
Role of Bank Lending in Sustaining Income/Wealth Inequality in Sri Lanka

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Attestation

I hereby declare that this submission is my own work and that, to the best of my knowledge and belief, it contains no material previously published or written by another person (except where explicitly defined in the acknowledgements), nor material which to a substantial extent has been submitted for the award of any other degree or diploma of a university or other institution of higher learning.

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Conference Papers

- Saliya, C. A. (2006a). *Bank capitalism in Sri Lanka favours protectionism under façade of nationalism or patriotism, as a mean to protect the affluent class*. Paper presented at the 6th Hawaii International Conference on Business, Honolulu, Hawaii.
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ABSTRACT

The purpose of this PhD thesis is to make a contribution to existing knowledge in the field of critical accounting by studying credit mechanisms and their link to income/wealth inequality in Sri Lankan society and the role of accounting technology in facilitating such mechanisms.

The literature review revealed that: a) Global inequality is aggravated by the disparity of economic development which is possible only through state intervention; b) Unemployment is considered as a dilemma for economic development in developing countries by most politicians/administrators/researchers; c) In any country, around 60-70 percent of employment is generated by small and medium sized enterprises (SMEs) and; d) Their major problem is access to credit. This research was designed to find out *how* the credit system works and *why* certain SMEs do not have adequate access to credit to develop their businesses; to provide employment; to increase the share of national income to the lower income groups; to narrow down the gap between the rich and poor within and between countries.

A case study research approach was followed to extract data on real-life experiences of the research participants. Reliability of data was ensured by using various verification techniques and maximum efforts were made to balance the two extremes of validity of the research; internal and external. The extent of representation by the cases and the bank was tested, and judged as high, with 12-14 characteristics common to the Sri Lankan credit culture and banking industry respectively. Marxian critical theories were used for theoretical guidance throughout the research.

The three case studies provide empirical evidence for the existence of the discriminatory nature of credit decision-making where two credit applicants were successful but a third credit applicant failed in obtaining credit. It is

contended that the two successful applicants were powerful enough to approach a more powerful bank Chairperson and to obtain credit outside the normal credit rules with the support of accounting technology and using masks such as patriotism and social responsibility. The other applicant, who was initially accommodated with credit at the lower level, could not convince the credit decision-makers at the higher level with expensive professionally prepared accounting reports. This applicant was not from an influential social network and could not reach the powerful credit decision-makers informally was rejected through strict application of credit rules. Deep analysis of these facts supports the Marxian claim that credit and exploitation mechanisms work towards concentration of wealth and sustaining income inequality.

Credit decisions supply money to influential individuals and it is argued that such economic power enhances the social powerbase of those individuals, which in turn reinforces the propensity to make preferential credit decisions, thereby making them richer. In contrast, a lack of money translates into powerlessness, deprivation and exclusion from social activities for the majority of the poor. In this process opportunities are lost to disadvantaged social groups and this necessarily results in poor people's economic status remaining stagnant.

These power-driven, discriminatory decision-making systems not only restrict the availability of financial capital for feasible projects, but also deny credit to potential enterprises. Further, wasting resources on unfeasible projects, while ignoring the need for nurturing potentially viable projects, are a double blow to efforts towards employment generation and economic development and therefore, are detrimental to the economic well-being of the general population.

These findings provide insight for policy formulators for more productive financial capital mobility systems in Sri Lanka. It is suggested that suitable State intervention in regulating SME financing could remove such credit-related obstacles to economic development, and work towards a fair distribution of economic benefits to the people in Sri Lanka and beyond.

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CHAPTER ONE

1 INTRODUCTION

1.1 Research motivation

Entrepreneurship promotion and enterprise development have been commonly identified as the main sources of employment generation by most development-policy formulators. These policy formulators include governments and academics as well as international development agents and experts (Bank of England, 1999; The World Bank, 1998). Enterprises, especially small and medium-sized enterprises (SMEs), provide a solution to unemployment/underemployment problems and therefore, improve the economic well-being of people. This research was initially motivated by the researcher's interest in finding out why developing countries like Sri Lanka do not produce adequate successful enterprises and generate sufficient employment opportunities so that the majority of poor people can improve their living standards.

The preliminary investigation, which is described in the next section, into this real-world problem shows that credit systems are playing a significant role in providing necessary financial capital for enterprises to start, grow and achieve economies of scale. Also, this preliminary investigation provides research findings that criticize certain bank credit systems and methods. On the other hand, irrespective of the status of the country and whether developed or not, there is a widely accepted consensus on the increasing gap between rich and poor not only within countries but also among countries because of an unequal distribution of income and wealth to all people throughout the whole world. Goulet (2001) explains this phenomenon as follows: "It is now apparent that development does not deliver economic well-being to all nations and people: in its distribution of benefits, it is not just (p. 2)".

The preliminary investigation raised doubts on the following issues: Is it common that certain credit decisions have been made without adhering to the principles of credit evaluation but have been based on other motives of the decision makers? Do such credit decisions work against enterprise development and employment generation? Does this social mechanism called a credit system act as a road-block for distributing economic benefits fairly and justly to all people in any country? What is the role of accounting technology in credit decision making? Therefore, the researcher decided to investigate and explore possible explanations for the existence of such links between credit mechanisms and income and wealth inequality in Sri Lanka.

1.1.1 Preliminary search

The preliminary literature review revealed that the contribution from SME businesses is significant to the tune of 60 or 70 percent of both the gross domestic product (GDP) and the employment generation of a country in general (Bank of England, 1999). However, the Governor of the Bank of England says, “A particular problem at this end of the scale is access to start-up or early-stage finance for disadvantaged groups in poor-neighbourhoods (1999, p. 207)”.

It is also argued that budding entrepreneurs from different demographic groups do not have similar opportunities in accessing finance; some groups have less access while other groups have more access to finance capital.

The Nobel Peace Prize in 2006 was awarded to Prof. Muhammad Yunus for his role in promoting financial services to the poor under the concept of Grameen Banking in Bangladesh. This highest level of recognition for Prof. Yunus’s effort in facilitating disadvantaged social groups of the society shows that there is a need for credit facilities to be extended to the poorer levels of society and that the banks are ignoring the potential of lower class enterprise (The Economist, 2006).

However, questions such as: “Is discriminatory credit decision-making a common phenomenon in Sri Lanka as well? If so, “How and why do bank

officers employ such decision-making methods into practice?” remain unanswered.

There are arguments that credit systems are part and parcel of a total socio-economic mechanism which, according to Marxism, is structured for continuous accumulation of capital to its owners. Marxism is a socio-economic theory which tries to uncover the way in which certain groups gain power in society and then hold that power for their own benefit (S. Moore, 1994).

According to this theory, bankers may generally prefer to lend to people who already have capital, so that capitalists can compete more effectively while eliminating new entrants to the market. Also, such lending approaches could act as road-blocks for enterprise development and aggravate unemployment problems especially in developing countries. Moreover, this chronic unemployment/underemployment problem could contribute towards a disproportionate delivery of economic well-being, increasing the income/wealth inequality in society. Therefore, the researcher’s interest was then further focused towards the role of the credit system in the context of entrepreneurship promotion and enterprise development and, accordingly, this thesis was entitled ‘The role of bank lending in sustaining income/wealth inequality in Sri Lanka’.

1.1.2 Motivation to adopt critical approach and positioning of the researcher

A dramatic increase in research interest on the roles of state and economic policies in economic development has been visible during the past decade especially from the critical theory school under Marxism with various neo-Marxian analyses and theories emerging. Neo-Marxism refers to theories within the Marxist tradition with certain variations to some of the original concepts of Marxism. These critical researchers (for example, Allahar, 2004; Goulet, 2002; Korzeniewicz & Moran, 2003; Lapavistas, 1994, 1997, 2000, 2003; M. Moore, 1997; Passe-Smith, 2003; Saad-Filho, 2003; Seligson & Passe-Smith, 2003b; Tinker & Gray, 2003) argue in favour of state intervention as against complete free-trade economic policies especially in facilitating a more conducive

entrepreneurial environment. Based on these theories, the researcher positions himself to investigate the research problem from the standpoint of Marxian critical theory.

Prominent economists (for example, Alan Greenspan, Muhammad Yunus, William Pesek) openly advocate the importance of state intervention and often treat credit as an important tool in dealing with poverty. Yunus says that, “credit is a human right and poverty is created by social systems” (2006, p. 27) while Pesek suggests that, “if developing nations are to become mature economies central banks must do their jobs” (Pesek, 2006, p. 15). These views also influenced the researcher to be more critical in his approach because a critical approach exposes and challenges the prevailing thoughts, systems and practices (O’Leary, 2004) which are fundamentally mediated by historically constituted social power relations (Kincheloe & McLaren, 2005).

1.1.3 The knowledge gap

The above preliminary search provides evidence for the importance of enterprise financing in employment generation and improving the well-being of people. Various development theorists (for example; Korzeniewicz & Moran, 2003; Seligson, 2003; Passe-Smith, 2003 and Abramovitz, 2003) have discussed uneven economic development and its link to income/wealth inequality among (as well as within) countries. The literature review discusses in detail the link between social mechanisms such as credit systems, exploitation and accounting technology and the disproportionate distribution of economic benefits among the people. But, what methods are used to justify such credit decisions and what motives and social factors drive the decision-makers in making such decisions, are further to be researched and explained.

1.2 Research questions

In light of the above knowledge gap, the research interest was narrowed down to investigate how and why a certain group in a society could have more access to credit than some other demographic groups. Similarly, how and why the

credit decision-makers facilitate credit applications from one group but deny credit applications from another group. These two questions are two sides of the same coin; *how and why certain bank lending processes* are discriminatory in nature.

Then, the researcher seeks to provide evidence from the literature for the existence of the mutual relationship between such lending and the disproportionate distribution of economic benefits among society at large. Mutual relationships between variables could generally create a reinforcing-mechanism. This dynamic nature of variables, which are complementary to each other's survival and enhancement, is called a co-integrated function. According to Marx, credit systems transform into powerful social mechanisms for the centralization of capital (Marx, 1867 in De Brunhoff, 2003) which in turn result in income/wealth inequality in societies. On the other hand, income/wealth inequality divides people into groups and, some groups are capable of enjoying credit while some groups are not (Bates, 1973 & 1991 in Cavalluzzo *et al.* 1998). Therefore, the credit mechanism and increasing social/economic inequality are two co-integrated functions which could create a mutually reinforcing chain of proceedings.

Based on the above explanations and arguments, the researcher seeks to explore what theoretical perspectives could be applied to explain the rationale behind this social mechanism and, therefore, the first research question of this research is defined as follows:

1. *Do credit mechanisms and income/wealth inequality create a mutually reinforcing cycle in Sri Lankan society?*

In other words, this research attempts to explore the nature of providing finances to SMEs in Sri Lanka and to explain *how* certain credit decisions are made and whether such credit decisions contribute to the creation of a mutually reinforcing cycle and *what* is the impact of such credit decisions on the inequality in the society. To facilitate the critical analysis and theoretical

explanation of this research question the investigating process proceeds in three stages:

- First, it seeks to explore the nature of credit decisions made in Sri Lanka by studying a few cases.
- Second, it focuses on how and what methods were used by decision-makers to make those credit decisions.
- Third, it attempts to explain the decision-making procedures applied and if applicable, to expose the motives behind such bank credit decision-makers.

The other research questions for this investigation are formulated from the literature reviews carried out in this research. The following research questions were derived from the preliminary investigation especially from the comments made by the Governor of the Bank of England (1999) discussed in section 1.1.1 of this chapter:

2. *Are credit decisions made in favour of influential businesspeople?*
3. *Are certain demographic groups at a disadvantage in obtaining credit?*
4. *As a result of favourable credit decisions, could influential groups of people get richer and more influential?*
5. *Are “ability to obtain credit” and “becoming more influential” mutually reinforcing?*

Such multiple research questions could provide useful insights about where to look for relevant evidence, especially when the researcher’s approach is critical and, when structural changes are expected towards more a fair and just financial capital mobility system as the end goal (Lincoln & Guba, 2003). Therefore, such research questions could provide a strong foundation to theorize the research findings more effectively and meaningfully.

1.3 Research methodology

An extensive literature review was done to frame the methodological philosophy behind this research. Significant overlapping and commonality are inevitable among the research strategies and methods used in social research today (Hammersley & Gomm, 2000).

The main data-collection techniques used in this research were conducting interviews and obtaining answers to questionnaires. Further interviews and cross-questioning were necessary for revalidation of data descriptions and in the story-building exercise.

In a multiple case study approach within a single inquiry, a considerable depth of investigation could be achieved towards a cogent conclusion by broad and deep analyzing of data of several cases comparatively and cohesively whereas in a single case study research, the amount of data collected and thick descriptions may be vital to develop more convincing arguments.

Propositional knowing is instrumentally valuable when the critical approach is followed by the researcher. Many researchers (for example; Hooper, 2001; Lincoln & Guba, 2003) advise that stating some theoretical statements when designing research will move the researcher in the right direction. According to Hooper (2001), these initial theoretical statements facilitate the researcher in building explanations and eventually, to compare the findings with the theoretical statement. The theoretical framework developed for this research is based on critical theories.

The conclusions, which are critical and subjective, are composed primarily by abductive inferencing (something might be the reason) supported by inductive reasoning based on empirical evidence. From the literature, some secondary data analysis on inequality and development measures was also necessary to support certain arguments.

1.3.1 Case study research

As case study research is often used in social research today, the soundness of the researchers' arguments is refined and ensured by investigating the cases in considerable *depth* rather than the *number* of cases studied and/or quantity of data collected on each case.

The case study research method is more appropriate in this research because, a study of individual elite political identity can be used as a lens to examine larger political processes, as identities are aggregated in political power and culture in which they are embedded (Hite, 1996). Most research on practical issues are case studies and some are reconstructed from evidence gathered by the research participants' personal experiences because they are relevant, interesting, politically 'hot' or even misunderstood (O'Leary, 2005). Also "case studies can take us to places where most of us would not have an opportunity to go" (Donmoyer, 2000. p. 61). This research is in a field where access to data is restricted and the researcher's personal experience was used to develop one case out of the three cases discussed.

1.3.2 Research design

The whole methodological process of this research consists of several components. The preceding sections described the research objectives, the research questions and the arguments on which the research questions are formulated. The following sections briefly deal with other components of the model namely: the theoretical framework; unit of analysis; field, site and the number of cases; case selection; data collection; and data management including in-depth analysis and theorization.

1.3.3 Theoretical framework

According to Lincoln and Guba (2003), the application of critical theories (for example: Marxism; neo-Marxism; feminism; constructivism; critical sociology; Freudian or Foucaudian theory, etc.) in researching real-life problems is more appropriate when the research is about an anticipation of social transformation,

particularly towards more equity and justice. Therefore, Marxian critical theory is considered as more appropriate to interpret and theorize the research findings in this research. Wolcott (1994) advises that “if a theory (or theories) works well as a starting place, to use it and, to let theories to guide the researcher” (p. 13). Accordingly, this selection of a critical theory at the beginning helped the researcher to maintain focus especially in the data collection and analysis stages.

1.3.4 Unit(s) of analysis

In the investigation process of this case study research, the subunits of analysis of the cases were identified as the incidents and events which have taken place, leading up to decision-making (Hooper, 2001). In the process of theorization these subunits of analysis collectively explain a macro-level holistic unit of analysis; the *credit mechanism* which significantly possesses the power of controlling financial capital in Sri Lanka. Cases were selected from different perspectives to represent this credit mechanism.

1.3.4.1 Data collection and case selection

Case study is a main method. Within it different sub-methods are used: interviews, observations, document analysis and record analysis, work samples and so on. ...are part of what is called the *multi-method* approach...If they *converge* (agree) then we can be reasonably confident that we are getting a true picture (Gillham, 2000. p. 13).

The multi-method data collection approach employed in this research consisted of interviews, questionnaires followed by further interviews for revalidating and story building complemented with document and record analysis. Direct observations connecting with personal experience (Wolcott, 1994) and daily diary narrations (Hyers, Swim, & Mallett, 2006) of the researcher were reconstructed using the same interview questions and questionnaires as were used with other research participants.

Initially nine senior bank officers (with more than 20 years of experience) were interviewed several times over the phone to gather basic information about

lending instances where they were involved and/or were aware of the decision-making process. Among the cases reported by the participants, two participants reported three cases comprehensively. Data was available for another case by reconstructing the researcher's own personal experience, through interviews of other participants and, also by document and record analyses.

1.3.5 Number of cases

After considering the boundaries, access to fields, sites and data it was decided to select at least two cases which could represent the five scope criteria (see below) concurrently and/or separately. However, an additional case was also considered because it is politically interesting and linked to the economic policies of Sri Lanka. Also, providing evidence from multiple cases is often considered more compelling, and the overall study is therefore regarded as being more robust (Herriott & Firestone, 1983). Further, several case studies in one inquiry is advisable when the inquiry is about relationships between variables, rather than generalization to a population (Woodside & Wilson, 2003). Therefore, it is concluded that a maximum of three cases would be selected out of the cases presented by the participants on the grounds explained below.

The scope of this inquiry is based on five criteria: credit decision-making processes (formal and informal); size of the enterprise and entrepreneurship (small and medium); outcome of credit decisions (granted and denied/not granted); hierarchical level of the decision-makers (high and medium); and type of credit applicant (influential/capable and not influential). The following table (Table 1-1) summarizes the five scope criteria for the three selected cases.

Table 1-1: Representation of the scope criteria by the three selected cases

	<i>Case I</i>	<i>Case II</i>	<i>Case III</i>
Scope criteria			
Decision-making process	<i>Informal</i>	<i>Informal</i>	<i>Formal/informal</i>
Size of the enterprise	<i>Medium</i>	<i>Medium</i>	<i>Small</i>
Outcome of the decision	<i>Granted</i>	<i>Granted</i>	<i>Not granted</i>
Decision-maker	<i>Chairperson</i>	<i>Chairperson</i>	<i>Middle-management</i>
Credit applicant's status	<i>Influential</i>	<i>Influential</i>	<i>Not influential</i>

All three credit applications which have been considered for this inquiry, are typical in nature in the Sri Lankan context and therefore represent the general credit culture in Sri Lanka.

Apart from the primary data collected through interviews and questionnaires, document and record analyses were done for all three cases with relevant archival records such as legislation and enactments, circulars issued by the subject bank and the regulatory authorities, annual reports, rating reports published by rating agencies such as Capital Intelligence and FITCH, research reports published by stock brokers, newspaper and magazine articles and management reports.

1.3.6 Data management; story building and in-depth analysis

The method used for data analysis within the framework of this case study research approach is story building through narrative analysis. The literature provides secondary data to elaborate the uneven distribution of economic benefits among and within countries (see Kegley Jr. & Wittkopf, 1989; Maddison, 1983, 2002, 2003; The World Bank, 1998, 2003a, 2003b).

Narrative analysis (Riessman, 1993) or the narrative mode of knowing, also referred to as the paradigmatic mode of knowing (Bruner, 1990) is the primary analytical strategy employed in this data analysis because: first, as Llewellyn (1999) claims that, narrating is a mode of thinking and persuading that is as legitimate as calculating (p. 220); secondly, as Czarniawska (2004) points out, “narrative” in Latin probably comes from *gnarus* (knowing) (p. 7).

Qualitative researchers are story tellers (Wolcott, 1994). Therefore, the three cases were constructed and reported as stories. According to Polkinghorne (1987 cited in (Czarniawska, 2004) plot is the basic means that brings all the events and incidents into one meaningful whole. In this staging process, first, main characters are introduced and then the story is presented following a sequential and/or a logical order, whenever appropriate. And then these stories were further investigated with considerable depth by cross-questioning the research participants and examining post-event developments.

Therefore, the data collection, analyses and interpretations are done through continuous interaction with the research participants. It was a reiterative process with a focus on story building, in-depth analysis and interpretation.

1.3.7 Interpretation and theorization

The literature review was structured to cover Marxian critical theories and their application in accounting. The analytical interpretation and theorization of research findings were based on Marxian critical analysis of social interaction and social life described and analyzed from the case stories.

In theorizing the findings of this research, the researcher attempts to convey a message to the policy formulators of developing countries on the importance of credit mechanisms in financing SMEs as a solution for unemployment, if they want to guide their countries to prosperity and improve the well-being of the people.

1.4 Significance of the study

The significance of this study is two-fold: first it critically analyses and documents the prevailing credit culture and systems practised by a particular Sri Lankan bank. Second, the research findings may help the policy formulators of developing countries to understand micro-influences within the credit system and make necessary reforms if they want to develop their economies and to distribute the benefits to all people fairly and justly.

