conditions prevailing in their divisions. Apart from this, the report of the survey itself pointed out three possible sources of error.

First, the people surveyed were unsophisticated villagers who were not always able to give correct information. Second, the data being of varying degrees of complexity, cannot be said to be uniformly accurate. However, the report claimed a high degree of accuracy for the data on indebtedness. Third, the personal bias of investigators could have led to error. In addition, there is the possibility that some people, fearing damage to their prestige, understated their debts while others overstated them expecting to be included in some scheme of relief. Such sources of error would be present to . . extent in any kind of survey and are, therefore, of a general character. There are, however, two more specifice criticisms that could be made about the survey data.

First, the timing of the survey was somewhat unfortunate especially from the point of view of gauging the extent of indebtedness. The entire survey fell within the Korean-boom period when the prices of Ceylon's major exports were uniformly high and inflationary conditions prevailed throughout the economy. During periods of high export prices village incomes are affected in two ways. On the one hand, there are greater opportunities for employment on estates and village labour is absorbed into estates for temporary employment; on the other, the general inflationary situation results in higher demand for rural products. Both these factors lead to higher village incomes. Such higher incomes may be absorbed to some extent by the higher prices of commodities bought by the villager from outside. It is not possible to say whether such relative price increases result in a net advantage to the rural scetor;

the additional employment certainly does. With higher incomes there would be a lowering of indebtedness both due to a smaller need to borrow because of higher liquidity and higher ability to repay existing debts. This does not necessarily mean that as incomes rise people borrow less. All that happens is that when the same individual gets a higher windfall income he would be in a position to borrow less and to repay some of his existing debts. If the boom lasts long enough the individual may settle down to a higher level of living but in the short-run he would tend to reduce his debt. Consequently, the extent of indebtedness revealed by the 1958 survey would be an under-estimate.

A second criticism of the survey data is that they show the extent of indebtedness of any family at one point of time. That would ignore the probable seasonal variation in debt, which it is important to know especially from the point of view of providing suitable credit facilities. The seasonal pattern of indebtedness of any particular family or homogenous rural area may be expected to show a trough immediately after a harvest rising to a peak immediately before the harvest. This pattern may be repeated a number of times in each year depending on the crop which each family or area cultivated. Since different families were investigated at different points of time over a six month period, the effects of such seasonal variations on the sample aggregate debt may be considered to have been ironed out, in so far as there is homogeneity of seasonal variation within the sample. However, the data do not provide any information regarding the probable seasonal variation in the extent of rural indebtedness.

To sum up the limitations of the data, the pre-war data are not fully representative of the rural sector and can provide only a rough indication of the extent and nature of rural indebtedness in that period. The 1950 survey data are not based on a truly random sample of the rural sector. They are, therfore, subject to sampling bias. Further, the period of survey was a boom period; consequently, the extent of indebtedness may be somewhat understated. The

data are also inadequate to investigate seasonal variations in indebtedness. The observations made in subsequent paragaphs are all subject to these limitations.

Incidence of Indebtedness.

The table below shows the number of families in debt as a percentage of the total number of families surveyed at each of the seven pre-war surveys and at the 1950 survey. As already stated the pre-war data do not represent an adequate sample of the rural sector and the post-war data may be somewhat understated. However, the contrast between the periods is too marked to be explained by the limitations of the data alone.

TABLE I

INCIDENCE OF RURAL INDEBTEDNESS

SAMPLE	Total No. of families.	No. of familes in debt.	% of indebted families.
1) Pre-war selected villages in:-			
Chilaw District	340	254	75.3
Galle ,,	1249	947	75.8
Hambantota District	311	180	57.9
Kurunegala ,,	2041	1415	69.3
Matale ,,	692	512	74.0
Matara ,,	645	382	59.2
Puttalam ,,	173	128	74.0
All districts	5451	3818	70.0
2) 1950-51, All-Ceylon	22082	6659	30.2

SOURCES. Calculated from-1) Ministry of Labour, Industry and Commerce, Ceylon, Bulletins Nos:-

7. Rpt. on the economic survey of 5 villages in Chilaw District
8. ,, ,, ,, ,, ,, ,, 5 ,, in Puttalam ,,
9. ,, ,, ,, ,, ,, ,, 6 ,, in Matale ,,
10. ,, ,, ,, ,, ,, ,, Kurunegala ,,
11. ,, ,, ,, ,, ,, ,, 9 ,, in Galle ,,
12. ,, ,, ,, ,, ,, ,, 6 ,, in Matara ,,
13. ,, ,, ,, ,, ,, ,, 5 ,, in Hambantota,,

(2) Department of Census and Statistics, Final Report on the economic survey of rural Ceylon, 1950-51. S. P. XI of 1954.

The incidence of indebtedness in the pre-war samples ranged between 57.9 per cent. in Hambantota District to 75.8 per cent. in Galle District. The average for the seven districts was 70 per cent. The position as shown by a more reprsentative sample in 1950-51 is that the proportion of indebted families has fallen to 30.2 per cent. The contrast is even more pronouced in view of the following comments. made in 1934[1] :- "We have heard appalling stories of the indebtedness of the agriculturist. In districts such as Negombo and Chilaw, 90 per cent. of coconut planters are said to be in debt, the total amount of debt exceeding the present value of their lands. In southern areas the proportion of debt is said to be 50 per cent. In the Eastern Province paddy land is said to be fast going into the hands of the Moor moneylenders. The position in the other parts of the Island is no better."

Why has there been such a remarkable change in the incidence of rural indebtedness between the immediate prewar period and 1950-51? No specific answer to this question can be given. There are a number of general reasons which can be adduced to show why a lower proportion of rural families should be in debt in 1950–51. First, during the war and post-war years the market for rural produce was buoyant. For instance, the price of coconut which stood at about Rs. 35 per thousand nuts pre-war rose almost continuously to Rs. 214 per thousand nuts in 1951. Paddy which was hardly considered to be an economic crop in pre-war years found a ready market at "black-market" prices, due to shortages of imported rice, during the war and immediate post-war years. Since then, Government has intervened to offer a guaranteed price scheme covering practically the whole range of rural agricultural produce. Even so, it was only over the last two years that Government has been called upon to purchase considerable quantities of paddy at the guaranteed price because open market prices were much higher until then. Of course, the prices of commodities bought by the rural sector too increased during the period but there was so little of such commodities available while essentials like food and textiles were rationed and distributed at controlled prices through a net-work of consumer Co-operatives. The rural sector would have had substantial liquid funds with very little to spend on. Consequently, they must have utilised their liquid resources to retire their debts and, of course, under such circumstances there was little need to borrow.

(1) **Report of the Ceylon Banking Commission,** 1934 Vol. I p. 136, S. P. XXII of 1934

A second reason why the incidence of indebtedness could have fallen is that Ceylon enjoyed a period of full employment during the war, especially after the Japanese entry into the war. The whole economy was geared on to war-time production. The South-East Asia Command had its headquarters in Kandy and provided employment for a large number of Ceylonese. Camps and aerodromes in other parts of Ceylon offered a variety of jobs to Ceylonese [1]. The armed forces too attracted a large number of young Ceylonese who left their families in the villages; the families received additional incomes in the shape of separation allowances. Meanwhile, the estates

(1) Foreign military expenditure alone reached a peak figure of Rs. 245 million in 1942; even as late as 1950 it amounted to Rs. 32 million-vide national income estimates, of the Dept. of Census and Statistics and B. B. Das Gupta, **A Short Economic Survey of Ceylon, 1949.**

especially the rubber estates, worked at high pressure to produce as much as possible to help the allied war-effort. All these created substantial avenues for employment for the rural population. These additional employment opportunities at very lucrative rates of pay and allowances would have further enhanced the prosperity of the rural sector.

Thirdly, the Government colonisation and village expansion schemes, agricultural extension services, better marketing facilities, co-operatives, rural development schemes and welfare measures which made considerable headway in the war and post-war years would also have had some favourable effect on indebtedness. Educational and medical expenses have been minimised while rural development and agricultural extension services tend to make the farmer a more economic man. In general it could be said that such measures tend to make the farmer more prudent in his expenditure and to utilise his income better. Both these tendencies would lead to a reduction in debt at least for non-productive purposes.

A fourth point, which bears repitition is that 1950-51, the period of the survey was a particularly prosperous period throughout the economy.

It is not possible to gauge the precise effect on the incidence of indebtedness of any of these causes discussed above. That each of them would have had some effect cannot be doubted. The resulting incidence of 30.2 per cent. can be said to be low especially in comparison to the pre-war position and the position in India where typically about 70 per cent. of rural families are in debt [1]. Incidence, however, is only a first step in assessing the magnitude of the rural indebtednes problem.

(1) See **All India Rural Credit Survey, Report Vol II.** In some parts of India such as Bhagalpur in Bihar the incidence of indebtedness was as high as 91.5 per cent. only a few villages had less than 30 per cent incidence of debt.

Burden of Indebtedness.

In table II below the average debt per family has been expressed as a percentage of average income per family and the average value of property owned per family in respect of the pre-war surveys as well as the 1950 survey. In the per-war surveys the average indebtedness per indebted family ranged between 29.6 per cent. of average annual income per family in Kurunegala District and 89.9 per cent. in Chilaw District. When all districts are taken together debt per indebted family was 40.4 per cent of average annual income per family. In 1950-51 the average debt per indebted family had fallen to 22.6 per cent of average annual income

TABLE II

BURDEN OF RURAL INDEBTEDNESS.

SAMPLE.	Av. debt per in debted family Rs.	Av.annual Income per family Rs.	Av. value of pro perty per family Rs.	Av. debt as % of Average Income.	Av. debt as % of value of property
(1) Pre-war selected villages in:-					
Chilaw district	348	387	1171	89.9	29.7
Galle ,,	107	252	610	42.5	17.5
Hambantota ,,	156	288	592	54.2	26.4
Kurunegala ,,	146	493	709	29.6	20.6
Matale ,,	120	156	539	76.9	22.3
Matara ,,	118	389	665	30.3	17.7
Puttalam ,,	163	322 (a)	539	50.6	30.2
All Districts	145	359	674	40.4	21 5
(2) 1950-51, All Ceylon	263	1162	2765	22.6	9.5

(a) Excluding one family with an exceptional income of over Rs. 4,000 per month.

SOURCES—**Same as Table I.**

per family. A fall in the burden of indebtedness, measured as a percentage of average income, can take place while the average debt itself increases due to a more than proportionate rise in income. Average income per family rose from Rs. 357 in the per-war sample to Rs. 1126 in 1950-51, or by 226 per cent; meanwhile the average debt per indebted family increased from Rs. 130 to Rs. 263, or by 102 per cent. As a result of the proportionate increase in the size of the debt lagging behind the proportionate increase in income, the burden of indebtedness has fallen. It would be interesting to draw the conclusion that as incomes increase indebtedness increases less proportionately; however, the available data is only for two points of time which were separated by a period in which a complex of causes reacted on debt as well as income. It would be dangerous to rush to any such conclusion on the basis of such inadequate material. The only possible conclusion is that the burden of rural indebtedness, as measured by the criterion used, has fallen over the period.

There is no basis for deciding what is the right percentage which debts should bear to income. In a recent study the following generalisation has been made, namely "In countries of chronic indebtedness among peasants or of heavy captial investment by more prosperous farmers the total of debt may range between one and two years' cash income, becoming a heavy burden and a serious danger in times of declining prices (because of inability to meet interest and amortisation charges and the foreclosure of mortgages) when it materially exceeds one year's income. The total of debts also often, if not normally, exceeds the liquid reserves commanded by the family in such countries at any given time."(1) The data on income available in the Ceylon samples are not separated into cash and non-cash income. Even if non-cash incomes were as high as 50 per cent of total incomes, neither in the pre-war samples nor in 1950-51 would the average debts exceed average annual cash

(1) R. Galetti, K. D. S. Baldwin and I. O. Dina—**Nigerian cocoa farmers**, p. 513

incomes. However, the averages themselves might have concealed cases in which debts were higher than annual incomes, In the case of six pre-war samples for which more detailed data are available the position was as follows:-

No. of families with debts of less than one year's income	2750	83.2%
No. of familes with debts of more than one year's but less than two year's income	269	8.1%
No. of families with debts of more than two years income	287	8.7%
Total	3306 (1)	100.0%

Here again both cash and non-cash incomes have been taken together. Taking income as a whole, there were 536 families or 16.8 per cent. of all indebted families with debts amounting to over one year's income. Judged by this criterion, there appears to have been some chronic indebtedness in the pre-war period. Comparable data are not available for 1950-51.

However, it is possible to draw certain inferences from the available data. The average income per family was Rs. 1162 of which about 50 per cent or roughly Rs. 500 may be assumed as cash income. The data on size of debt shows that there were only 697 family debts or 10.5 per cent of total number of debts which were over Rs. 500 each. In the pre-war sample we used total incomes; if we do the same with the 1950-51 the percentage of debts over Rs. 1162 would be substantially less than 10.5 per cent. Chronic indebtedness, as judged by this criterion, would have been confined to less than 10 per cent of the indebted familes in 1950-51.

(1) Excluding villages in the Matale District for which similar data were not published.

A further criterion of the burden of indebtedness would be to express the average debt as a percentage of the average value of property owned per family. This has been done in the last row of table II. Before commenting on the results it must be stated that the valuation of rural property is subject to a wide margin of error. The report of the 1950 survey commented that "Family property generally consists of land, livestock, household and personal goods, building and other capital assets (including savings and investments, if any). Some of them are admittedly very difficult to assess. Savings and investments are very seldom disclosed in full. A margin of error is thus inevitable."(1) These comments would apply probably with even greater force to the pre-war data. There is probably an element of under-valuation in rural property because some assets would not be fully disclosed. On the other hand, the valuation of rural housing, which has little or no marketable or rental value, may introduce an element of over-valuation. The data on the value of assets are, therefore, not very reliable.

The results, as revealed by table II, are that the average debt per indebted family as a percentage of average value of property owned per family in the pre-war samples ranged between 17.5 per cent. in Galle District and 30.2 per cent. in Puttalam District, the average for all districts being 21.5 per cent. In 1950-51 the proportion had dropped to 9.5 per cent.

It is not possible to state from any absolute standpoint what particular proportion debts should bear to annual income or the value of the property of the debtors. The income of the debtor enables him to meet the amortization, interest and other charges on the debts. These can be met only if the debtor can save a sufficient margin for them out

(1) op. cit p. 42

of current income, i.e. he must have an excess of current income. There were a number of deficit families as shown below:-

Sample.

		% of families with excess of expenditure over income.
(1)	**Pre-war Surveys:-**	
	Chilaw district	59
	Galle ,,	55
	Hambantota ,,	47
	Kurunegala ,,	44
	Matale ,,	53
	Matara ,,	33
	Puttalam ,,	61
	All districts	48
(2)	All-Ceylon sample	33

The pre-war income and expenditure pattern of a number of families, ranging from 33 per cent. of all families in Galle district to 61 per cent. in the Puttalam district, did not enable them to repay any of their debts. On the contrary, during the year they would have had to dis-save or accumulate debts to balance their family budgets. The over-all position in respect of all districts was that 48 per cent. of the families had a deficit of income. In 1950-51 too there were 33 per cent. of the families surveyed whose expenditure exceeded income. Such families, apart from being able to meet their debt charges, would have to incur further debts for their continued survival. What is more, this was the position in a boom year. The report of the 1950 survey takes pride in this position and claims, "Families with excess of income over expenditure predominate in rural Ceylon....This is in striking contrast to pre-war conditions when few families were able to balance their budgets."[1] That the position has improved since the pre-war period cannot be denied. At the same time, 33 per cent, of the families, in 1950-51, had a short-fall of income while 30.2 per cent, of the families were indebted; in the pre-war samples 48 per cent. of the families had a short-fall of income while 70 per cent. of the families were indebted. The deficit families in one period may not be the same families which have accumulated debts as well, Nevertheless, the situation in the pre-war samples of a lower percentage of deficit families than indebted families was more conducive towards a reduction in the then existing incidence of indebtedness than was the position in 1950-51 when, apart from the existing indebted families, a further 3 per cent. at least of the families were on the brink of indebtedness and were actually dis-saving. It is not suggested that this is a bad thing by itself for the dis-saving might have been for very necessary purposes. The only point of relevance is that complacency about the 1950-51 position is not completely justified because it contained the seeds of a higher incidence of debt in the future.

