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**Entrepreneurial Processes in An Apparently Uniform Context:  
A Study of Rural Farmers in Sri Lanka**

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*To my beloved family Badra, Sonali, Wasath, my parents, and my dearest friend Rohan...*

## ABSTRACT

### **Entrepreneurial Processes in an Apparently Uniform Context: A Study of Rural Farmers in Sri Lanka**

The primary focus of this research is the role of entrepreneurship in the economic success of rural farmers in Sri Lanka. The village in which this research takes place was created (administratively) from a cleared jungle, and populated in 1984 by similarly-endowed individuals not generally known to each other, thus controlling a significant number of success-influencing socio-economic variables (arising from past generations). This study, therefore, represents a “unique natural experiment” as it focuses on the “entrepreneurial process” and demonstrates how differentiation arises.

A Multiple Embedded Case-Study strategy is adopted: the selected village provides the socio-economic and physical boundaries, and the farmers and their income generating processes are sub-cases. Successful inhabitants are identified through the folk definition of economic success: in terms of both social and economic values. Qualitative field methods are supplemented by quantifiable evidence. Research questions are answered by contrasting the socio-economic value-extraction processes of the successful farmers with the routine paddy-based socio-economic activities of the unsuccessful farmers.

The environment in which inhabitants operate is constrained by limited resources and various other biophysical and socio-economic factors. The pressure exerted by these environmental constraints restricts the farmers’ choices of action and forces the economically-unsuccessful farmers to form a cycle of routine socio-economic activities. This routinely ‘vicious cycle’ is production-oriented paddy-farming and culminates in consumption activities. The eventual result is often crop-failure and consequently economic failure brought about by inefficient and ineffective resource use. This pattern shows a significant degree of uniformity. In contrast a variety of opportunities are perceived and capitalized on by entrepreneurs.

The task of the entrepreneur, within the same environment, is to extract value by spotting these opportunities and match them with available or mobilised resources, resulting in capital-accumulation and wealth-creation.

The findings illustrate how entrepreneurial and managerial value extraction strategies, in a limited resource context, complement each other and demonstrate that the managerial function is an integral component of entrepreneurship. By distinguishing amongst the different tasks of the entrepreneurial and managerial functions, the findings also confirm that these two functions are interdependent elements in influencing economic success. The thesis findings also indicate that certain entrepreneurship and strategic management principles, which have been proven applicable for the affluent Western world, are also relevant to small-scale rural farmers in the third world context who might be expected to struggle in abject poverty in order to scrape an existence.

The findings also contribute a new dimension to the entrepreneurship literature, by explaining how “pluriactivity” is being adopted as an entrepreneurial value-extraction strategy, demonstrating how the terms “pluriactivity” and “diversification” can be utilised in relation not only to entrepreneurship and management but also to the economic growth of farmers.

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## Beginning.....

*“The Farmer is an undertaker (entrepreneur) who promises to pay to the Landowner, for his Farm or Land, a fixed sum of money (generally supposed to be equal in value to the third of produce) without assurance of the profit he will derive from this enterprise. He employs part of the land to feed flocks, produce corn, wine, hay, etc. according to his judgement without being able to foresee which of these will pay best. The price of these products will depend partly on the weather, partly on the demand; if corn is abundant relative to consumption it will be dirt cheap, if there is scarcity it will be dear. Who can foresee the number of births and deaths of people in a state in the course of the year? And yet the price of the Farmer’s produce depends naturally upon these unforeseen circumstances, and consequently he conducts the enterprise of his farm at an uncertainty” (Cantillon, 1755:49).*

## **CHAPTER ONE**

### **The Problem Background And The Justification Of The Study**

#### **1 Introduction and overview**

The underlying generic question upon which this thesis is based is “Why do certain small scale rural farmers become economically more successful?” This allows us to locate the research interest within the rubric of the processes by which entrepreneurs match opportunities and resources in innovative ways and thereby add value in terms of capital accumulation and wealth creation. This type of research is warranted by the lack of grass root level investigations to see why there is a large heterogeneity in socio-economic status despite macro policies to achieve equity. The research will focus on the rural agricultural sector in Sri Lanka, where farmers are heterogeneous in respect of a multitude of socio-economic factors.