A substantially prolonged debate is apparent among many economic, social and political theorists, psychologists, anthropologists and other various scholars (for example, Abramovitz, 1986; Firebaugh, 1999; Khan, 1979 Korzeniewicz & Moran, 1997; Kuznets, 2003; Maddison, 1983;) on the rising inequality of world income distribution and the widening of internal gaps between rich and poor people (Lewis, 1966; Ranis, 1972; Rostow, 1990). The experts have developed and been redeveloping various theories to explain the situation and explore the crux of the matter with a view to finding a solution to this problem. Access to productive knowledge, access to capital markets, population stress, lack of natural resources, quality of human capital, culture, religion, ethics, quality of institutions and policies, lack of leadership and vision, power-hungry leaders or nations, imperialism or colonization, globalization, bureaucracy, corruption (Gray, Owen, & Adams, 1996), familial cronyism, lack of corporate governance and others are most popular among the numerous causes proposed. In this light, it would be timely to investigate particular bank-lending practices on development/underdevelopment of a country.

1.5 Limitations, remedies and some notes to the reader

The following issues were identified as the major barriers to the research study, analysis and theorization. First, to evaluate the effectiveness of the credit decisions observed in these case studies, availability of post-event information was limited to published data and to the responses of the research participants, as the researcher left the bank in 2003.

Secondly, all the cases belong to one private bank in Sri Lanka; however, according to Hooper (2001), it does not affect representativeness because “explanations are sought and the validity of the explanations or theory derived depends on the logic of the analysis not on how typical the cases may be” (p. 1). On the other hand, Gluckman (1961) argues that “clearly one good case study can illuminate the working of a social system in a way that a series of morphological statements cannot achieve” (p. 9 cited in Mitchell, 2000). Also, according to Chua, case studies conducted in the real-life-world of actors are preferred to distant large scale sampling or mathematical modeling of human intention” (Chua, 1986. p. 615).

Thirdly, organizing and getting comprehensive responses to questionnaires, and prompting participants’ memories, etc. were challenges. Fourth, because the cases are from Sri Lanka, where socio-cultural and political backgrounds are different from that of developed countries, the reader might be unfamiliar with some of the situations, however, every attempt was made to make the case studies easy to read and understand and, also a full chapter has been dedicated to describe the background of Sri Lanka.

Then, anonymity was necessary to protect the real case and its real participants, therefore, the names used in these cases are fictitious and therefore, some important background information had to be suppressed which made the story-building challenging.

Finally, effective organizing of the description, analysis and interpretation of three case studies and integrating them into a cogent conclusion were challenges. Traditionally, the cases are analysed case by case. However, it seems more effective to consider similar cases together when the research is done using multiple-case methods. Every attempt was made to avoid confusion by providing cross-references and drawing attention to the relevant events of the case in the analysis chapter. However, this issue would not be a critical one because they are presented as simple stories.

The researcher was unable to find related research in Sri Lanka, although this likely increased the originality of this research topic, it also prevented the researcher building on, and comparing this research findings with previous research findings regarding this research topic.

1.6 Chapter framework

This thesis consists of nine chapters. The rest of the thesis is organized through the next eight chapters as follows:

Chapter two reviews the literature; the first part this chapter discusses about global inequality and its integration to credit mechanism and, it attempts to justify briefly why Marxian theories are appropriate and convincing in explaining the research findings of this research. Then it portrays the need for theoretical analysis of the research problem under study, and explains why the literature review focused on critical theories, especially Marxism, from an accounting perspective.

Chapter three illustrates the methodology applied in this research. The first two sections of the methodology chapter were dedicated to elaborate the strength of the critical theory perspective, with a literature review on the historical evolution of theoretical and methodological thought and paradigms. Then, it proceeds with justifying the appropriateness of qualitative research methodology, and the application of the case study research approach in this research. Chapter four describes the application of specific research methods and techniques used in this research.

Chapter five provides a brief description of Sri Lanka and its socio-economic and political background drawing special attention to money, credit, power and the culture of informal methods. Chapter six presents the three case study stories. Chapter seven analyses those case studies and discusses the mutual relationships with continuous validation and reliability checks with the research participants and peer scholars. Chapter eight interprets the research outcome from theoretical perspectives and Chapter nine draws conclusions.

1.7 Conclusion

This thesis seeks to explore the nature of particular credit decisions made in Sri Lanka by studying three cases. According to Marxian analysis, money means power and success depends mostly on power. Similarly, lack of money deprives the majority of the poor from social activities even if they have the necessary skills and abilities. Bankers, commonly known as the guardians of public funds, have indirect possession of money. Especially in a country like Sri Lanka the bankers enjoy much power through their lending decisions irrespective of the extent of their authority for decision-making.

In the final analysis, this thesis seeks to analyze the *credit mechanism* in Sri Lanka and examine the role played collectively by the social-cultural and economic-political factors in credit decision-making. It also seeks to explore possible links (positive or negative) between such credit decisions and the increasing inequality in Sri Lankan society (The Central Bank of Sri Lanka, 2008). Therefore, the research findings might be helpful in restructuring the financial capital mobility system towards economic development and for just income/wealth distribution in Sri Lanka, and beyond.

CHAPTER TWO

2 LITERATURE REVIEW

2.1 Introduction

This chapter, firstly, presents and reviews the available literature on long-term income/wealth inequality trends both between and within countries. Then it applies Marxian critical theory and a Marxian explanation of historical development to explain these long-term income/wealth inequality trends by linking social power and access to financial capital to income/wealth. Finally, this chapter extends Marxian interpretations of linkages between social power, access to financial capital and income and wealth to explain the ineffectiveness of credit mechanisms in developing countries in relation to SMEs.

Marxism has earned vast acceptance as one of the grand theories which tell the story of social history (George, 2003) and, according to Tinker, “Marxist value theory provides a rich vein of research analysis and practical engagements” (1999, p. 643). Neo-Marxism is a critical theory developed upon the core principles of traditional Marxism which is widely called classical Marxism. Therefore, in this thesis the term ‘Marxian’ is used to represent both the classical and neo-Marxism.

These Marxian critical interpretations provide the basic theoretical framework for interpreting and theorising the findings of this research.

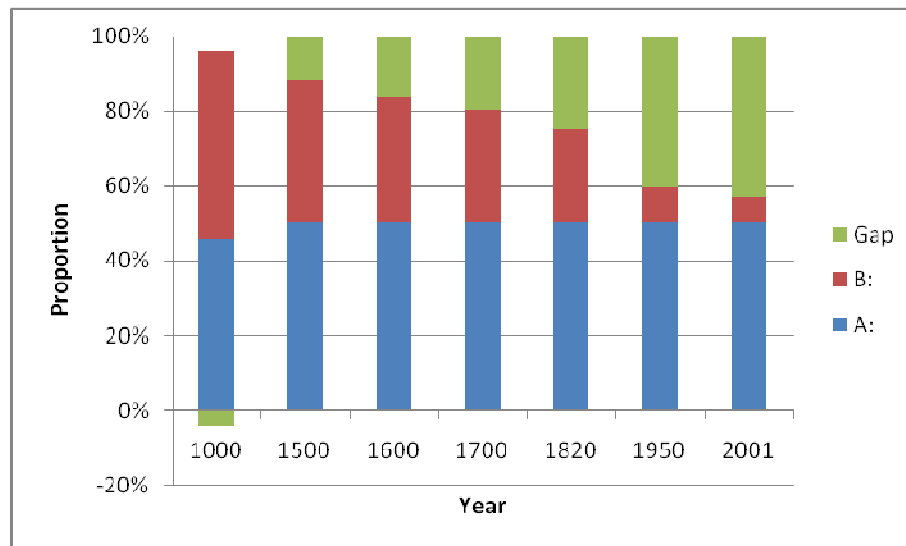
This chapter consists of ten sections. In the next two sections (2.2 and 2.3) there is a discussion of potential mechanisms inherent in the vertical inequitable relationships both among countries and within Sri Lanka. Then it critically reviews the accessibility, affordability and availability of credit to SMEs. Then (in 2.5) there is a brief introduction to Marxism and a review of literature on the application of Marxian concepts to show why critical Marxist lenses are useful in critical accounting research. In the sixth place, it reviews the Marxian

critiques on global inequality and associated links to credit. The chapter proceeds to illustrate the influences of national capitalist forces in the weakening of state power and sustaining inequality within a country. The next section (2.8) elaborates the role of the financial capital mobility system with a view of explaining the coalition between financial and industrial capitalists followed by how the credit system impacts on unequal income distribution. Then there is an outline of the Marxian interpretation of social structure and credit system. Finally it summarizes the chapter contents and provides conclusions.

2.2 Inequality among and within nations

To frame the theoretical foundations for this research it is important to examine how world economic inequality and credit mechanisms are co-integrated through different levels. Wealth generation and capital accumulation in the world's economy exist at different levels—from the international to the national, from local to institutional and finally to the individual, and there is a vertical relationship across these levels (see Baumol, 1986; Korzeniewicz & Moran, 2003; Seligson & Passe-Smith, 2003b). That is, the existence of inter-country economic inequality creates intra-country inequalities which finally result in sector/industry inequalities (Wickrama & Mulford, 1996). Reciprocally, sectorial inequalities reinforce intra-country inequalities which, in turn, contribute to maintain inter-country inequalities (Wickrama & Mulford, 1996). This discussion exposes the knowledge gap in this field with regard to *how* and *why* credit mechanisms facilitate this world system.

According to Maddison (2003), inter-country inequality of world economic growth has been evident since the year 1000. Gross national product, per capita GNP and their growth rates are the traditional measures used to assess the progress of economic development. The proportional share of poorer countries has been drastically reduced while the richer nations have been able to maintain their share and therefore the gap between rich and poor countries is widening significantly every year (Maddison, 2003) as shown in Figure 2.1 below.



A: Rich countries; Western Europe, Australia, Canada, New Zealand, USA and Japan

B: Poor countries; Eastern Europe, Former USSR, Latin America, Africa and Asia (excluding Japan)

Compiled by the author (Source: Maddison, 1983 & 2002)

Figure 2-1: Proportional impact of the increasing gap between rich and poor countries

As shown in Table 2.1 below, this widening gap continued and recorded close to \$20,000 GDP in 2001 with rich countries enjoying \$22,832 of GDP per capita while poor countries recorded only \$3,339 of GDP per capita (Maddison, 2002). In fact, in 1950, rich countries had a GDP per capita nearly 5.2 times of that of poor countries. These rich countries had increased their GDP per capita from \$5,663 in 1950 to \$22,832 in 2001: 6.8 times of that of poor countries (Maddison, 2002). Maddison (2002) argues that the gap continues to widen, in absolute terms, if those countries continue with their present economic growth rates. He predicts that the gap will be nearly \$25,000 by the year 2015.

Table 2.1 below elaborates the gradual increase in this gap. It provides data for each group of countries separately compared to the average world GDP per capita income.

Table 2-1: Widening gap between rich and poor countries measured by GDP per capita (1990 international \$)

<i>Year</i>	<i>1950</i>	<i>1962</i>	<i>1973</i>	<i>1990</i>	<i>2001</i>	<i>2015</i>
Group of countries	<i>Projected</i>					
Western Europe	4,594	7,512	11,534	15,988	19,196	24,226
Australia, Canada, NZ & US	9,288	11,537	16,172	22,356	27,892	36,400
Japan	1,926	4,778	11,439	18,789	20,722	23,472
"West" (Group A) Average	5,663	8,466	13,141	18,798	22,832	29,156
Eastern Europe	2,120	3,250	4,985	5,437	5,875	8,886
Former USSR	2,834	4,130	6,058	6,871	4,634	6,450
Latin America	2,554	3,268	4,531	5,055	5,815	7,163
Asia (Excl. Japan)	635	837	1,231	2,117	3,219	5,487
Africa	852	1,038	1,365	1,385	1,410	1,620
"Rest" (Group B) Average	1,091	1,478	2,073	2,707	3,339	5,101
World Average	2,114	2,921	4,104	5,154	6,043	8,100

Source: Maddison, 2002

Further evidence has been provided by the World Bank for the continuation of this widening gap between rich and poor due to the differential growth rates of their economies (see The World Bank, 1998, 2004). Sri Lanka is no exception when compared to other countries. Sri Lanka would have to grow for 445 years to close the gap with rich countries at an annual growth rate of 2.9% (average growth rate between 1960 and 1998), while the Dominican Republic; the poorest, would need 923 years (Seligson & Passe-Smith, 2003b).

This disparity in economic growth (wealth generation) between rich and poor countries is depicted in Figure 2.2 (below) to show that growth rates of both the rich and poor countries gradually lowered until the 1980s and thereafter stagnate at around 2.5 percent for the rich and about 0.3 percent for the poor countries.

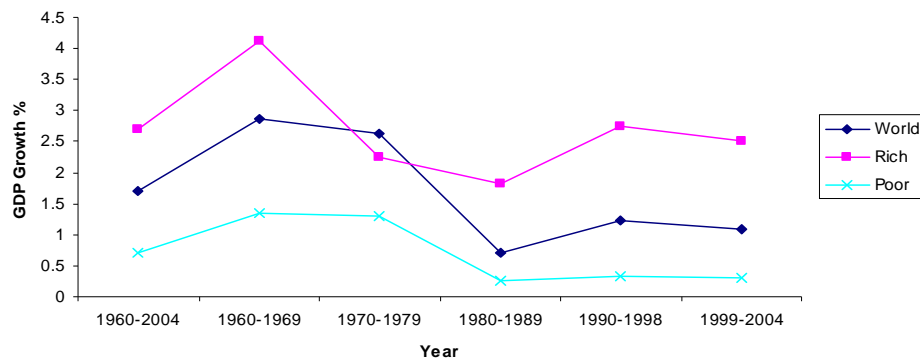


Figure 2-2: The uneven development growth between the rich and poor countries

Source: Compiled by the author

World system theory, a neo-Marxian approach, argues that peripheral developing countries are nested in world system under rigid influence of core developed countries (Schuurman, 1993). Most developing countries are trapped in the production of primary agricultural and mineral goods of which prices are largely determined by developed countries (Wickrama & Mulford, 1996). Within this system the peripheral countries are not able to escape, instead their resources and labour are exploited by the core countries resulting inter-country inequalities between core and peripheral countries. Furthermore, dependent economies (e.g., plantation) in peripheral countries are inherently inequality-generative because of the disarticulation among economic sectors as well as disparities between urban and rural sectors (see Wickrama & Mulford, 1996; Wimberley, 1990).

2.3 Global inequality and Sri Lanka

Although as country Sri Lanka has improved its position compared to other countries in the region, the poor segment of the population has not benefited proportionately. According to the Central Bank of Sri Lanka (CBSL), 40.73 percent of the Gross National Income (GNI) is shared among the top 10 percent (the affluent class of the society) while the low-income 40 percent of the population shared only 11.83 percent of the total national product (The Central Bank of Sri Lanka, 2004). However, the corresponding averages for the whole world are worse. More than 65 percent of the world GNI is consumed by the richest 10 percent of the world's population. Professor Muhammad Yunus ascribed this disparity to credit systems and stressed this point in his Nobel Lecture (2007):

Ninety four percent of the world income goes to 40 percent of the population while sixty percent of people live on only 6 percent of world income. Half of the world population lives on two dollars a day. Over one billion people live on less than a dollar a day. This is no formula for peace (p. 1).

The comparative figures in 1996/7 for Sri Lanka show that the gap is widening. In 1996/7 the poorest 40 percent of the population had 12.83 percent (11.83% in 2004) of the national income while the richest 10 percent enjoyed 37.28 percent as against 40.73 percent of the national income in 2004. Table 2.2 below shows the pace of this widening gap between per capita income of the poor and the rich countries. The per capita national income of wealthy countries was 23 times that of the per capita national income of the poor countries in 1950. After undergoing development dilemmas for more than 50 years, this gap had increased to 62 times by 2001.

Table 2-2: Gap is widening: average per capita national income (US\$) comparison between low-income countries and high-income countries

<i>Year</i>	<i>High-Income Countries (A)\$</i>	<i>Low-Income Countries (B)\$</i>	<i>Absolute Gap (A)-(B)\$</i>	<i>(A)/(B) Times</i>
<i>1950</i>	<i>3,841</i>	<i>164</i>	<i>3,677</i>	<i>23</i>
<i>1980</i>	<i>9,648</i>	<i>245</i>	<i>9,403</i>	<i>39</i>
<i>2001</i>	<i>26,710</i>	<i>430</i>	<i>26,280</i>	<i>62</i>

A: The rich countries

B: The poor countries

Source: (The World Bank, 1998, 2004)

Some studies conclude that there has been little or no change in inter-country inequality in recent decades (Berry, Francois, & Christian, 1983; Peacock, Greg, & Charles, 1988) whereas other studies conclude that national incomes have continued to diverge (Jackman, 1982; Maddison, 1983, 2002).

Table 2.3 shows that 82.7 percent of the world income is shared by 20 percent of the world population while the poorest 20 percent enjoyed only 1.4 percent of world income in 1989. The disparity has been aggravated during the last 15 years, decreasing the share of world income to 1.2 percent to the poorest 20 percent of world population and the richest 20 percent had increased their share to 83.1 percent by 2004.

Table 2-3: Distribution of World GDP, 1989 and 2004 (percentage of total with quintiles of population ranked by income) compared with Sri Lanka

	<i>World</i>		<i>Sri Lanka</i>	
	<i>1989</i>	<i>2004</i>	<i>1989</i>	<i>2004</i>
Population quintiles				
<i>The Richest 20%</i>	82.7%	83.1%	56.7%	55.1%
<i>The Second Richest 20%</i>	11.7%	11.9%	19.5%	19.9%
<i>The Third 20%</i>	2.3%	2.2%	12.5%	13.1%
<i>The Fourth 20%</i>	1.9%	1.6%	7.8%	8.3%
<i>The Poorest 20%</i>	1.4%	1.2%	3.54%	3.6%

Source: (The Central Bank of Sri Lanka, 2008; United Nations Development Program (UNDP), 1999, 2008)

The reduction or stagnation of the GDP share to the poorest quintile does not necessarily mean that poor people are getting poorer in absolute terms. However, it is evident that the disparity in distribution of income among the population of the world, as well as in Sri Lanka, is being sustained. A banking system is an essential facility for the survival of the world economic and social system. Social structures are reflected through systems and mechanisms such as the banking system and credit mechanisms. Moreover, banking facilities in developing countries were originally established to fulfill the financial and credit needs of planters, mine owners and businessmen in those countries (Wickrama & Mulford, 1996). Even today, in developing countries banking systems basically serve the upper class of society and provide a significant support to the sustained inequality in the society as a whole. This preferential and potentially discriminatory nature of banking services in developing countries, especially in providing debt capital for SMEs, is discussed in the next section, citing relevant literature.

2.4 Accessibility, affordability and availability of credit to SMEs

The section 1.1.1 of Chapter one outlined problems of accessing finance for disadvantaged group in the poor segment of the society. Many researchers (for example; Bank of England, 1999; Dunn & Cheatham, 1993; Ivy, 1997) are of the view that the lack of financial capital is the main reason for most SME failures. More importantly, these researchers argue that access to credit is limited to certain groups of society. Cavalluzzo et al. quote Bates (1973 & 1991) and explain this theory as follows:

In order to facilitate that growth, those businesses often turn to institutional sources for credit. It is a concern, therefore, that a growing body of evidence suggests that owners of small businesses from some demographic groups may have less access to institutional financing (Bates, 1973; 1991; Cavalluzzo & Cavalluzzo, 1998) (2002, p. 641).

This theory suggests that some demographic groups are discriminated against in the provision of credit because they lack certain qualities or/and factors which are the prerequisites for obtaining credit. Many researchers who attended the “Workshop on the Challenges in SME Financing” held in Sydney in 1999 have discussed pertinent international experiences principally from Australia, the UK, the USA and New Zealand. They argued that there were not adequate finance providers for SMEs. Most of the research papers presented in this workshop were critical of the inability of small or budding enterprises to obtain finance. They criticized banks’ dominating role in providing finance to SMEs because there are very few lenders who facilitate them (Whincop, 2001).

Further, instead of microenterprise development, Powell (2008), after studying encouraging success stories from nations in Asia (China, India), Europe (Ireland) and even Africa (Botswana), concludes that encouraging small-business entrepreneurs is the best way to achieve and maintain general affluence.

In 1976 Professor Muhammad Yunus instituted the “Grameen Movement” which was considered a revolutionary step to address the low per-capita-income

issue in Bangladesh. Yunus, who won the Nobel Peace Prize in 2006 for this concept and its implementation in Bangladesh, says,

One can reasonably state that people are poor today because of the failure of the financial institutions to support them in the past. Like the right to food, clothing, shelter, education and health, credit should also be recognized as a fundamental human right (Yunus, 2007, p. 2)

The Economist criticized this programme by questioning “whether this form of lending has led to peace, the presumptive reasoning behind the award [Nobel Peace], is just as big an unanswered question” (The Economist, 2006, p. 71). After implementing this micro-finance scheme for nearly 40 years Bangladesh is still one of the poorest countries in the world.