The amount of annual income which a debtor has is a first line of defence against chronic indebtedness. In 1950-51, 67 per cent. of the families had an excess of income over expenditure. The other 33 per cent. of the families had an excess of expenditure over income and would, therefore, have not been able to meet their debt charges. The sample as a whole was saving, in 1950-51, at the average annual rate of Rs. 3 million whereas its total debt amounted to only Rs. 1.8 million. On the average, the sample could afford to repay the entire debt out of savings over the year. However, this saving figure works out to 12.6 per cent. of income which may have been possible in that boom year. Such high rate of saving cannot be expected in a normal year. Thus for instance, an island-wide sample revealed, in 1953, that saving amounted to only 4 per cent. of income and that

(1) op. cit. p. 42

spending units earning below Rs. 200 per month were spending more than their earnings. [1] Although the position in 1950-51 was satisfactory the same situation cannot be expected in a normal year.

The second line of defence to meet debt commitments is property. As seen in a foregoing paragraph the value of assets was approximately ten time the average debt per family. All this date is in terms of averages and do not bring out the conditions of sub-average families whieh might have been considerably worse off than the average family. All that can be said about the burden of debt, as shown by the 1950-51 data is that, on the average, the debt of families were well within their ability to meet the debt charges. Moreover, not all loans would be a charge on single year's income as some of them would be a charge on a single year's income as some of them would be repaid over a longer period of time. The sample as a whole would have been able to meet its entire outstanding debt out of its annual savings. However, self-sufficiency within the sample does not mean that individual members too were self-sufficient. Thirty three per cent of the families were unable to save, and in fact were dis-saving during the period under review.

The size of debt.

In table III below debts are classified by size into four groups. The average size of debt has more than doubled bet ween the er-war eriod and 1950-51. This is but to be expected

TABLE III-**Size of debt**

Size	No. of families in debt: Pre-war, Villages in 7 districts No.	% of total	1950-51, All-Ceylon rural sample No.	% of total
Below Rs. 50	2357	61.7	2360	35.4
Rs. 50 to Rs. 100	521	13.6	1151	17.3
Rs. 100 to 500	758	19.9	2451	36.8
over Rs. 500	182	4.8	697	10.5
	3818	100	6659	100
Average debt	Rs. 145		Rs. 263	

SOURCES: Same as Table I

(1) Central Bank of Ceylon, **Survey of Ceylon's consumer finances, TABLE 36.**

for the purchasing power of the Rupee has fallen to less than half during the period. According to an "implied price index", calculatcd by working through national income at constant prices, the price index, with 1948 as base year, rose form 33 in 1938 to 118 and 130 in 1950 and 1951 respectively.(1) With this drastic fall in the value of the Rupee, the loans required for any purpose would tend to get larger. Hence, the increase in the average size of loan is more apparent than real.

The available data do not enable us to say whether the size of debt was correlated with the level of income. In the pre-war data, 61 per cent of the debts were in the below Rs. 50 class; in 1950-51, only 35 per cent. were in this class. The general size pattern has shifted upwards, no doubt due to the lower purchasing power of money.

Purpose of loans.

The original purposes for which the debts had been incurred are show in table IV. The purchase, lease and development of land, the buying of cattle and cultivation may be classified as strictly agricultural purposes. Between them they accounted for 13.9 per cent. of the pre-war debt and 17.1 per cent. of the debts in 1950-51. Some part of the unclassified debts in the pre-war data may have been incurred for agricultural purposes. Hence it is not possible to say whether a greater proportion of the post-war debts have been incurred for agricultural purposes. Items 1 to 6 in the table may be considered as debts incurred directly in the production of all rural produce. In the pre-war data these

(1) W. Rasaputram, "Gross national product of Ceylon at constan (1948) prices." **Central Bank of Ceylon Bulletin, January, 1956.**
In this article the component parts of the gross nattonal product estimates were deflated by appropriate indices. The results for each year were aggregated to form the g.n.p. at constant (1948) prices. The "implied price index" was obtained by dividing g.n.p. at current prices by g.n.p. at constant prices.

TABLE IV

PURPOSE OF LOANS

Purpose	Pre.war villages in 7 districts Amount (Rs)	% of total debt	1950-51 sample Amount (Rs.)	% of total debt
1. Purchase, lease and development of land	77031	13.9	162997	9.3
2. Buying cattle	n.s.c.	—	17328	1.0
3. Cultivation	n.s.c.	—	118516	6.8
4. Trade	130991	23.7	150854	8.6
5. Buying carts	n.s.c.	—	38252	2.2
6. Building of houses	n.s.c.	—	137106	7.8
7. Purchase of food and household goods	72022	13.0	177898(a)	10.2
8. Medical purposes	52914	9.6	331200	18.9
9. Education	35689	6.5	n.s.c.	—
10. Ceremonial	30709	5.5	138055	7.9
11. Debt redemption	49950	9.0	91423	5.2
12. Unclassified-Productive	103684(b)	18.8	308736	17.6
Unproductive			78046	4.5
TOTAL	553170	100.0	1750412	100.0

n.s.c.- not separately classified

(a) only food.

(b) not separately classified into productive and un-productive includes Rs. 5554 of ancestral debt and Rs. 70659 for litigation.

SOURCES—Same as Table I.

items comprised 37.6 per cent. of the debt, in 1950-51 they accounted for 35.7 per cent of the total debt. Both these figures are somewat under-stated since a part of the unclassified debts would have been for productive purposes. In the

1950-51 data, the unclassified debt has been further divided into productive and non-productive, although the definition may have been somewhat elastic. No such differentiation is available for the pre-war data. If the known unproductive items, ancestral debts and litigation, are deducted from the pre-war data and the balance of the unclassified debt is treated as productive, there would be a roughly comparable figure of pre-war unclassified productive debt. The total debts for productive purposes would then comprise 42.6 per cent. and 53.3 per cent. of the total debt in the pre-war and 1950-51 samples respectively. These figures suggest that there has been a shift towards borrowing for productive purposes. The position in 1950-51 was indeed a far cry from the alleged position in 1910, when it was categorically stated that the villagers do not borrow for productive purposes but only for weddings and funerals.(1)

Purchase of food and household goods, medical purposes and education are in the category of necessary though unproductive purposes. A well-fed, physically fit and educated rural population would enhance rural productivity substantially. At the same time such expenditure is strictly non-productive, although they may be considered as necessary inputs for producing the rural output. Together they accounted for 29.1 per cent. of total debts in both samples. In the 1950–51 figure debts incurred for educational purposes and for the purchase of household goods have been included under unclassified debts, hence the total would be higher and should account for more than 29.1 per cent. of the debt. Individually the proportion of debts for medical purposes has almost doubled.

The debts incurred for ceremonial purposes and the unclassified non–productive debt could be reckoned as the total of unproductive debts. In the pre–war sample they consisted of ceremonial, ancestral debts and litigation and accounted for 19.3 per cent. of total debts. In 1950-51, the total amounted to only 12.4 per cent. This overall fall in debts for unproductive purposes is encouraging. But

(1) **Agricultural Banks,** p. 3, (S. P. VIII of 1910)

there has been an increase in debts for ceremonial purposes. Apart from this the overall pattern is favourable because there has been a marked fall in the proportion of debts for non-productive purposes.

The remaining item is debt redemption. It stands half way between productive and non-productive purposes. In so far as existing indebtedness is a drag on efficiency and inhibits future development, its redemption through borrowing on easier terms would be a distinct contribution to productivity. Where, however, debt redemtion indicates the mere substitution of one creditor for another on the same terms, it only helps the debtor to postpone repayment. The proportion of debts for this purpose has declined from 7.9 to 5.2 per cent. of total debts during the period.

The list of purposes for which debts have been incurred is an indicator of the causes of rural indebtedness. The farmer, like his counterpart in the city, has to incur debts for purposes connected with his process of production His income especially from agriculture, is received in discontinous stocks while some of his expenditure for production constitutes a continuous flow. Even where such expenditure is discontinuous they may not coincide with the time at which he receives his income. The expenditure may also be such that it requires financing over a long period of time. One of the important causes of rural indebtedness in Ceylon appears to be the needs of the rural sector for productive capital. As we have already seen 53.3 per cent. of all outstanding debts in 1950-51 was for such purposes.

Table IV also shows that the purchase of food and medical requirements, especially the latter, accounts for a substantial proportion of debts. Those incurred for the purchase of food arise due to the same cause as productive debts, namely the continuous need for food either for the family or for the labourers or for both before discontinuous doses of income are received. The high percentage of debts for medical purposes is somewhat surprising because medical attention is granted free by the Government. Presumably some rural families do not avail themselves of the free medical facilities available. The more likely reason is that because Government hospitals are situated at a distance from some rural areas, although medical attention itself is free, the costs of transport to the hospitals result in heavy expenditure for some families. Further, the villagers rely to some extent on the indigenous physicians whose services are not normally free. Such expenditure, outside the Government medical facilities, appears to be a potent cause of rural indebtedness accounting for as much as 18.9 per cent. of the total debt in 1950-51.

Ceremonial expenditure also accounted for a fair proportion of total debts in 1950-51, although it was nowhere close to what popular belief would have us imagine. For the sample as a whole it cannot be said to be a very important cause of indebtedness but it is significant that debts for ceremonial purposes accounted for a higher percentage of the total debt than cultivation or building of houses. If the percentage of debts incurred for different purposes is a proper guide to priorities in rural borrowing, ceremonial expenditure holds fifth place after medical requirements, purchase of food, purchase, lease and development of land, and trade.

One other important cause of indebtedness in the pre-war sample, namely, litigation which accounted for about 13 per cent of total pre-war debts appears to have dwindled into insignificance. The rural cultivator is traditionally supposed to be a notorious litigant. The 1950-51 figures do not indicate that he gets heavily into debt as a result. Even if all the unclassified non-productive debts were taken for purposes of litigation, such debts would account for only 4.5 per cent. of the total. The actual figure would have been much less as there is no basis for assuming that all such debts were for purposes of litigation. If the villager was as notorious a litigant as he is said to be and as the pre-war figures seem to indicate, he appears to have overcome such tendencies in the post-war period, or at least he finances such expensive habits out of liquid resources and does not borrow for the purpose.

To sum up, the more inportant causes of indebtedness appear to be connected with the processes of rural production. The purchase of food, presumably between harvests, and medical expencses cause a high proportion of indebetedness. Ceremonial purposes, though not very important as popularly believed, contribute a fair proportion of rural indebtedness. Litigation, contrary to popular belief, does not appear to be an important cause of rural indebtedness.

Rate of Interest on loans.

The table below shows the debts classified according io the rate of interest payable. The most striking feature revealed by this data is the marked fall in the proportion of debts bearing no interest and rates under 6 per cent. The fall in this category of debts has led to increases in all the other categories but is most marked in the 6% to 12% category. At first sight it would appear as though the cost of rural credit has gone up in the post-war period. However, a closer examination of the contents of the "Interest free and under 6 per cent." category shows that such a

TABLE V—**Rates of Interest on loans.**

	Pre-war, Villages in 7 Districts. Amount (Rs.)	%	1950-51, All-Ceylon rural sample Amount (Rs.)	%
Interest free and under 6%	164,190	29.7	63,200	3.6
6% to 12%	97,?03	17.7	538,743	30.8
12% to 18%	63,363	11.4	294,348	16.8
over 18%	72,366	13.1	245,989	14.1
Usufructuary and other arrangements	155,448	28.1	608,132	34.7
	553,170	100.0	1,750,412	100.0

SOURCE. Same as Table I

conclusion is not warranted, for this interest category has been described in the 1950-51 Survey Report [1] as follows:- "Among the loans below 6 per cent interest are also included interest-free loans. These are generally given by boutiques to their customers against purchases. The price charged for the goods often more than compensates for the withholding of interest. Again the principal of the loan bearing low interest is often fictitiously inflated in the bond, the borrower agreeing to repay a bigger amount than he actually borrows. All these concealed charges do not of course appear in the figures shown." When such concealed charges are taken into account these low interest loans would become high interest ones. Hence the mere shift away from this category into the higher interest brackets does not necessarily mean that the rural rates of intereets have gone up.

Why then has this marked shift taken place? Most probably because in a period of high liquidity the normal boutique loans become unnecessary because ready cash would procure goods at low prices. In a period in which the rural sector had such liquid funds, as was the case in 1950-51, credit from the boutique keeper would have been unnecessary. In a normal year the boutique debts are likely to regain their importance especially because the rural co-operative retail stores do no sell their goods on credit terms.

The rest of the table shows that, even in 1950-51, as much as 30.9 per cent, of the outstanding debts had deen incurred at rates of interest highter than 12 per cent; in fact, 14.1 per cent, of the debts were at rates of interest higher than 18 per cent. In the pre-war sample debts at rates over 12% accounted for 24.5 per cent. of the total. The increase in this class too has been at the expense of the interest-free and under 6 per cent. class. This shift, as we have argued is not necessarily due to a rise in the cost of credit. That an increasing percentage of indebtedness was incurred in post-war years at rates of interest substantially higher than 12 per cent goes to show that the cost of credit is still high.

1) op. cit p. 46

This point is especially singnificant in relation to rates of interest prevailing in the commercial sector at about that time. The table below shows some representative rates of interest. The maximum rate of interest charged by commereial banks was 8 per cent. That a substantial proporation of debts in the rural sector were at rates over 12 per cent would go to show that there is a comparative shortage of supply of credit to the rural sector.

TABLE VI—**Commercial rates of interest, 1951.**

Class of debt.	**rate of interest per cent. per annum.**
Bank Rate	2½
Government Treasury Bills	0.4
Commercial Bank Deposit Rates:–	
3 months	1/4 to 1/2
6 months	1/2
9 months	1/2 to 3/4
Savings	1 to 2
Commercial Bank advances:–	
Bills	2½ to 6
Loans and overdrafts secured by-	
Govt. securites	2¼ to 5
Shares of Joint stock coys.	4 to 6
Stock in trade	3 to 8
Immovable property	4½ to 7
Others & unsecured	3 to 8

SOURCE **Central Bank of Ceylon Bulletins.**

This point is further strengthened by the fact that as much as 34.7 per cent. of the debt is under usufructuary and other arrangements. One of the rural economic survery reports [1] commented that "Usufructuary mortgage loans seem to cost the villager even a higher rate of interest. In most places the mortgage value of a coconut tree is 50 cents. At the rate of 50 nuts per tree per annum and on the basis of a price of Rs. 10 per 1000 nuts, the gross

(1) op. cit. Balletin No 10. p. 32

interest on the mortgage is 100 per cent." That was pre-war. Since then the mortgage value of a coconut tree as well as the price of coconuts have increased. In a period of rising prices, yield remaining constant, the rate of interest on existing loans automatically goes up and in a period of falling prices it falls. In some cases the debtor remains on the property as a share cropper. In other cases the creditor takes effective possession of the property and cultivates it himself. In either case the effective rate of interest is likely to be even higher than 18 per cent. especially because only about half the value of the property would be given as a loan. The fact that it is widely prevalent strengthens the contention that all is not well with the supply of credit to the rural sector. If all the usufructuary mortgages are also classified as bearing rates of interest over 12 per cent the debts bearing rates of interest over 12 per cent. work out to 65.1 per cent of the total debt.