#### **1.1 Specific research context: the agricultural sector in Sri Lanka**

The agricultural sector in Sri Lanka currently accounts for about 24 percent of the nation's GDP. About 2.2 million people are directly employed within this sector, which remains an important source of income for about 70 percent of the population. About 31 percent of the total land area in Sri Lanka is under cultivation (Samarathunga and Dasanayake, 1991), of which about one-half is devoted to plantation crops, 45 percent to paddy production and the remainder to the production of other crops including fruit and vegetables (Schermerhon, 1986).

The major characteristic of the Sri Lankan agricultural sector, as in many other developing countries, is that it is dualistic. Two different sub sectors i.e. plantation and the rural subsistence (with diffused boundaries), exist side by side.

As indicated before, the Sri Lankan rural farming sector is composed of a heterogeneous farming group with a minority of economically successful (Gunatilake *et al*, 1992; Hettige, 1982; Karunan, 1992 Paravithana, 1985; Shanmugarathnam, 1984) farmers. This minority of wealthy farmers control the bulk of the means of production and exchange in the rural sector. On the whole these farmers possess the basic characteristics of small scale Limited Resources Farmers (LRF), i.e. “a group of farmers that is not endowed with adequate productive factors, skills, and organizational support to move into the mainstream of economic activity in the farm sector” Davis (1991:1477) (see also Colette and Wall, 1978; Cornaman *et al*, 1982; Dagher and Christy, 1991; Gebremedhin, 1991; Jones, 1991; West, 1979; Wysong and Handwerker, 1989 for basic characteristics of LRFs).

### **1.2.1 Problem background: pre and post 1977 economic policies and their relevance to entrepreneurship**

Before 1977, the rural agricultural sector was highly protected. Efforts concentrated on the import substitution of rice and other food crops (Gunatilleke *et al*, 1992; Thorbecke and Svejnar, 1987; Lee, 1977). Guaranteed price schemes (GPS), combined with state purchase of products, provided the farmers with an assured market with stable prices. This was possible because the state was both the importer and largest distributor through food rationing. Furthermore, farmers benefited from subsidies until 1988 including

fertilizer subsidies (Gunatilleke *et al*, 1992). Other inputs such as agrochemical and tractors benefited from low import duties or even exemption from duty (Gunatilleke *et al*, 1992; Moore, 1984). Therefore the rural agricultural sector, with its heavily protected and regulated market and its wide array of subsidies and other forms of state support such as agricultural extension services, developed in an environment which was heavily dependent on the state.

In contrast to the above policy regime, the package of policies introduced by the UNP government (i.e. the United National Party) in November 1977 and thereafter, was mainly aimed at an export-oriented free market economy (Gunatilleke *et al*, 1992; Bruton *et al*, 1992; Shanmugarathnam, 1984, Karunan, 1992). The post 1977 reforms dismantled most of the exchange controls and import quota systems, removed subsidies and administered prices (Gunatilleke *et al*, 1992), thereby liberalizing the internal trade of farm products (Karunan, 1992:114). Furthermore, the role of the government sector in marketing agricultural products (RONCO, 1986) and providing agricultural extension services gradually diminished. The open economic policy sought to provide incentives to private investors in agricultural production. The fundamental objective was to promote export-oriented agribusiness industry through multinational collaborations (Karunan, 1992). Consequently, a trend emerged which involved the moving of large scale export-oriented agricultural firms into the rural sector. This was in order to organize the small producer - through providing technical know-how, credit and marketing - of certain export items such as gherkin, ornamental fish, cut flower, foliage and so on (Gunatilleke *et al*, 1992).



It has been observed that the introduction of open economic policies replaced the personal non-market ties (such as exchange of labour relations) that determined the reproduction of production units of the typical peasant household with market ties such as hired labour relations (Shanmugarathnam, 1984:22). As a result individual farmers were required to respond to market forces (though with a certain degree of imperfection according to Shanmugarathnam, 1984) which operated in a dynamic, and therefore very uncertain, environment - one that provided various economic opportunities for those who could rely on their entrepreneurial abilities to pursue them.