Further, Shaw (2004) reveals from her study in Sri Lanka on two such micro-financing programmes in the rural Hambantota area that post-credit incomes are unlikely to increase because of financial, infrastructural and socio-cultural barriers. She concludes her case study research outcome by stating that:

Microenterprise development programs need to be complemented by investment in social and physical infrastructure; they are no substitute for it. In arid rural areas, where microenterprises face severe market and infrastructure constraints, microenterprise development is unlikely to facilitate poverty exit (Shaw, 2004, p. 1262)

When the project is larger the owners could have access to MOP if they are adequately financed. Microfinance is too little and does not constitute capital.

Researchers in this field have also challenged that some bankers lack fundamental knowledge about credit evaluation and posed questions/statements such as:

- Do bankers always know best? (Dunn, Cheatham, & Cheatham, 1991, p. 1);
- Are the banks doing enough for small business? (Chadwick, 1982, p. 1); and

- 30 percent of bank loan officers do not understand appropriate financing (Dunn & Cheatham, 1993, p. 3).

Credit systems which are under the control of a privileged class provide evidence in support of Goulet's claim that "an economy that distributes its benefits in ways which exclude many is unjust and inequitable" (Goulet, 2002, p. 3).

2.5 Marxian critical theory and its application in critical accounting

Neimark (1990) refers to Marx's notation that the role of philosophy is not to describe the world but to change it and suggests that "the aspirations of critical accountants should be no less" (p. 111). According to Therborn (1996) Marxism became the theoretical perspective for a generation of radicals who found it the best way to understand social and economic injustice. Therefore, the privileged position of Marxism as a mode of analysis and interpretation of the capitalist system and its consequences became dominant and legitimate (Cooper, 1997; Jameson, 1984 cited in Cooper, 1997) but Cooper further advises to abandon "the traditional Marxian version of revolution and socialism" (1997, p. 27). Referring to the criticisms on development agents such as the World Bank; Annisette (2004) suggests that brave attempts are necessary "to draw accounting scholarship into an arena where critical accounting voices need desperately to be heard" (p. 321).

Literature relating to critical accounting and Marxist critical research, which are more focused on money, exploitation, class conflict and consciousness, the role of credit, social relations and their dynamic links to income/wealth equality, reviewed in detail from a critical accounting perspective to develop the theoretical framework to interpret the findings of this research.

2.5.1 Marxism: a brief introduction

Marxism is an economic and political philosophy developed by Karl Marx (1818-83), along with Friedrich Engels (1820-95). According to Marxism, throughout the course of human history, a profound struggle has developed

between the “haves” and the “have-nots”. Marx (1891) suggests that the capitalists allow the masses access to the means of production and the workers are paid a wage which is just enough for the worker to survive and to have family and children for replacements. According to Marx (1891), neither capitalist nor labourer is conscious of this exploitation and, therefore, workers think they are paid fairly and “the capitalists think that they are rewarded, not because of their exploitation of the workers but for their cleverness, their capital investment, their manipulation of the market, and so on” (George, 2003, p. 25). Therefore for Marxists there has been exploitation of the masses by a dominant group of people, throughout history, creating a conflict called “class struggle” between two classes; the bourgeoisie (the capitalist class that owns the means of production) and the proletariat (the working class, which is at the mercy of the capitalists) and this class struggle has been the main agency of historical change of world systems.

The capitalist class, which owns the means of social production controls society and constructs values and social relationships in their own interests (Marx & Engels, 1848). In this process the *credit system* including bank loans plays a decisive role in the battle of competition, and is finally transformed into a powerful social mechanism for the centralization of capital (Marx, 1867 cited in De Brunhoff, 2003).

2.5.2 Application of Marxian theories in critical accounting research

This section aims to describe how and why certain Marxist concepts have been utilized in critical accounting research. With regard to the Marxist concept of exploitation, Hooper and Kearins (2008) refer to the wealth confiscation from Maori in New Zealand through ledger accounts and argue that administrations wanted to be seen as demonstrating sympathy for Maori, while maintaining in fact “a figurative distance” to enable the mechanism of exploitation. According to Marx, the main purpose of the capitalist is to extract the greatest possible surplus value and consequently to exploit labour-power to the greatest possible extent (Marx, 1847 cited in Cauter, 1967). This concept of extreme extraction of

value from a group of people in a society, termed as exploitation in Marxism, provides a powerful tool for scholars to explain other unfair extractions as well. Hooper and Kearins (2008) suggest that “accounting acts as a key technology in achieving a redistribution of assets” (2008, p. 1262) which means it could facilitate exploitation “particularly where accounts can be shown to reveal a poor return on assets” (p. 1262). They further point out that accounting can function as a macro-pricing mechanism and also is “deeply-embedded” in serving the masters means the owners of assets (capital) in accumulating wealth. Hence, the accounting function plays a significant role in the exploitation of wealth in a capitalist society in sustaining income/wealth inequality.

Harney (2005) argues that “the crisis of measurement brought on by the growing dominance of what Marx named ‘general intellect’ is a profound challenge not only to management but specifically to its recording-machine, accounting” (p. 579). According to Marx, the ‘general intellect’ (knowledge as the main productive force) fully coincides with capital (Marx, 1974 cited in Virno, 2001). General intellect is a crucial factor in production. Marx describes it as a combination of technological expertise (which includes accounting) and social intellect or general social knowledge. This concept insists the increasing importance of intellectual systems in social organization. Virno (2001) explains that the general intellect includes formal and informal knowledge, imagination, ethical tendencies, mentalities and “language games” as well. “Thoughts and discourses function in themselves as productive ‘machines’ in contemporary labour and do not need to take on a mechanical body or an electronic soul” (Virno, 2001, p. 1). This Marxist theory influences critical accounting researchers to examine accounting as part and parcel of general intellect and provides an important lens to investigate accounting and social phenomena in a radical point of view.

James (2008) uses the Marxist concept of alienation to study the accounting academics’ labour market in Australia. According to Marx, capitalism is an alienating force that separates workers from products, the process of production, the true nature of the worker and also from other people and, under late

capitalism, their own integrity (Marx, 1975; Blumberg, 1989 cited in James, 2008). Further, according to James (2008), in the contemporary context, capitalism promotes separation of the worker from the whole environment. This alienation is apparent in the newly commodified fields as well such as care services, education, the leisure industry and even religion, etc, and now popularly termed as “commodification of every-day life” (Dominelli & Hoogvelt, 1996; Tinker, 1999). This reasoning process based on Marxist concept of alienation provides a good lens to investigate into techniques and means of protecting and/or strengthening one group of people at the cost of another group in a society.

Catchpole, Cooper and Wright (2004) attempt to view the state, capital and accounting from a holistic perspective seeing the social relations and argue that accounting has been a central part of capitalism. According to them, “what is crucial to remember is that, in the process of accumulation...capitalism [is] characteristically uneven” (p. 1047). Also Chiapello (2007) suggests that “capitalism and a certain kind of double-entry bookkeeping practice that was able to highlight the circuit of capital were inextricably linked” (p. 263) and therefore, show that the notion of capitalism itself is rooted in accounting notions. However, according to Bryer, the true involvement of accounting to capitalism is not double-entry bookkeeping (DEB) but the capacity to calculate rate of return on capital (2000a, b cited in Chiapello, 2007). Meanwhile Carruthers and Espeland assert that the relationship between accounting and capitalism is not merely technical but a rhetorical bond and a justification (1991 cited in Chiapello, 2007). Chiapello further insists that “even when badly kept and useless as a decision aid, accounting contributes to the legitimacy of practices originally considered illegitimate” (2007, p. 264). She also argues that not only the capitalist system but also the concept of capitalism itself is an outcome of influence of accounting ideas on economic and sociological thinking and therefore, “the concept of capitalism is indissociable from representation of economic life shaped by an accounting outlook” (2007, p. 264).

Armstrong (2008) refers to “the capitalist social relations of production” and “social structure” and asserts that the economic power is wielded through the medium of accounting. The idea of capital *accumulation* also developed through DEB especially with the introduction of capital account, profit and loss account and the balance sheet in the 15th century (Sombart, 1992 cited in Chiapello, 2007). However, according to Webber, “the important fact is always that a calculation of capital in terms of money is made, whether by modern book-keeping methods or in any other way, however primitive and crude” (Webber, 1992, p. 18 cited in Chiapello, 2007). More relevant to this research Yamey suggests that the DEB system “was able to record affairs of the most unscrupulous money-lender or crooked businessman” (Yamey, 2005, p. 81).

Bishop and Boden (2008) utilize a broadly Marxist approach to explore regimes relating to disability in the transition from feudal to capitalist societies and to show how such a transformation placed new emphasis on the maximization of the surplus value of labour utilizing accounting technologies. According to Tinker “labor and value are synonyms for each other...for Marx, the phrase, ‘the value of labor’ is meaningless” (1999, p. 658). Therefore, this Marxist lens provides valuable insight in studying utilizing accounting technologies to maximize wealth by way of unpaid labour; surplus value (Caute, 1967).

With reference to Sri Lanka, Wickramasinghe and Hopper (2003) use the Marxist concept of modes of production (MOP) to analyze and interpret the cultural political economy of management accounting controls of a textile Mill in a traditional Sinhalese village in Sri Lanka. Wickramasinghe and Hopper (2003) disagree with many Marxist writers who argued that production relations constitute the base for legal and political superstructures. They argue that those approaches are too economically deterministic and “neglect[s] free will, individual autonomy, and the effect of factors, such as religion, culture and ethnicity” (2003, p. 3). They point out how contradictions between capitalist MOP and traditional culture in Sri Lanka “were inflamed by a coalition of workers and local managers against foreign owners, who fled when financial irregularities are discovered” (Wickramasinghe & Hopper, 2003, p. 1).

Alawattage and Wickramasinghe (2008) rely on a theoretical framework drawn from Marxist discourses on hegemony to explain “the emergence and sustenance of political hegemony as the dominant mode of control in Third World enterprises” and argue that “the role of accounting has assumed within political hegemonies of the Third World” (p. 293). The above study is on plantation industry in Sri Lanka and Alawattage and Wickramasinghe (2008) interpret some findings (as follows) using Marxian critical lenses:

- Managers can exercise a relative autonomy in decision-making and control.
- This situation is an essential condition for accounting to perform towards capital accumulation.
- Like many other industries in the Third World, plantation labour control mobilizes extra-economic social relations.

According to Lincoln and Guba (2003), the application of critical theories (for example, Marxism, neo-Marxism, feminism, constructivism, critical sociology, and Freudian or Foucaudian theory) in researching real-life problems is more appropriate when the research is about an anticipation of social transformation, particularly towards more equity and justice. More specifically to critical accounting research, prominent scholars argue that Marxist critical theory provides strong lenses for critical accounting scholars. For example, Tinker (1999) promotes using Volume I of Marx’s *Capital* to underpin and guide critical accounting; Dominelli and Hoogvelt (1996) emphasise identifying the problem is a major intellectual responsibility and exposing the roots of exploitation is a precondition for liberation; Dillard and Tinker (1996) insist that bringing structural contradictions into consciousness and to develop them to the highest level of instability is one purpose of critical accounting research.

2.6 Marxian critical theory on global inequality and credit

Many Marxian critical theorists (for example, Abramovitz, 1986; Korzeniewicz & Moran, 2003; M. Moore, 1997) argue that though development theories

(classical, modern, post-modern and neo-liberal theories in explaining inequality) provide extensive analyses on inequality they do not provide a comprehensive framework to unfold the total picture of inequality and its causes. According to Moore, “these explanations are generally unconvincing...[and] have a poor track record in prediction” (1997, p. 3). Moore further suggests that:

In the Marxian framework, capitalism is the defining dimension of contemporary societal organization, subsuming such lower-scale concepts such as modernization, markets, or globalization...when look at published research this ceases to be Marxist versus non-Marxist issue (1997, p. 4).

According to modernization theory, the Third World countries were advised to adopt, mimic, imitate and import development patterns of the West (M. Moore, 1997). Also for their financial crisis and development initiatives, borrowing from Western financial institutions such as the World Bank, the International Monetary Fund (IMF) was prescribed as the overriding way out (Hite, 1996).

Meanwhile, development that was basically conceived in terms of economic growth, industrialization and liberal democracy did not bring marked change to the problems of the Third World countries (Schuurman, 1993). The establishment of infrastructures, the importation of machinery as well as adaptation of Western technology did not bring significant change (Sklair, 1991). Eurocentric development praxis that did not take the internal situation of developing countries into account became a source of multiple problems, rather than the solution to them (Hite, 1996).

Credit--money that the Third World countries borrowed--for development projects made them sink into a debt crisis (Hassan, Hagen, & Haj, 2005). Also, the imported technology made them dependent on foreign expertise, therefore, the situation inversely served the purpose of the developed nations (Foster, 2002). Development particularly served the economic and political motives of the United States (Michael, 1995). Politically, the United States used development discourse and practices to halt the expansion of communism from

the east. Economically, it generated a double income to the developed countries; first, from the sale of its manufactured goods to the Third World countries; second, from the interest of the money they lent to them to purchase those goods (Hassan et al., 2005). The penetration of financial and industrial capital, when they are possessed and disbursed in an arbitrary manner, not being helpful to improve the condition of the developing countries, instead aggravated the situation (Foster, 2002). These arguments are primarily based on cultural-Marxist discourses on hegemony which concerns the construction of consent and the exercise of leadership and social relations by the dominant group over the subordinate group (Gramsci, 1971 cited in Alawattage & Wickramasinghe, 2008; Gramsci, 1971).

In 1976 Professor Muhammad Yunus introduced the “Grameen Movement” which was considered as a revolutionary step to address the low per capita income issue in Bangladesh. Grameen Bank (rural bank) is a financial institution that exists for one purpose, that is to turn into deed Yunus’s philosophy that the poorest of the poor are the most deserving in the land; that, given a decent break, they can lift themselves out of the mire of poverty and fend for themselves (Yunus, 2007). The break that Grameen Bank offers is a collateral-free loan. Yunus, who won the Nobel Peace Prize in 2006 for this concept and its implementation in Bangladesh, says,

One can reasonably state that people are poor today because of the failure of the financial institutions to support them in the past. Like the right to food, clothing, shelter, education and health, credit should also be recognized as a fundamental human right (Yunus, 2007, p. 2)

By 2003, the Grameen Bank had 1042 branches, 11,000 employees, disbursed US\$20 billion to 1.6 million borrowers (Grameen Communications, 2003), however, a deeper question is how helpful such tiny loans really are? The average size of the loan is less than US\$200. In fact, after restructuring the Grameen programme in 2001, savings (deposits) now exceed loans. The Economist criticized this programme by posing the question “whether this form of lending has led to peace, the presumptive reasoning behind the award [Nobel

Peace], is just as big an unanswered question” (The Economist, 2006, p. 71). Further, Shaw (2004) reveals from her study in Sri Lanka on two such micro-financing programmes in rural Hambantota area that post-credit incomes are unlikely to increase because of financial, infrastructural and socio-cultural barriers. This outcome partially agrees with Marx’s interpretation of credit with regard to lenders towards centralizing capital but works against the borrower because terms and conditions are exploitive. She concludes her case study research outcome saying that:

Microenterprise development programs need to be complemented by investment in social and physical infrastructure; they are no substitute for it. In arid rural areas, where microenterprises face severe market and infrastructure constraints, microenterprise development is unlikely to facilitate poverty exit (Shaw, 2004, p. 1262).

According to Marxist writers (for example; M. Moor, 1997; Saad-Filho, 2003, Isbister, 2003; Korzeniewicz & Moran, 2003) State interventions play a significant role in allocating resources and providing such infrastructure facilities for enterprises to start and grow.

Further, instead of microenterprise development, after studying encouraging success stories from nations in Asia (China, India), Europe (Ireland) and even Africa (Botswana), Powell (2008) concludes that encouraging small-business entrepreneurs is the best way to achieve and maintain general affluence. When the project is larger the owners could have access to MOP if they are adequately financed. In other words, according to Marx, entrepreneurs must own adequate capital for them to have comfortable access to MOP and perform. Microfinance is too little and does not constitute capital in the Marxian sense.

De Soto (2005) suggests that developing countries already have the assets they need to eliminate poverty in their hands. If this is the case, a news paper article asks a compelling question: “Why are these assets ‘dead’ and not being used to help stimulate economic growth and generate employment?” (The Sunday Island, 2006, p. 3). De Soto argues that the legal property system is the “hidden

architecture” of a successful economy. If this hidden economic architecture is not in place, the economic activity takes place outside of the legal system or in what economists call the “informal sector”. It has been estimated that the informal sector in Sri Lanka comprises about one-third of all economic activity (The Island, 1999).

2.7 Marxian interpretation of the roles of states, capitalist forces and nationalism in sustaining inequality

However, the Marxian perspective is that state intervention is part and parcel of capitalist development, though the promotion of capitalism did not mention that explicitly. Isbister (2003) says; “it is a serious misunderstanding of capitalism to think that it consists of a private sector alone or that stands in opposition to government” (p. 38). In fact, capitalists, while opposing certain government policies, widely depend on the governments. According to Moore, the Smithian/neo-liberal arguments about governments as an obstacle to capitalism in the contemporary Third World are analogues and he stressed that “states and capital prefer to co-operate with one another” (1997, p. 28).

According to Marx, the government is an extension of the ruling capitalist class: “The executive of the modern State is a committee for managing the common affairs of the whole bourgeoisie” (1977, p. 35). Social scientists and liberal economists now argue that, the State should level out the increasing inequality in capitalist society and should compensate for the lapses and injustices generated by private actions and provide public goods (Isbister, 2001).

Agencies including the International Monetary Fund (IMF), The World Bank, European Central Bank, World Trade Organization (WTO), General Agreement on Tariffs and Trade (GATT) and the United Nations (UN) promote structural programmes such as privatization, deregulation, tight fiscal and monetary policies, and liberalization of capital flows, import laws and others primarily to dilute state power so that the capitalist class can become the super power. These international institutions were founded for the purpose of re-establishing the

international market capitalist system and permitting it to grow to new heights (Isbister, 2003). Also, there seems to be a contradiction between the advices of these agencies and practices in the developed markets, as Saad-Filho points out:

...developed markets arise only through state intervention. The state establishes the institutional and regulatory framework for market transactions, including property rights and law enforcement. It regulates the provision of infrastructure, ensures that a healthy, trained and pliant workforce is available, and controls social conflict. The state establishes and regulates professional qualifications and the accounting conventions... (2003, p. 9).

2.7.1 Neo-liberal capitalism

Neo-liberal capitalism has not been helpful reducing the wealth gap between nations, however the promoters of neo-liberal economic policies admit that there has been some decline in within-country wealth inequality. They point out that there is a general theoretical and empirical consensus that until the 1950s, the development of capitalism was characterized by growing disparities in the distribution of income between the poor and rich nations (Korzeniewicz & Moran, 2003).

There is a similarity between today's neo-liberal policy promoters and early years' colonial rulers of powerful nations in justifying their exploitation under the facade of civilization, human rights, environmental protection, sustainable growth and poverty elimination, etc. It is worth to note that, Saad-Filho asserts that "Today's evangelists pay lip-service to human rights and the elimination of poverty, but their faith lies elsewhere, in the sacred tablets of copyright law and in the charter of the International Monetary Fund (2003, p. 1). Lenin observed this situation as the final stage of capitalism where bankers and industrialists set the ground rules in distributing the benefits between capital and labour (Lenin, 1939).

The external pressures, including privatization and import liberalization, eventually create more opportunities for accumulation of wealth to the group of

influential capitalists, making them more socially powerful. Hence, the issue of income/wealth inequality in a country cannot be separated from that of the widening gap between rich and poor countries through globalization of business and through propaganda for privatization to weaken State power especially in developing countries.

2.7.2 The influence from international capitalist forces on the economic-political environment through controlling access to financial capital

Korzeniewicz and Moran (2003) refer to Lenin and Luxemburg and say that, “A long-standing Marxist interpretation portrays inequality as a structural component of capitalist accumulation in a world-economy (Lenin, 1939; Luxemburg, 1951)” (p. 185). These structural forces exist at different levels with a vertical relationship that can be observed across these levels. For example:

Dependency studies argued that the very existence of a capitalist international economy, as embodied in global trade, entailed a continual transfer of surplus from poor (or satellite) to wealthy (or core) areas (e.g., Cardoso 1974, 1977; Cardoso & Faletto 1969; Dos Santos 1970; Frank 1966, 1967, and 1978) (Korzeniewicz & Moran, 2003, p. 185).

The ultimate result of these influences from international capitalist forces is a continuous widening of the gap between rich and poor nations further increasing inter-country inequality. The major tool used for this purpose is the heavily conditional hold of financial capital controlling the access to it by the poor countries. Despite the huge differences among development studies scholars, they all agree on one fact: that economic development in the developing countries can continue to be hindered by continuous structural roadblocks including access to credit.