Security for loans.

The table below shows the type of security on which

TABLE VII—Type of Security for Loans.

Type of Security.	Pre wir, villages in 7 Districts.		1950-51, All-Ceylon rural sample.	
	Amount (Rs)	% of total	Amount (Rs)	% of Total
Mortgages	325724	58.9	643016	36.7
Pawns	15666	2.8	102093	5.8
Promissory notcs	72187	13.1	230601	13.2
Boutiques and other unsecured	139593	25.2	472448	27.0
Usufructuary mortgage	n.s.c.	..	302254	17.3
Total	553170	100.0	1750412	100.0

Note: n.s.c. — not seperately classified; persumbly included in mortgages.

SOURCE: Same as Table I.

the loans had been taken. In the pre-war data usufructuary mortgages were not separately classified and would have been included under mortgages. If 1950-51 data are also similary aggregated, the total under mortgages would be 54.0 per cent. of total debts. The pattern has changed very little between the two periods There has been a very small shift towards pawns and promissory notes from mortgages and unsecured debts. If seperate data for usufructuary mortgages were available for the pre-war samples, a comlete comparison would have been possible. Apparently the pattern of borrowing, in so far as security for loans is concerned, has changed very little over the period.

The mortgage continues to be the predominant form in which loans are taken. It accounted for as much 54.0 per cent. of total debts in 1950-51. Of the two forms of mortagages the straightforward ordinary mortgage is more popular than the usufructuary mortgage, although the latter in itself accounted for 17.3 per cent. of debts in 1950-51. Debts without any security from boutiques and elsewhere accounted for 27.0 per cent. of debts. Possibly the share from boutiques is small, as was seen in the section on interest rates. Promissory notes accounted for 13.2 per cent and pawns for 5.8 percent. of the debts. Not much can be said about the general pattern except that the usufructuary mortgage which is not a very satisfactory arrangement, accounted for a high proportion of the debts.

Period of Debts.

There were no data pertaining to period of loans either in the reports of the pre-war surveys or of the 1950-51 survey. Consequently, it is necessary to infer from other data whatever little information possible about the period of loans. The data on security for loans shown in Table V is useful in this connection. The mortgages would be for long periods, the pawns for short periods.(1) It is not

(1) The period within which a pawn has to be redeemed is 12 months and seven days.

possible to be definite about other categories, except that they would not be for long periods. On this basis the period of loans would be as follows:-

	Pre-war, villages in 7 districts. Amount (Rs)	%	1950-51, All-Ceylon rural Sample Amount (R)	%
Short-term	15666	2.8	102093	5.8
Short and Medium-term	211780	38.3	703049	30.2
Long-Term	325724	58.9	945270	54.0
	553170	100.0	1750412	100.0

Now, the period of loan is imtimately connected with the purpose of loans. In the classification by purpose in table IV, the amounts which may justifiably have been borrowed for long-periods in respect of 1950-51 data, would be as follows:-

	Amount (Rs.)	% of Total
Purchase, lease and development of land.	162997	9.3
Building of houses	137106	7.8
Debt-redemption	91423	5.2
Total.	391526	22.3

The fact that as high as 54.0 per cent. of the debt was for long periods shows that more than half of those long-period debts have been incurred for short or medium -term purposes. That would be an unsatisifactory feature in the rural debt picture.

The Aggregate Rural Debt.

The discussion, so far, has been based on samples and no attempt was made to estimate the aggregase indebtedness of the entire rural sector. The pre-war surveys do not provide an adequate sample for the purpose. The 1950–51 survey, as was argued earlier, has its weaknesses in this respect. Nevertheless, it was an All-Ceylon sample and

there can be less objection to a national estimate based on its data. The only basis available for inflating the sample data to national proportions is population. Taking the total indebtedness of the sample, it can be multiplied by the ratio of the national rural population to the population of the sample. We have to use for the pupose the mid-year estimates of population published in the **Statistical Abstract of Ceylon** on the assumption that the same percentage of the population lived in rural Ceylon in 1950-51 as at the Census of 1946. On these assumptions, the estimate of the aggregate rural debt of Ceylon would be as follows:-

Total estimated population of Ceylon in 1950— 7,544,000
" " " " " " 1951— 7,742,000
" " " " " " 1950-51— 7,643,000
(i.e. about Dec. '50 or mid-way during the survey)
Percentage of rural population in 1946 — 71.9
Rural Population in 1950–51 on the assmuption that 1946 pattern still remained unchanged — $\frac{71.9 \times 7,643,000}{100}$

Population of Sample — 101,793
Total Debt of sample — Rs. 1,750,412
Therefore, Aggregate rural debt of Ceylon — Rs. $\frac{1750412}{101,793} \times \frac{71.9 \times 7643000}{100}$
— Rs. 94,496,270.

There is no data on aggregate rural indebtedness for any earlier date. Therefore, no comparison can be made. As a percentage of rural income, the debt, as was shown earlier, was 22.6 per cent.

Sources of Credit:

Neither the pre-war surveys nor the 1950-51 survey collected any data on the sources of debt. This was an unfortunate omission. Consequently, we are forced to come to whatever inferences we can from the available data. This too is possible only in respect of the 1950-51 data as the pre-war data are an inadequate sample for comparison with All-Ceylon data of certain lending institutions. We have therefore, to work with the 1950-51 data only

The average debt outstanding from Co-operative Credit Societies with unlimited liability, which are the rural credit societies, about this period was approximately Rs. 3.75 million. In addition approximately Rs. 3.25 million was outstanding from Co-operative Agricultural Production and Sales Societies.[1] The total outstanding debt of the rural sector to Co-operative Sociesies at or about December 1950 was approximately Rs. 7 million, or 7.4 per cent of the total rural debt.

This information can lead us to a further inference. Table VII showed that the total debts without security from boutiques and other sources was 27.0 per cent. of the total debt. Loans from Co-operative Societies are given without security. If, therefore, the entire debt to the Co-operatives is subtracted, the debts without security from boutiques and sources other than Co-operatives would be 19.6 per cent of the total debt. These other sources would consist of boutiqe keepers, moneylenders and landlords. Further, Table V on interest rates, enabled us to divide the total debt into debts at interest rates higher than 12 per cent and those at rate below 12 per cent. The debts at rates below 12 per cent. interest accounted for 34.4 per cent. of the total. The Government sponsored credit institutions and the Co-operatives charge rates of interest below 12 per cent; thus, all debts owing to them would fall within this class. Further, the boutique debts too would fall into this class, as they would be reckoned as interest-free debts. The boutique debt, as we have seen, is likely to be small because the total debt within the interest-free and under 6 per cent. class amounted to only 3.6 per cent. of the total. If we assume

(1) Calculated from the **Administration reports on the working of Co-operative Societies 1949–50 and 1950-51.**

that the total of such debts were owing to boutiques then the composition of the below 12 per cent interest class would be as follows:-

Total debts	...34.4 per cent
Owing to boutiques	3.6 ,, ,,
Owing to Co-operatives	7.4 ,, ,,
Owing to Govt. sponsored credit institutions and private sources	23.4 ,, ,,

The Government sponsered credit institutions, namely, the State Mortgage Bank and the Agricultural and Industrial Credit Corporation lend only on first class security of immovable property and they also lend for purposes other than agriculture like industry and housing. The total outstanding from these two institutions about this period was approximately Rs. 32 million for all purposes. How much of agricultural debt was outstanding and how much of it was from the rural sector is not known. The proportion owing from the rural sector to these two institutions is likely to be small for reasons which will be explained in Chapter VII. As a consequence, the bulk of the 23.4 per cent of loans falling in the under 12 per cent. interest class would also be from private sources. The over 12 per cent interset class would be entirely from private sources, as no part of the institutional credit system lends at rates over 12 per cent. The usufructuary mortgages are likely to be taken from landlords or non-professional village moneyleders as such loans result in the creditor obtaining a working interest in the property.

The few inferences we can draw from the available data lead us to the following rough classification:-

Debts from boutique—less than or equal to —	3.6 per cent
,, ,, Co-operatives — approximtely —	7.4 per cent
,, ,, Government sponsored credit institutions and private sources	23.4 per cent
,, ,, private sources	65.6 per cent
	100.0 per cent

It is seen that private sources of credit accounted for more than 65.6 per cent., perhaps, as high as 90 per cent. of total debts. The highest proportion of debts to Government sponsored institutions and Co-operatives would have been under 30.8 per cent. of total debts, the minimum may have been as low as 7.4 per cent. These data reveal that the rural sector is still largely financed from private sources. Co-operative societies account for as low as 7.4 per cent. of total debts. This is, of course, better than in India where only 3.I per cent. of rural credit is from Co-operatives. (1) Nevertheless, there is a vast field in which Co-opealives and Government sponsored credit institutions have created little or no impression at all.

Concluding remarks on the basic features of the rural debt problem

The over-all impression created by the data is that the burden of rural debt has diminished considerably as between the pre-war period and 1950-51. However, the 1950-51 data pertain to a boom period in which the need for loans would have been lower and some outstanding debts would have been settled. Consequently, if data were available for a normal year, rural debts would have been higher than and the pattern different from those reveald by the 1950-51 data.

Nevertheless, the difference between the pre-war period and the 1950-51 is so marked that it would still be correct to conclude that the debt position has improved in the post-war period though it may not have improved as much as was shown by the 1950–51 data.

Although the amount of debts outstanding in 1950-51 was well within the repaying capacity of the rural sector there were ceitain features which would have led to chronic indebtedness in individual cases. First, while only 30.2 per cent of the families were indebted, 33 per cent of the families had deficit income. Eeven though the deficit families may

(1) **All-India Rural Credit Survey,** Vo II.

not be the same as those in debt the position is suggestive of an increasing incidence of debt in the future. Secondly the rural sector as a whole was able to bear the burden of the 1950-51 debt because of an abnormal rate of savings of 12.6 per cent of income. Such rates of savings cannot be expected in normal times; 1953 data pertaining to both rural and urban families revealed a saving rale of only 4 per cent. With such a low rate of saving the rural sector cannot be expected to meet the high interest rates being paid on debts. There would thus be a certain amount of chronic indebtedness. The point is that the rates of interest on 65.6 per cent of the debts was over 12 per cent and in normal times rural savings are unlikely to be large enough to meet such interest rates while repaying the loan as well. Sooner or later the people who have contracted loans at such high rates would lapse into a state of chronic indebtedness unless repeated windfall incomes like those of 1950-51 come to their aid. Windfalls have not occured since 1951. Meanwile the tendencies apparent in 1951 must have worked themselves out and the rural sector in Ceylon must at present be having a larger incidence of debt as well as a larger burden of debt some of which must be in a chronic state.

A further disconcerting feature is the small share of the debt held by Co-operatives and Government-sponsored credit institutions. The rural sector is financed largely from private sources and at very high rates of interest. Thus, although the over-all impression created by the 1950-51 data is one of little indebtedness, the pattern of debt leaves no room for complacency. The seeds of chronic indebtedness are present in rural Ceylon; only, in 1950-51, the climate was unfavourable for their germination. The conditions are far from being satisfactory. The basic problem of supplying credit at reasonable rates of interest to the rural sector has not been solved.

CROP INSURANCE AND ITS APPLICATION TO CEYLON.

by

V. T. NAVARATNE

In every enterprise there is an element of risk. This is more so in the case of farming which has to be carried on in the face of constant elemental and other unavoidable hazards. Our farmers, for the most part peasants ekeing out an existence from agriculture are, with their poor means and resources, the least equipped to bear these farming risks. A crop failure would have serious repercussions on them. Not only would it mean to them a loss of family income but they will also find that the sweat and toil they had lavished on the season's cultivation had been in vain. Further they would find themselves without the means of repaying the debts incurred by them and also without the resources to start on the next season's cultivation. They will in fact be reduced to a position of destitution.

2. Impoverishment of farmers consequent on crop failure has even more wider effects. The faimer's place in our economy is important not only for what he produces but equally so for what he buys[1]. The consequential effect of crop failure would thus be felt by the entire community. It creates general uncertainty, prices tend to go up and even the budgetary position of Government is affected[2].

Expedients such as suspension of water rates and other taxes, cancellation of accumulated agricultural debts, free issue of seed materials and direct relief have been adopted by the Government in the past to assist farmers affected by crop failures. Although without doubt these measures are really

1. All Risks Crop Insurance, James L. Buckler (U.S.D.A. p. 1)
2. Report on Crop (Paddy) Insurance P. K. Ray—Ssnl. Paper XIV 1957 p. 19.

useful their fundamental defect is that farmers cannot expect them as a right and the extent and scope of such assistance would depend to a large degree on the policies and resources of the Government.

Some advanced countries when faced with this very same problem, experimented with Crop Insurance as a possible solution. Crop Insurance simply means the farmers are assured of a minimum protection against uncertainties of crop yields in return for the payment of stipulated small sums or premiums. In consideration for relatively small amounts paid by them they purchass the right to be compensated against loss of crops. Such amounts are determined in proportion to the losses suffered in the past on the basis of actuarial analysis[1]. Insurance makes indeterminate invidusl losses largely determinate by considering them in groups and thus enables such losses to be met with relative ease through measures taken in advance[2].

The great merit of such a scheme is that a farmer can claim benefits under it as a matter of right and losses are shared wholely or partly by the farmers themselves. Moreover crop insurance spreads losses over persons, areas, and years and thereby enables farmers to substitute a regular annual premium cost for irregular losses[3].

Apart from these general features crop insurance also ensures certain specifie benefits. It would minimise the disastrous effects of a serious crop failure by guaranteeing farmers a minimum protection. By assuring farmers of a certain security of income it conributes to greater stability in general economic conditions, for if the purchasing power of farmers who form the bulk of our population is diminished by crop failure, the entire community is adversely affected.

1. Working Paper on Crop Insurance problems and its application to underdeveloped countries "F. A. O. P. 20.
2. Report on Crop (Paddy) Insurance by Dr. P. K. Ray p. 20.
3. "Federal Crop Insurance" W. H. Rowe F. C. I. C. p. 7

Crop Insurance will also improve the credit worthiness of farmers by guaranteeing protection against crop failure. This would help farmers to free themselves from their traditional dependance on money-lenders and middlemen who are the blight of our entire economy. Further the consequent improvement in the economic position of our farmers would considerably strengthen the financial position of the Co-operative Agricultural Credit institutions. Presently one of the greatest weaknesses of the Co-operative Agricultural Produce & Sales Societies is that members are unable to repay their debts regularly due to crop failures. Moreover, the use of crop insurance policies as collateral security would open to farmers credit from established banking institutions which would in turn eliminate the need for money lenders and also relieve the ever increasing pressure on Government for agricultural credit.

Crop insurance has also tremendous potentialities in the field of agricultural extension. Our farmers are yoked to the traditional and time honoured methods of agriculture and despite the advice of Extension Officers workers are hesitant to expend anything but their labour on their cultivations. However, with the protection they are assured under Crop Insurance they would have greater confidence in venturing upon the adoption of new and improved methods of farming and in making greater investments in agriculture for improving crop yields and increasing production.

Another very important resultant benefit of crop insurance will be that it would to a certain extent relieve Government of the financial burden of providing relief to farmers in case of crop failures and make available money thus saved for more important development activities. Finally, if Crop insurance were combined with a storage of commodities programme, it would help to normalise the availability of supplies and also stabilise prices[1].

1. Working paper on Crop Insurance F. A. O. p. 14.

Now that we have stated the general features and benefits resulting from crop insurance it would be opportune for us to examine how a scheme of this nature could be applied in Ceylon, in the context of conditions obtaining here. A scheme of Crop Insurance here would naturally have to start with paddy for it is the problem of paddy production we are most concerned with and a scheme of this nature has to be viewed as a part of a larger programme for providing more incentives to famers to increase the production of paddy.