### **1.2.2 Free market economy, entrepreneurship and economic success**

Much of the literature suggests that entrepreneurs exist and thrive mainly in societies with decentralized economic power (Cole, 1964; Casson, 1982:25, Kirzner,1984; Gilad,1982; Pulver, 1987:94; Timmons, 1994:30,34). This is because certain institutional practices in market economies tend to encourage a high level of entrepreneurial activity demonstrated by (i) a free and open economy that permits equal access to entrepreneurial opportunities (ii) a guarantee of ownership in property legally acquired and (iii) stability of institutional practices that establishes previous points i and ii (Kirzner, 1984:55). It may be argued, therefore, that societies with decentralized economic power provide environments of economic freedom (i.e. environments free from special privileges or blockages against new entrants Kirzner,1984:57) which stimulate entrepreneurial spirit (Gilad, 1982) resulting in economic growth. It follows that the entrepreneur, as the creator of new wealth (Schumpeter,1934), is the central figure in economic (for example Baumol,1968:65; Broehl,1978; Hoy, 1983; Hoy, 1987; Gilad,1982; Kirzner,1984; Schumpeter,1934; Wortman,1990a:222) and business

(Anderson, 1995; Fredrick and Long, 1989:4; Jacobson, 1986:29; Reynold, 1991:57; Jacobson, 1986:26) development as well as the basis of change and growth in society (Broehl, 1978; Chell, 1990:187; Thropman and Morningstar, 1989).

### **1.2.3 Basic research issue: the role of entrepreneurship in the economic success of rural farmers**

It may be argued that the above points have a very practical relevance to Sri Lanka's rural farming sector. Research findings (Gunathileka *et al*, 1992:185; Gunatilleke, 1992:10) suggest that the pre-1977 economic policy regime of the country retarded the growth of the market-oriented entrepreneurial population which would have been capable of identifying economic opportunities and diversifying the rural economy.

This contrasts markedly with the post-1977 policy regime, as empirical research findings indicate that the environment created by open economic policies has facilitated the generation and accumulation of wealth by some rural farmers. This is visible in terms of: (a) widening of the gap between the previously-noted (see section 1.1) economically successful and poorer groups of farmers (Gunathilleke, *et al*,1992; Karunan, 1992; Shanmugarathnam,1984) and (b) the formation of a new stratum of accumulation- motivated "dynamic entrepreneurs" (Shanmugarathnam, 1984). This latter finding is closely related with that of similar findings by Manchin and Szelenyi (1985) on the influence of market reforms which led to the emergence of a new entrepreneurial stratum in Hungary.

On the whole these economically successful farmers have been labeled by researchers as “entrepreneurial farmers” (Hettige,1982:21; Shanmugarathnam,1984:23) and distinguished from the rest of the farming population based on the following criteria:

- (i) they do not engage in the process of physical production themselves i.e. their land is worked entirely by wage labourers (however, the above-noted accumulation-motivated “dynamic entrepreneurs” use their family labour and supplement it with hired labour during peak seasons (Shanmugarathnam, 1984:23);
- (ii) they produce mainly for the external market (i.e. they are market-oriented) and
- (iii) they engage in various other non-farming activities in the countryside.

It appears that these researchers tend to use the term entrepreneur to designate anybody who is engaged in small business operations (see Bryant, 1989:340 for a similar argument). However, much of the literature suggests that not all small business operators are entrepreneurs (Bryant, 1989: 340; Kirchoff, 1994:423; Saylor, 1987:58; Wortman, 1990b:338). There has been little or no research (in the field of entrepreneurship) to investigate how entrepreneurial these economically successful farmers are. Therefore, the validity of the label “entrepreneurial farmers” and their above-noted basic characteristics are questionable. It may be argued, in this setting, that research is warranted to differentiate/distinguish entrepreneurial farmers from the rest of the rural farming population so that their fundamental contributions to economic/business development could be meaningfully analyzed (Brazeal and Weaver,

1988:134). This issue leads to the generic research issue of this thesis i.e. “the role of entrepreneurship in the economic success of rural farmers in Sri Lanka”. This type of research is indeed further warranted as there has been little or no grass-root level farmer-oriented research in the country (Abeygunawardena, 1991:3)

#### **1.2.4 Basic research questions and objectives: the role of entrepreneurial activities/processes in the economic success of rural farmers**

The field of entrepreneurship has been theoretically contributed to by researchers from a variety of subject areas such as economics, sociology, anthropology, psychology and political science (Fredrick and Long, 1989). Despite these contributions, it is quite clear that there are still disagreements on how to differentiate the terms entrepreneur /entrepreneurship (Casson, 1982; Chell, 1990; Frederick and Long, 1989; Gartener, 1989; Kent, 1984; Low and MacMillan, 1988; Morris *et al*, 1994; Pridavka, 1979; Rosa and Bowes, 1990; Binks and Vale, 1990; Wortman, 1987). Casson (1982:1-22) puts forward two approaches to define entrepreneurship i.e. (a) the indicative approach and (b) the functional approach (p22). The indicative approach, according to Casson, provides a description of the entrepreneur by which he<sup>1</sup> may be recognized whereas - in the functional approach - the entrepreneur is identified by what he does.