2.7.3 Influence of national capitalist forces in sustaining inequality within the country; internal roadblocks.

“Wealth and poverty are generated by the same process” (Tinker, 1999, p. 661)

Most debate on the internal gap between rich and poor people in developing countries started with a seminal presidential address of Simon Kuznets titled “Economic Growth and Income Inequality” in 1954. He argues using limited data from Germany, the United Kingdom and the United States that there has been a trend toward equalization in the distribution of income. Therefore, there could be increasing inequality in the early phase of industrialization but that is followed by declines in the later phases of development (Kuznets, 2003). Then he opened the debate over the relevance of these findings for the developing countries by examining data from India, Sri Lanka (then Ceylon) and Puerto Rico (Seligson & Passe-Smith, 2003a).

The data showed that income distribution in these underdeveloped countries is more unequal than in developed countries. The share of the lower three quintiles were 28 percent in India, 34 percent in Sri Lanka and 24 percent in Puerto Rico compared to 34 percent in the United States and 36 percent in the United Kingdom. The shares of the top quintile were 55 percent in India, 50 percent in Sri Lanka and 56 percent in Puerto Rico compared with 44 percent in the United States and 45 percent in the United Kingdom (Kuznets, 2003).

However, Kuznets’s assumptions, inferences and even “facts” such as “share of the lowest decile could not fall far short of 6 or 7 percent” (2003, p. 69) and “the fact remains that the lower limit of the proportional share in the income structure is higher when the country-wide per capita income is low than when it is high” (p. 69) have been proven false by history. For example, the share of the national income enjoyed by the lower three quintiles in Sri Lanka has been continuously reducing since then and in 2003 it was reported as 24.9 percent (30.9 percent in 1973) and the lowest decile was always below the limit of two percent and reduced further to 1.1 percent in 2003 (The Central Bank of Sri Lanka, 2008).

Goulet (2002) criticizes the 1971 Nobel Prize winning economist Kuznets’s hypothesis, which suggests that, in the early stages of economic growth, income

distribution will worsen and in the later stages it will improve, by pointing out that “the reversing point” is yet to come. Also, according to Torado (1997),

Theorists who argue for the inevitability of the Kuznets process – especially political leaders in countries with large and growing inequalities – more often than not are simply searching for a convenient conceptual smokescreen behind which to mask their goals of economic aggrandizement or to cover policy failures (pp. 161-2).

It is very common that the political leaders of newly elected governments in Sri Lanka demand that the public “tighten the belts” in the short run; until they recover from the disasters caused by the previous government, and promise to deliver election-promises in the long run. But it is apparent nothing happens other than defeating incumbent at the next election and the current opposition coming to power on the same old grounds and promises, and same scenario repeats endlessly.

Evidence suggests that there may be country-specific characteristics that influence within-country income inequality independent of external international factors. According to Goulet (2002), there could be numerous other obstacles to a just economy which also exist. In addition to those operating in the international arenas, others serve as internal roadblocks to development. Among the internal roadblocks, one counts the vested interests and disproportionate political power of privileged groups. The findings of this research provide evidence to show how this vested interest and disproportionate power (political or social) of privileged groups contribute to social power which, in turn, influences decision-making in the banking sector.

Some postmodernists believe that the “vision” of the poor is impaired and should be improved by the vision of rich capitalists. For example, Udayakumar (1995) suggests mutual co-operation between the rich and poor for a “mediated, sustainable and co-operative path; and a bleak future awaits both of them if they take unmediated selfish and confrontational path” (p. 348). He oversimplifies the process by suggesting “The rich and the poor are like a blind person and a

paralyzed person undertaking a journey together through life. The former needs the latter's vision, and the latter requires the former's sustenance" (p.348). However, this is in line with his preaching as "Imagining and dreaming are far important and difficult than predicting" (Udayakumar, 1995, p. 340). What is apparently happening is that the persons with power make use of the powerless poor to achieve the mission of the former. He uses this approach to show that powerless poor people do not possess the necessary skills and capital to prosper by themselves, therefore they must rely on the powerful rich class if they want to come out of poverty. He also asserts that the rich class, though they are visionary and capable, needs workers' support to accumulate wealth. This is what Marx pointed out in his surplus-value concept that the capitalist system makes use of labour without adequate compensation and therefore the workers will never get out of poverty trap.

Goulet (2002) says that equity is a straightforward notion: just and impartial treatment for all. An economy that distributes its benefits in ways which exclude many, is unjust and inequitable. Goulet further justifies his claim by quoting from Harvard University's Bryan Hehir as follows:

...first that we accept the common destination of the goods of creation and recognize that the resources of the earth are to be used for the good of all, second, that we adopt an option for the poor, similar to the 'difference principle' of John Rawls which favours those proposals for change that best serve the least well-off in the world; and third, that we establish institutions that seek to build a just international order...(Hehir, 1998, p.11).

The question remains whether these institutions, which are established to build a just international order, are genuine in their intention or are just paying lip-service by promoting globalization with neo-liberal economic policies, which most of the scholars from the Third World reject, saying that globalization is nowadays' colonialism or imperialism (Goulet, 2002).

2.7.4 The theory of the petty bourgeois and the mask of nationalism

According to Marx's class analysis there is a dependent class in between the capitalist class (bourgeois) and the working class (proletariat) called petty-bourgeois (Tucker, 1978). According to the class-bound nationalism (Allahar, 2004) the "petty-bourgeois nationalism" may be the best fit theory for the Sri Lankan traditional capitalists, because the petty bourgeois is more traditionally in favour of protectionism. They are unable to compete internationally and their scale of operations is limited to the domestic market. Therefore, they use masks such as nationalism and patriotism to promote and protect their specific spheres of operation: local industry, local manufacturing, and the exchange of locally produced goods and services (Allahar, 2004). With regard nationalism, it is noteworthy to mention that, according to Munck nationalism matters because people die for it but the motive is not clear (1986, cited in Allahar, 2004). Further, this social class might place their egoistic interests and symbolic gains before economic interests at large (Williams Jr., 1994) in the guise of nationalism. Therefore, analyzing and interpreting the behaviour of such petty-bourgeois through a Marxist lens is useful and important in explaining the findings of this research.

2.7.5 Productivity is secondary to political motives

States make political compromises to preserve power whilst maintaining their central planning role. Therefore, productivity motives become secondary to political ones, and accounting reports are rarely discussed or used for accountability. Accounting systems are maintained only as a regulatory requirement to legitimize events to external bodies and the populace (Wickramasinghe & Hopper, 2003). As a result, public enterprises became a drain upon state coffers; their policy failures contribute to fiscal crises of the state and political unrest (Gray, Owen & Adams, 1996). From 1977, over the last three decades, heavy pressure from donor institutions/countries forced Sri Lanka to privatize state-owned corporations leaving only the health, education, defence, state finance and a few authorities such as railways, forest and water under the control of the state. This situation created a very conducive

environment to the capitalist class to penetrate into many national-level industries such as telecommunication, energy and construction and to strengthen their social power base further.

Although import protection is seen as an evil in the process of reaping the advantages of comparative advantage, Petras and Veltmeyer (2001) argue that the growth of protectionism and national industry stimulated the growth of domestic industries and the relative decline of global flows as against capital accumulation.

The debate between “openness” and “infant industry protection” is still attractive with concepts such as “comparative advantage”, “globalization” and “learning curve” and others, especially in countries with low levels of industrialization. Deraniyagala and Fine say “...poor countries are shown to specialize in low technology products if free trade is allowed, but trade restrictions allow them to develop complex industries (see Reddy, 1999)” (2001p. 815). This research elaborates and places an emphasis on these techniques of maintaining disproportionate power systems (political, social or economic) for certain groups of people and also the access of the financial capital to entrepreneurs for feasible projects.

2.8 Financial capital mobility system

“The stronger the power of my money, the stronger am I. The properties of money are my, the possessor’s, properties and essential powers. Therefore what I am and what I can do is by no means determined by my individuality. I am ugly, but I can buy the most *beautiful* woman. Which means to say that I am not ugly, for the effect of *ugliness*, its repelling power, is destroyed by money. As an individual, I am *lame*, but money procures me twenty four legs. Consequently, I am not lame. I am a wicked, dishonest, unscrupulous and stupid individual, but money is respected, and so also its owners. Money is the highest good, and consequently its owner is also good” (Marx, 1975, p. 377 cited in James, 2008, emphasis original).

The wealth of a country could be distinguished between financial wealth and real wealth. Financial wealth is ‘the value of pieces of paper’ such as shares, bonds and cash while real wealth is the value of tangible assets such as plant, machinery, infrastructure and stocks or inventories as well as knowledge and technology. Financial wealth is an asset to some people and a liability to another (Isbister, 2001). Further, De Brunhoff argues that, “The visible domination of financial markets does not imply that industrial capital has lost its fundamental importance. Rather, we could say that a new capitalist coalition has emerged, in order to restore profitability after the crisis of the 1970s” (2003, p. 143).

This finance capital is playing a vital role in controlling the political power in developing countries, compared to the other capital elements such as land, buildings and managerial know-how. Isbister (2001) quotes from Gurley and Shaw and argues that, in capitalist economies over time, financial assets typically grow faster than real assets or national product, for example, they estimated that financial assets were about one-half the level of real national wealth in the early 1880s in the United States, rising to about twice the level of real wealth in the early 1960s.

2.8.1 Coalition between financial and industrial capitalists

Therefore, the finance providers have become very powerful and have gone to the extent that “the state is captured by capital and operates on its behalf to protect, reinforce and support capital’s expansion and to maintain the suppression of labour” (Gray *et al.*, 1996, p. 34). The new Sri Lankan economy was driven by an international capitalists’ coalition of financial and industrial capitalists with the help of neo-liberal policies. The case studies under discussion provide evidence to argue, these coalitions between financial and industrial capitalists could be formed within a country under masks of nationalism/patriotism or theories such as social responsibility/sustainable growth or posing as against neo-liberal policies.

The accumulation process of capital requires both industrial and financial capital. Therefore, the banking system has become a crucial instrument which

creates a powerful social mechanism for the centralization of capital (see De Brunhoff, 2003). Critical analysis shows that pressure from the owners of finance is very common on the management of production. The most common example of this is appointment of bank officers as directors to the board of directors of heavily indebted customers. According to De Brunhoff:

These directors not only have high salaries, but also obtain important share portfolios by means of stock options or in other ways. And they agree to change the organization of industrial production in order to maximize both profits and financial rewards. This is the objective basis for a coalition of financiers and top industrial directors (De Brunhoff, 2003, p. 147).

In Sri Lanka, though bank officers serve as directors on the boards of their highly indebted clients, to look after the banks' interest, there is no compelling evidence that those clients rewarded them with another salary. However, they enjoy various other benefits such as free holidays and large hampers in the festival seasons.

According to Keynes (1936) the least useful economic group comprises rich owners of money capital, the parasitic "rentiers". They want high returns from their financial investments; otherwise they will keep their money idle and provoke a scarcity of finance for economic needs. This is quite evident in Sri Lanka because banks can safely park their excess money with government securities and still make a contribution margin. According to De Brunhoff (2003) such irrational behaviour by owners of financial capital has no justification and he further suggests that:

...financial activity should be taken out of the hands of the rich owners of money capital and regulated by the state. The active economic agents, entrepreneurs and workers should not be dependent upon the interest of idle rentiers. This kind of analysis is often used today by people who ask for the cancellation of the debts of less developed countries, and by those proposing a new regulation of finance (p. 145).

But De Brunhoff (2003) warns that this new regulation should involve major changes in the whole structure of capitalist accumulation of wealth. Therefore, he suggests that:

It is necessary to understand more fully the complex relationship between financial and industrial capital, and the respective roles of financiers and entrepreneurs in capital accumulation. Then we will come back to the general notion of capital, whether 'real' or financial (p.146).

2.8.2 Lack of state support for SMEs providing facilities including credit

According to Marx, the exploitation of labour is the basis of capitalist profit. However, a capitalist credit system is required for financing new industrial investments, and it also centralizes the money of all social classes. Owners of small savings are passively involved in the process, while the ownership of financial assets is highly concentrated in the hands of a few wealthy people, including some industrial managers.

According to De Brunhoff, "Keynesian policy involves a social compromise between capitalist entrepreneurs and workers. Financial markets and 'rentiers' who own money capital should be disciplined by public rules" (2003, p. 150). It is worth noting that a survey of small businesses in Sri Lanka and Tanzania has revealed that problems of access to finance and the high cost of finance, materials, equipments and also regulatory problems concerned businesspeople in both countries (Levy, 1993 cited in M. Moore, 1997). Therefore, lack of support from the government in developing business enterprises appears to have a detrimental impact on the formal banking systems pushing decision makers towards arbitrary decisions with regards to financing enterprises. That is, in the absence of regulatory policies and conducive economic-political environment, the contribution of individual characteristics may be fostered and amplified.

2.9 Marxian interpretation of social structure and credit system

According to Marxian analysis (for example, De Brunhoff, 2003; Lapavistas, 2000; M. Moore, 1997), the distribution of profits between venture capitalists

and finance providers is problematic but the accumulation of capital needs both of them. The credit system is such that it transforms idle money into loanable money capital that is earning interest, and directs it back to accumulation (Lapavistas, 2003). This “loanable capital”, i.e. money capital, Marx says, “no longer passive but active, usurious, [and] proliferating capital” (1978, p. 569 cited in Lapavistas, 2003, p. 70). And, in societies where commodity exchange is widespread, the economic power afforded by money naturally leads to social power. “Money is the monopolist of the ability to buy, or in Marxist terminology the ‘universal equivalent’”(Lapavistas, 2003, p. 70-71).

Therefore, the researcher’s argument is based mainly on broad theoretical framework of Marxist class analysis and neo-Marxian critical theory, because: first, it is appropriate to apply these theories to the case studies under review where the financier and the industrialist are not in the same business; second, as Moore (1997) explains, Marxian interpretations inspire empirical and historical research. Also, Marxism has been identified as the main single source of inspiration, political as well as intellectual, for research into Third World capitalism (see Barrow, 2007; Kiely, 1998, 2005; Watson, 2004).

Marxism has been used extensively to explain inequality or uneven development and therefore has evolved through different perspectives especially addressing its weak points such as bi-class society and inevitable victory of proletariats. According to Sherman the:

Marxian perspective has led to a new Marxism, which is unofficial, independent, profoundly democratic, and critical of all societies and all rigid ideas. The new Marxism has often been called critical Marxism (1995, p. 3).

Therefore, it is not only the need for individual power that drives arbitrary decision-making but also the systemic stimulants induced by the institution and the social network as a whole, because the Marxian critique suggests that:

- power is held by capital and exercised on its behalf;

- there is a conflict between capital and labour;
- the state is captured by capital and used to suppress labour; and
- the emergence of the middle class is privileged by the situation (Gray *et al.*, 1996).

2.10 Summary and conclusions

This section summarises this chapter and provides conclusions on why the Marxist lens of credit mechanism is used in this research to study the role of bank lending from a critical accounting perspective. Many scholars argue that the relationship between accounting and capitalism is not merely technical but a deep-rooted bond and a justification. They insist that not only the capitalist system but also the concept of capitalism itself is an outcome of the influence of accounting ideas on economic and sociological thinking.

According to Marx, money is highly respected and therefore, money owners are powerful irrespective of their methods of earning and accumulation of money. Some researchers argue that powerless poor people do not possess the necessary skills and capital to prosper by themselves, therefore, they must rely on the powerful rich classes if they want to come out of poverty. They also say that the rich classes, though they are visionary and capable, need workers' support to accumulate wealth. These theories suggest that powerful-rich make use of the powerless-poor to achieve these goals. The poor, though they may have ideas and skills but no access to money (or sufficient credit) will arguably never get out of poverty trap.

According to Marx, the government is an extension of the ruling capitalist class and Marxian critical theorists argue that developed markets arise only through state intervention. The state establishes the institutional and regulatory framework for market transactions. It regulates the provision of infrastructure, ensures that a healthy, trained and pliant workforce is available, and it controls social conflict. The state establishes and regulates professional qualifications and the accounting conventions.

With reference to Sri Lanka, researchers argue that production relations are not only constituents of legal and political superstructures but also comprise free will, individual autonomy, and factors such as religion, culture and ethnicity. Research on micro-financing programmes in Sri Lanka reveals that post-credit incomes of borrowers are unlikely to increase because of financial, infrastructural and socio-cultural barriers. Micro-finance is too small and does not constitute capital in the Marxian sense.

Despite the huge differences among development studies scholars, they all agree on one fact: that the economic development of the developing countries will be hindered by continuous structural roadblocks including access to credit for potential projects of ordinary people.

2.10.1 Conclusions

Marxism was considered as the theoretical guide in this research for several reasons. Marxian theory can be applied to different level analyses and is capable of explaining not only within-level relationships but also between level relationships. Marxism has earned widespread acceptance as one of the grand theories which narrate social histories (George, 2003) compared to other critical theories especially with regard to power relationships and credit mechanisms. Marxian critical theories are useful tools to analyse power relations associated with wealth and financial resources. Classical Marxian economic theories have proved not to be practical.

State intervention discussed here is not about state ownership but conscious interventions by the state as performed in developed countries for the interest of the general public.

The Marxist concept of credit mechanism is the main analytical tool used in this research. According to Marx, the credit system is a serious weapon in the battle of competition and forms a significant social mechanism for the centralization of capital. Equally, lack of money translates into powerlessness, deprivation and exclusion from several social activities for the majority of the poor under

capitalism. In capitalist society, successful participation in social affairs depends less on a person's abilities and skills and more on possession of money. There seems to be a barrier between ordinary people's potential (through abilities, ideas and skills) and access to money capital in capitalist society. In the meantime, people (with or without abilities, ideas and skills) who possess money gain the potential and reap the benefits. More gravely, when access to money capital is coupled with ideas, abilities and skills, there will be could have an undue advantage over moneyless people and this would increase exponential effect in accumulating wealth.

The petty-bourgeoisie is traditionally in favour of protectionism. They are unable to compete internationally, use masks such as nationalism and patriotism to promote and protect their specific locally produced goods and services. This social class places their egoistic interests and symbolic gains before the economic interests of a country at large.

Marxian critical theorists argue that, in capitalism bankers and industrialists set the ground rules in distributing the benefits and control the ultimate balance of power between capital and labour. Their studies investigate how capitalist forces influence decision-making/lending processes by weakening state power (economic-political environment) and ignoring the role of individual's abilities, and the skills of bank professionals--and at the same time enhancing the social power of a few "real" decision-makers in the sector. It is evident that most individual, social-cultural and economic-political factors are collectively directed towards protecting the social power of an advantaged class of the capitalist society. Social power, privilege and inclusion in various activities are intertwined with possession of money in capitalist society, meaning that the economic power afforded by money eventually leads to social power. Therefore, social power becomes the fundamental driving force for decision-making based on preferred social norms in the state and private institutions, particularly in the finance sector.

The Marxian critique suggests that it is not only the need for individual power that enhances social inequality but also the systemic stimulants induced by the institution and the social network as a whole. Accounting systems were maintained as a regulatory requirement to legitimate the capital-concentration process. Accounting provides the intellectual service for smooth and effective functioning of the credit mechanism. This research investigates and shows how and why individual, social and economic-political factors collectively contribute to social power which in turn influences credit decision-making in a private bank in Sri Lanka. It also seeks to find what impact would such decision-making have on the economic-political environment, especially with regard to the possibility of sustaining income/wealth inequality in Sri Lanka? That is, examining the nature of the link between the inequality in society and certain decision-making processes of a Sri Lankan private bank.

CHAPTER THREE

3 RESEARCH METHODOLOGY

3.1 Introduction

This chapter discusses in detail the methodology employed in the realm of academic research in social sciences and specific relevance of certain methodological perspectives to this research. Recent publications (for example: Creswell, 2007; Denzin & Lincoln, 2005) on qualitative research methodology show that research methodology can no longer be confined to a set of universally applicable rules, conventions and traditions (Guba & Lincoln, 2005). According to Guba and Lincoln (2005), various disciplines and perspectives (such as Marxism, feminist theories and queer theory) have been integrated with certain methodologies in an unavoidable manner and they suggest that, “...indeed, the various paradigms are beginning to ‘interbreed’ such that two theories previously thought to be irreconcilable conflict may now appear, under a different theoretical rubric, to be informing one another’s argument” (p. 191-2).

This chapter describes how and why the qualitative research methodology is employed in conducting this research. A case study research approach is used to explore and investigate how financial capital is provided to SMEs in Sri Lanka by a private commercial bank. Gillham (2000) says that, “case study research is very much like detective work. Nothing is disregarded: everything is weighted and sifted; and checked or corroborated” (p. 32). Within the main method of case study research several sub-methods are employed for data collection, data analysis and interpretation (Gillham, 2000).

According to O’Leary, when research is focused on real-world problems the research questions are often connected to a need for knowledge that can facilitate problem solving (2005). However, O’Leary (2005) says that such

situations do not mean that research outcomes would resolve social problems but she insists that:

Research can be a key tool in informed decision-making. It can be central to determining what we should do, what we can do, how we will do it, and how well we have done it. Research may not be the answer to our problems, but it can supply some of the data necessary for us to begin to tackle the real-world problems that challenge us all.