Next is the question who should undertake this activity? Crop Insurance is by its very nature a hazardous venture and this explains why private enterprise has so far failed to step into this field of business. Moreover, the interests of private enterprise which is guided solely by the profit motive and the needs of society are so often not coincidental. Even in the United States where State initiative has never been popular, the Federal Government had to undertake the responsibility for crop insurance after experimentation by private Firms had ended in failure. Wherever crop insurance has been started it has been State sponsored, except for limited types of insurance like Hail Insurance obtaining in certain European countries and the United States. Hence in under-developed countries like Ceylon the natural agency to undertake Crop Insurance should be the government.

Another very important matter that has to be decided is whether there is any justification for making crop insurance compulsory to all farmers. The Japanese Mutual Relief Crop Insurance system is a compulsory, heavily subsidised, semi-governmental system for the benefit of the farmers[1]. In the U.S.S.R. Crop Insurance is part of a general scheme of rural insurance and is administered as a Government monopoly by the State Insurance Administration[2]. In the United States Crop Insurance has been operated from the beginning on a voluntary basis, but despite the obvious benefits of crop insurance to the type of large scale farming that is being carried on

1. Crop Insurance in Japan W. H. Rowe F. C. I. C. p. 1
2. Working Paper F. A. O. p. 4

in the U.S. and in spite of the fact that the general ideas and principles of insurance are not new to American farmers, (most of them carry Fire and Car Insurance) participation in the Ferderal Crop Insurance Programme has maintained a comparatively low level of about 23 per cent of the eligible farmers, in those counties where crop insurance is offered. This level of paricipation is indequate to make the project very stable. Some officials there are of the opinion that even in the United States Crop Insurance should be made compulsory at least to those farmers who benefit from the various Aid Programmes of the United States Department of Agriculture.

In Ceylon there is every reason to make Crop Insurance at least in regard to paddy, compulsory. For one thing if it is not compulsory very few farmers will participate in it, for the very idea of insurance is alien to the large mass of our peasants. Moreover our farmers receive various types of assistance from the Government, more perhaps than their counterparts in other countries. Government at present gives agricultural loans to the tune of obout 20 million rupees a year, and with the possible withdrawal of the landlord from the scene consequent on the introduction of the Paddy Lands Act, this amount will have to be considerably stepped up. These loans are given to farmers with practically no security. Therefore it is certainly not too much for the Government to expect farmers to improve their credit-worthiness by insuring their crops, which after all is ultimately in their own interests.

Furthermore our farmers are the unique recipients of a double subsidy. They sell their paddy to the Government under the Guaranteed Price Scheme at a price far above the world market price for paddy, and are at the same time provided with subsidised rice for consumption under the rationing scheme. The objectives of these heavy subsidies have been to induce farmers to increase their output to the maximum, but it is a fact that very little of the money that farmers receive under our price support scheme is diverted to the fields, to increase production, and much of it is frittered away on wasteful expenditure, thereby perhaps even contributing towards promoting inflationary tendencies. It is clear that

a system of collective saving against future calamities should have considerable attraction from an anti-inflationary point of view [1]. Once established it is never easy to bring down the Guaranteed Price but a compulsory scheme cf Crop Insurance would achieve the laudable purpose of temporarily immobilising a part of the surplus purchasing power in the hands of farmers, thereby keeping down inflationary tendencies and also using it for providing a much needed protection to the farmers themselves.

The case for compulsory crop insurance in Ceylon, at least of paddy, is very strong but the element of compulsion would have had no justification if the farmers had no security of tenure.

Crop Insurance has to be viewed from a long term point of view. It takes care of not only the present but also the future. Hazards might occur not this year but 8 years hence, and the farmer continues to pay his premium in all these years in order to secure for himself protection against the hazards which may occur in the 8th year. But if the farmer has no security of tenure his interest in insurance would be confined to a particular season or year alone and compulsion would then have been grossly unfair. Fortunately however this position, no longer exists, as the Paddy Lands Act has ensured security of tenure to all tenants who could now be called upon to look at insurance from a long term point of view, as an essential part of operational costs and as a purchase of protection against unpredictable and unavoidable hazards.

Although we are settled in our own minds as to the necessity for crop insurance and the urgency for its introduction, neverthiess, the need for caution cannot be overstressed, and becomes apparent from the fact that so far only three countries in the world, U.S.A., U.S.S.R. and Japan, have undertaken all risk crop insurance schemes. The United States programme, in the first 10 years of its operation resulted in a

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1. Crop Insurance under Indian Conditions, Govt. of India pbn, p 11

net loss of 76 million dollars. Even today, after nearly 20 years experience the reason that in the U.S.A Crop Insurance is not available to all farmers on all crops is that it is still in an experimental and developing stage [1]. The Japanese programme is a heavily subsidised one, which Japan with her high degree of industrialisation can afford, but we cannot.

The normal difficulties which are attendant upon the introduction of a crop insurance scheme are aggravated here in Ceylon by the lack of adequate statistical data and trained personnel. In the United States a minimum of 20 years statistics is considered necessary before starting insurance in any crop, but in Ceylon reliable statistics on paddy is available only for a period of about 5 years.

However, as the Indian Report on Crop Insurance states "No amount cf research and study can provide essential information on certain features of the scheme and experimentation on an adequate scale can alone suffice for this purpose [2]." Hence a limited crop insurance pilot project in specially selected areas, representative of the whole country, would serve as an excellent background to the introduction of crop insurance to the whole Island. A limited scheme has the added merit of not risking too much, for if too much is risked without experience there is always the tendency to tighten up, often by strangling restrictions, which may warp the natural development of the programme.

The Insurance premium is worked on the basis of actuarial experience and in relation to the coverage that is offered. Consequently the tendency is to keep coverages low in order to keep premiums as low as possible. This is also influenced by a belief in the principle that crop insurance should take care of only catastrophic loss and also by a desire to make collection of indemnity under insurance less attractive than harvesting the crop, i.e. to lessen moral hazards. In the United

1. Federal Crop Insurance W. H. Rowe F. C. I. C. p. 1

2. Problems of Crop insurance under Indian conditions Govt of India Publication p. 18.

States coverages are set at a level commensurate with farmers' investments in the crop [1]. F.A.O. after examining the problem also recommended that in cases where the investment value in the crop can be ascertained protection may not exceed such value [2]. Insurance of only the investment in the crop, that is the cost of cultivation, is a good starting point, but nevertheless it is a concept that should not be pushed up to the level of a dogma, particularly when we are dealing with farmers who depend solely on the crop they expect to harvest. Under commercialised agriculture this is an adquate concept but when it relates to individual farmers who from the profits out of their crops expect to meet their expenses, pay their debts and carry on the business of living, then it does not go far enough. Thus while being a cautions starting point Insurance guaranteeing only the investment in the crop might not be adequate at least in the future.

Another very important feature of crop insurance is the unit of insurance. In Japan the unit of insurance is the individual field of the farmer, but in the United Sttates the unit of insurance includes all the interests a farmer has in different farms in an area. Under this principle premiums, coverages, and loss adjustments are all based on all those interests taken as one single unit, and even though a farmer may have losses in one farm he may not receive any indemnity if the crops from all the farms approximate to more than the coverage establised for his insurance unit. From an insurance point of view this is a better system to follow because the main idea behind crop insuranee is really to insure farmers against catastrophic loss. Even Japan is, veering towards this system and is experimenting with "houshold" insurance, in the light of past exprience.

Loss adjustment is the "key" to insurance and on the proper adjustment of losses would depend the success of any crop insurance scheme. One of the chief faults of the

1. All risks Crp Insurance by James L. Buckler U S D A pbn p.3.

2. Working Paper on Crop Insurance F A O p. 21

Japanese programme relates to loss adjustment[1]. There are two principles generally followed in the matter of loss adjustment. Losses could be adjusted either on the basis of individual farms or insurance units or on the basis of homogenous tracts. The latter makes for administrative convenience particularly in a country like Ceylon where the average size of a holding is about one acre. But this method has very serious shortcomings. For one thing it does not take into account individual farmers. The farmer who has had severe losses receives only as much as a farmer who has had no losses at all. This, to say the least is inequitable. It does not accept a distinction between good farmers and bad farmers, for all farmers in an area are grouped together. It does not take into account the personal factor which is very important. Furthermore under area loss settlement it is hardly possible to provide incentives to farmers to avoid losses by giving bonuses and rebates to individual farmers. Therefore despite the extra administrative work involved, adjusting losses on the basis of individual insurance units is a desirable feature in any scheme of crop insurance.

The idea of pro rating losses has been developed in insurance circles to safeguard reserves from being wiped out by catastrophic losses. Although it has the advantage of limiting risks, its great deficiency is that, it in a sense defeats the fundamental aim of crop insurance, which is to provide a fair and reasonable protection to farmers against losses. If the principle of pro rating is applied when catastropic losseses occur farmers who have suffered heavy losses may receive very much less than what they have been promised under their contracts. Under such circumstances they are no better than if they had no insurance at all, and they may even begin to question why they are being forced to put up with insurance payments at all.

Particularly in under-developed countries like Ceylon where farmers form part of a subsistence economy, even if loss claims ar settled on a preo rata basis, Government would

1. Crop Insurance in Japan W. H. Rowe p. 3.

be obliged to assist with other types of assistance such as free issue of seed material and even direct relief. It would therefore be more advisable for Government to underwrite the insurance contracts and in case of widepread catastrophic losses bear the difference between what premium collections and the insurance Reserve can comfortably pay and what is due under the insurance contracts. This would, while strengthening crop insurance and eliminating the evils attendant on direct relief, achieve the laudable object of crop insurance and direct relief supplementing each other, for crop insurance cannot be an complete alternative to relief.

In a economy like ours where the progress of farmers and farming is for the most part dependent on governmental initiative, crop insurance should be developed not merely to afford a negative protection, but in a more positive sense as part of a larger and comprehensive programme aimed at increasing production and raising the economic levels of the farmers. For instance, crop insurance can be tied up with the agricultural extension programme. Farmers could be obliged to follow minimum standards of cultivation as an essential condition under insurance. In this way the crop insurance programme opens up possibilities of being used in a direct way for ensuring the maintenance of good standards of cultivation. It could be used to induce our farmers to take to new methods of cultivation and modern cultural practices. Our tradition encrusted farmers have so far been showing a great deal of hesitancy in undertaking such practices but they may be encouraged into them by the offer of a higher coverage and a higher indemnity to those farmers who follow such practices. Crop insurance would thus be programmed as a direct and positive measure for increasing production.

Crop insurance is, thus a very important economic measure and would, if developed with care and caution prove extremely beneficial to a country like Ceylon where the fortunes of the entire nation are tied up with the fortunes of the farming community, even though the farmers are economically the weakest section of the population. However it should be remembered here that a Crop Insurance scheme has become possible in Ceylon today only because of the changes that have been brought about by the passage of the Paddy Lands Act. That Act has ensured security of tenure to tenants. Now they could be called upun to take a long term point of view of Crop Insurance, and not consider it as a means of collecting indemnities each year but as a very necessary safeguard for today, tomorrow and the future

THE DEVELOPMENT PROBLEM OF UNDERDEVELOPED COUNTRIES*.

by

A. D. V. de S. Indraratna

Before I go on to discuss the development problem of underdeveloped countries, it might, perhaps, be useful to make clear at the outset what I mean by "development" in general, and "underdeveloped countries" in particular.

It is difficult to define "underdeveloped countries" without introducing some element of arbitrariness. The group of experts appointed by the Economic and Social Council of the United Nations [1] defined them as countries in which the per capita real income is low when compared with the per capita real incomes of countries such as the U. S. A., Canada, Australasia and Western Europe, which I shall henceforth refer to as economically mature countries. Professor Nurkse[2] uses the words in a somewhat similar sense. He classifies the world population by income into three groups, and describes the countries in the lowest group as underdeveloped. The average per capita annual income (measured at 1949 purchasing power of the dollar) of these countries is 54 $ or

* This is a revised version of the talk given by me to the University Economic Society on 10th March 1958.

I am grateful to Mr. F. R. Jayasuriya and Dr S. J. Thambiah for reading through its first draft and making a few comments. But for the views expressed and any errors and omissions, here, I am solely responsible.

1 United Nations, Department of Economic Affairs—Measures for the Economic Development of Underdeveloped Countries. New York, 1951. p. 3.

2 Nurkse, Ragnar—Problems of Capital Formation in Underdeveloped Countries. Oxford, Basil Blackwell, 1955. pp. 63—64.

£ 19 or Rs. 257, as againsts 310 $ or £ 111 or Rs. 1476 for the middle income countries, and 915 $ or £ 327 or Rs. 4360 for the high income countries. These definitions, however, are not 'altogether satisfactory, because the most we could conclusively deduce from the criterion adopted in these definitions is that these countries are relativaly poor. The word underdevelopment, to my mind, also carries with it the notion of a desire more or less keenly felt for economic development and a potentiality for such development. Supposing all the available resources in Antartica or even for that matter in Mongolia were developed, they would not in the present state of our technical knowledge, be able to realise a per capita real income even approximating that of Nurksian middle—income countries. Is it appropriate to call them underdeveloped? Before one christens any country as underdeveloped or mature one must ascertain whether the country is poor in the resources necessary for development.

Professor Viner [3] made an attempt to meet this difficulty. According to him a country may be underdeveloped irrespective of whether it is densely or sparsely populated, whether it is relatively abundant in capital or relatively deficient, and whether it has a high or low income per capita. His basic criterion of underdevelopment is that the country should have "good potential prospects" of maintaining or raising the existing level of living when the population is respectively rising or stationary. But it is not, however, quite clear what he means by "good potential prospects."

Professor Frankel [4] points out the inadequacy of known definitions, but fails to give his own. Nevertheless, he rightly points out that "whether a society is regarded as economically

3 Viner, Jacob—International Trade and Economic Development, (Lectures delivered at the National University of Brazil). Oxford Clarendon Press, 1953. pp. 94—120.

4 Frankel, S. Herbert—"Some Aspects of International Economic Development of Underdeveloped Territories" in The Economic Impact on Underdeveloped Societies, (Essays on International Investment and Social Change). Oxford, Basil Blackwell, 1953. p. 56,

developed or underdeveloped will depend on the specific criteria of development applied by the observer and the position occupied by him." In line with this I shall like to classify a country as underdeveloped only if it satisfies the following two criteria: (1) It should have a low per capita real output relative to mature economies; (2) It should possess known resources which lie idle at present because the necessary real capital and "know—how" are not available. If these complementary factors of production can be obtained the resources can be made productive. My defintion can therefore be restated, if a little elaborately, in this way: A country which has (1) a low per capita real income relative to mature economies, (2) a low rate of per capita reproducible capital, (3) a favourable ratio of unused resources to population, and (4) a scarcity of entrepreneurship in the population, can be termed underdeveloped.

Development can be said to take place when (a) the total real output is increasing and (b) at the same time the per capita output is not decreasing. To many, economic development means increasing per capita real output. But I have adopted the double criteria to take stock of the relatively rapid rate of growth of the population of these countries, as well as to make some allowance for the possibility of per capita output rising with a fall in the total output on account of a sudden decline in population.

Economic development in underdeveloped countries consists of a series of economic activities directed towards bringing about an increase in productivity in the economy as a whole, as well as of the individual earner, and also an increase in the ratio of earners to the total population. The various phases of increasing productivity and of the structural changes in the economy which constitute the process of development may be concerned with such fields as utilisation of resources, acquisition of skill and knowledge, selection of relevant production—techniques, labour efficiency and capital formation. Most of these changes must be forced upon the economic life of the society from without, unlike the case of Schumpeter [5], which

5 Schumpeter, Joseph Alvis—The Theory of Economic Development. Harvard University Press, 1954.

leaves it almost entirely in the hands of the private entrepreneur. Schumpeter in his "The theory of Economic Develop ment," considered development to consist primarily in the carrying out of new combinations affecting mainly the following categories of economic activity :

(1) The introduction of a new good or a new quality of a good.
(2) A new method of production.
(3) A new source of supply.
(4) New markets.
(5) New organisation of industry.