As far as the indicative approach is concerned, attempts have made to differentiate successful entrepreneurs from the rest of the population based on diverse criteria i.e. diligence, thrift, sobriety and prudence coupled with capital, innovation and ownership of factors of production (Weber, 1930); “desire for independence” (Collins and Moore

1964); “need for achievement” (Hornaday and Abound, 1971; McClelland,1967); initiative, assertiveness, efficiency-orientation, systematic planning, commitment to work contract (McClelland, 1986); internal locus of control (Brockhaus,1982; Brockhaus and Horwitz,1986; Brockhaus and Nord, 1977; Begley and Boyd, 1986 ); risk-taking propensity (Begley and Boyd, 1986; Sexton and Bowman,1985); tolerance of ambiguity (Schere,1982; Sexton and Bowman,1985) need for autonomy, dominance, independence combined with a low need for support and conformity, and a capacity for endurance (Sexton and Bowman,1985). These approaches can mainly be categorized into three main areas viz. personality traits, values and behavioural traits (See Brazel and Weaver, 1988:134).

With regard to personality traits, it can be argued that there is as much difference amongst entrepreneurs as between entrepreneurs and non-entrepreneurs (see Gartner,1985). Grasley (1986:145) states that “there is no universally accepted profile in specifying personal characteristics that would facilitate in identifying (sic) potentially successful entrepreneurs”. Rigorous empirical research has failed to identify any trait strongly associated with entrepreneurship (Aldrich and Zimmer,1985:5; Anderson, 1995:135). It has also been argued that personality traits or qualities may change within an individual over their life cycle, or even as a business matures, or as circumstances/context change (Anderson,1995:135; Binks and Vale, 1990:57).

As for behavioural attributes, Chell (1990:190) notes that an entrepreneur learns through experience and modifies his behaviour accordingly. The same author also argues that the need for modification of the existing behaviour or development of a new behaviour

by the entrepreneur is necessitated by the development of his business (p 191). According to Bygrave (1994:4) there appears to be no neat set of behavioural attributes that separates entrepreneurs from non-entrepreneurs (Bygrave, 1994:4).

It has been argued, in the above context, that the entrepreneur and his success should be studied in a more useful manner by looking at the “entrepreneurial activity/process” (Bryant, 1989; Bink and Vale, 1990:18; Morris *et al*, 1994) in which the entrepreneur is identified/differentiated by what he does (or how he acts) and the outcome of his actions i.e. creation and accumulation of wealth<sup>2</sup> (see Chell, 1990:192; Kilby, 1971; Morris *et al*, 1994; Shapero, 1984:23, Stevenson and Jarillo, 1990:18 for arguments of a similar nature). This stance is based on the argument that success is determined by the behaviour of the entrepreneur, as it is expected that he behaves in a manner that is likely to increase his economic/business success (see Lawrimore, 1988:76 for a similar argument).

The previously-noted basic research issue (i.e. section 1.2.3) can therefore be rephrased as “what is the role of entrepreneurial activity/process in the economic success of rural farmers in Sri Lanka?”. This in turn leads to the major research objective of this study i.e. to study the roles of entrepreneurial activity/process in the economic success of rural farmers in Sri Lanka.

The rationale of applying this approach to the Sri Lankan rural context is (a) to identify (for sampling purposes) the entrepreneurial farmers based on the outcome of their economic actions (i.e. selecting wealthier farmers as winners) and (b) to compare and contrast their processes of income-generating (i.e. commercial) activities with that of economically unsuccessful farmers so as to investigate the influence of economic behaviour on economic

success/failure in the context of entrepreneurship theories. This is under the assumptions that: (a) every farmer had equal access to the new economic opportunities created by open economic policies and (b) the higher the impact and frequency/intensity of entrepreneurial activity/process associated with any particular farmer (or business entity) the greater that farmer (business entity) approximates to the construct of the entrepreneur (see Morris *et al*, 1994; Vale and Binks, 1990:9).

