

# SMALL FARM AGRICULTURAL CREDIT IN IRAN (\*)

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## 1. Introduction

In Iran like in many other countries, the advancement of credit through formal institutions has been considered as one of the strategies for agricultural development. For example, the amount of credit advanced to farmers through Cooperative Agricultural Bank of Iran (CABI) which is one of the major formal source of credit to small farms has increased from 14,381 million Rials (215 million Dollars) in 1972 to 38,062 million Rials (563 million Dollars) in 1979<sup>1</sup>. The amount of credit advanced through Agricultural Bank of Iran (New name for old CABI) in first half of 1983 (1361) fiscal year reached 64,015 million Rials (800 million Dollars). Nine percent of this amount of credit was advanced through rural cooperatives<sup>2</sup>.

Unsettled questions exist with regard to performance of agricultural credits in less developed countries (LDCs)<sup>3</sup>. These questions include the impacts of institutional credits on farm income distribution and how effectively formal credit reaches small farmers where policy goals emphasize more economic help to these farmers to eliminate informal money lenders. Some research results show that subsidized interest rate which are generally advanced through formal sources<sup>4</sup> might worsen income distribution (see Gonzalez-Vega, 1977, p. 975). It is stated that, « Large farmers have been the main beneficiaries of institutional credit. It is common to find 70% or 80% of small farmers in a given country with virtually no access to such credit » (see World Bank, 1975, p. 5)<sup>5</sup>. Another question is to what extent agricultural credits can be used as one of the strategies to reach agricultural development goals such as stimulating adoption of technology and increasing productivity as well as rising the levels of use of inputs purchased from non-farm sector. Some researches conclude that credit would have positive effects on the adoption of new technology while inadequate amounts of credit would halt the adoption of new technologies (see Rask, 1971, p. 54; Agarwal and Kumawat,

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1 Statistical Center of plan and Budget Organization, Islamic Republic of Iran, *Yearly Statistical Year Book*, 1359 (1981), (in Farsi).

2 Agricultural Bank of Iran, *The Summary of Credit Activities of Agricultural Bank of Iran in First Half of Year 1361* (1983), (in Farsi).

3 For a good review of credit questions and assumptions see Adams (1978).

4 Including banks, cooperatives and other formal institution which are mainly or partly involved in credit advancements.

5 For more elaboration on institutional credit distribution see Lele (1975, Chapter 5).

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1974, p. 75; Singh, Bhati, and Jain, 1971, p. 474 and 479; Singh and Jha, 1971; Sharma and Prasad, 1971, p. 511; Bhanja, 1971, pp. 518-519). Other research results show that formal credit is not necessarily required and other strategies such as price policies are more effective (see Gonzales-Vega, 1977, p. 975; Von Pischke and Adams, 1980, p. 725).

Limitation of data especially farm level detailed data with regard to costs and returns and type of loans make such evaluation difficult and this is one of the reasons for the existing conflicts among these credit research results. Other problems with regard to evaluation of credit programs include (1) fungibility of the credit as is explained by Von Pischke and Adams (1980) and (2) the fact that the amounts of fund involved in credit programs are small and their impact has been masked by other development policies (see de Araujo and Meyer, 1977).

This study is an attempt to analyse the relative impact of formal<sup>6</sup> and informal credits distributed to small farms in Iran. Using farm level data and separating formal from informal credit make this study more meaningful in evaluating the credit programs. Three agricultural regions were selected for this study. Toward this end, a brief description of background, data sources, and methodology is presented first. The results and the implications of the study are then discussed.

## 2. The Regions and the Data

Marvdasht, Remjerd and Abarj are the three regions which were selected for this study. They are located within the Droudzan irrigation Project near Shiraz, capital city of the Fars province.

Most data utilized in the analysis were collected through a 1972 survey of some 280 small farms with an area of 15 hectares and less, chosen on a stratified random basis<sup>7</sup>. In terms of access to banks as one of the sources of formal credits the following points should be mentioned: Marvdasht region is adjacent to the city of Marvdasht and hence its farmers have a good access to banks and other credit institutes. Abraj, on the other

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6 Informal credit includes all sources of credit other than banks, cooperatives, and other officially sponsored lending institutes.

7 The data were collected for a farm survey by the Department of Agricultural Economics, College of Agricultural Economics, College of Agriculture, Shiraz University, Shiraz, Iran.