He insists that his concept of development comprises only such changes in economic life as are not forced upon it from without, but arise by its own initiative from within. His concept of development may apply to mature economies but not to underdeveloped countries like ours, in which the economic structure, social framework, attitudes and ethical values of the people are very different from those of the former which are more favourably disposed towards innovation. My point here is that both a different definition and a different theory of economic development are necessary to take account of the conditions of the underdeveloped countries[6].

Having thus tried to explain what I mean by an underdeveloped country and what I have in mind when I talk of economic development, I should also wish to mention, before coming to the discussion of the development problem itself, that there should be certain aims and targets of development. In most countries the immediate need for economic development is to raise the standard of living, which can be attained by a rise in the per capita real income to be used for the attainment of (1) (a) decent levels of nutrition, (b) decent levels of housing and (c) decent levels of education, and (2) improvements in the field of employment and income distribution. Targets of development depend on the extent to which the above can be achieved or it is desired to achieve

6 The same point of view has been put forward by Professor Myrdal Cf. Myrdal, Gunnar—Economic Theory and Underdeveloped Regions. Duckworth and Co. Ltd., 1957.

them, taking account of population changes and within what horizon it is desired to achieve them. I shall come to this aspect later on.

In discussing the development problem of underdeveloped countries one is apt to make the mistake of generalising excessively. Some generalisation is inevitable when one is not fully conversant with the conditions of all underdeveloped countries. To be on safe ground, therefore, I may only say this: The major development problem in underdeveloped economies like Ceylon can be briefly stated as the existence of a chronic state of underemployment of the available manpower and an imperfect utilisation of the natural productive resources. The former appears largely as disguised unemployment in agriculture and industry which is still largely in the handicraft or cottage craft stage. The natural resources may lie idle reflecting the inability to contribute to profitable production under the existing scarcity of real capital and the rigidity of the productive system. The resulting low productivity is responsible for the low standard of living.

Some advocate increased money outlay as a remedy because there are both a large volume of unemployed labour and unused natural resources. But the beneficial effect of an increase in money outlay depends not so much on the existence of idle resources, but on the elasticity of their supply. The existence of idle resources is, in the short run, made less significant by the scarcity of complementary factors of production, the great measure of immobility of labour and structural rigidity, (the specific bottlenecks and the dependence on imports for complementary factors of production). The scarcities of specific factors are so great and expansion so much checked by the lack of technical skill and capital equipment that "full employment" is reached long before underemployment of labour and imperfect utilisation of natural resources are reduced. This situation can be represented by the working of the Quantity Equation ($MV = PR$, where R is real income), in a classical full employment economy: An increase in money outlay (M) would, under the above conditions, lead to an increase in the price level P, with R remaining more or less constant.

RESOURCES FOR DEVELOPMENT

The development problem can be solved if all the factors necessary for economic development can be simultaneously obtained. The factors necessary for economic development may be broadly classified as (1) generating factors such as entrepreneurship, technology, capital formation and (2) conditional or limitational factors, namely natural resources, population and social institutions. In other words, real output per head depends on some six factors: entrepreneurship or "the will to economise" (to borrow a phrase from Professor Arthur Lewis)[7] technology, the stock of capital, the size of the population, natural resources and the institutional framework. The same thing can be restated in this way: The problem of economic development centres round the question of enterprise and technical skill, the problem of capital (both real and finance), of resources, of markets, and of the institutional framework necessary for economic growth.

In a paper of the present scope it is not possible to discuss in detail all these factors. Therefore I may give more space to the relatively important ones to the neglect of the others.

Entrepreneurship or the "will to economise" is a thing which cannot be created from without but which grows from within, with changes in the economic organisation and in the process of economic development. In a developed industrial society like the U. K. or the U. S. A., this factor is of considerable importance in determining average productivity, while in an underdeveloped economy like Ceylon it is markedly lacking. That is one important reason why, an economy like Ceylon is not favourably disposed towards innovation, as a country of the Schumpeterian model.

In technology I include the procurement of human technical skill and the selection of techniques of production. Technical skill may have to be imported to begin with, but it

7 Lewis, W. Arthur—The Theory of Economic Growth. George Allen and Unwin Ltd. 1955.

is bound to improve with economic expansion. Given the necessary capital and natural resources, it is not so difficult to obtain technical skill and knowledge. By the definition of underdeveloped countries adopted here, I limited my discussion to those with a plentiful supply of labour. For instance, in a country like Ceylon, where there is at present a practically "unlimited"* supply of labour, technical skill can be acquired to some extent, by sound technical education and training programmes. The external assistance too, in this field, has been far more liberal than the external financial assistance. Both the Technical Co—operation Scheme of the Colombo Plan and the Technical Assistance Programme of the U. N. and its Specialised Agencies have undertaken to provide both expertise and training facilities, to these countries. Ceylon, for instance, has received up to the end of 1956, as many as 211 experts, and training facilities for 710 Ceylonese. Of the experts, 17 have been in the field of agriculture, 21 in education, 56 in health, 22 in industry and trade, 41 in engineering and 26 in fisheries. Of the trainees sent out, 117 have been in the field of health, 129 in agriculture and forestry, 99 in industry and trade and 85 in engineering. Under the United Nations' auspices training facilities have been provided for 93 Ceylonese. Approximately Rs. 4 million worth of technical equipment has also been received from these two sources[8].

The selection of production techniques is a bigger problem than the procurement of technical skill. Production functions applicable or suited to mature economies may be quite out of place in underdeveloped countries. This aspect I shall deal with, in greater detail, when I discuss the problem of capital.

* An "unlimited" supply of labour may be said to exist when the ratio of population to natural resources is such, that the marginal productivity of labour is either negligible, zero or even negative. Cf. Lewis, W. Arthur "Economic Development with Unlimited Supplies of Labour" in the Manchester School of Economic and Social Studies, May, 1954. and "Unlimited Labour:" Further Notes by the same author in the same journal, January, 1958.

8 The Colombo Plan for Co—operative Economic Development in South and South East Asia. Fifth Report of the Consultative Committee, Wellington, New Zealand. December, 1956.

By our definition, there is no scarcity of natural resources; the problem is how to bring the available resources into productive use, and this is the crux of economic planning. By way of describing the natural resources of a country, however, I may add this here. Natural resources can be divided into two broad groups: land resources and sea resources. Land resources which are by far the more important, are of three kinds: agricultural, water and mineral resources, while sea resources are fisheries, building stones and salts.

In this paper, it is not possible to devote any special time to a discussion of the institutional framework necessary for economic development. But reference to it, whenever relevant, will be made in the discussion of other aspects of the development problem.

The question of population, however, occupies a central place in any study of economic development. The size of the population is important from a number of angles. It will determine not only the size of the market but also the size of the labour force. The increase in the population also means, other things remaining the same, a fall in the per capita income. The fall in the per capita income will reduce the size of the market particularly for industrial goods. The size of the market ultimately depends not so much on the size of the country or the size of the population as on the per capita productivity. (I implicitly assume here an equitable distribution of the national income). Development should be planned with a view to absorbing the increase in population as well. If employment increases in proportion to the increase in population and there are constant returns (or real income rises in proportion to the increase in the volume of employment) we have a constant per capita income. If the total real income increases with the per capita income remaining the same the demand for agricultural products expands, but the demand for industrial products increases comparatively very little. Therefore in the initial period at least, in order to promote the growth of the industrial sector (I assume here a balanced growth of sectors), not only an effort should be made to increase the per capita income, but also an effort

should be made to substitute imports by local industrial production. It could be easily shown how a process of cumulative growth can be sustained, with an initial substitution of imports with home production[9]. This also will save the foreign exchange much needed for the import of specialised capital equipment.

Capital is the scarcest factor in the underdeveloped countries and let us exmine this in detail next. I treat capital formation here as the proces of creating tangible plant and equipment or fixed assets or capital equipment (whichever term we may choose to use, which either directly or indirecly produces goods or services). This is one aspect of the problem of capital. The financing of capital formation (or the procurement of funds for increasing the capital stock) is the other aspect. These two aspects are separated, here, only for convenience of analysis.

As mentioned earlier, the main prerequisites for economic development are (i) natural resources (ii) technical skill (iii) entrepreneur ability or the will to economise and (iv) capital. In underdeveloped countries, the procurement of capital is relatively more difficult than the procurement of other factors. I shall now go on to show (i) why, theoretically speaking, the problem of capital formation occupies such an important place in any study of economic development, (ii) examine briefly the causes of low capital formation in underdeveloped countries in general, (iii) discuss various ways of promoting capital formation in underdeveloped countries and (iv) show what criteria should be applied in order that relatively abundant factors may be most advantageously used.

CAPITAL FORMATION

Economic growth can also be defined as the rate at which the stock of capital goods increases. It could reasonably be assumed that net national output which ceteris paribus determines the level of consumption is the function of change in

9 Salgado, M. R. P.—"Planned Industrial Development and the Problem of Markets" in The Ceylon Economist, Vol. 4, No. 1, January, 1958. pp. 4—24

the stock of capital equipment. To put it more simply, with a given labour supply, techniques and natural resources, output is an increasing function of capital stock. If, therefore, it is desired to raise the living standard of the people through an increase of national output the rate of capital formation must be increased. The level to which this must be raised depends mainly on three conditions: (i) to what extent it is desired to improve existing living standards (or the targets in view) (ii) the annual rate of population growth and (iii) the output-capital ratio at the margin or marginal return of investment. The last of these depends not only on the rate of capital formation but also on the composition of capital stock. The composition of capital stock is specially important in those underdeveloped countries where most of the available savings are often invested in relatively unproductive enterprises whose marginal social costs may be higher than the marginal private costs. Most of the savings of the richer classes of these countries are used for conspicuous expenditure; savings may be invested either in real estate (housing and land) or hoarded either in the form of gold or local currency. If new houses are built capital stock is increased but no external economies are created and productive capacity not increased. If savings are used to purchase houses or land no new capital is created, there being only a transfer of ownership; new savings in this case may be equal to sellers' margins which may be dissipated by landlords in their conspicuous consumption. If they are used for imports as they are likely to be in these countries, there will be adverse repercussions on the balance of payments. In the case of hoarding, no new capital is created; hoarding of gold or jewellery or foreign currency is deflationary since they cannot be mobilized to increase purchasing power directly, while hoards of local currency may be perhaps tapped by proper savings campaigns. Therefore it is necessary not only to step up the savings of the community to a required level but to divert them to productive channels depending on specific requirements, so that maximum external economies are created, and difference between private and social costs reduced. As I have shown earlier, this cannot be left in the hands of the private entrepreneur as Schumpeter envisaged, but must be forced from without.

In this connection, the role of the state in the economic development of underdeveloped countries must be emphasised. It is not possible to discuss adequately, here, the special role that governments of underdeveloped countries have to play in their economic development. I may only say, that at least in the initial period of development, the state may have to be the biggest entrepreneur and shoulder the greatest part of the development responsibilities. While being aware of the peculiar characteristics or conditions of underdeveloped countries which place limitations on the activity of their governments, it must be admitted that governments have four important functions in the economic development of these countries[10]. They are :–

(i) The deciding and executing function i.e., deciding on and accepting certain development plans and executing them,

(ii) The nursing function i.e., provision of a steady flow of funds to the private sector and granting of other inducements to the private entrepreneur.

(iii) The pruning and clearing function i.e., the removal of obstacles, social and otherwise, in the way of development, and

(iv) The controlling and guiding function, by designing the fiscal and the monetary system for development purposes[11].

All these come within the field of planning, which in itself forms the basis of an entirely new study.

My main task in the remaining part of this paper is to examine the causes of low capital formation in underdeveloped countries, then find out ways of promoting it, what

10 Deyrup, Felicia J–' Limits of Government Activity in Underdeveloped Countries" in Social Research Vol 24, No. 2. Summer 1957.

11 Bonne, Alfred–Studies in Economic Development (with special reference to conditions in the underdeveloped areas of Western Asia and India.) The International Library of Sociology and Social Reconstruction, Routledge and Kegan Paul.

criteria should be used in selecting relevant production techniques and what methods of finance are open to these countries.

Causes of Low Capital Formation :— Capital formation is mainly a function of savings. The concept of the "vicious circle of poverty" applicable to these countries is well known;[12] where the per capita income is low, savings are low, low savings lead to low capital, and low capital to low productivity, to low income and low savings and so on. But it is more reasonable to suppose that savings depend not so much on the per capita income, as on the degree of income inequality. That is why it is so often argued, that in these countries economic inequality promotes savings, and it is also for this reason that inflationary financing is advocated to increase the share of profits; for the ratio of savings to money national income is a function of the ratio of profits to money national income because profits are the main spring of savings[13]. If, however, the average income through time increases, it is reasonable to assume that the annual income saved will also increase, though of course it must be admitted that the extent to which average income must be raised before it begins to yield positive savings is quite considerable. To promote savings through inequality is easier, but in these countries where the standard of living of about 90% of the people is very low it is economically the most inequitable and politically the least expedient. In Ceylon, for instance, 91% of income receivers get onlv 59% of the total income while top 10% enjoy about 43%[14]. Since raising the standard of living of these people is the immediate reason for economic development, to promote savings by raising the per capita income without further depressing their living standard seems preferable. A start has to be made somewhere to break the vicious circle of poverty by increasing the per capita productivity.

12 Nurkse. op. cit., Chapter III.

13 Lewis, W. A–The Theory of Economic Growth. P. 227

14 Survey of Ceylon's Consumer Finances. Central Bank of Ceylon, Colombo, 1954. P. 16. Table 10.

Ways of Promoting Capital Formation :— A higher productivity can be achieved by having (a) a higher rate of capital investment per worker, (b) an adequate physical fitness of workers, (c) the spread of elementary education, as a rule, by the introduction of compulsory school attendance, (d) a higher standard of scientific research and knowledge and the ability of entrepreneurs and managers to turn them to good account and (e) a system of incentives directed at releasing optimum efforts on the part of workers. Capital formation may occur in (a) agriculture through the use of better tools and the application of fertilisers and through mechanisation, irrigation and better processing facilities, (b) in mining through new exploration, the use of more efficient extracting and refining equipment, (c) in industry through the growth of light consumer industries or the establishment of heavy industry and (d) in such other fields as housing, transportation, communications and power. Improvement in general education and health and technical knowledge are also indispensable concomitants of economic development; what precise ways, each country chooses depends on the availability of its productive resources, technical skill, labour and capital and on its priorities of develoment. In other words it depends on what lines or directions of development, an economy chooses, and what sectors can and should contribute most to capital formation. This is determined by whether the country continues specialisation in a few products or strikes a "balanced growth"[15].