This chapter consists of 10 sections. The first three sections outline the type of research perceptions and explain what research perceptions are shared by the researcher. The fourth section illustrates the designing of research methodology employed in this research. The fifth, sixth and seventh sections describe the case study research design and portrays how the “explanatory multiple case study method” (Yin, 2003) is used in this research, and then it reviews the methods of data collection and analysis. Eighth, it explains how the trustworthiness, dependability and credibility of this research were ensured. The ninth section discusses the application of theories and finally, it provides the conclusion.

3.2 Paradigms, perspectives, assumptions and theories

True knowledge is limited to the objects and the relationships between them that exist in the realm of time and space. Human consciousness, which is subjective, is not accessible to science and thus not truly knowable (Polkinghorne, 1989, p. 23 cited in Guba & Lincoln, 2005, p 203).

A research perspective is the standpoint researchers use to study the world, and a paradigm is a set of propositions that explains how the world is perceived (Sarantakos, 1998). Guba suggests that “the net that contains the researcher’s epistemological, ontological, and methodological premises may be termed a paradigm or an interpretive framework; a basic set of beliefs that guide action” (Guba, 1990, p. 17 cited in Denzin & Lincoln, 2003).

In this thesis, the term *perspective* is used when the discussion is about the standpoints of researchers such as the *Marxian perspective* while the term

paradigm is used in a broader and a deeper sense when the discussion is about the worldview of the members of a particular community such as *positivist*, *interpretive* and *critical paradigm*. For example, many religious perspectives belong to the positivistic paradigm while feminist and neo-Marxian perspectives belong to the critical paradigm and social constructivist and participatory perspectives belong to the interpretive paradigm. Therefore, studying and understanding paradigms and clarifying the researcher's standpoint (perspective) and the worldview (paradigm) are important because this sets the basic guidelines for how research should be designed and conducted (Creswell, 2003; Laughlin, 1995).

3.2.1 Objectives of paradigms

Objectives of paradigms vary from discovering “the Truth” to constructing/building theories in proposing solutions. Positivists aim to explore, explain, evaluate, predict and to develop/test theories. The aim of interpretivists is to understand human behaviour which means “sympathetic understanding”. Critical theorists aim to criticize social reality, emancipate, empower and liberate people, and propose solutions to social problems (Sarantakos, 1998). Contrarily, constructivists aim to build theories through consensus (Jones, 1991) and the participatory/cooperative paradigm (Heron & Reason, 1997) aims to know practically, by participation.

Criticisms are now common on purists' view that their paradigms are the ideal for research, and they advocate the incompatibility among paradigms (Johnson & Onwuegbuzie, 2004), for example, Guba insists that “accommodation between paradigms is impossible...” (Guba, 1990, p. 81) while Johnson and Onwuegbuzie insist that “obviously, the conduct of fully objective and value-free research is a myth” (2004, p. 16).

3.2.2 Assumptions underlying paradigms

Assumptions of the researcher play a vital role in choosing a particular methodology for his/her research of social inquiry. Creswell summarizes the

assumptions on which the research paradigms are based on into five categories: the axiological, ontological, epistemological, rhetorical and methodological assumptions (Creswell, 1994, 1998). Many sociologists place paradigms in simple bipolar continuum of each assumption (for example: Burrell & Morgan, 1979; Creswell, 2007). However, Laughlin argues that this “...a simple bipolar dualism... is too simplistic...” (Laughlin, 1995, p. 66) and, Guba and Lincoln (2005) provides five stances of beliefs for ontology, epistemology and methodology in the continuum from positivist, post-positivist, critical, constructivism to participatory paradigms.

Axiology (ethics) refers to the role of values incorporated into the research. Ontology refers to the nature of reality—what actually exists? Epistemology addresses the questions, “Do you really know what you think you know?” and if so, “How do you know what you know?” Rhetorical assumptions mean that, instead of terms such as internal validity, external validity, generalizability, and objectivity, the qualitative researcher writing the case study may employ terms such as credibility, transferability, dependability, and conformability (Lincoln & Guba, 2003) as well as naturalistic generalizations (Stake, 2000). Methodology refers to a model entailing the theoretical principles and frameworks that provide the guidelines that show how research is to be done (Sarantakos, 1998).

Laughlin places some of these assumptions together in a meaningful statement as: “...a position on being (ontology), on the role of the investigator...on perceptions on understanding (epistemology) and ways to investigate the world (methodology) are implicit in the various approaches to empirical research” (1995, p. 66).

3.2.3 The positivist paradigm

Positivism, which is sometimes referred to as a scientific ideology, is a social research philosophy developed and introduced by Auguste Comte in 1848. Positivists argue that the only authentic knowledge should be scientific knowledge. Their ontological belief is that an objective reality exists and can be known through research in contrast to post-positivists who concede that “we

might never know reality perfectly but ...accumulated efforts will move us toward discovering what is real” (Bailey, 2007, p. 52). Contrarily, constructivists argue that the truth is constructed within the minds of individuals and between people in a culture. Constructivists’ view is that the truth is constructed from a continuous process of research and by developing consensus among individuals. The epistemological position of positivists is that knowledge which can be gained does not depend on the researcher. There are numerous research traditions, schools of thought or perspectives which are non-positivist, followed by qualitative researchers who represent either interpretive or critical paradigm.

3.2.4 The interpretive paradigm

The unsuitability and inappropriateness of the positivist paradigm have been observed by many researchers in understanding a social issue (Laughlin, 1995). These researchers seek understanding of the world in multiple realities and often these subjective meanings are negotiated socially and historically (Creswell, 2007). The ontological belief of interpretivists is that there is no objective social reality instead there are multiple realities. The epistemological position of the interpretive paradigm is that what is learned in research does not exist independently of the researcher. The methodological approach of interpretivists is qualitative. An inductive process is followed and often includes interactions with, and observations of, participants (Bailey, 2007). Their axiological belief is that value neutrality is not essential or even not possible in the research process.

3.2.5 The critical paradigm

The common understanding is that researchers who belong within the critical paradigm often want to document, understand and even change the way that powerful groups oppress powerless groups (Bailey, 2007). Similar to interpretive paradigm, critical paradigm too bear the ontological belief that there is no single reality and they stress that “social reality is shaped by historical, social, political, cultural, and economic factors, as well as ethnic, racial, and

gendered structures among others” (Bailey, 2007, p. 55). The axiological belief within the critical perspective is that values are important and should be clearly articulated in the research work. The methodology often followed within the critical paradigm takes a macro approach rather than the study of a phenomenon. According to Bailey (2007), analysis that springs from a critical paradigm often includes emphasis on the negative effects of racism or unequal power relations. This paradigm often focuses on historical, social, and cultural events and “documenting the negative implications of capitalism, imperialism, and unequal power relationships lies at the heart of much work undertaken within the critical paradigm” (Bailey, 2007, p. 56).

3.2.6 Paradigm of this research

This research belongs to the critical paradigm because it aims for critique and transformation and, the issues addressed in this research are social power relations and inequality (Bailey, 2007; Guba & Lincoln, 2005). Further, the researcher wants to document, understand and even suggest change to the negative implications of capitalism and unequal power relationships (Bailey, 2007).

The ontological belief of the Marxian perspective is that reality is shaped by social, political and economic values, crystallized over time (Guba & Lincoln, 2005). The epistemological stance is that the knowledge discovered by this research depends on the researcher and is therefore, subjective. The main question asked in this research is: *Do credit mechanisms and income/wealth inequality create a mutually reinforcing cycle in Sri Lankan society?*, therefore, the answers are inferred from the views of research participants and empirically backed by their experience. The methodology follows dialogic (Guba & Lincoln, 2005) strategies within the case study research methodology from the point of story-building through data analysis and interpretation to theorization chapters.

3.2.7 Basic beliefs

Some scholars such as O’Leary (2004) use the term *post-positivist* to refer non-positivist paradigms but for others, for example Guba and Lincoln (2005), post-positivism is a paradigm with slight variances from positivism in basic assumptions such as ontology, epistemology and methodology. Therefore, for some scholars, the paradigms such as interpretivism, constructivism and critical are classified under post-positivism whereas others identify post-positivism, interpretivism, constructivism and critical worldviews as four separate paradigms. The qualitative school rejects the objectivity because it implies distance and neutrality from the researched; that reality is objectively given; and it emerges out of subjectivity (Sarantakos, 1998).

3.2.8 Business/accounting research

In accounting research, Chua (1986) identifies two basic paradigms; the positivistic or scientific paradigm and the interpretive paradigm. However, according to her, in the broader sense, this interpretive paradigm consists of more “pragmatic” kind of paradigms, like “post-positivist” (for example, Bruner, 1990) as well as very “radical” nature paradigms such as critical theories (Tinker, 1980).

The positivistic paradigm views accounting as a mere technical process (Smith & Taffler, 1992). However, the interpretive school of thought claims that accounting is a social process with human interactions (Jonsson & Macintosh, 1997). They argue that the aim of research should be to uncover the meaning and interpretation of the accounting process. Further development of this interpretive school of thought paved the way for critical accounting theory (Power, 2003; Sikka, 2001; Tinker, 1980). They argue that the aim of research should not be limited to uncovering meanings but also focused on finding reasons for change (Laughlin, 1995) and even suggesting solutions for social issues (Jones, 1991).

3.3 Qualitative research strategies/approaches/traditions

There are several qualitative approaches for social inquiry. According to Creswell these “approaches to research” (Creswell, 1998), have also been identified as “strategies of inquiry” (Denzin & Lincoln, 2003) and “varieties” (Tesch, 1990), etc. Creswell explains the complexity of these approaches in different research paradigms as follows:

Tesch (1990), organizes 28 approaches into four branches of a flowchart, sorting out these approaches based on the central interest of the investigator. Wolcott (1992), classified approaches in a “tree” diagram with branches of the tree designating strategies for data collection. Miller and Crabtree (1992), organized 18 “types” according to the “domain” of human life of primary concern to the researcher, such as focus on the individual, the social world, or the culture...(Creswell, 1998, p. 245).

Creswell (1998) classified all these “types” of inquiry into five “traditions” namely: biography, phenomenology, grounded theory, ethnography and case study. However Creswell (2007) updated his analysis and the major change is that he has renamed the research approach “biography” as “narrative research”.

3.3.1 Creative and strategic researcher

Many researchers feel a need to position themselves as a particular type of researcher, and identify themselves with a defined way of knowing. The question is to consider is whether there can be value in accepting various assumptions. O’Leary (2004) places the researcher in a creative and strategic position and suggests that:

Can divergent, disparate, and distinct understandings of the world, and in particular research, simultaneously exist? For the researcher who approaches research as “thinking game”, the answer is yes. Each research situation and research question is unique, and assumptions can be as varied as the situations. The trick is to understand what assumptions you are working under and how they might affect your study (p. 8).

As explained in the next section this researcher too has taken a sort of strategic position in designing the research methodology of this research.

3.4 Designing the research methodology

A methodology is the selection, justification and sequential arranging of activities, procedures and tasks in a research project. These activities, procedures and tasks include the selection of: cases to study, methods of data gathering, analytical techniques of data (Silverman, 2006), a theory, a range of solutions (Gobo, forthcoming cited in Silverman, 2006) and approaches. On the other hand, according to Yin (2003) the “role of theory development, prior to the conduct of data collection, is one point difference between case studies and other related methods such as ethnography and grounded theory” (p. 28). However, according to O’Leary (2004), in designing the research methodology “one approach is not necessarily better than the other. What is important...is that all researchers work towards reflexive awareness and informed choice. There are no easy answers. Methodological design is about informed decision-making that involves weighing up pros and cons, and deciding what is best given your specific context” (p. 87).

O’Leary (2004) explains that research generates knowledge and the purpose of the knowledge varies from just “building understanding” to “action change within a system” to “emancipate through action” or further to “expose the systems”. Therefore, the research methodologies could vary from “basic” to “applied/evaluative” to “participatory” or further to “critical/radical ethnography” accordingly.

3.4.1 Choosing a research methodology

In one sense all research is case study: there is always some unit, or set of units, in relation to which data are collected and/or analyzed (Hammersley & Gomm, 2000. p. 2)

In supporting to this claim, O’Leary (2004) argues that case study is not really a “methodology” but rather, an approach to research. She explains, “since ‘cases’ in a case study can involve individuals, cultural groups, communities, phenomena, events and, in fact, any unit of social life organization, virtually all methodologies and/or data collection tools can be called upon dependent on the

case at hand” (O’Leary, p. 117-118). The research question under study is analysed using the “exploring methodologies” model (O’Leary, 2004, p. 90) as illustrated in Figure 3-1 to provide a holistic view of the researcher’s position and the approach followed.

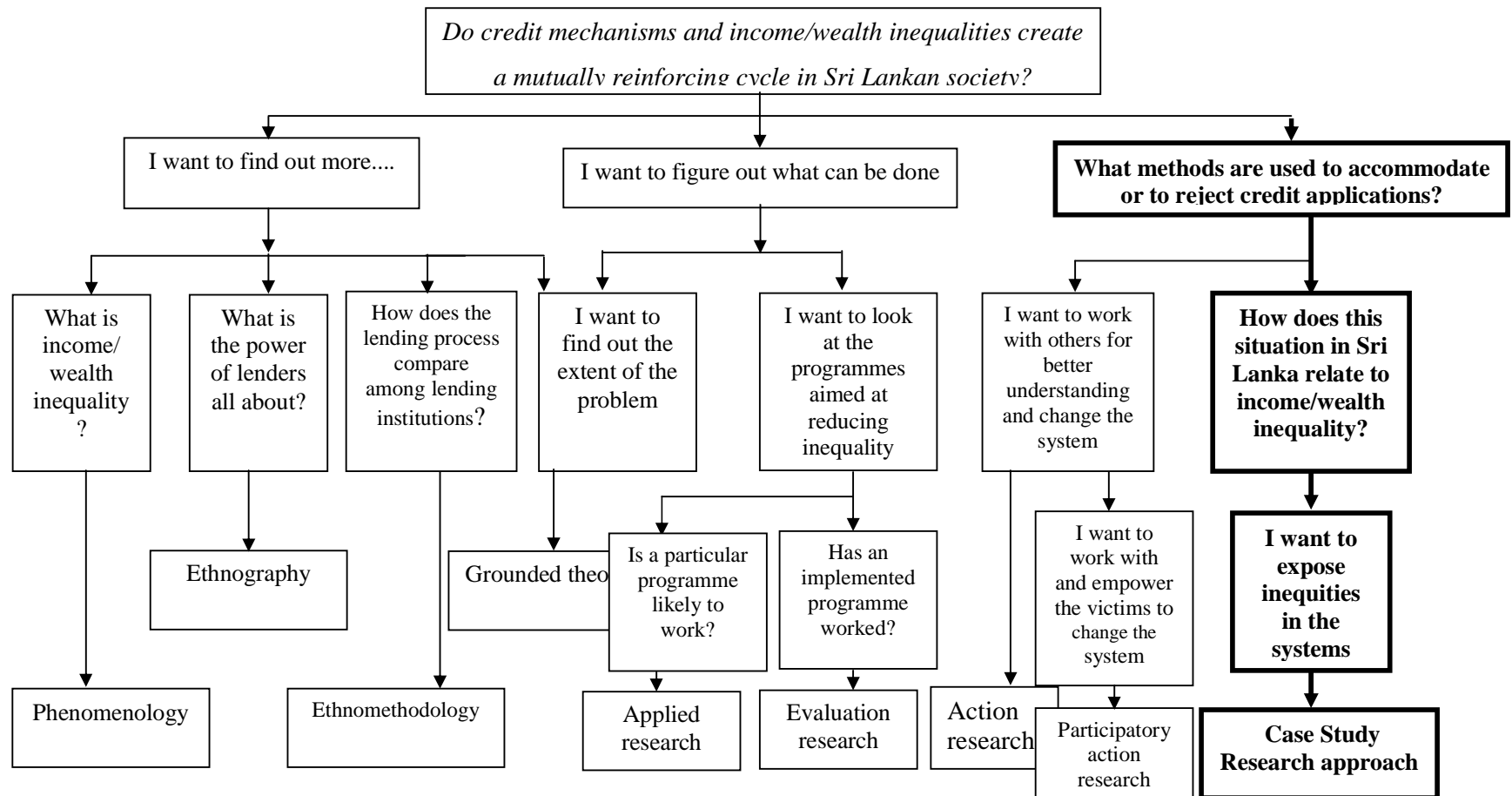


Figure 3-1: Exploring methodologies (adopted from O’Leary (2004, p. 90) to illustrate this research methodology)

3.5 Case study research design and method

According to Yin (2003), "...case study is an empirical inquiry that investigates a contemporary phenomenon within its real-life context, especially, when the boundaries between phenomenon and context are not clearly defined" (p. 13). Therefore, Woodside and Wilson suggest that, case study research should have a broader definition as "inquiry focusing on describing, understanding, predicting, and/or controlling the individual (i.e, process, animal, person, household, organization, group, industry, culture, or nationality)" (2003, p. 493).

In the case study method used in social research today, the soundness of researchers' arguments are refined and ensured by investigating the cases in considerable depth (Hammersley & Gomm, 2000) rather than the number of cases studied and/or amount of data collected on each case. Gluckman insists that, "clearly one good case study can illuminate the working of a social system in a way that a series of morphological statements cannot achieve" (Gluckman, 1961, p. 9 cited in Mitchell, 2000, p. 1). This claim is further strengthened by Skinner (1966) who asserts that "...instead of studying a thousand rats for one hour each, or a hundred rats for ten hours each, the investigator is likely to study one rat for a thousand hours" (p. 21, cited in Woodside & Wilson, 2003, p. 493). As Woodside and Wilson (2003) point out, this view can be misunderstood as that, case study research is always limited to the sample size of $n = 1$.

3.5.1 Why case-study methodology is preferred over other methodologies

O'Leary (2005) points out that the nature of the research question is the key determining factor in choosing the appropriate research methodology. The empirical research questions in this study involve investigating whether credit decisions are made in favour of influential applicants while certain groups are at a disadvantage in accessing credit and, if so, to explore how and why these decisions are made.

The vision of the researcher is set towards better systems by challenging existing systems and the objectives of the research are to expose and understand a current situation: in this case, the credit mechanism in Sri Lanka. However, this research does not intend to suggest remedies or solutions such as programmes and policies through which the state should interfere with the banking system. Future research should focus on potential state-intervention policies and programmes.

After evaluating the various research methodologies outlined in Figure 3.1 the researcher was convinced that the case study research methodology was the most appropriate for this study. This is further explained below.

Due to the controversial nature of the subject, the credit mechanism and its link to income/wealth inequality, acceptance of the researcher by interviewees plays a vital role in capturing genuine and honest responses and ensuring the reliability of the data gathered (Krathwohl, 2009). On the other hand, to study the decision-making process for a considerably long period of time it was necessary to maintain prolonged involvement with the interviewees to collect data over time (Krathwohl, 2009). Therefore, it was determined that survey-based methodologies would not accommodate these requirements.

Methodologies such as participatory action research, action research and applied research are far from being practical in this situation as the researcher access is restricted in the banking sector (Fontana & Frey, 2005; Lee, 2000). Also the acceptance of, and free interaction with, the researcher by participants are arguably less likely to provide the data needed in the banking sector.

Phenomenology focuses on understanding the essence of experience of a topic or a concept (Miller & Brewer, 2003). The focus in this research is to analyse certain causal relationships in the process of decision-making. Therefore the scope of this research is beyond the framework of phenomenology. On the other hand, ethnomethodology covers the study of the methods that people use to make sense of the social world (Miller & Brewer, 2003). Ethnomethodology is

about methods of understanding everyday life in a broader sense whereas this research focuses on a specific complex social mechanism: the credit decision-making process.

Grounded theory is a set of integrated steps guiding the research process to completion and finally to generate a theoretical statement (Miller & Brewer, 2003). Because Marxian critical theories were considered as the theoretical guide for this research, the Grounded theory methodology was not considered.

Ethnographic studies are generally done in a six-months-to-one-year time frame (Creswell, 1998, p. 245). Studying processes like credit mechanisms needs a longer period in order to understand and analyse mechanisms and relationships. On the other hand, financial institutions are closely regulated by a central authority and they maintain the highest levels of integrity and confidentiality about their practices (The Central Bank of Sri Lanka, 1988-2008). Therefore, a major barrier to employing an ethnographic methodology in this type of study is access to data. Information about clients, decisions and the amount of money involved are kept highly confidential by financial institutions mainly because for ethical and regulatory reasons and, also because of the highly competitive nature of the banking business (The Central Bank of Sri Lanka, 1988-2008). Therefore, “observation”, even from within, is not allowed or possible, due to the very personal nature and confidentiality of customer information. Due to the personal characteristics of the interviewer and interviewees, sometimes, face-to-face interviews can create an uncomfortable atmosphere for respondents (Krathwohl, 2009). Further, such interviews are exposed to the possibility of providing biased data because issues are generally on current events, activities and processes and the interviewees may be under direct influence of supervisors on those credit decisions (Lee, 2000).