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hand, has less access to formal credit institutes since it is far from the city with about 60 kilometers distance including 40 kilometers of gravel roads. Ramjerd falls in between the two regions. It has access to the city of Marvdasht through asphalt road with a distance of at least 20 kilometers. Another source of formal credit is rural cooperatives which supply credit to farmers at subsidized interest rate. Generally the amounts of credit granted to farmers through the rural cooperatives are more limited than those granted by banks so that the variations in the amount of credit received from formal sources stem from the bank's share of credit.

The average size of cultivated plots are 6.62, 4.46, and 4.95 hectares and net crop returns per farm are 66,043, 48,615, and 67,478 Rials in Marvdasht, Ramjerd and Abarj respectively. Besides wheat and barley which are the two major crops for the three regions, Marvdasht is allocating a considerable amount of land to sugar-beet and Abarj to rice production. The farmers of Marvdasht have more access to informal credit and larger amount of chemical fertilizers supplied by the sugar-processing factory than those in the two other regions.

### 3. Methodology

The analysis includes comparison of formal and informal loans between regions and within the region. Factors such as credit-cost ratio, credit per farm, and credit per hectare are used to explain the credit situation. Loan concentration for both kinds of credits are presented. Regressions are run to show the signs of coefficients for the effects of farm size on credit-cost ratios and on credit per hectare figures.

### 4. The Results

#### 4.1. *Formal and Informal credit Distribution - Between the Region Comparison*

Distribution of formal and informal credits for the three regions in 1971/72 are shown in Table 1. Considering the three regions, only 32% of credits are provided through formal sources. In Marvdasht 42% of total credit is provided through formal sources and the related figures for Ramjerd and Abarj are 27% and 25% respectively. The important factors for the differences in percentage of formal credit are three. First, access to the credit institutions: Marvdasht is adjacent to the city of Marvdasht and hence its

farmers have easy access to formal credit institutions, whereas, Ramjerd and especially Abarj, as mentioned before, are located far from the city; the second factor is the level of the credit worthiness. Marvdasht farms have relatively higher level of credit worthiness since they have larger area of land and generally larger value of farm assets. The value of assets including land are 756,237, 600,178, and 635,346 Rials per farm in 1971/72 for Marvdasht, Ramjerd and Abarj respectively. The third factor is the size of the loan. Marvdasht farmers borrow larger amounts from formal sources i.e. 16,253 Rials per farm as compared to 6,241 and 6,812 Rials in Ramjerd and Abarj respectively (Table 1), and granting larger loans is preferable for the formal sources of credit.

**Table 1**

FORMAL AND INFORMAL CREDIT DISTRIBUTION FOR MARVDASHT, RAMJERD AND ABARJ, IN 1971-72

Regions	No. of obs.	Credit/farm			Formal non-borrowers			
		Formal <sup>a</sup> (Rials) <sup>c</sup>	Informal <sup>b</sup> (Rials) <sup>c</sup>	Total (Rials) <sup>c</sup>	as % of Total Credit %	Formal %	Informal %	Total %
Marvdasht	72	16,253	22,215	38,468	42	14	6	1
Ramjerd	183	6,241	17,297	23,538	27	56	9	3
Abarj	32	8,812	20,219	27,031	25	41	3	—
3 regions	287	8,816	18,857	27,673	32	44	7	2

a Includes banks and cooperatives.

b Includes sugar beets factories, merchants, etc.

c 67 Rials = 1 U.S. Dollar.

Source: Calculated from interview data.

#### 4.2. The non-borrowers

Table 1 shows that the non-borrowers from informal sources of credit are only 6%, 9%, and 3% for Marvdasht, Ramjerd and Abarj respectively which are relatively low.

However, a considerable percentage of non-borrowers from formal sources are observed in these regions. Marvdasht has 14% of non-borrowers from formal sources and the related figures for Ramjerd is 56% and for Abarj 44% which are very high as compared to Marvdasht<sup>8</sup>. The same factors which were mentioned above for lowness of the share of formal credit in Ramjerd and Abarj can be mentioned for their high percentage of non-borrowers of formal credit as well. It is interesting that with the exception of few farmers, all of them have benefited from either formal or informal sources of credits. That is the non-borrowers for total credit are only 1% for Marvdasht, 3% for Ramjerd, and zero for Abarj.