Capital per worker depends on the production techniques chosen. This depends on the relative scarcities of labour and capital and the capital–labour ratio required by each degree of mechanisation. In selecting a particular technique it is sometimes confused that only the value of the final output should be the determining factor. In other words, the techniques that produce the biggest volume of output should be chosen. But this is wrong. Both inputs of labour and capital (assuming only two factors of production) and output should be considered in determining the production technique. In

15 The case for balanced growth in Ceylon will be argued by me in a forthcoming publication.

underdeveloped countries where there is an abundant labour supply relatively to capital, the capital intensive methods of developed countries which are relatively abundant in capital may be unprofitable. A number of production techniques (or production functions involving varying degrees of capital and labour intensities) may be available for a single line of production. It is up to the technical experts to make input—out put calculations of these alternative methods and select that method which gives the greatest increase in output for the least increase in inputs or the least decrease in output for the biggest decrease in inputs. Lot of work has to be done in this field in underdeveloped countries. Let us assume that the same investment I is made either on equipment for technique B with N labour or equipment for a more mechanised technique A with $N-\triangle N$ labour. If the difference in the output using the latter (assuming there is no index number problem) is greater than saving in wages, (or to put it the other way round, if $\triangle W$ in B technique is less than the increase in output, then the less mechanised B technique is more profitable. It could also be argued that if with I and with a still less mechanised technique D and with $N + \triangle N$ labour, the increase in wages is greater than the increase in output, B technique should still be preferred. It could therefore be said that the extent to which mechanisation is profitable depends on the relative scarcities of capital and labour on which their prices depend. It could also be shown that in underdeveloped countries (except those sparsely populated) for a long time to come labour will be much cheaper than capital and less capital intensive methods more profitable, "They will do better by developing efficient methods of using man power than by imitating capital using techniques evolved in advanced countries[16]" This applies to Ceylon today. But the time for mechanisation will come depending on the rate of development and on the absorption of surplus labour into industry when the increase in wages is no longer less than the increase in output at the B techniaue referred to earlier. This, however, may take more than a

16. Robinson, Mrs. Joan-The Accumulation of Capital. MacMillan, 1956 p.p. 101-126.

few decades. This section can be concluded this way: In countries where there is a surplus labour and a scarcity of capital, the former can be put into better advantage in the early stage of development by using it to expand transport and other public utilities, (public works sector) irrigation and other agricultural requirements. Then attention should be drawn to manufacturing industry, where the advantage of large scale production with highly labour intensive methods, is greatest, and to setting up of cottage industries in order to use immobile rural labour.

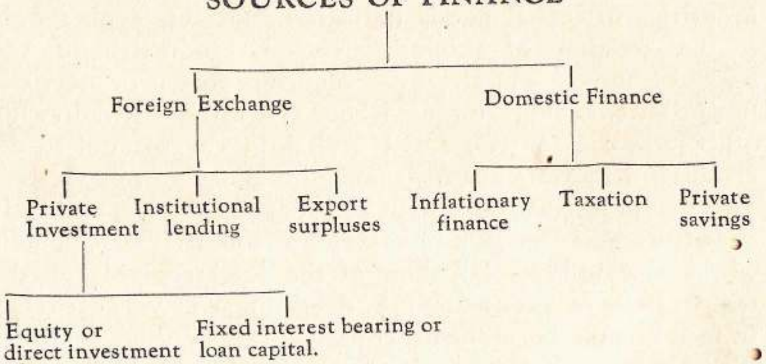
It could also be shown how the 'capital potential' in the absorption of disguised unemployed can be utilised to step up capital formation in the ways I discussed above either by institutionally planned schemes or self-help schemes.

The removal of surplus rural population from the land to investment projects is by far the best method by which capital formation can be promoted in these countries. It may be argued that capital cannot be created with surplus labour without reducing the output of consumption goods, for productive resources such as land and capital may now have to be withdrawn from consumption goods industries to capital goods industries. But this applies only to the creation of produtive capital, productive in the sense of 'now' or already producing goods or services. But by withdrawing surplus labour and without withdrawing other scarce resources, social capital in the form of roads, viaducts, irrigation channels and buildings can be created. This would increase the output of goods and services indirectly and after a time lag. In underdeveloped countries where public works and utilities fall short of the level required for the required rate of economic growth, this may be very desirable. In fact, it could be argued that particularly in those countries like Ceylon, where there is plenty of cultivable land, not at present cultivated, surplus labour can be removed for creating productive capital without reducing output in other sectors. Colonization schemes serve as an example. To whatever projects the Government decides to shift this surplus rural population, financing of such projects must be least inflationary. If it is done by borrowing from the public or budget surpluses, inflationary effects will be at a minimum. But if it is done by credit creation effects will be relatively much harmful. Not only should capital formation be pursued with the least inflationary pressure but it should also proceed with the maximum absorption of the surplus labour. It should try to reduce the present disguised unemployment, as well as make provision for the absorption of the annual increase in population, in these countries.

FINANCING OF ECONOMIC DEVELOPMENT

The financing of economic development too presents peculiar problems to underdeveloped countries. Certain methods of finance like inflationary finance, which may be innocuous in mature economies, (provided there are unemployed resources) are positively injurious to underdeveloped countries. For such reasons financial planning occupies a very important place in an overall plan of economic development of these countries. Sources of funds for development can be classified as in the diagram below.

SOURCES OF FINANCE



The need for external finance arises from the requirement of foreign exchange both for the import of capital equipment and technical skill and for the additional import of consumer goods resulting from the process of economic development. The former is the direct need, the latter the indirect one.

Any programme of economic development requires a certain precentage of foreign exchange and this can, as shown in the diagram, come from private foreign investment which may be equity or fixed interest bearing or from foreign governments or institutions or from the use of external assets created by export surpluses. The extent of foreign exchange requirements in any programme can be shown by an algebraic example.

(i) M = net increase in imports generated by the progamme,

(ii) D = direct expenditure on imports for the programme,

(iii) W = expenditure at home (this I shall call "spot" expenditure),

(iv) T = taxes specially levied on the present income (Y) to finace the programme,

(v) Y = domestic income,

(vi) m = marginal propensity to import,

(vii) g = proportion of marginal income automatically taken away in the form of taxes (additional to T),

(viii) c = marginal propensty to consume domestically produced goods, and.

(xi) s = marginal propensity to save.,

T is assumed to reduce consumption expenditure by an equal amount.

Then $\Delta Y = \frac{1}{m+g+s}(W-T)$

$$M = D + m\Delta Y = D + m\,\frac{1}{m+g+s}\cdot(W-T)$$

Indirect requirements of foreign exchange as given by $m\frac{1}{m+g+s}\cdot(W-T)$ will be the greater the greater the marginal propensity to import (m), and smaller the margjnal rate of taxation (g) and the margionl propensity to save (s). In primary producing countries like Ceylon, m is likely to be relatively high and g and s are likely to be relatively low. Indirect requirements could therefore be relatively large and this could be greater or less than direct requirements depending on whether $\frac{D}{W-T}$ is $>\!<$ m. $\frac{I}{m+g+s}$. Given the level of domestic saving in these countries, if they are to step up capital formation, without high taxation or inflation, they will need additioanl foreign exchange equal almost to the whole cost of their additional programme, (where $W + D \longrightarrow > M$, where m. $\frac{I}{m+g+s} \longrightarrow > I$).

Theoretically speaking, while foreign borrowing may appear to be the best method of raising capital stock of these countries there are serious objections and impediments to their inflow.* My point here is that an increased demand for foreign exchange is bound to ensue from a programme of development. This is one of the big problems facing some of the underdeveloped countries like India, which have embarked upon development plans.

I should like to conclude this section as follows. No development programme can be carried through successfully, without creating an additional pressure on foreign exchange resources. Foreign exchange may be obtained through (1) the mobilization of existing hoards of gold and foreign currency, (ii) by foreign assistance, and (iii) the building up of export surpluses. The hoards cannot in practice be either located or mobilized conveniently. Therefore not much reliance can be placed on them. It should, however, be the concern of any government to discourage such hoarding habits by propaganda and the creation of development consciousness. Foreign aid from either the private or the instituitonal sector seem to be the most desirable from the point of view of external and internal stability of these countries. But, very little can be expected from this source for a number of reasons. The sources of foreign exchange which can reasonably be counted upon (in addition to the little external aid from the Colombo

* I have disussed this in detail elsewhere. cf 'The Economic development of a Primary producing Export Economy: Experience and Possibilities of Ceylon. Thesis approved for the M. Com. degree of the University of Birmingham. (unpublished)-

Plan, I. B. R. D., the U. N., and other such external agencies) are accumulated external assets and future trade surpluses. In this connection, I may exphasise the need for maintaining (at least) the present value of exports, and the need for import substitution as far as possible. (This implies a balanced growth of sectors). Indirect requirements of foreign exchange should also be minimised by import restrictions. In primary producing countries like Ceylon which are subject to wide fluctuations of their export prices relative to their import prices, the foreign exchange problem would be more acute, because they have always to set apart a 'safety margin' of external assets to take care of unforeseen slump conditions in their export markets. This safety margin is bound to be larger when these countries have embarked upon development programmes, because of the internal inflationary pressure that is bound to arise as a result of development, even in spite of it being carefully controlled by direct measures.

I shall now attempt to show in what ways the counterpart local funds for the 'spot' expenditure of development programmes, can be procured. As shown in my diagram, they could be obtained in three ways: credit creation, savings of the private sector and budget surpluses or taxation.

Inflationary Finance:—

In many underdeveloped countries, as has been mentioned earlier, incomes, and therefore savings are low. The level of taxation required to provide funds in the initial stages of development programmes may be higher than governments are willing to impose for political reasons. This may, perhaps, induce the Government to adopt the path of least resistence, deficit financing by credit creation. This method of financing is harmful in view of the conditions of these countries particularly if deficit financing is used to finance capital construction in the public works sector.

I mentioned earlier, that it is not the shortage of unused resources that presents a problem in these countries, but the relative inelasticity of supply of these resources. Deficit financing under such circumstances, could lead to both internal and external disequilibrium. Additional money incomes will create an additional demand for imports and also raise the prices of domestic goods. The former will lead to balance of payments difficulties. The latter may depress still more the existing living standards of the majority of the people, thereby defeating the very purpose for which deficit financing would have been probably resotted to. If exchage control or import quotas are used to counteract the adverse effects on the balance of payments, the pressure on domestically produced goods will be higher. Rationing and price control may then be advocated. War economics of primary producing countries has shown us that these measures cannot do it alone. [17]

The planners must be aware of these difficulties and if inflationary finance is used at all, it must be for the removal of obstacles, which restrain the flow of consumer goods, for example, the financing of an agricultural extension service; but for the purpose of creating 'social overheads' only if the other methods are inadequate; even then it should be used with extreme caution and should be accompanied by fiscal and monetary measures and other direct weapons which are designed to curb inflation at home and to prevent adverse effects on the balance of payments. The best methods of financing, therefore, open to these countries are domestic savings and taxation.

Promotion and Mobilization of Domestic Savings:—

Fiscal policies exercise an important influence on the direction and extent of the mobilization of domestic capital. Fiscal policy, for instance, can help in the mobilization of savings by counteracting inflationary pressures, thus providing a more favourable climate for voluntary personal savings. To promote personal savings, (which are at present negligible), the following general measures may be advocated; (i) measures of general economic policy, such as the avoidance of inflation

17 Prest, A. R.—War Economics of Primary Producing Countries. Cambridge, 1948. also by the present writer—The Economic Development of a Primary Producing Export Economy: Experience and Possibilities of Ceylon. opit. Ch. III.

and the pursuit of economic and financial stability, (ii) the tailoring of Government securities to suit the different requirements of different classes of savers, (iii) measures to improve the provision of banking facilities (such as mobile banking in rural areas), and (iv) publicity through propaganda and education to encourage small savings. The mobilization of savings, particulrlay among the subsistence farmers depends to a considerable extent on the provision of security against crop failures and on the financial assistance required for economic cultivation. The Government can make a significant contribution to sound economic development, by creating a favourable setting for privat saving and for private investment. This can be done not only by providing a good example in its own 'financial housekeeping' but also by establishing the necessary institutional framework, by providing an atmosphere of political and legal security and by setting up an honest and efficient administration. The Government effort is also needed to mobilize the 'savings potential' in the disguised unemployed.

Taxation:—Generally speaking, taxation provides a very effective method of raising the finance required for public investment. In economies where private investment is as, important if not more important than, public investment, the raising of sufficient investment funds for the public sector may seriously conflict with private inducement to invest. This may not happen if taxes are so chosen as to aviod (or at least to minimise) unduly adverse repercussions on the rate of capital formation in the private sector. To raise taxes by taxing the poor (which is relatively easy in underdeveloped countries), conflicts with egalitarian ideals. Thus a judicious system of taxation must strike a balance between the principle of equity, which calls for a progressive income taxation, but is likely to have harmful effects on private investment, and the principle of incentive, which favours a less progressive one, and taxes expenditure more heavily than income.

In underdeveloped countries public finance assumes a new significance for two reasons, firstly because private saving and invesment is small and secondly because there is a great need to direct resources into desirable investment channels. There are two main functions of taxation, (i) function of revenue and (ii) function of direction. Both these functions are more important in underdeveloped than in developed economies. There is less objection to the use of taxation as an instrument of forced saving where voluntary saving is meagre. In order to reduce the disincentive effects of taxation, it may be more desirable to tax expenditure rather than income. In underdeveloped countries, where for a long time to come, greater reliance has to be placed on indirect taxation, i, e., excise and customs duties, taxing expenditure may be administratively easier, and, to conform to egalitarian ideals, taxation could be heavier on luxuries, as against necessaries (in other words on commodities for which income elasticity of demand is high).

In its directive aspect, taxation has to perform he function of diverting the resources, that would otherwise be used for consumption or non-development expenditure. Taxation together with the other apparatus of fiscal and physical control must be planned to take account of the specific economic and social conditions of these countries. The planning authorities must not overlook the preponderence of agricultural production, the relatively less monetised subsistence sector, the dependence upon foreign suppliers for manufactured goods, the imperfection or the absence of capital markets, the pressure of population, the general immobility of labour, the lack of external economies, which might promote private investment, and inflationary bias of the rigid economic structure.

The outlines of a tax structure tailored for development will look substantially different in an underdeveloped country from those in a mature economy like the U.K. The relevant differences are these: (i) in an underdeveloped country more of the responsibility for development, must be shouldered by the Government than is necessary where industrial skills are already available and other external economies operate; there are two broad types of projects which require Government investment, (a) social services: health, education and others and (b) investmet in the constructional sector. By developing

the constructional sector, (where private enterprise is not able or ready to invest), private investment in complementary activities can be encouraged. Providing the basic industries is the responsibility of Government finance, while the actual production of goods and services can be left to be undertaken by private enterprise. (ii) The Government of an underdeveloped country needs more tax revenue since it faces considerable difficulty in borrowing at home and more in borrowing abroad. (iii) A much greater burden in achieving the "optimum" rate of growth falls on fiscal policy than in developed economies like the U. K. where monetary controls and other direct weapons are relatively effective[18].

CONCLUSION

In discussing the development problem of underdeveloped countries, I first of all, clarified what I mean by underdeveloped countries and what I mean by economic development. Second, I went on to show that the existing economic and social conditions of underdeveloped countries, present problems of development, which are not equally shared by their developed counterparts. It was emphasised, that while in mature economies investment responsibilities can be left largely in the hands of the private entrepreneur, in underdeveloped countries they become chiefly the responsibility of the state (at least in the initial stages).

Factors necessary for development are many. Simultaneous procurement of these factors needs economic planning. It is overall planning of underdeveloped countries that is necessary; mushroom plans made in isolation would be of very little use. A co—ordinated system of planning must take account of the repercussions of Government expenditure on the private sector; it should include not only investment programmes, but financial planning as well, namely the choice of the best methods of finance open, and the designing of fiscal and monetary structure to suit development purposes. Planning authorities must always be aware of the peculiar

18. Hicks, Mrs. Ursula - "Direct Taxation and Economic Growth", in Oxford Economic Papers, September 1956. p.p. 303-308.

conditions of the economies they are planning for, and make allowance for them in their plans. Targets must be fixed, lines and directions of development determined and investment expenditure planned to realize the targets with the given rate of population growth and the assessed output/capital ratio. Finance necessary for development of underdeveloped economies must be obtained largely from the home front.

In this paper, it was neither possible nor intended to cover in detail all aspects of the development problem of underdeveloped countries. I may have, as a result, either omitted certain aspects entirely, or not paid sufficient attention to certain others. My only hope, therefore, is that this paper will arouse further interest in the subject among at least some of my readers.