### **1.2.5 Practical difficulties of applying the process approach: all the wealthy farmers in a given rural location may not be entrepreneurs**

The practical difficulties of applying this approach lie mostly in the sampling stages (i.e. in picking wealthier farmers as winners), as all the wealthier farmers in a given rural location may not necessarily be entrepreneurs. This is basically due to a large number of external factors (other than the entrepreneurial function) that influence the economic success of rural farmers. The main extraneous factors are (a) land (ownership, control, size, productivity, location in terms of access to water and roads), (b) acquired or inherent positions in the local power structure and (c) access to working capital and technical know-how (Gunatilake *et al*, 1992; Shanmugarathnam, 1984).

Ownership of productive land, access to it and control over the resources such as water, finance etc. are critical and the most important determinants of economic failure (Gunathileke *et al*, 1993:171,186). These factors have also formed the basis of the agrarian social structure and the source of power held by the rural elite (Gunathileke *et al*, 1993:186). In particular, the control of land has always been a source of power and status in Sri Lankan rural society (Dunham, 1982:50). The acquisition of land (which is a measure of social standing (Paranavithana, 1985:23), has therefore proved to be vital

in consolidating any new positions achieved in the society through upward mobility (Dunham, 1982:50). However, the majority of rural inhabitants are either landless households (Praranavithana, 1985; Bruton *et al*, 1992) or households with uneconomical holdings (Praranavithana, 1985; Schemerhon, 1986), which has resulted in substantial inequalities in the distribution of land in the rural sector (Moor, 1989:184).

As far as the rural sector is concerned, there exists - within a large group of smallholdings - a gradation with few relatively large holdings at the level of family farms. Alongside these owner-cultivators there is a large segment of landless agricultural labour (Gunatileke *et al*, 1992; Paranaivithana, 1985; Sanmugarathnam, 1984; Hettige, 1982). The size of the land holding (in general the average size of land holdings remains at two acres, with a very high proportion of holdings below one acre, Gunatilake, 1992) owned by poor peasants is becoming smaller day by day through fragmentation in the process of inheritance of property by family members (Hettige, 1982; Paranaivithana, 1984). Those who do not inherit land often become landless wage labourers. Though paddy is the predominant (i.e. staple food) crop in Sri Lanka (Samarathunga and Dissanayake, 1993:89), studies reveal that the rural poorest typically do not own paddy land (e.g. Moor, 1989:188).

As far as the poor peasants (who constitute a substantial share of the rural population) with small plots of lands are concerned, their holdings are uneconomical (i.e. due to their small size) and, therefore, they produce a surplus so small that it is often not enough to settle loans and meet the subsistence requirements (Moor, 1989) of their families. This condition has been further aggravated by the low profitability of paddy



(Weerahewa and Abeygunawardena, 1989) coupled with the high cost of production (which is mostly unbearable for the majority). It could be suggested that the high cost of (crop) production is a result of the introduction of open economic policies. This is through: (a) replacement of exchange labour relations by hired labour forms (Hettige, 1982; Shanmugarathnam, 1984, Moor, 1989) and (b) high input prices caused by the removal of production subsidies.

Cash, which is a fundamental requirement for agricultural production, is usually obtained by most of the peasants either through the sale of the products of their labour and/or sale of their labour for a monied wage. In the case of the majority of farmers, the gap between the cash requirement for production and the consumption and total cash receipts is very high (Shanmugarathnam, 1984). Institutional credit is strictly geared for creditworthy farmers, leaving the bulk of farmers at the mercy of the informal credit sector where annual interest rates are extremely high i.e. about 190-240 percent per annum (Hettige, 1982; Shanmugarathnam, 1984).

The structure of the rural market is also complex and heterogeneous. This is partly because of the character of the specific relationships that link the farmer to the market through intermediaries. This structure differs from product to product. Each system has specific characteristics related to its credit, storage and accumulation of stocks, seasonal availability and timely access to market (Gunatilake *et al*, 1992). All these factors affect the producer prices, as the bargaining power of the household is determined in each case by the characteristics which are specific to the pattern of exchange for a given commodity (Gunatileka *et al*, 1992). Many of the small farmers live in relatively