#### 4.3. *Loan Concentration - Within the Region Analysis*

Questions with regard to loan concentration include: How are the farms distributed between different categories of credit size? and how is the distribution of formal credit as compared to informal? The figures for loan concentration are shown in Table 2.

4.3.1. *Total Credit*: The distribution for total credit is skewed toward larger size loans. In Marvdasht 67% of the farms received only 43% of total credit, in Ramjerd 61% of farms received only 30%, and in Abarj 50% of the farms received only 27% of the total credit (Table 2). These figures show that the credit is not normally distributed among the farms and the distribution is worse for Ramjerd and Abarj which have less access to formal credit sources and are benefited from smaller amounts of credit.

4.3.2. *Formal credit*: Loan concentration for formal credit tends toward larger size loans and is to some extent worse than total credit distribution. This is, however, due to the fact that larger percentages of the farms fall into non-borrowers category (Table 2). Among the borrowers however, the distribution of credit is better than informal credit and hence better than total credit distribution. This could be due to the fact that formal loans fall within a narrower range of size than informal ones.

4.3.3. *Informal Credit*: Loan concentration for informal credit is better than formal since the non-borrowers of informal credit are fewer than formal (Table 2). Among the

8 The percentage of farmers receiving institutional credit varies widely in the developing world. In certain African countries, around 1% of the total number of farmers use institutional credit, while in the Republic of China (Taiwan) nearly all farmers have access to it. About 5% of farmers in Africa obtain institutional credit, while the proportion in Latin America and Asia (excluding the Republic of China) is about 15% (see World Bank, 1975, p. 5).



borrowers however, the distribution of credit is worse than formal loans. This can be explained by the fact that informal loans are paid within a wider range of size than formal ones. Who are the beneficiaries of the large loans is another question which can be studied. In other words, is it the large farmers who receive the main part of institutional credit? Criteria such as credit - cost and credit per hectare ratio can clarify the answer to this question. The following part deals with these two criteria.

**Table 2**

LOAN CONCENTRATION FOR MARVDASHT,  
RAMJERD AND ABARJ, 1971/72

Total credit per farm		Total credit		Formal credit		Informal credit		Formal credit as % of total cr.
Category numbers	Amounts (Rials)	% of farms	% of credit	% of farms	% of credit	% of farms	% of credit	
Marvdasht (72 farms)								
1	Zero (non-borrowers)	1	—	14	—	6	—	—
2	0 - 20,000	18	6	12	7	17	5	49
3	20,001 - 40,000	49	37	42	36	46	38	41
4	40,001 - 60,000	15	21	15	18	15	23	37
5	60,001 - larger	17	36	17	39	17	34	45
Total		100	100	100	100	100	100	42
Ramjerd (183 farms)								
1	Zero (non-borrowers)	3	—	56	—	9	—	—
2	0 - 20,000	61	30	19	21	56	37	19
3	20,001 - 40,000	20	26	13	27	20	26	27
4	40,001 - 60,000	10	22	7	25	9	20	31
5	60,001 - larger	6	22	5	27	5	20	32
Total		100	100	100	100	100	100	27
Abarj (32 farms)								
1	Zero (non-borrowers)	—	—	41	—	3	—	—
2	0 - 20,000	50	27	11	23	50	28	22
3	20,001 - 40,000	31	36	22	24	31	40	17
4	40,001 - 60,000	16	30	16	44	13	25	38
5	60,001 - larger	3	8	3	9	3	7	31
Total		100	100	100	100	100	100	25

Source: Calculated from Interview data.

#### 4.4. Credit-Cost and Credit per Hectare Ratio

As table 1 shows, the absolute amount of formal credit per farm is the largest in Marvdasht and the smallest in Ramjerd. The costs for crop production per farm are 50,615, 17,307 and 29,704 Rials per farm for Marvdasht, Ramjerd and Abarj respectively. Although the costs for crop production are one of the major determinant of the size of total credit acquired by the farmers, however within-the-region comparison show that other costs affect the size of the acquired credits as well. The following part is a further elaboration on this point.