SHOULD WE BUILD AS THE ANCIENT SINHALESE BUILT?

by

M. K. SAMUEL

Dr. Sarkar in an article in the Ceylon Economist of January 1958 makes a plea that we should 'build as the ancient Sinhalese build'. This idea of using the methods of the ancient Sinhalese–particularly the institution of Rajakariya-seems to be gradually gaining currency among many.

There is no doubt that there is a large element of glamour attached to the idea of using the methods of the ancient Sinhalese. Their irrigation works command the admiration of modern engineers. This glamour attached to the prospect of going back to the days gone by seems to spring from a combination of factors. The most important of these seems to be misguided nationalism which sees everything that was in Ceylon as good and everything that the West brought in as bad. Others see in this retrogression a way out of our economic impasse.

In the social set-up of the ancient Sinhalese kingdom, the possession of land was the pivot on which the entire administration revolved. In a predominantly agricultural society, the importance and value attached to land is understandable. This enabled the organization of the machinery of the State and the decentralization of State authority on the basis of land-holding. "Even paraveni—right to land, which conferred heritable title in perpetuity and was the highest property—right in land which an individual could legally have, was, with few exceptions, subject to some service associated with the land–either personal service, or a payment in money or in kind. This was known as rajakariya. It attached to land, not the persons, and failure to perform rajakariya rendered the purappadu............"**

** Peiris, R.—'Sinhalese Social Organization. pp. 44—45.

The concept of service-tenure (rajakariya), wherein land was held on the basis of certain services rendered, was thus deeply ingrained in the life and thought of the community as a whole. In a society where money (as we know it now) was almost non-existent, "the system of service-tenures practically eliminated the payment of wages to State Officials who held land in consideration of rajakariya".* In the light of all this the place of rajakariya in such a social set-up is obvious. It was the basis of social stratification, administrative authority and the collection of taxes. One could almost liken it to the place that money occupies in the economy of today. Rajakariya was no one-sided contract. In the reciprocal scheme of rights and duties which bound one and all, rajakariya was the key-stone of the social arch.

The suggestion to introduce this system into an entirely different economic and social set-up is apparently beset with difficulties. In an economy characterized by division of labour, payments in money, and ability to draw on the experience of other countries, one can see that the climate is entirely different to that which produced rajakariya.

The intention of the author is to see whether even a slightly modernized version of rajakariya would aid solve the difficulties facing Ceylon.

As seen earlier, rajakariya 'attached to land, not the person'. It is obvious that we could not use this same criteria in enforcing rajakariya. If, however, we did, then, we would be placing an undue and unjust burden on a section of the population. If, as with Dr. Sarkar, this is to apply to every able bodied man in Ceylon, then, of course, we are introducing an element whose entire basis is different from the basis on which the rest of the economy is organized. If this were in any way to prove useful, it would be worth the trouble. It is left to us to see whether it could be of any worthwhile use.

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* Peiris. P. 124.

Dr. Sarkar suggests that labour should be paid in kind (food) together with a small cash allowance. If this, **in toto** equals the normal wage-rate, it may as well be paid in cash as now. If however, Dr. Sarkar's suggestion implies that in effect a lower wage-rate should be paid, it is, to say the least, undesirable. When the large majority of the people live at subsistence level, the payment of anything less than the normal wage-rate would amount to gross exploitation. This is indefensible on any. grounds-least of all being that of 'national service'.

There does appear in this article of Dr. Sarkar's a good deal of contradiction. It appears as though he is labouring to bring in a system of 'state exploitation,-not very different from the exploitation under capitalism as far as the labourer is concerned-while maintaining the ideological basis of the present structure of society-democratic socialism. It is difficult to see where his contention that 'the free supply of food should be a sufficient attraction for them to volunteer' fits in. This is almost tantamount to an attempt to exploit the need for food amongst the underemployed and unemployed. Moreover, this food is in no sense 'free'. If this is payment for labour (or part-payment), it cannot be regarded as 'free'-it is the legitimate price of labour.

In Dr. Sarkar's article the suggestion which is bound to give the most amount of trouble in actual implementation is without doubt the 'Construction Tax'. This tax is seen as an alternative payable by the able-bodied instead of actual physical labour. If this tax is very small in amount, it may not be worth the while collecting it; while, if it is high, it may not be possible to collect it at all from the mass of the people. If, then, in order to eliminate these difficulties, the tax is graded according to ability to pay, it becomes income-tax and one might as well call it so and collect it so.

This 'construction tax' may, thus, in effect be a coercive force impelling people-those who cannot afford to pay it-to perform rajakariya. Many would, under these circumstances, be forced to 'volunteer'.

The root cause of the difficulty apparent in the suggestion to use rajakariya seems to spring from the difficulty of finding the necessary capital for developmnt. Labour–especially–unskilled labour–there is in plenty in Ceylon. The dificulty is to find the wherewith-all to pay them and to buy the necessary machinery for them to use. In Ceylon, where even those who are willing to work cannot find work, it would be anamalous to force people in other fields also to come in here. The labour force is already there–the need is for money.

Given these conditions, what is needed is not the rajakariya of labour but the rajakariya of capital. If it is found necessary for the State to take unto itself most programmes of construction and capital formation, then private capital would have to be used for this purpose. I do not propose to deal with questions of compensation, expropriation and other allied questions as they are the realm of the politician and not the economist.

This rajakariya of capital would necessitate taking from those who have–as one cannot take from those who have–not. A steeper–more progressive–tax scale may be of much greater value than the 'construction tax'. Why not an upper limit on incomes? Or an expenditure tax on the higher incomes if they are not invested but spent on 'conspicous consumption' (Veblen)? There is no doubt that these measure would yield more than the 'construction tax' would have. Equally important is the fact that this woud be drawn from those who can afford to pay.

It may be well worth investigating the collection of capital on these lines as the State is coming on to take onto itself more and more of the process of investment in Ceylon. With the curtailment of unmitigated free enterprise, the question of investment incentives to the upper–income brackets is coming to be largely an academic question. In any case, private capital cannot, particularly in Ceylon, show any worthwhile reason why it should be allowed more freedom of action (if any). The collection of taxes on this basis would aid in providing more money for development, cutting

large private incomes and reducing social and economic inequality—all of which are equally important................if not aspects of the same thing.

A higher tax on corporation profits would provide more capital for development. The State could, in effect, force reinvestment of profits by imposing a 100% tax if dividends of, say, more than 10% are paid. Private enterprise, in the past, has been used to be given a more or less free hand. If it be the intention of the Government to give private enterprise also a place in the economy of the country, there is no reason why it cannot be made to fit into the general pattern of the economy. These high taxes would not kill private investment because—to use the argument of the apologists of private enterprise—some return on one's money would be better than no return. Of course, this depends to a very large extent on the security which the State could provide for investors.

Hand in hand with this, there could be a system of State Development Bonds paying as high a rate of interest as that paid for loans obtained from abroad. Tax—exemption could be granted to those investing in these bonds while corporations could be forced to reinvest a certain % of their profits in these bonds. These measures would while cutting down large unearned incomes also provide capital for development.

Economic development is not good for its own sake but for certain results that follow, If, along with economic development we can tackle the problems of social inequality and opportunity, it would greatly assist the process of economic development. Dr. Sarkar suggests an "appeal to their patriotism, the feeling that they are doing an act of self–sacrifice for the good of the country" to induce people to perform rajakariya. Would it not be better to direct this call to those who can make these acts of 'self—sacrifice' without inconveniencing themselves much?

If it be found necessary to find unskilled labour to work for below the normal wage—rate, voluntary organizations like the Ceylon Cadet Corps could be used for this purpose. Since this orgnization is already extant and maintained with

State funds, it could be easily adapted to fit National needs. This type of constructional work while helping to build up the country would also serve to build in these voluntary workers a spirit of national 'self sacrifice'.

Expenditure on the Social Services covers a very large part of the Annual Budget. It would be retrograde to suggest that this expenditure should be withdrawn but it may be possible to effect a number of economies. It may be possible to grade payments for both educational as well as medical facilities on the basis of ability to pay.

One of the main features of the economy of the island has been its overdependence on the 'Big Three', of Tea, Rubber and Coconut. As the demand for these products is very elastic, the economy of Ceylon has suffered due to fluctuations in demand over which we have no control. It is also worthy of note that, except in times of severe depression, the producers of these crops have always made for themselves a fair margin of profit. The greater part of this profit could be channelled into development through the intermediary of a State Trading Company which should have a monopoly of trade in these commodities. The producers could be paid a 'fair price' for their produce while the rest is used for development. In addition to obtaining additional money for development , this could aid in serving as a 'buffer' shielding the economy from the vagaries and fluctuations of external trade. (The above measures are suggested as an alternative to the nationalization of the estates and most of the above measures would become irrelevant if nationalization is undertaken).

In the organization of unskilled labour, a system of Labour Co-operatives could be set up which could handle most, if not all, Government contracts in that field. These Co-operatives formed on a local level and given some kind of quasi-Governmental status would enable not only the easy mobilization of labour but would also aid to eliminate the middleman in this field-the contractor.

A programme of public works alone would be totally insufficient. The need is for forms of permanent employment at fair wage-rates. It would be difficult not to agree in the main with Dr. Sarkar when he says that electrification, industrialization and education are the three levers of social change which should be given highest priority in any scheme of national development in Asian Countries'*. In doing so, however, we must not forget that Ceylon is essentially non—industrial now and that therefore development has to proceeded with caution. This is, of course, assuming that the intention is to develop without imposing undue hardships on the people in the name of 'development'.

We have wandered far from the original issue of Rajakariya, but yet this is unavoidable. All these proposals are but attempts to solve the problem of the lack of economic development and inevitably it is there that we return to. Planning for economic development is not purely the work of the economist. Since the issues at stake are so varied and the means to the goal so many, the initial burden, without doubt, rests on the shoulders of the politicain who must set out the broad framework within which the economist can work. If the political philosophy governing Ceylon is to be that of 'Democratic Socialism', possibly we will have much more to learn from the example and mistakes of India than from the more spectacular achievements of the U. S. A., Great Britain, or Russia.

Department of Sociology.
12. 4. 58

* Sarkar, N. K. — Population Studies March 1959. p. 216.

"VISIONARY" PLANNING

by

M. N. *Bandaranayaka*

The National Planning Council was established in October 1956. In July 1957 it brought out a document called the "First Interim Report" the only report it has publised so far. The main purpose of this report "is to provide a basis for a general discussion both in Parliament and outside on problems relating to the development of the Ceylon economy." It is not an outline of a national plan but an academic essay on a worn-out theme; not an attempt to analyse the basic economic problems of the country and indicate the methods of solving them but an intellectual exercise to elaborate certain theoretical concepts and justify the status quo; not a complete breakaway from but a continuation of the same ideas on economic development that prevailed under the previous Government.

Behind any National Plan—whether it is of Socialist countries like the Soviet Union or of "mixed" economies like India—there is a goal, at least an ultimate goal. At a meeting of the National Development Council of India on the 9th November 1954, the Prime Minister of India, Nehru stated:

> "Now the first thing about planning is to have a definite picture of where we are going. The picture need not be very rigid. But we must have some specific and definite veiws about the structure of society we are aiming at...............The picture I have in mind is definitely and absolutely a socialistic picture of society. I am not using the word in a dogmatic sense at all. I mean largely that the means of production should be socially owned and controlled for the benefit of society as a whole............"

The present Government of Ceylon has declared that its aim is to build a socialist society (although each Minister seems to have his own brand Socialism). But has the National Planning Council got a clear picture of where we

are going? Does it believe in Socialism? All that the Report says is "In the tasks of Planning, the Council had in mind the policy of the Government to work towards a socialist society." Note carefully, there is no admission that the Planners believe in a socialist society—only that they had the Government's policy in mind. The question is can the National Planning Council seriously plan the development of the countiy when it has no ultimate goal?

It is not only that the Planners have given no indication that they believe in a socialist society, but they have also equated socialist society with a mixed economy.

> "In the task of Planning the Council had in mind the policy of the Government to work towards a socialist society. This policy means at present a mixed economy in such spheres as trade, industry, agriculture etc. where both the public and the private sectors will play their part. The State will play a predominant role, particularly in services essential to the life of the community."

According to this the building of a socialist society means the maintenance of the public and private sectors as they are now with the State playing the predominant role in essential services (as it is doing today, providing economic and social overheads, distributing essential commodities etc.) In other words in building a socialist society we must maintain the status quo. By Socialism we understand the social ownership of the means of production, and in building a socialist society the public sector has to expand and the private sector to diminish until after a fixed time the private sector disappears. Hence it is meaningless to say that a socialist society can be built by maintaining the status quo.

It is clear that the National Planning Council does not want a radical transformation of the status quo; it wants the mixed economy to continue as it is. In this regard there is no difference between the approach of the U. N. P. and that of the National Planning Council to national planning. The U. N. P. too believed in a mixed economy and in the foreword to the bulky Six-year Programme of Investment 1954/55, Sir John Kotelawala stated,

> "The Government and the private sector are therefore like oarsmen in a boat. While they must row together, they must ensure that they also row in rhythm, for it is only in a spirit of co-operative endeavour that we can reach the promised land of contentment and prosperity that will give us confidence in ourselves as a nation."

The National Planning Council is thinking along the same lines. We are not certain whether the Government is also thinking on the same lines, and hence that the approach of the Planning Council is a reflection of the Government's outlook. But whatever it is, it does not seem to have occurred to the Planning Council that the two oarsmen will row in two different directions–one towards Capitalism and the other towards Socialism, and the country will not move in the direction we all want it to move.

The Planners are silent on the scope and speed of public investment, the relation between public investment and private invesment over a period, priorities in economic development etc. because they have no ultimate objective If they were guided by socialist considerations they would have paid attention to all these problems and given us at least the basic principles on which national planning should be based. There cannot be Socialism without national planing just as much as there cannot be national planing without socialist aims. Interference in private enterprise like restricting and regulating certain activities, State-ownership of a few industrial projects here and there, and the use of fiscal and monetary policy–do not mean national planing. National planning can be effective only when the State can plan the utilization of all the resources of the country to achieve its objectives, and this cannot be done until the State owns the principle means of production. The present crisis in the Indian Second Five Year Plan only confirms this.

The Report of the Planing Council points out "there is no real solution to the economic problem of Ceylon outside of an effective transformation of the productive capacity of the economy." Now one would have at least expected the Planing Council to recommend the ways of transforming the economy so as to increase production, remove unemployment and to secure a better distribution of income–even if they are not guided by Socialist considerations. But strangely enough the basis of planning of the Planners is given as follows:

> "The basic question that has to be asked then is how this necessary transformation can best be achieved and what measures and programmes will contribute towards it. An answer obviously requires a long term perspective. It is useful therefore to ask what sort of a productive structure is visualised for Ceylon over a long period, say twenty or thirty years from now, when the development process is well advanced and then to formulate programmes and plans of action which will enble this stucture to be built as rapidly as possible, It is essentially this approach that has guided the initial work of the Council."

The procedure followed by the National Planning Council is first to visualise a certain productive structure for Ceylon twenty or thirty years from now, and then to formulate programmes and plans of action which will build this particular productive structure. The implication is very clear. The National Planning Council is formulating economic development plans for the country *not* to build a socialist society, *not* to raise production, remove unemployment, increse income, reduce economic instablity and to secure a better distribution of income, *but* to build up a particular type of productive structure which they want Ceylon to have 20 or 30 years from now! Whether it increases production or secures full employment is incidental. National Planning is not considered in terms of human beings or production but in terms of a "vision" in the minds of our Planners!