Due to the restriction on access to data in banks and the need for long-term data analysis, the most appropriate and useful option left to the researcher is to carry out a retrospective study of life experiences of several relevant individuals using multiple sources: interviews, observations, documents, archival records,

questionnaires (not survey questionnaires), internet chats and exchange of e-mails. This requirement is facilitated well in case study research methodology. The multiple-case method is employed to enhance validity and allows for more cogent theorization.

In summary, because of the complexity of the processes under study (credit decision-making processes), the nature of characters involved (rich and powerful individuals and senior bank officers), the length of the period of observation warranted (3-5 years) and the nature of the research field involved (confidentiality, integrity and regulatory issues), the case-study method was identified as the most appropriate methodology in line with the research questions and the knowledge gap identified.

Also, in business, case-study research is considered as useful especially for practical real-world problems where the experience of the actors is important and the context of the situation is critical (O'Leary, 2005). According to Yin (1993), the case study approach is especially useful in situations where contextual conditions of the events being studied are critical and where the researcher has no control over the events as they unfold.

3.5.2 Types of case-studies

Yin (2003) identifies four basic types of case study designs based on two variables namely the number of cases involved and the number of units of analysis covered. The number of cases could be single or multiple and the number of units of analysis can be single-holistic or multiple-embedded. "Among these designs, most multiple-case designs are likely to be stronger than single-case designs" (Yin, 2003, p. 19).

Stake (2005) identifies three different types of case studies namely intrinsic (unique cases; not representative), instrumental (to provide insights or enhance an existing theory) and collective (generalization is aimed at) based on their purpose and nature. On the other hand Yin (1993) classifies case study research into three major categories based on their approach, issues and applicable

theories. They are exploratory case studies, descriptive case studies and explanatory case studies. Each category of case study research can be carried out using a single-case type or multiple-case type. Each case study research type may employ different designs either with one holistic unit of analysis or embedded several units of analysis. These characteristics of different types of cases are summarized according to their nature and purpose (Stake, 2005), and approach, research issues, number of cases, nature of units of analysis and applicable theories (Yin, 1993, 2003) as shown below in Table 3-1.

Table 3-1: Characteristics of three types of case study research

<i>Case type</i>	<i>Exploratory</i>	<i>Descriptive</i>	<i>Explanatory</i>
Item			
Common approach	Field work is done prior to the definition of research problem. Aimed at defining the issues of subsequent study.	Aimed at a complete description of a phenomenon within its context.	Aimed at presenting a causal relationship; explaining which causes produced which effects.
Research Issues	Broad design determined well ahead. Emphasis on actual behavioural events rather than perceptions.	Encounter enormous problems in limiting the scope of the study.	Emphasis on <i>How</i> and <i>Why</i> do research findings get into practical use?
Theories	Search for causal theories.	Requires theory to guide data collocation.	Search for explanatory theories.
Nature	Intrinsic	Instrumental	Instrumental
No. of cases	Single	Single	Collective
Unit/s of analysis	Holistic unit of analysis	Sub-units/Holistic unit of analysis	Sub-units/Holistic unit of analysis

Sources: Yin (1993; 2003) and Stake (2005), compiled by the author

3.5.3 Characteristics of case study method employed in this research

Reports and authors often do not fit neatly into one of these set of characteristics (Stake, 2005), especially when a multiple case study method is chosen they can

share characteristics of different categories. However, studying collective cases is not intended to generalize the research outcome but, as Stake (2005) suggests, it will strengthen the optimizing process of creating a better understanding of the credit system and its relationship to social power and income/wealth inequality in Sri Lanka. This case study research shares characteristics of both the explanatory and descriptive types. The research question in this research is about the possible relationship between certain bank lending decisions and unequal income/wealth distribution, therefore it shares the characteristics of explanatory type case studies.

However, this case study research can be also identified as descriptive because a theoretical guidance was used for data collection and this theory was explicitly disclosed in advance: the Marxian critical theory. This research is an instrumental one because it provides insight to an existing theory and, whether the selected cases themselves are of particular interest or not, the focus was maintained towards optimizing the understanding of the credit system within which they operated. Although studying collective or multiple cases goes beyond optimizing understanding to near generalization because of the representative nature (Stake, 2005) of the cases under review, the researcher maintains focus towards inductive reasoning and abductive inferencing/reasoning for a better understanding of patterns in certain credit decisions in Sri Lanka.

3.6 Triangulation and data analysis

According to Woodside and Wilson, “achieving deep understanding in case study research usually involves the use of multiple research methods across multiple time periods (i.e. Triangulation; see Denzin, 1978)” (2003, p. 498). Triangulation includes direct observation of incidents and events, analyses of archival records, exchange of e-mails, interviews, seeking explanations/interpretations from the case participants (Woodside & Wilson, 2003). These qualitative data were analyzed using various analytical tools/techniques/strategies in order to develop them logically towards a

conclusion. Data analysis strategies are numerous. The data collection, analyses and interpretations in this research need to be iterative with a focus on story building.

Creating stories or creating narratives is identified as a way of analysing data not analysing stories. It is worth noting Bailey's comments on narratives in this regard:

Although I refer, at times, to the creation of narratives as a narrative analysis, other researchers reserve the term narrative analysis to refer to the procedures for analysing the stories, or narratives, told by the participants. When used in this sense, a narrative analysis might focus on how the participants' stories are organized, the rhetoric with which they are told, why they are being told, and their major themes (Bailey, 2007 p. 162).

3.7 Credibility, dependability and conformability

Now it is argued that gaining traditional "thick description" (Geertz, 1973; Sanday, 1979 and Arnould & Wallendorf, 1994, cited in Woodside & Wilson, 2003, p. 497) alone is not enough to ensure the validity and reliability of a case study research because, it may be limited to different levels of depth and detail (Woodside & Wilson, 2003). On the other hand whether the description is "thick" or "thin", if it provides adequate evidence to the claim, the description is considered as dependable (Bailey, 2007). Therefore, the description of case studies were supported by other validation techniques and collaborative evidence such as financial accounts, newspaper and magazine articles, comments of fellow bankers, and finally through inter-rater reliability checks (Schutt, 2001) with peer scholars. O'Leary (2004) suggests an additional indicator that can be used to assess credibility in change-oriented research, and that is "usefulness". If a research objective is to expose an inequitable/unjust situation, then a measure of success or credibility will be how useful the research outcome is in proposing a remedy. Therefore, taking the seriousness of the research problem in this research, it would be appropriate to claim that the

credibility of this research outcome is high because the “usefulness” of the findings is substantial in exposing certain social mechanisms.

Hammersley (1992) suggests three evaluating criteria to evaluate the quality of research: plausibility, credibility and relevance. However, Denzin and Lincoln (2005) criticize Hammersley’s three criteria because they require social judgment and claim that, “within Hammersley’s model there is no satisfactory method for resolving this issue of how to evaluate an empirical claim” (p. 911). Smith and Hodkinson (2005) insist that “method is thereby the crucial factor in any judgment made about the quality of research” (p. 917) and the methods applied in this case study research are discussed in detail in the next chapter.

3.8 Application of theories in the field of business

There are non-social approaches and social approaches to study human behaviour. Naturalistic and individualistic explanations are the most resilient in non-social approaches to human behaviour and, the structural theories and interpretive theories are prominent in social approaches (Jones, 1991). Jones criticizes these non-social approaches complaining that “we are, like animals, biologically programmed by nature ... or human behaviour must therefore always rest ultimately on the particular and unique psychological qualities of individuals” (Jones, 1991, p. 92). According to Jones (1991), there are two rival structural theories; structural-consensus theory and structural-conflict theory. Social conflict theories are so-called because for them, there is an inherent conflict of interest between its “haves” and “have-nots” in an unequal society (Jones, 1991). Society as a structure of inequality; the influence of advantages on behaviour is explained as:

Where advantages are unequally distributed, the capacities of the advantaged to choose how to behave are much greater than those of the disadvantaged (Jones, 1991, p. 96).

Therefore, “social conflict theory” differs from consensus theory not only because it is interested in the way an unequal distribution of advantage in a

society structures behaviour but also differs because it is interested in the conflict, not the consensus, inherent in such a society (Jones, 1991). Comparing the two theories, he says, “The best known kind of consensus theory is Functionalism. The best known kind of conflict theory is Marxist theory” (Jones, 1991, p. 98). According to Denzin and Lincoln (1998) Marxism is not a theory but a criticism and they quote from Guess and assert critical theories are reflective:

Critical theories differ epistemologically in essential ways from theories in the natural sciences. Theories in natural science are ‘objectifying’; critical theories are ‘reflective’ (Guess, 1999). And Marxism, it is called criticism and not theory, or it is interpreted politically, as a disguised version of Marxism, or humanism (1998, p. 12).

3.9 Conclusion

The researcher’s worldview in this research belongs to the critical paradigm. This research seeks to analyse and interpret the relationship between certain bank-lending decisions and unequal income/wealth distribution in Sri Lanka. And because Marxian critical theories primarily guided the data collection process this case study research shares the qualities of both the descriptive and explanatory type of case study research. Although studying multiple cases could go beyond optimizing understanding towards a near generalization, the researcher prefers to be more subjective in his interpretations of the research outcome.

This research topic is not just a phenomenon of study--it broadly covers contextual conditions and relies on multiple sources of evidence. This research shares some characteristics of critical/radical study because it adds a political agenda of exposing inequitable, unjust influences and social systems. This research is a critical research conducted in the field of accounting using the case study research approach/methodology. This methodological approach is illustrated in the Figure 3-2 below showing the research paradigm, the theoretical framework and lenses used within the case study research approach.

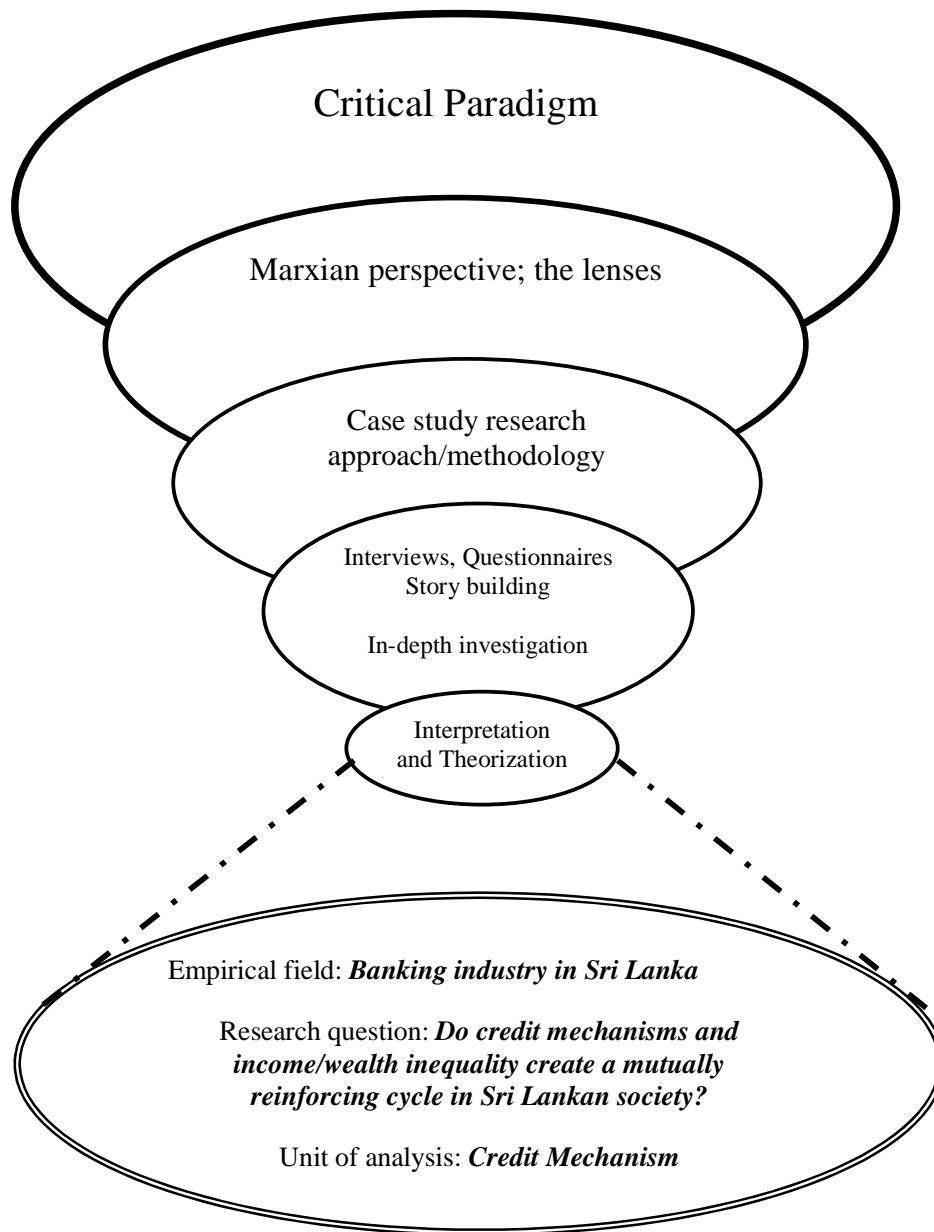


Figure 3-2: Lenses of the research and application of case study approach

Source: Compiled by the author

CHAPTER FOUR

4 RESEARCH METHODS

4.1 Introduction

When effective systems are in place for any process, the outcome is considered as more reliable or trustworthy. Systems are treated as more effective when appropriate methods are followed with proper procedures. Smith and Hodkinson (2005) point out that, “no special epistemic privilege can be attached to any particular method or set of methods” (p. 917) but they insist that:

If the proper procedures are applied, the subjectivities (e.g. opinions, ideologies) of the knowing subject would be constrained and the knower could thereby gain an accurate and objective depiction of reality. Those researchers who adhered to method would thereby possess, in contrast to all others, what one might call the well-polished Cartesian mirror of the mind (p. 916).

This chapter describes the specific research methods, sub-methods, procedures techniques and tools employed in this case study research. The research methods used in this research share characteristics of both the explanatory and descriptive type case study research methods because these case studies not only describe but also explain the credit mechanism in Sri Lanka and explore the motives behind the decision made.

This chapter consists of seven sections. First, it explains how the research questions were articulated. The second section explains how the research participants were selected and educated in this research, and third section concerns how the cases were selected. The fourth section describes data collection methods and interviewing techniques. The data-gathering process of this research was carried out by employing multiple methods: a combination of filling out questionnaires, interviewing, reconstruction of research participants’ own experiences and observation of events and document analysis. Fifthly, it

discusses the data-description processes outlining the presentation framework of case study research reports, which are presented in Chapter six. Sixth section explains the data analysis strategies employed in this research. “Story building”/ “narrative analysis” (Reisseman, 1993) and “relying on theoretical premise” (Yin, 2003) were the primary strategies used for data analysis of these case-study “stories”. Finally, it discusses and elaborates on the interpretation and theorization process of the research outcome.

Each one of the seven sections discussed in this chapter starts with an introductory paragraph to provide an overview of different methods and views relevant to the subject matter to provide a background to explain why and how the particular method, sub-method or technique was practically employed in this case study research. Also relevant theories are cited when justifying the selection of method, strategy or technique.

4.2 Articulating the research questions from a real-world problem

Often, it is the researcher’s insight and experience that directs the researcher towards a problem that needs to be researched (O’Leary, 2005). However, figuring out a problem depends on the ontological and epistemological stance of the researcher therefore, the chosen paradigm and theoretical perspective provided the necessary guidance to identify the subject problem of this research; how and why the credit mechanism contributes to income and wealth inequality. The preliminary investigation into literature provided evidence to form the foundation to make initial assumptions on which the research questions were articulated. O’Leary says that “extending beyond your own workplace experiences are problems tied to broader societal/political agendas” (p. 29) and suggests five steps to clarify the issues. The researcher followed these five steps as described below to articulate the research questions from the real-world problems reviewed in the preliminary investigation as follows:

1. What is the topic? *The financial problems faced by entrepreneurs and their connection to accounting technology, unemployment and inequality.*
2. What is the context? *Banking industry and credit system in Sri Lanka from a critical accounting perspective.*
3. What is the goal of the researcher? *To optimize understanding of the credit mechanism and its link to exploitation, accounting and income/wealth inequality in Sri Lanka.*
4. What is the nature of the question? *What methods (how) do credit decision-makers follow and why?*
5. Are there any potential relationships that could be explored? *Loanable money translates into social power and, social power in turn influences credit systems that ensure more access to credit to certain groups of applicants. Relationship between access to credit and social power. Relationship between accounting technology and credit-decisions.*

4.3 Selection of participants and cases

Access to data seems as an obstacle but is a critical part of doing research (Feldman, Bell, & Berger, 2003). Many scholars stress the hardships that the researchers undergo in obtaining access to private organizations, especially banks as this could expose motives of certain powerful individuals (Lee, 2000). Buchanan *et al.* (cited in Feldman *et al.*, 2003). recommend a pragmatic, almost opportunistic approach to fieldwork in organizations and assert that;

Research access has become more difficult to obtain, for at least two reasons. ... We have been denied in some cases only because someone else got there first, second, as the economic climate has become harsher, in the private and public sectors, managers increasingly feel that they and their staff have little time to devote to non-productive academic research activities. (1988, p. 55).

Therefore, as Feldman *et al.* (2003) noticed, obtaining access through friendships has become more common in organizational research where these barriers exist for researchers. The case study site involved in this research is a banking organisation in Sri Lanka. Banks, as the custodians of public funds, are expected to maintain utmost faith and confidentiality and therefore, they are protected by laws and regulations with regard to divulging customer information. Therefore, the researcher followed the recommendation of Feldman *et al.* (2003): obtaining access through friendships and also he made use of his past banking experience as well.

4.3.1 Number of cases

The cases considered in this research are about typical credit applications and decision-making processes practised in a commercial bank in Sri Lanka. The number of cases studied was determined using the five criteria below:

1. Credit decision-making processes followed; formal procedures and informal approaches.
2. Size of the credit applicant; small and medium-sized enterprise/entrepreneurship.
3. Outcome of credit decisions made; credit was granted and denied/not granted.
4. Hierarchical level of the decision-makers involved; top management and medium-level management.
5. Type of the credit applicant: powerful/capable applicants and powerless/poor applicants.

At least two cases were necessary to represent the five criteria outlined above concurrently and/or separately. However, after going through the cases reported by the research participants, an additional case was considered because it is about manufacturing motor vehicles in Sri Lanka, import substitution, saving

foreign exchange, nationalism, patriotism and protecting the country from being a dumping ground for used cars, etc. Also, this case provides strong support to Marxian critical analysis of the cases. Therefore, it is concluded that a maximum of three cases would be selected on the grounds explained in section 4.3.3.

4.3.2 Selection of participants

The participants of this research are senior bank officers having more than 20 years' banking experience. They were invited to participate entirely on a voluntary basis after it was explained that the research findings would be helpful: a) to expose the weaknesses of the existing finance capital mobility system; b) to provide an insight to policy formulators in promoting potential entrepreneurs; and c) to accelerate the economic development of Sri Lanka, in the final analysis.

As for the questionnaires, initially nine senior bank officers were contacted twice over the phone during the month of June 2006 to gather basic information about lending cases where they were involved in or aware of the decision-making process. While conversations with two participants lasted for about 20 to 30 minutes on each occasion, the conversations with the other seven participants lasted only about 10 to 12 minutes. The two participants, who showed much interest and who were willing to recall and share their banking experiences with the researcher, were selected as they seemed have adequate information on the credit decisions that they were going to talk about. The other seven participants had similar experiences but they appeared busy and their recall was vague and, because only three cases were needed in this research, they were considered only for cross-checking for accuracy of data provided by the other participants.

4.3.3 Selection of cases

Three credit decisions were revealed by two participants. Two medium-size credit applicants, who were socially connected, had been handled directly by the

Chairperson of the bank and credits had been granted. The other small-size credit applicant had been handled by middle management. One case was developed mainly by reconstructing the researcher’s own personal experience supported by the comments of other research participants. Two cases were adequate to cover the five criteria discussed above and to enfold the scope of this research. But a supplementary case was added as a bonus because of its interesting nature, to enhance the enthusiasm of the research and, more importantly, it could provide more empirical evidence.

The cases reported are summarized in the following table, Table 4-1.