The figures in Table 3 show that (1) the credit-operating cost ratios increase as credit per farm increases implying that credit is demanded to meet other credit needs than only crop operating costs. Credit-cost ratios higher than one support this point strongly; (2) the amounts of credit per hectare increase as the size of credits increase, which again supports the point that credit is acquired for other purposes than only cash crop cost.

For further explanation on this point credit-cost ratios and credit per hectare figures are calculated for different size of cultivated land (Table 4).

**Table 3**

CREDIT-OPERATING COST RATIOS AND CREDIT PER HECTARE FOR MARVDASHT, RAMJERD, AND ABARJ IN 1971/72

Total credit per farm		Credit-operating cost ratios <sup>a</sup>			Credit per hectare		
No.	Amounts (Rials)	Marv.	Ramj.	Abarj	Marv. (Rials)	Ramj. (Rials)	Abarj (Rials)
1	Zero (non-borrowers)	—	—	—	—	—	—
2	1 - 20,000	0.34	0.80	0.66	3,228	3,066	4,238
3	20,001 - 40,000	0.76	1.59	0.92	5,489	5,684	5,102
4	40,001 - 60,000	1.01	2.90	1.55	8,161	11,196	9,046
5	60,001 - larger	1.07	4.20	1.55	8,880	11,446	10,833
Total		0.76	1.36	0.91	5,815	5,280	5,465

a Total credit divided by crop production cost. More than 95% of the costs are cash operating costs.

Source: Calculated from interview data.

**Table 4**

CREDIT OPERATING COST RATIOS AND CREDIT PER HECTARE FIGURES FOR DIFFERENT FARM SIZES FOR MARVDASHT, RAMJERD, AND ABARJ IN 1971/72

No.	Size of cultivated land/farm (Hectare)	Credit-operating cost ratios <sup>a</sup>			Credit per Hectare		
		Marv.	Ramj.	Abarj	Marv. (Rials)	Ramj. (Rials)	Abarj (Rials)
1	0 - 2.50	1.18	2.63	1.10	9,052	10,190	7,150
2	2.51 - 5.00	0.85	1.60	0.82	6,837	6,166	5,593
3	5.01 - 7.50	0.83	0.82	1.03	6,453	3,308	5,919
4	7.51 - 10.00	0.67	0.88	0.72	4,628	3,252	2,919
5	10.01 - larger	0.44	0.55	0.51	3,167	2,134	2,270
Total		0.76	1.36	0.91	5,815	2,280	5,465

a Total credit divided by crop production cost. More than 95% of the costs are cash operating costs.

Source: Calculated from interview data.

The credit-cost ratios and the amount of credit per hectare decreases as the size of land increases<sup>9</sup>. These facts support the above mentioned point and the ratios higher than one support the point strongly. Besides crop, credits are also used for livestock, carpet production, and household consumption costs. The data for household consumption costs are not available. However, when credits are divided by the total cost of crop, livestock and carpet production the following credit-cost ratios are obtained: .60, .67 and .63 for Marvdasht, Ramjerd, and Abarj respectively (Table 5).

Comparison of these ratios with those in Tables 3 and 4 shows that credit is acquired to meet the costs of all three types of activities and that relatively sufficient amount of credit is acquired whether from formal or informal sources<sup>10</sup>.

9 Regressions are run to see the effects of farm size on credit-operating cost ratios and credit per hectare figures see Appendix.

10 Noncredit policy requirements are emphasized by different literatures as well. World Bank (1975, p. 34) states that, « However, it must be recognized that credit is but one facet of economic policy. Increased availability of credit may have little effect on production if other economic policies militate against the profitable use of credit. In such a situation, credit will become effective only if those policies are modified ». For more emphasize on noncredit policy requirement as complement to credit policies (see Johnson 1971, p. 55).



**Table 5**

THE RATIOS FOR CREDIT OVER TOTAL COST OF CROPS, LIVESTOCK, AND CARPET PRODUCTION FOR MARVDSHT, RAMJERD, AND ABARJ IN 1971/72

Credit and costs per farm	Marvdasht	Ramjerd	Abarj
	(Rials)	(Rials)	(Rials)
Crop, livestock and carpet costs <sup>a</sup>	63,775	35,085	42,712
Total credit <sup>b</sup>	38,468	23,538	27,031
Credit-cost ratio	.60	.67	.63

a *Economic and social survey of villages under Doroodzan Dam, Final Report*, and unpublished report by the Department of Agricultural Economics, College of Agriculture, Shiraz University, Shiraz, Iran, Table 20.

b Taken from Table 1.