This arbitrary approach of the National Planning Council is indeed unique. On what grounds have they chosen this basis of planning? If it is an attempt at original thinking-the National Planning Council has made itself only a laughing stock. As far as we are aware no other country in the world is planning on this basis. The moment you begin to plan on the basis of visualised pictures, you abandon objective for subjective criteria, and national planning for "**visionary**" planning.

What after all is the long-term economy visualized by the Planning Council? Although they consider it not useful to work out all the properties of this vision, they point out that it will have four major components:-

(a) Export sector.

(b) Dry zone sector.

(c) Peasant Agricultural sector.

(d) Industrial sector

But the present economy of Ceylon has these four sectors. Thus the long-term economy visualized by the Planning Council appears to be nothing new but the same old economy we have today! The Planning Council says we must imprve the productive potential of the export and peasant sectors, speed up Dry zone cultivation and create new industries. Surely an Interim Report by the Planning Council is not necessary to point these out. And to say that we must expand and improve the four existing sectors of the economy there was no need to visualize a long-term economy except for the purpose of investing the report with an air of seeming profundity.

It is also difficult to see how the Planning Council could visualize a productive structure for Ceylon thirty years hence. The longer the period, the greater is the number of unknowns and uncertainties. And it is no easy matter to predict what will happen in five years' time let alone thirty years. This can be illustrated by reference to Ceylon's exports. The Report of the Planning Council states that tea, rubber and

coconut are likely to be of great importance always and that we must increase their production. But have they taken the world market conditions into consideration? With the expansion of synthetic rubber industry, the increase of tea production in China, East Africa and India, and the growth of substitutes to coconut oil, we have no reason to be complacent about our export markets. We might sell all what we produce, but can we be certain that the price at which we sell will be economic in thirty years time?

The fact that the Planning Council was on the wrong track was even pointed out by the tea producers themselves. The following news item appeared in the Daily News of 10th December 1957.

> "The Government has been warned that if the proposal to double the the output of tea, now before the Planning Council is carried out a complete depression of the tea market would result. Mr. S. Pathmanathan who has put this point of view forward to the Planning Council has given reason to back his claim. He has pointed out that the two—way plan to increase production—expanding the acreage under production and using high yielding planting material' would probably bring down the cost of production through increased yields. But this would create a glut and bring about a depression of prices unless there is a corresponding expansion of consumption."

In fact there is a world overproduction of tea now and tea prices have fallen. Thus it is not reasonable to take a long—term view—as the Planning Council does—and keep on increasing production.

As a result of the arbitary approach to national planning, the Planning Council has ignored the basic obstacles to economic development in the country. The planners want the economy to have the same four sectors in 30 years time; that is their main concern. But whether the continuation of these four sectors will solve the basic problems of poverty, unemployment and production has not been considered. Take for instance peasant agriculture. The report says,

> "Here again is another major source of improvement in the future productive potential of the economy. Its attainment would involve a host of measures—the adoption of improved cultural practices, of better control over water, of suitable organizational relations, of marketing facilities and so on. Clearly a vigorous and full scale drive along these lines, aimed at stepping up yields and modernising techniques, must constitute a vital part of any development effort."

Improvement of technique, according to this, will solve the problem. But the Planners have not asked the question why peasant agriculture is still stagnant today despite various attempts by the previous Government to activise it. They have not asked why the policy of the previous Government failed, That improvement of technique and increase in production are not possible under the present system of tenure where over half the paddy fields are tenant cultivated and the rest are short of credit facilities has not occurred to Planners. In short it does not seem that they believe agrarian reform is a necessary precondition of increasing paddy production.

The opening up of the Dry Zone was begun about 20 or 30 years ago on the basis of "Colonization Schemes." Apart from being gigantic social service schemes providing homes and livelihood to the landless unemployed, these Colonization schemes have been economic failures. The National Planning Council has not considered whether Colonizations is the best possible way of developing the Dry Zone or whether paddy alone is the best crop for the Dry Zone. They assume these to be so and recommend "maximum utilization of all productive and cultivable land" In this connection it is important to note the remarks of Professor Hicks in respect to Drv Zone development.

> "But in fact more land (to be used in the same sort of way the existing cultivated land is used) is not available except at very great cost in the investment of capital; capital is soaked up at Gal Oya to provide the same facilities as are provided in the West Zone by Nature herself. The natural obstacles to this method of expansion can thus be alternatively expressed by saying that the capital costs of uniform expansion are prohibitive [1]."

The report for the National Planning Council by the Technical Working Group on Agricultural Development in the Dry Zone also says practically the same thing [2]. It says that the initial investment cost per irrigable acre for irrigation and settlements costs is Rs. 3,650. ! Apart from the high cost, the paddy yield in these new areas is not exceptionally high. It would be far more economic if the yield of the existing paddy lands is doubled without bringing new areas under cultivation of paddy, for by doubling the yield of the existing paddy land we can become self sufficient. Further it may be that cotton, sugar cane, oranges *etc.* are more suited to the Dry Zone than paddy. And the cost of growing these are likely to be lower than that of paddy. The Planning Council has not investigated into these problems at all, but just advised us to carry on with the present system of opening up and cultivating the Dry Zone. This again results from the peculiar approach to planning of the Planning Council—the desire to build up a visualized productive structure without examining whether that productive structure is conducive to higher production and increased human happiness and without considering the most efficient and economic ways of realizing the objectives.

As regards the fourth sector—Industry—the Report merely says Ceylon must have industries because development of the other three sectors is inadequate to create new employment

1. Reflections on the Economic Problems of Ceylon by J. R. Hicks' Central Bank of Ceylon Bulletin February 1958
2. First Interim Report, National Planning Council p. 36.

opportunities. Apart from mentioning that Ceylon has a plentiful supply of hydro,—electric power and constructional materials required for industrialization and that industialization provides a self-sustained and cumulative process of expansion, there is very little said about industry in Ceylon. There is however much theorization and speculation on industrialization. It states that the problem of industrialization is 'complex'' and "elusive" and "many difficult issues are involved". The relevant questions however are left unanswered. What type of industrial stucture should we have? Should we concentrate on heavy industry or consumer goods? Should, industry be large—scale or small—scale? Capital intensive or labour intensive? What tariffs and subsidies are necessary for industrialization? Is foreign capital necessary? These questions have been raised in the Report—but that is all. No attempt has been made to answer them.

These are the questions in everyone's mind, and one would have expected the Planning Council to do some original thinking on these problems and given the public at least some sort of idea of how we should tackle these problems. That is the essential task of National Planners. But what they have done is to ask the public to give the answers. The object of the Interim Report it is stated, is "to establish a general framework within which further processes of planning could be undertaken." But nothing of this sort has been done. There is no need for a Planning Council if it is merely to point out that Ceylon must have an industrial sector without examining the general pattern of this sector. Further the Report of the Technical Working Group on Industries has published in the Interim Report an impressive list of industries which might be established in Ceylon. The Planning Council has not even considered this. The Interim Report points out that it is in the field of industry "that planning should seek to make an effective contribution." But judging from the substance of the Report one wonders whether our Planners have made any contribution at all.

The Planning Councils has also attempted to "assess in concrete terms the physical potential for expansion that actually in exists respect of each of the relevant spheres." As this required the opinions of experts, Technical Working Groups were appointed to make a systematic study of the potentialities; these groups consisted of personnel from the Planning Secretariat, and other officials and people with technical experience. There were nine Technical Working Groups to cover (*a*) Tea (*b*) Coconut (*c*) Cocoa (*d*) Dry Zone (*e*) Paddy yield (*f*) power supply (*g*) atomic energy (*h*) Demand for electric power in Ceylon and (*i*) Industrialization. There were however no extensive surveys and investigations, and the assessments made by these Technical groups, are of a preliminary nature. Each of these Technical groups has produced a report assessing the potentialities in specific fields of development and outlining the measures to exploit them. All these reports are published with the Interim Report of the Planning Council. The findings of these groups can be summarised as follows:—

(1) The average yield of Tea can be increased from 672 lbs. per acre today to 1200 lbs. in two decades to yield 300 million lbs. of tea anew.

(2) Rubber replanting will yield 50,000 tons of rubber by 1960

(3) Coconut output can be increased from 2000 million nuts to 3000 million nuts per year by 1970.

(4) Cocoa output can be increased by 253,000 cwts. in 10 years.

(5) Net irrigable area (but not yet developed) in the Dry Zone is 968,000 acres.

(6) Paddy yield per acre can be raised from the average of 30 bushels per acre today to about 38—41 bushels over a period of 5 to 7 years; and to 70 bushels over a "long period." (how long is not stated).

(7) Hydro—electric power capacity can be increased from 37. 5 M W to about 450 M W by 1975.

(8) A long list of industries that might be established in Ceylon.

This is useful information no doubt. But the Planning Council has not given at least on outline of a plan or a system of priorities in regard to the development of these resources. Probably this plan will be published before the next Budget—unless there is a second Interim Report.

The Report also states:—

"The work of the Technical Working Groups have themselves indicated the need for a variety of specialised surveys and investigations in several fields. Many of these will have to be commenced in the period ahead with expert assistance and advice. It is only by these measures that the data and material initially needed for the formulation of sound programmes and projects can be obtained."

One gets the impression that sound programmes of economic development cannot be conceived without further surveys and investigations. These surveys will take years, and even then we might not have enough data and still further investigation may be necessary. If we are waiting for a comprehensive survey of all our resources we mighit as well forget national planning. It must be pointed out to the Planning Council that national planning is a continous process. We must plan on the basis of information, statistics and experience at our disposal now, and constantly correct and revise our plans and estimates as our information and experience increase. A national plan is not a rigid thing; it has to be flexible so that it can be adapted to changing conditions. If we are making a start, the information provided by the Technical Working Groups alone is more than adequate to formulate our plans. To wait for more information is to postpone national planning indefinitly.

Apart from producing the Interim Report, has the National Planning Council and the Planning Secretariat made any progreas in the work of national planning in Ceylon? Have they at least made a start in drawing up the outline of a plan of development in the 20 months since the inception? This is what Professor Kaldor had to say about their work:

"The most unsatisfactory feature of the present situation is the slow progress made in planning—both in the elaboration of projects at the technical level, and in working out a consistent set of targets for an overall plan, and exploring its implications on finance, taxation, foreign exchange requirements etc. For this the lack of co-ordination between the various Government departments and the general inadequacy of the central planning machinery are largely responsible."

We are glad that at least one visiting foreign economist had the courage to point out the incompetence of our planning machinery. We should only like to add that the slow progress made in "working out a consistent set of targets for an overall plan" has resulted not only from the "inadequacy of the central planning machinery," but also from the unique theory of planning on the basis of arbitrarily visualized pictures instead of on the basis of production and employ ment targets.

It is also important to point out that national planning i.e. the planning of the utilisation of the country's resources is the sole responsibility of the Government, and all final decisions have to be made by the Government (in this context, the Cabinet). This fundamental responsibility of the Cabinet cannot be transferred or delegated to any other body least of all to one which is not in full sympathy with the political and social aims of the Government, and which consists of part-time amateur planners like bank managers, businessmen and feudal landlords. Ceylon is a poor country, and we cannot afford to take too many risks and make too many mistakes by allowing national planning on the basis of untried theories and trial and error methods. The sooner the National Planning Council is disbanded and the Government shoulders the full responsibility of national planning, the better for the country.

In national planning, the Cabinet as one body should determine the rough outlines of the Plan, and each Ministry should endeavour to work in conformity with this Plan. But what is happening now is not this. The Cabinet as a body has not drawn up a national plan. The result is that we have partial plans i.e. plans by various Ministries based sometimes on the whims and fancies of the Ministers or their subordinate officers, and more often than not worked out without consulting other Ministries and sometimes in opposition to them, and without taking an overall view of the economy. There is no co-ordination, and "departmentalism" is at its worst. In this context the Planning Council and the Planning Secretariat may only dovetail various Ministerial plans usually by arbitrating between rival Ministries, and then putting together these partial plans (or estimates of expenditure) as a national Plan. This clearly is not national planning.

It should also be realized that national planning cannot be successful unless the masses are taken into active partnership in the task of economic development. The people who do the actual building of the economy are not those who enjoy the sea breeze at Galle Buck, but the workers and peasants who from 90 per cent of the population. A national plan imposed from above will have little chance of success in the face of labour unrest and class hatred. It does not seem to be yet realized that it is from the lack of a contented and co-operative labour force rather than from the lack of planning experts or the lack of finance that economic planning runs the danger of failing in Ceylon today. We can expect co-operation from labour only if they are convinced that they are building a Socialist economy.

Planners, economists and politicians in Ceylon are in the habit of treating economic development as a financial problem. It is fashionable in these circles to regard

the lack of finance as the main obstacle to economic progress. The Interim Report for instance states:

"It is the financial factor which will finally determine what in fact can be done"

A prominent member of the National Palnning Council–Mr. C. Loganathan–too points out that lack of funds is the main difficulty in economic development, and in fact has devised a Savings Bank to maximise financial resources for development. The usual argument of those who believe in the "lack of finance" theory runs as follows: Ceylon being a poor country, the amount of savings available for capital investment is very small; the volume of savings can be increased by cutting down consumption of the people, but this is socially and politically inexpedient; hence we can accelerate the rate of development only by receiving foreign private capital; without these, we can increase the rate of development only if we have a "dictatorship," and being believers in democracy, we would not tolerate it. This argument however is fallacious. It is true that increased investment requires increased saving or a wider gap between income and consumption. But what is ingnored is that this margin between income and consumption could be enlarged not only by reducing consumption but also by increasing income, and that the implementation of well thought out Plans of capital investment itself will raise income from the very beginning. In fact savings could be increased (or the gap between income and consumption widened) without lowering consumption of a part or whole of the community if the country possesses unemployed and under-employed human and material resources which could be utilised for capital construction without competing with the production of consumption goods. And no one can deny that Ceylon is in this position today.

Quite apart from the untapped and unexplored material resources, Ceylon has a large number of unemployed and under-employed persons. According to the Central Bank Consumer Survey of 1953 there were 540,000 involuntarily unemployed and 386,000 severely under-employed in the country–mainly in the rural sector. This means that at the present level of low technique of production, the rural sector is having a "surplus" population which could be removed from land and employed in new industries without a significant fall in food production. The only difference is that the part of the food supply consumed by the peasants in the village is now sent to them in the towns. There will be no fall in the per capita consumption of food if there is a simultaneous reorganization of social and property relations in the village–agrarian reform, abolition of landlordism, consolidation of uneconomic holdings, introduction of large scale farming on a co-orperative basis, rational utilisation of labour and land etc. which will result in an actual increase in food production and consumption side by side with increased industrial investment. In fact this increase in food production could even meet the increased demand for food arising from the higher incomes of new workers in industry. But this cannot be achieved by financial policy. It could be achieved only by means of economic re-organisation. Our problem therefore is not inadequacy of savings but the deficiency of economic organisation. There is unfortunately no indication that our Planners have realised this.

Thus planned acceleration of the rate of economic development does not necessarily involve a lowering of consumption provided the appropriate organizational measures are taken. The critics however point out that rapid industrialization necessarily involves this, and to illustrare their argument they refer to the experience of the Soviet Union. What is normally not realized is that the First Five Year Plan of the Soviet Union never envisaged a lowering of consumption as an essential prerequisite of rapid industrialization, but on the contrary, actually planned for an increase in consumption. The fall in consumption which took place in the initial years was not due to any deliberate planning but to accidental factors like slaughter of livestock by kulaks,

unfavourable terms of trade, crop failures and unexpected defence expenditure resulting from war threats. It is because of the absence of such accidental factors that China has carried our industrialisation with an actual increase in consumption of the people. No national planning can ever be successful if we turn a blind eye to the experienece of the Socialist countries We are only deceiving ourselves if we persist in believing that the tremendous economic progress in those countries has been achieved by dictatorial methods.

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