Table 4-1: Summary of the characteristics of the cases

<i>Participants:</i>	<i>Researcher</i>	<i>Participant 1</i>	<i>Participant 2</i>
Methods:	Reconstruction of experience	Questionnaire and interviews	Questionnaire and interviews
Decision maker			
The Chairperson	<i>Case I</i>	<i>Case II</i>	<i>Case IV</i> (Not chosen)
Middle Management			<i>Case III</i>

According to O’Leary (2004), the selection of cases is generally done through a strategic process. Three successful credit applications (Cases I, II and IV) were handled by the Chairperson and only Cases I and II were considered for this research because participants had hands-on experience with them. Case IV was not considered because considering another typical case would not increase the rigor of the research but instead would increase data unnecessarily. Case III, a differently treated credit application, had been handled by middle-level decision-makers and was considered for the research so that balanced representation is fulfilled according to the five selection criteria discussed above. These selecting factors are summarized in Table 4-2 below.

All three credit applications, which have been considered for this inquiry, are typical in nature in the Sri Lankan context as explained in the next chapter and therefore represent the general credit culture in Sri Lanka.

Table 4-2: Five conditional criteria covered by the cases selected

<i>Cases</i>		<i>Case I</i>	<i>Case II</i>	<i>Case III</i>
<i>Criteria</i>				
<i>Level of the Decision-Maker</i>	Chairperson	√	√	
	Middle			√
<i>Decision-making Process</i>	Formal			√
	Informal	√	√	√
<i>Size of the applicant</i>	Medium	√	√	
	Small			√
<i>Nature of the applicant</i>	Influential	√	√	
	Not influential			√
<i>Accommodation</i>	Credit granted	√	√	
	Credit denied			√

According to O’Leary (2005), “a prerequisite to all case selection should be access” (p. 78). The researcher and the participants had substantial access to all the cases considered and they also complied with guidelines suggested by various scholars. The main points are:

- (a) representation for typical examples of credit application and approval;
- (b) relevance and interesting nature;
- (c) link to the Marxian critical theories and accounting;
- (d) nature of decision-making process adopted;

- (e) representation of both small and medium-size credit applications;
- (f) publicity given by the media;
- (g) politically topical and interesting;
- (h) practical reasons; connected to researcher's own workplace; and
- (i) purposiveness; enable to make particular arguments.

All three cases are from one large private bank. In privately owned banks, the major shareholders are heavily involved in day-to-day operations unlike in state-owned banks. This bank enjoys approximately ten percent (8-9%) of the market (customer deposits/assets) of the commercial banking sector in Sri Lanka, which accounts for approximately thirty percent (41%) of the private commercial banking market.

The research participants were in constant touch with the researcher until completion of the case study research reports, which they volunteered to do so showing strong support towards this research. The organizing and conducting of interviews, and probing participants' memories from the past five to 10 years, etc., were challenges. However, the overwhelming support from participants is commendable.

4.4 Data collection methods

Max (2001) identifies five main methods of qualitative data collection (research); observation, interviewing, ethnographic field work, discourse analysis, and textual analysis. According to Max, method is a set of techniques that could be used in researching any group or social setting. However, some sociologists, (for example, O'Leary, 2004) have identified discourse and textual analysis only as qualitative data analysis strategies and not as "research methods".

Among these methods of data collection, observation, interviewing and textual analysis stand undisputed for social research. Therefore, the major data

collecting methods used in this research are interviewing supported by document analysis wherever applicable. Interviewing technique applied in this research is informal-unstructured which facilitates cross-questioning in the process. These methods explained in detail in proceeding sections.

4.4.1 Reconstruction of research participants' own experience

Reconstruction of direct observations and events “connecting with personal experience” (Wolcott, 1994, p. 44) were the primary sources of data collection in this research. A set of guidelines provided by Crawford and others (Crawford, Kippax, Onyx, Gault & Benton, 1992, cited in Stephenson & Papadopoulos, 2006, p. 58) was followed to document the life experiences of the participants. For example, according to Crawford et al., writing memories means “...writing a memory of a particular episode, action or event in the third person in as much detail as is possible ... but without importing interpretation, explanation or biography” (2006, p. 58).

The researcher has over 25 years' experience from auditing to financial management across industries such as manufacturing, service industries and banking in Sri Lanka and other countries since 1983. With over nine years' banking experience from 1994 to 2003, the researcher had the opportunity to observe, as a regular participant at board meetings of the Soft Bank, the decision-making procedures at the highest level of decision-making authority. The other participants had been in banks throughout their careers and held various positions from Teller to Chief Manager, a middle level position. The other colleagues/interviewees (peer scholars, fellow bankers and accountants) were contacted where necessary for cross-checking and reliability checking (see Table 4.1).

4.4.2 Interviewing techniques

The interviews were guided primarily by questionnaire. Timing and places of interviews were predetermined and initial preparation for interviews included

making the interviewee comfortable, checking on their moods and attitudes and ensuring maximum freedom from any superior influence, if any, or bias (negative or positive). The following techniques were followed to ensure comfortable atmosphere for colleagues/interviewees.

- The talking times were carefully selected to avoid emotion-charged situations.
- As the researcher is well known to the interviewees personal contact elements were kept to a minimum.
- Preliminary friendly overtures were made and moods were noted before getting into the subject. If there was any sense gained that the interviewees were not in a relaxed state (i.e. overly positive or negative) s/he was contacted at a different time.
- Most interviews were conducted at weekends when they were free from stress and any adverse influences.
- Continuous refinements were made when interviewees were on incidents from previous interviews and therefore, saturation point was gradually reached as repetition occurred.
- All 20 respondents, including the two research participants, were enthusiastic because: they were participating in useful research with a prestigious university in New Zealand; research findings would be shared with them; and participation in future research was also discussed.

4.4.3 Data sources

Data collection was done through both primary and secondary sources. The primary sources are the main participants, including the researcher, for each case study and also include cross-referencing from participants and colleagues for further explanations on each others' case stories at data analysis and

interpretation stages. Secondary data mainly consist of documents and records analysis and the sources include central bank publications, legislations and enactments, directives issued by regulatory authorities, circulars and policy manuals of the subject bank, annual reports, management reports such as corporate plans and treasury reports, research reports published by stock brokering companies and rating reports published by rating agencies such as Capital Intelligence and FITCH, Newspapers and magazine articles and personal communications. Research data for corruption published by Transparency International was helpful in developing the background chapter, Chapter five.

4.4.4 Data-collecting process

Data collection was carried out for three case-studies through reconstruction of the participants' own experiences (the researcher and two other research participants) and those of 18 other colleagues. That makes total of 20 interviewees. All of them were contacted over the telephone, web based teleconferencing, internet chats, e-mails and obtaining answers to questions via e-mails. The research participants, including the researcher himself, were the account managers for the identified cases and had adequate data to build stories of the cases. These interviews were one-to-one conversations with multiple sessions. There are several advantages of having interviews over the phone or via e-mail and internet chat over face-to-face interviews (Krathwohl, 2009). The main advantage of e-mail interviews is that transcripts are readily available because they are in writing. E-mail interviewing avoids a certain level of discomfort when discussing sensitive or controversial issues such as those in this research; it avoids spontaneous responses and enables respondents to be consistent in answering. As with questionnaires, it allows the interviewees more time to prepare as questions can be given in advance.

It is noted that the views expressed by the participants were likely to be biased given that they knew the way in which their views would be used. However, it is an important ethical consideration that they should be informed about the aim

of the research before the study and also the outcome of the research after completion of the study (see Appendix 2: Participant Information Sheet).

Preliminary interviews with nine bankers lasted for about 10-30 minutes each in June 2006, the researcher exchanged a few e-mails and had several internet chats and several telephone conversations with the participants and colleagues/interviewees. Based on the questionnaires and the answers provided, two lengthy interviews were conducted (35-45 minutes each) with the participants. Cross-checking with the other 18 colleagues/interviewees was as short as five to 10 minutes but they were conducted in multiple sessions. Responses to the questionnaires were used mainly to develop case-descriptions (they are now stored as anonymous). Interviews, e-mails, internet chats and secondary sources were used basically to fill the gaps, link events and incidents towards building the stories, ensure accuracy. Finally those responses were used in the stage of in-depth analysis to find answers to *how* and *why* questions reliably.

4.4.5 Saturation

The interview data was incorporated into the analysis by building links between events, tracing commonalities, patterns and relationships or/and posing critical questions towards theorization, for example: “Was the decision made for personal gratification?” After managing the three credit-client accounts for more than five years, a lot of data was generated and the volume was adequate to achieve saturation point. Further clarifications and verifications in the analytical stage were helpful in reaching saturation point. Saturation of data collection was further ensured after obtaining independent feedback from the reviewers and the participants at presentations of conference papers.

4.4.6 Primary data collection: when, by whom, how and to what extent

After conducting preliminary interviews with nine bankers in June 2006, the descriptive-type questionnaire (Appendix 1) together with “Participant Information Sheet” (Appendix 2) was sent to them via e-mail in July 2006. Two

participants responded in detail about their experiences on three credit decisions by the end of August 2006. The researcher exchanged a few e-mails and had several internet chats and short telephone conversations with these two participants during the months of September and October 2006. These communications were helpful in designing the analytical-type questionnaire (Appendix 3) for in-depth investigation with no restrictions imposed on the length of their answers. They were encouraged to describe in detail, as much as possible, the series of events and incidents that they had observed and/or experienced. They responded, with detail, events and procedures that they had observed during the period of 1994 to 2004 with regard to the credit decision to which they were referring. Since, these data were provided by e-mails, cross-questions were posed repetitively by return mail, through internet chats and via phone calls and most of them had answered promptly during the three-month period from September to November 2006. Draft case study stories were sent to the participants in mid-December 2006 and requested to provide feedback as to their opinions in relation to the research topic: “the role of bank lending in sustaining income/wealth inequality in Sri Lanka”. Their feedback was received within one to two weeks, by the end of December 2006.

The data provided by the participants through questionnaires, e-mails and internet-chats on Case III was nearly 4,000 words which has been transcribed to five single spaced pages under appropriate headings. The participant who reported on Case II provided another five pages of data which also consists of 4,000 words. Even for Case IV (not considered), one of them provided another five pages of single-spaced data which accounted for another 3,500 words. All these data had been received by the end of December 2006. In the meantime, with regard to Case I, the researcher reconstructed his personal experience on a credit-decision made by the Chairperson in the year 1997 by using the same questionnaires. Further primary data were collected through other interviewees and, that provided another 5,000 words of data. All the e-mails total approximately 600 words. Therefore, primary text data available for this research is over 16,000 words (16,260 words in Table 4-3) in addition to the

data collected through telephone interviews and internet chats (a total of more than 300 minutes). The data-collection techniques employed, their timing, nature and the amount of data collected are summarized in Table 4-3 below separately for different participants and cases.

Table 4-3: Primary data collection techniques & timing, nature & amount of data collected from different participants

ITEM	TECHNIQUES	Initial Telephone Interview (i)	Descriptive type Questionnaire (1)	Series of Short Interviews (ii)			Analytical type Questionnaire (2)	Further Feedback Phone/e-mail (iii)
				E-mails	Chats	Phone		
<i>When</i>		June 2006	July-August 2006		September 2006		October-November 2006	December 2006
<i>Amount of data: Approximate No. of Minutes/ Words</i>	<i>Case I</i>	N/A	650 words	13	Once	3 Calls 45 minutes	3700 words	100 words
	<i>Case II</i>	25 Minutes	680 words	14	Twice	2 calls 35 minutes	2400 words	150 words
	<i>Case III</i>	26 Minutes	530 words	12	Twice	4 calls 45 minutes	2800 words	200 words
	<i>Cross-checking; All cases</i>	105 Minutes	250 words	41	Nil	30 calls 62 minutes	3200 words	800 words
	<i>Nature of data</i>	Background information of the bank/credit applicant, nature of involvement of the participant	Basic information on participants' experience on credit decisions considered	Friendly chat with the view to design the analytical type questionnaire to obtain more explanations on the credit decisions and to obtain critical analytical data through cross-questioning		Analytical and explanatory data of the credit application, approach, negotiation and decision-making		Verifications/ cross-checking/reliability checks
<i>Total Duration (7 months) / Words (16,260 words)</i>	One month 156 Minutes	Two months 2110 words	600 words	One month 137 Minutes	Two months 12,100 words	One Month 1,050 words		

4.4.7 Secondary data collection

Secondary data covered different sources and provided sound understanding to design questionnaires and prepare for interviews. On the other hand, secondary data helped to validate certain primary data provided by the participants while learning about major events, technical details, historical development and main organizational players and their roles. They also supported exploration of responses during e-mail exchange, internet-chats and interviews.

Publications of the Central Bank of Sri Lanka such as annual reports, Sri Lanka socio-economic data, quarterly research reports and press releases from 1995 to 2008 were referred to to gather data relating to regulatory directions, income distribution, employment levels, and SME development in Sri Lanka. Legislation and enactments such as the Banking Act 1993 and the Securities Exchange Act 1989 provided supporting data to validate certain restrictions imposed by the directives issued by regulatory authorities on the issues such as single-borrower limit, liquidity requirements, capital adequacy requirements and shareholding restrictions.

Internal circulars and policy manuals issued during the period from 1995 to 2003 of the subject bank provided data with regard to credit-evaluation processes, credit approval authority levels and procedures relating to bad loans and provisioning. Annual reports of the subject bank for the years from 1994 to 2007 provided data in relation to liquidity position, capital structure and profitability. Management reports such as corporate plans for 1998 and 2003, budgets for the period from 1998 to 2005, cash flow statements and treasury reports provided data on efficiency and effectiveness of operations and solvency status of the bank as well as of the credit applicants. Market statistics from 1999, 2000 and 2003 published by the Colombo Stock Exchange, research reports published by stock brokering companies and rating reports published by rating agencies such as Capital Intelligence and FITCH provided data on the performance of the subject bank. Newspapers and magazine articles provided data on publicity given for the credit decisions and also post-event/research

performance of the credit applicants and the bank. The World Bank Development Reports of 1987, 1995 and 2005 and the World Bank Development Indicators Database of The World Bank were also used. Scholarly research publications such as *The West and the Rest in the International Economic Order*, *Poverty Reports of 1999* published by the United Nations Development Program provided valuable information. Research data relating to corruption levels of various nations published in the Corruption Perception Index of 2006 and 2007 by Transparency International were helpful. Personal communications with fellow professionals were useful to gather data on the financial situation of the credit applicants. Data obtained through personal communication are mainly financial data of the credit applicants which were not publicly available.

The gathering processes of the above-mentioned secondary data and their sources and uses are summarized in the following Table 4-4: Secondary data and their sources and uses.

4: Secondary data and their sources and uses

AVAILABILITY	World-wide	Sri Lanka	Organizational	Personal
	Web sites Data bases Research reports	Official publications, websites, newspapers, Research reports Regulatory directives	Regulatory publications Internal documents	Telephone conversations E mails
<i>Period</i>	1995-2008	1997-2008	1994-2004	1997-2008
<i>Subject area</i>	Development- economics Poverty Corruption	Development economical, Legal and regulatory information Stock market and rating performances	Public; Annual reports Confidential; policy manuals and circulars	Financial statements Project proposals
	Analysis of income distribution and inequality	Analysis on inequality and unemployment Understand legal and regulatory requirements Share prices	Understanding policy procedures Assess liquidity, solvency and activity levels	Understand and assess potenti Support primary data
<i>Referenced in</i>	Chapters II & V	Chapters II, V, & VI	Chapters VI & VII	Chapters VI, VII & VIII

4.4.8 Record-keeping and storing data

All the answers and descriptions provided by the participants via e-mail have been printed and kept as hard copies anonymously. The draft logically-arranged “chain of evidences” (Yin, 2003, p. 105) developed from the case study data base were sent back to the participants for verification and they were returned with minor amendments. No special software was necessary to store or analyze data.

The names used in this case study reports are fictitious and the most common rationale is that “when the case study is on a controversial topic, anonymity serves to protect the real case and its real participants” (Yin, 2003, p. 158). But maintaining anonymity makes the mechanics of composing the case difficult, and also some important background information had to be eliminated (Yin, 2003). Also the original documents were permanently deleted after taking prints of the texts, (after building case stories and completing analysis and interpretation) which are now anonymous, to ensure the confidentiality of the participants.

Wolcott (1994), in his DAI formula, insists that description, analysis and interpretation should be well balanced in a qualitative inquiry. However he says, “[N]o single combination can be regarded as best, nor is a researcher required to include all three” (p. 49).

4.5 Data description

Data description is the first part in Wolcott’s DAI formula. He identifies a number of ways to organize and present the descriptive section of a qualitative inquiry and insists that, “qualitative researchers need to be story tellers” (Wolcott, 1994, p. 17). The most appropriate method for story telling” is “plot and characters” because “individuals and sociological roles are central to a study, the researcher may proceed as through staging a play” (Wolcott, 1994, p. 20). Polkinghorne (1987 cited in Czarniawska, 2004) says that “plot” is the basic means that brings all the events and incidents into one meaningful whole.

In this staging process, first, main characters are introduced, then the story is presented following a sequential and/or a logical order, whenever appropriate. This analytical framework provides the linking mechanism to build the stories more logically and to depict a more meaningful picture of the case under study.

The following procedure was followed to build the case-study stories. First the background information of main actors of the cases is provided. Then the negotiation process between the bank and the borrower is explained. This process is presented as a logically arranged chain of events, based on the project proposals forwarded by clients (borrowers). Then, the researcher reports the decisions made, with the extent of credit facilities approved, paving the way for an in-depth analysis and, for a brainstorming exercise towards theoretical discussion.

After providing background information on Sri Lanka in a separate chapter, each case study report is organized and presented with separate subheading as follows:

- (a) the background of the case;
- (b) the credit proposal;
- (c) the negotiation process;
- (d) the decisions made; and
- (e) the logical analysis of how and why the decisions were made.

An example of this linking exercise of evidence from data to case-study story is provided in the Appendix 4 for the case-study I.

In the meantime, every attempt was made to keep the case study reports as brief as possible while providing relevant and essential data which are sufficient enough to understand the basis for analysis and interpretation. The data collection and analysis are iterative with a focus on “story building” (Reissman, 1993). The case study reports were repeatedly validated through inter-rater reliability checks with the participants and colleagues to improve the credibility

of the reports. Therefore, data description in case study stories presented in the narrative form is part and parcel of the data analysis process as well.

4.6 Data analysis

Data analysis methods for quantitative and qualitative data follow distinct strategies. They are known as statistical analysis and thematic analysis. O’Leary (2004) explains these methods as follows:

- Statistical analysis – can be descriptive (to summarize the data), to inferential (to draw conclusions that extend beyond the immediate data)
- Thematic analysis – can include analysis of words, concepts, literary devices, and/or non-verbal cues. Includes content, discourse, narrative, and conversation analysis; semiotics; hermeneutics; and grounded theory techniques (p. 11).

Thematic analysis is the data analysis method applicable to this research. “[N]arrative analysis” or narrative mode of knowing (Polkinghorne, 1987) also referred to as the paradigmatic mode of knowing (Bruner, 1986, cited in Czarniawska, 2004) is the primary analytical strategy employed in this data analysis because first, as Llewellyn (1999) claims, “narrating is a mode of thinking and persuading that is as legitimate as calculating” (p. 220); secondly, as Czarniawska points out, “the narrative mode of knowing consists in organizing experience with the help of a scheme assuming the intentionality of human action” (2004, p. 7); and also Bruner asserts that “‘narrative’ in Latin probably comes from *gnarus* (‘knowing’)” (1986, cited in Czarniawska, 2004, p. 16).

Further, Llewellyn (1999) insists that, “...narratives can be explanatory but, more significantly, for accounting and management research, narratives can make some stronger research claims than calculative research” (Llewellyn, 1999, p. 220).

4.6.1 Narrative approach leads to story building

The primary analyzing techniques applied within this narrative analyzing strategy are “story building” (Reissman, 1993) and then “fleshing out” (Wolcott, 1994, p.21). The “cross-case synthesis” (Yin, 2003, p. 109) technique was also appropriately applied because this research is a multiple case study research.

As Wolcott (1994) suggests, the narrative technique could be used as “a fleshing out process of the analytical framework that guided the data collection” (p. 21). Therefore, the following questions were raised to develop an analytical framework for those stories in Chapter seven in order to provide for more plausible and credible (Hammersley, 1992) interpretation in Chapter eight:

- (a) How did the borrowers approach the decision-makers of the bank?
- (b) How and why did the decision-makers accommodate or deny credit?
- (c) How was the transaction concluded?
- (d) Why were those decisions concluded in that manner?

This analytical process supports to build the cases as stories and therefore, in this case study research the data description and data analysis activities are complementarily linked together.

4.6.2 Theoretical propositions, rival explanations and case description

According to Yin (2003), there are three strategies available for analyzing case study data; “relying on theoretical propositions”; “thinking about rival explanations” and; “developing a case description” (pp. 112-114). These strategies are not mutually exclusive in application. However, “thinking about rival explanations” is not employed here because the focus is on Marxian critical interpretation. Therefore, the other two strategies are appropriately followed in analyzing data in this research, as explained in the next section.