#### 4.5. Distribution of Farms, Land, and Credit

Comparison of figures for percentage of farms, percentage of land, and percentage of total credit (Table 6) show that the distribution of land is skewed toward larger size farms and that credit is distributed more on the basis of number of farms and less on farm size.

Comparison of the figures for formal credit as a percentage of total credit in different farm size brackets (Table 6) show that where (Marvdasht) the region has benefited from higher percentages of formal credit, the small farms have to some extent benefited as well although larger farms may have benefited more in absolute amount than small farms. In Marvdasht, farms with a size of 2.5 hectares and less received some formal credit while in the other two regions the same size farms did not receive any formal credit. In Marvdasht the percentages of formal credit are higher than in the two other regions in all of the farm size brackets.

Considering the demand side, the limiting factor to borrowing formal credit for small farmers in Ramjerd and especially Abarj is their geographical distance from the sources of formal credit. The long distance and low quality roads cause inconvenient and costly trips for acquiring formal loans so that farmers prefer to borrow from informal sources. On the supply side however, control and supervision of loans and mortgage problems are more difficult when the lending institutions are located far from the borro-

wer. Therefore, in order to reach small and poor farmers it is necessary to supply formal credit in some locations or through some agencies which are geographically close to the farms, otherwise, high credit costs resulting from the long distance and inconvenient trips to formal credit sources would discourage the small loans from being granted and the small farmers from borrowing.

**Table 6**

DISTRIBUTION OF FARMS, CREDIT, AND LAND FOR MARVDASHT, RAMJERD, AND ABARJ IN 1971/72

No.	Size of cultivated land/farm (Hectare)	Percentage of farms			Percentage of land			Percentage of total credit			Formal credit as % of total credit		
		Marv.	Ramj.	Abarj	Marv.	Ramj.	Abarj	Marv.	Ramj.	Abarj	Marv.	Ramj.	Abarj
1	0 - 2.50	4	6	13	1	2	5	2	5	6	20	—	—
2	2.51 - 5.00	25	59	31	13	37	23	18	57	27	42	27	9
3	5.01 - 7.50	40	20	41	34	21	45	43	17	52	40	30	36
4	7.51 - 10.00	11	6	9	13	9	14	12	7	9	38	36	37
5	10.01 - larger	20	9	6	39	31	13	25	14	6	52	32	10
Total		100	100	100	100	100	100	100	100	100	42	27	25

Sources: Calculated from interview data.

## 5. Summary and Conclusion

The need for credit is not confined to meeting cash operating costs for crops. However, credit is generally borrowed to cover cash costs for livestock, carpet production, and household consumption costs as well. Considering only crop operating costs, the credit cost ratios are .76, 1.36, and .91 for Marvdasht, Ramjerd, and Abarj respectively. The credit cost ratio higher than one for Ramjerd implies that credits are borrowed to cover more than only crop costs. When the costs for crops, livestock, and carpet production are considered, the credit-cost ratios are .60, .67, and .63 for the three regions respectively. Credit-operating cost ratios for different amounts of credit and different farm sizes within each of the regions (Table 3 and 4) also indicate that credit is acquired to cover other needs than just cash operating costs of the crops. Ratios

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higher than one supports this fact strongly. Credit per hectare figures (Tables 3 and 4) and regression results (Appendix) show the same conclusions.

The results show that farmers would meet most of their credit need regardless of the source of credit. They, however, would prefer to obtain the credit from formal sources where the supply and demand factors allow them to do so. Considering all three regions, only 32% of credits are borrowed from formal sources. In Marvdasht region which is adjacent to the city of Marvdasht, however, 42% of credit is borrowed from formal sources and the related figures for Ramjerd and Abarj are 27% and 25% respectively. Factors affecting the between-the-region differences in the percentage of formal credit include access to credit institutions, level of credit worthiness of the farmers, and size of the loan.

The percentage of non-borrowers for total credit is small, implying that almost all of farmers borrow from one or both formal or informal sources. The non-borrowers of informal credit are at most 9% whereas, the non-borrowers of formal credit are considerable. The non-borrowers of formal credit in Marvdasht is 14% and the related figures for Ramjerd and Abarj are 56% and 44% respectively.

Loan concentration within each of the regions is skewed toward large size loans and it is more skewed for formal credits. Loan concentration is less skewed for Marvdasht where larger size loans are borrowed and which is adjacent to the city or Marvdasht than for the other two regions.

In terms of beneficiaries of formal loans, in the first stage when formal loan granting starts until some point formal credits are paid through larger size loans and to larger size farms. Ramjerd and Abarj are examples of this situation. However, when the amount of formal credit supplied to a region increases it begins to cover poorer and smaller size farms as well and this situation is observed in Marvdasht. Therefore, it might be concluded that formal credit at first stage would worsen the income distribution and when a larger amount of credit is supplied it will improve it. Expanding formal credit granting to areas where there is shortage of formal credit can improve the loan concentration through (1) decreasing the number of non-borrowers of formal credit, and (2) increasing the share of formal credit from total credit.

In order to reach small and poor farms it is necessary to supply formal credit in some locations or through some agencies which are geographically close to the farms, otherwise, high credit cost resulting from the long distance and inconvenient trips to formal credit sources would discourage the small loans from being granted and small farmers from borrowing.

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## Appendix

THE EFFECTS OF FARM SIZE ON CREDIT-OPERATING COST RATIO AND CREDIT PER HECTARE  
FIGURES IN MARVDASHT, RAMJERD, AND ABARJ IN 1971/72

Region	No. of Observa- tion	Constant term A	Coeffi- cients B <sup>a</sup>	SEE	F	R <sup>2</sup>	Regres- sion Number
Credit-operating cost ratio as the function of farm size							
Marvdasht	72	0.96	-0.28.5	0.0107	5.96*	.08	1
Ramjerd	183	1.59	-0.1779	0.0162	5.92*	.03	2
Abarj	32	1.14	-0.1839	0.0404	1.05	.03	3
Credit per hectare as the function of farm size							
Marvdasht	72	7415	-0.3207	75	8.03**	0.10	4
Ramjerd	183	6164	-0.1743	63	5.67*	0.03	5
Abarj	32	8213	-0.3722	231	4.82*	0.14	6

a Negative signs for B coefficients shows that credit-cost ratio and the amount of credit per hectare decrease as the size of land increases. The reason for this, as explained before, is that credit is acquired for not only cash operating cost but to meet cash needs for livestock, carpet production and household consumption costs as well.

\* Significant at 5% level of significance.

\*\* Significant at 1% level of significance.

Source: Calculated from interview data.

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## LE SYSTÈME DE CRÉDIT AGRICOLE POUR LES PETITES EXPLOITATIONS EN IRAN.

### RÉSUMÉ

L'amélioration du système de crédit agricole au moyen des institutions formelles a été considérée une des stratégies pour promouvoir le développement de l'agriculture. On peut toutefois se poser beaucoup de questions quant'aux réalisations du système formel de crédit et il suffit de rappeler 1°) comment le système peut influencer les exploitations de petite dimension? 2°) peut-il éliminer les prêteurs informels? 3°) quel est son rôle sur l'adoption de nouvelles technologies?

Cet article a pour but d'analyser les différents effets du système formel et informel de crédit sur les exploitations de petite dimension. L'analyse se base sur des données tirées de l'expérience de 280 exploitations agricoles dans trois régions agricoles ira-



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*niennes. Pour expliquer la situation des crédits on a utilisé plusieurs facteurs tels que le rapport crédit/coût, le montant de crédit par exploitation agricole et le montant de crédit par hectare. On a présenté des données sur la concentration des crédits dans les deux catégories envisagées.*

*Les résultats montrent que les agriculteurs désirent obtenir du crédit pour satisfaire leur besoin indépendamment de la source du crédit même. Les agriculteurs toutefois préfèrent obtenir le crédit par des sources formelles. La concentration des prêts favorise les prêts de grande envergure et elle est beaucoup plus accentuée pour les prêts formels.*

*Les crédits formels peuvent d'abord rendre la distribution du revenu plus inégale mais quand une plus large quantité de crédit est distribuée le phénomène opposé apparaît. Si on veut intéresser les exploitations de petite dimension, il est nécessaire d'octroyer des crédits formels géographiquement auprès d'elles si non les agriculteurs se décourageront d'utiliser le crédit.*