Yin (2003) suggests that, “the first and most preferred strategy is to follow the theoretical propositions that led to your case study” (p. 111). The theoretical

propositions in this research are derived from the Marxian concept of the credit mechanism. Further, Wolcott (1994) advises “if theory (or theories) works for you as a starting place, use it...let theories guide you...” (p. 402). Therefore, neo-Marxian critical theory was selected to guide the researcher in analyzing and interpreting the research questions, as justified in the preceding chapters. However, Wolcott (1994) further insists that “if the turn to theory (theories) does not help, then story telling is a good place to start, and good story telling is a great way to start” (p. 402). Therefore, the data analysis methods used in this research provide a strong foundation for data interpretation by presenting the data in a form of story telling supported by theoretical guidance.

According to Hooper (2001), “searching for themes ... which may be linked to a theoretical proposition” (p. 6) is the primary objective of this story telling. This objective is achieved by organizing the data to emerge a “linking logic” (Hooper, 2001). Therefore, this story-building structure was designed for logical data analysis and discussion, in order to lay the general foundation and, as a “rehearsal for interpretation” (Hooper, 2001) to explain, how and why those decisions were made. Then possible root causes and motives were critically examined towards theorization using qualitative validity techniques such as: collaborative evidence such as explanations and interpretations from the research participants, and inter-rater reliability checks (Schutt, 2001).

4.7 Reliability/credibility and validity/conformability

Reliability of data in qualitative data primarily depends on the rigour applied by the researcher. A triangulation of various data collecting methods was employed to link the events and incidents reported by the participants towards story building. O’Leary (2004) suggests an additional indicator that can be used to assess credibility in change-oriented research: “usefulness”. If a research objective is to expose an inequitable/unjust situation, then a measure of success or credibility will be how useful the research outcome is in proposing a remedy. Therefore, considering the seriousness of the research problem in this study, it would be appropriate to claim that the credibility of this research outcome is

high because the “usefulness” of the findings is substantial in exposing certain inequitable social mechanisms.

All preventive and remedial measures were followed to ensure the reliability and validity of data collected in this research: use of pre-tested questionnaires; improving question order, format and removal of inappropriate questions including “biasing”, “negative”, and “double barrel” questions (Krathwohl, 2009) life event calendars (to assist in avoiding memory loss); continuous improvement of cross-checking techniques and obtaining prompt feedback. Extensive efforts were made to maintain interviewee enthusiasm and a letter of participation was promised.

4.7.1 Verification process to ensure reliability of data

Reliability of data is significantly enhanced by the triangulation of data from multiple cases. The main characters of the case study stories are the four decision-makers (the Chairperson in respect of Cases I & II and the Branch Manager, Recovery Manager and Chief Recovery Manager in respect of the third case) and the three credit applicants themselves: Tony, Yousef and Silva.

The Chairperson was personally observed by the researcher for nine years. Tony’s account was handled by the researcher for two years and the researcher had the opportunity of sitting with the board of the Tony Group as the representative of the Soft Bank during those two years.

Tony, of Case I, has been in business for more than 35 years. Tony was frequently interviewed in the media for his contribution to the nation as the one of the largest foreign exchange earners and employment generators in Sri Lanka. As such, there is extensive public information available through independent media; therefore these reports are auditable if Tony’s identity is revealed.

Yousef, of Case II, and his automobile manufacturing businesses had wide publicity in Sri Lanka. There were numerous news articles about his

automobiles and his business plans. The researcher was able to contact Yousef’s accountant for verification of projections as well as actual performance. Officers of the Registrar of Motor Vehicles were contacted to verify certain assertions made by research participants and media reports.

In fact, most of the information analysed in this research where the Chairperson is involved as the decision-maker is freely available to the general public of Sri Lanka.

The credit managers of all credit applicants were thoroughly involved in this research. The researcher made the maximum efforts (choosing appropriate times, place etc.) possible to minimize bias and the effects of superior influence.

Silva (Case III) cannot be contacted as he was not in business but the researcher managed to contact all other players: the Branch Manager, the Credit Manager, Recovery Manager (I) and the Senior Recovery Manager (II).

The researcher had constant contact with his colleagues (contemporary fellow bankers and accountants) and made use of that social network to gather very pertinent, confidential and useful data.

An analysis of all the interviewees at initial, descriptive and analytical data collection stages is given in the Table 4.1 below:

Table 4-5: Number of interviewees

	<i>Participants</i>	<i>Colleagues/interviewees</i>	<i>Total</i>
Data collection stage			
Case descriptions	3	12	15
Analysis	3	18	21
Saturation	3	16	19
Total	3	18	21

4.7.2 Ensuring external validity/generalisability

External validity refers to the generalisability of study findings to other situations while internal validity refers to how well the study provides evidence for the causal process investigated. In any study, there is a trade-off between internal validity and external validity (Krathwohl, 2009). Although studies with large representative samples have high external validity, they may suffer from low internal validity. On the other hand, single case studies with thick descriptions (Geertz, 1973) have high internal validity. Internal validity is high in this research as it discusses processes, patterns and relationships in an organization with three case studies. However, these types of case studies may lack external validity. In the present study, the researcher attempted to maximize both internal validity and external validity by studying a representative bank with three representative cases.

Table 4.4 below shows the level of representativeness of the credit applicants in Sri Lankan enterprise financing through bank loans. The Soft Bank typically represents the private commercial banking sector as elaborated in Table 4.5 below. All appropriate, relevant and stringent measures were taken to ensure the validity of this research. These were as follows:

A sample of initial contact persons was selected to reflect a cross-section of the banking culture in Sri Lanka. Extremes were avoided:

- Not too young or too old (from 42 to 62 years of age);
- From different levels of decision-making (senior, middle and front; branch manager, credit manager);
- Different levels of qualifications—professionals, part qualified and experienced;
- Different departments – large and medium credit management, loans in the recoveries department and branch level credit; and
- No relatives, friends or connected parties of any credit applicants and credit decision-makers.

4.7.2.1 Representation of the cases

Twelve common characteristics of credit applicants were tested to assess the representativeness of the three credit applicants studied in this research as tabulated in Table 4.2 below. All the bank officers contacted for this assessment have had branch manager positions in various parts of the country. They were of the view that ordinary credit applicants face problems with collateral, rigid credit evaluation rules and lack of support from accountants with regard to the accessibility, affordability and availability of credit. Also they agree that medium and large credit applicants are beyond their authority and are mostly accommodated with extra effort by the senior officers. Customer get-togethers are common in all Sri Lankan banks and all respondents agree that only large and medium sized clients are invited to such functions. Representation is ranked as high, average and low compared with other credit applicants the respondents had been aware of for the last 10-20 years.

Table 4-6: An assessment of representation of Sri Lankan credit applicants in general by the credit applicants considered

<i>Level of representation</i>			
	<i>Tony</i>	<i>Yusef</i>	<i>Silva</i>
Characteristic			
Legal form of the business entity	Average; with 2-5 private companies	High; with 1-3 private companies	High; sole proprietorship
Ownership	High; with 80% with owner-manager	High; with 80% with owner-manager	High; with 100% with owner-manager
Credit amount involved	Low; US\$4 million is too large	Average; with US\$500,000	High; with US\$20,000
Type of business	High; labour intensive	Low; car manufacturing in Sri Lanka	High; labour intensive
Employment generation	Low (exceptionally high generation)	High	High
National interest	High with large exports	High with unique import substitution	High with high employment
Number of banks involved	Low (many banks)	High (a few banks)	High (only one bank)
Problems with collaterals	High	Average	High
Bank's authority level involved	Average with senior management	Average with senior management	High with middle management
Informal approach by the applicant	High	High	High
Informal methods by the decision-makers	High	High	Average
Success in credit approval	High	High	Low

Source: Compiled by the author through annual reports and interviews

Ranking high and average on most characteristics, it is evident that the three cases selected represent the SME sector in Sri Lanka in general.

4.7.2.2 Representation of the Soft Bank

Sri Lanka has a total of 22 commercial banks equally distributed between domestic and foreign (11 banks each) and, out of 11 domestic banks, nine private domestic banks, including the Soft Bank, share 40 percent of all banking business while the two state-owned banks share 57.5 percent in terms of branch distribution and approximately 41.1 percent in deposits, loans, assets and turnover in 2004 as well. That leaves only 2.5 percent of banking business to all of 11 foreign bank branches (The Central Bank of Sri Lanka, 2008). The Soft Bank alone enjoyed a 8-9 percent of market share in 2004.

Sri Lankan commercial banking business distribution is condensed and compared with the Soft Bank in the following Table 4.3.

Table 4-7: Distribution of market share of commercial banking industry in Sri Lanka in 2004 (percentages are given in parentheses)

Item	<i>State banks</i>	<i>Domestic private banks</i>	<i>Foreign banks</i>	<i>Total</i>	<i>The Soft Bank</i>
Number of Branches	778 (57.5)	535 (40)	39 (2.5)	1352	110 (8)
Assets LKR billions	576 (56.2)	423 (41.1)	29 (2.7)	1028	88.5 (8.6)

Source: CBSL, 2008

A set of common characteristics were tested to establish the representativeness of the Soft Bank compared to other domestic private banks which share 41 percent of the banking business in Sri Lanka. In Table 4.4, fourteen such characteristics were tested with interviewees to assess the level of representativeness of the Soft Bank in the Sri Lankan private banking sector. The representation level is indicated by Yes/High, Average/Likely/Medium and No/Low. The banks numbered as 1-5 represent listed privately owned

commercial banks, number 5 being the Soft Bank and number 6 comprises all other small/unlisted/private commercial banks.

Table 4-8: An assessment of representation of private banks in Sri Lanka compared to the Soft Bank

<i>Bank</i>	Level of representation					
	<i>1</i>	<i>2</i>	<i>3</i>	<i>4</i>	<i>5</i>	<i>6</i>
Characteristic						
A few large shareholders	Yes	Likely	Yes	Yes	Yes	Yes
Large number of shareholders	High	Likely	High	Likely	High	Low
Large shareholders interfere in decision-making	Yes	Likely	Yes	Likely	Yes	Yes
Bureaucratic management style	Yes	Yes	Yes	Yes	Yes	Yes
Rigid management policies and procedures	Yes	Yes	Yes	Yes	Yes	Yes
Regulated closely by CBSL	Yes	Yes	Yes	Yes	Yes	Yes
The external auditors are from Big Four audit firms	Yes	Yes	Yes	Yes	Yes	Average
Positive perception of investors; Measured by the PE ratio	Medium	High	High	High	Low	N/A
Branches are distributed all over the island	Yes	Yes	Yes	Yes	Yes	No
Catering to the same market	Yes	Yes	Likely	Likely	Yes	Likely
Similar deposit base structure	Yes	High	High	High	Yes	Average
Catering to corporate clients	Average	High	Average	Average	Average	Low
Level of non-performing loans	High	Low	Medium	Low	High	Medium
Level of similarity in transaction processing	High	High	High	High	High	Average

Source: Compiled by the author through annual reports and interviews

In addition to the above characteristics, they also share similar features such as: management hierarchy comprising of 15 levels (level one being the lowest grade for drivers and peons and level 15 being the General Manager/ Chief Executive Officer); very similar levels of decision-making authority assigned to each grade, similar salaries and perks pertaining to each grade, same levels of capital adequacy and liquidity and similar physical appearance of head offices and branch offices. Also, according to interviewees, though the Chairpersons of other banks (private or state owned) do not exercise executive powers, directions are commonly given by Chairpersons to Management and when this is done credit is granted in most cases.

Given the evidence for commonalities and the patterns observed in the three cases and, based on the 12 and 14 characteristics tested for representation of the cases and the Soft Bank respectively, the researcher argues that certain relationships are common in the Sri Lankan banking sector. Therefore, this research demonstrates nature of the credit culture of the Soft Bank which may be taken as a representative bank within the private banking industry in Sri Lanka. Hence, though the original aim of the research was not really to generalise the findings to claim a credit culture applicable to Sri Lanka, this representativeness encouraged the researcher to pose a theory that the credit culture of the Soft Bank may be replicated in other Sri Lankan private banks.

4.8 Interpretation and theorization

As emphasized by Stake (2005) this research too was designed primarily “to optimize understanding of the case rather than to generalize beyond it” (p. 443). Further, Bailey (2007) asserts that regardless of the analytical strategy applied, the goal of a research study remains as “to understand experiences and meanings attached to them” (p. 175). According to Bailey (2007), creativity plays a very important role in interpreting data and Jorgensen (1989) advises the researcher to imagine saying that, “use your imagination! The analysis of data

leading to discovery requires creativity” (p. 110 cited in Bailey, 2007, p. 175). Therefore, interpretation is seen in a more artistic sense rather than a scientific exercise in qualitative research. Bude (2004) says that, interpretation is an art, “to dealing with ambiguities, handling limitations and mixing separate components” (p. 321).

4.8.1 Inductive generalization and abductive inferencing/reasoning

Bude (2004) promotes abductive inferencing/reasoning as a more artistic way of interpretation, quoting from Charles Sanders Peirce (1839-1914) as follows:

Charles Sanders Peirce, in his famous methodology of “abductive inferencing” saw a way beyond inductive security of generalization and deductive certainty of derivation: deduction proves that, for logical reasons, something must be the case; induction demonstrates that there is empirical evidence that something is truly so; abduction, by contrast, merely supposes that something might be the case. It therefore abandons the solid ground of prediction and testing in order to introduce a new idea or to understand a new phenomenon (p. 322).

The strategies applied for the analysis of research data provide necessary background to think about data and, “this is step along the way to building up ideas and theories” (Coffey & Atkinson, 1996, p. 139). The widely accepted polar-opposite logics for interpreting research data are inductive generalization and deductive derivation. Hooper (2001) says, “...philosophically, it is argued, inductive and deductive methods cannot be combined” (p. 4). In this light, it is worth noting the comments of Coffey and Atkinson on these two logics:

Inductivism is based on the presumption that, laws or generalizations can be developed from the accumulation of observations and cases that the close inspection of ever more data can be made to reveal regularities. The polar opposite—a strict adherence to deductive principles—...is founded on the assertion that empirical research can be used only to test theories...Neither of the polar types is satisfactory in informing the actual

generation of ideas...One needs to break free of the strait-jackets imposed by conventional logic (1996, p. 155-156).

Much interpretation of this research relies on inductive generalizations especially in explaining the ‘*how*’ questions and, also on abductive inferencing/reasoning especially in explaining most of the ‘*why*’ questions. Therefore, the researcher first identifies a particular phenomenon; a surprising or anomalous finding, then tries to relate that phenomenon to broader concepts. Abductive inference/reasoning suggests to go beyond the data themselves and the researcher should not have to be restricted to fit themselves into existing ideas. Therefore, abductive inference is more appropriate for qualitative inquiry--an open-minded intellectual approach is normally advocated (Kelle, 1995b, cited in Coffey & Atkinson, 1996). However, the inductive approach is more applicable to answer “*how*” questions when the conclusions can be generalized from empirical evidence.

4.8.2 Subjectivism, objectivism, constructivism and criticism

In explaining interpretation, Umberto Eco (1990) suggests that:

To interpret means to react to the text of the world or to the world of a text by producing other texts...The problem is not to challenge the old idea that the world is a text which can be interpreted, but rather to decide whether it has a fixed meaning, many possible meanings, or none at all (p. 23).

However, Czarniawska (2004) says “explanation is often set in contrast to interpretation ... but all inquiry asks both ‘what does this text say? And ‘how come?’ ” (p. 63). Czarniawska classifies these different schools of thought concerning the modes of explanations or interpretation into three groups: Subjectivists (voluntarists), Objectivists (determinists) and Constructivists. She says that subjectivism is the “most traditional way of explaining texts...by deducing the intentions of the authors...comes from reading Bible, Talmud or Koran as authored by God” (p. 63). In contrast, she suggests “the meaning of a text is neither to be ‘found’ nor ‘created’ from nothing; it is constructed anew

from what already exists” (Czarniawska, 2004, p. 66). But she agrees that “there are great many excellent explanations of subjectivists and objectivists type” (p. 69).

On the other hand, the democratic nature of interpretation is well accepted, appreciated and consciously applied and this theoretical perspective is often called critical Marxism (Sherman, 1995). This research is about social injustice. Therefore, critical interpretation is deemed more appropriate in interpreting the outcome of this research as explained in the following section.

4.8.3 Interpretation of social injustice

The interpretations provided by the modern critical theorists (for example, Allahar, 2004; De Brunhoff, 2003; Faulks, 1999; Goulet, 2002; Gray *et al.*, 1996; Lapavistas, 1994; 1997; 2000; 2003; M. Moore, 1997; Neimark, 1995; Saad-Filho, 2003; Passe-Smith, 2003; Tinker & Gray, 2003; Tinker, 1980; 1999) based on Marxian theories provide stronger framework for explaining social injustice.

It is worth noting Czarniawska’s arguments on discovering knowledge: “The task of critical social sciences – and therefore of critical reading – is to unmask interests that underlie the enterprise of knowledge (Habermas, 1972)” (2004, p. 66). Czarniawska argues that the Marxist theory of interpretation, which is based on “dialectical criticism” (Jameson, 1981), “does not analyze isolated works; each work is but a part of a wider historical situation, and so is each reading. A dialectical criticism seeks to unmask the surface ... to reach the depth of the concrete historical ideology...” (p. 66).

In line with this argument, because this research problem is a part and parcel of the problems of the Third World hegemonic-economic systems (see Saad-Filho, 2003) and because it is a part of a wider historical ideology, the socio-economic issues, especially in the Third World which cannot be “isolated” from the present-day globalized world economy (see Robinson, 2004; Goulet, 2002; Perelman, 2003) the Marxian interpretations are appropriately employed in

explaining the research findings. As (House, 2005) says, “there are political reasons why qualitative studies were viewed as too subjective and illegitimate. Ultimately, it has to do with social justice” (p. 1074) or injustice.

4.8.4 Theoretical framework

According to Llewellyn’s “differential realities”, this research study overlaps mainly structural and cultural realities because; “the structural world is dependent upon human activity – it is not self subsistent” (2007, p. 60). The realities which the researcher attempts to discover and explain are not “the mental world” because, the research findings are not private to the researcher and they do exist outside human minds. The Marxian analysis and interpretations used in this research are not orthodox Marxian “objectivist explanations” or “constructivist-subjectivist claims” because, as Smith and Hodkinson (2005) point out “the subject-object dualism of empiricism is untenable” (p. 915) and “there is no possibility of the objective stance or view – often called the ‘God’s eye’ point of view” (p. 917). Therefore, as Bude (2004) suggests, the more appropriate method of understanding the outcome of this research is “abductive inferencing or reasoning...[means] ‘something might be the case’ ” (p. 322) as opposed to deductive derivation where something *must* be the case. But this abductive inferencing is well supported by inductive reasoning wherever possible and applicable which “demonstrates that there is empirical evidence that something is truly so” (p. 322).

The purpose of this case study research is “to develop a form of cultural criticism revealing power dynamics within social and cultural texts” (Kincheloe & McLaren, 2005, p. 311). According to Hooper (2001), “the purpose of a case study may be to develop a theory or test a theory, or use a theory to critically analyze phenomena” (p. 6). This research is primarily designed to use Marxian theories to critically analyze the credit mechanism in Sri Lanka.

CHAPTER FIVE

5 BACKGROUND: SRI LANKA

5.1 Introduction

This chapter provides information about Sri Lanka and its people--the socio-cultural, economic and political background of the case studies discussed in this research. Changes in socio-cultural values, beliefs and habits of a society are strongly intertwined with the historical development of the economic and political systems within it.

Sri Lanka covers 65,610 square kilometres. The population was 3.5 million a century ago in 1901 and 20 million in 2007. This tiny island has characterized its nationality differently in the midst of numerous invasions from the South, the East and the West. This information is useful in understanding the significance of the role played by such invasions and colonisations in influencing the lifestyle of its people. The chapter proceeds, first outlining briefly the political history of the island. Second, it explains how these changes in governance influenced the socio-cultural habits and values of Lankan society especially with regard to decision-making methods and monetary systems. It also compares the inequality status of Sri Lanka with global inequality.

5.2 History

Sri Lanka has been ruled by more than 200 Kings since 543 B.C. In 1815 Sri Lanka became a colony of Great Britain. Beginning with a land-based capitalist structure after gaining independence in 1948 Sri Lanka followed mixed economic policies of both capitalism and socialism. In 1977, a capitalist-centred (right-wing) government revolutionized Sri Lankan politics, marking the end of the state-centred economic system. Stimulated by IMF and World Bank

initiatives, public enterprises were seen as economic burdens and the government sought a more competitive market environment and privatization.

5.2.1 Currency, mortgages and money-interest in medieval times

According to Siriweera (2004), medieval literature refers to *kahavanu* a kind of currency used by villagers to pay for ghee, venison and lime and coins have been found at sites in the city of Anuradhapura in layers datable to a period around 100 B.C. People have deposited their money for interest returns and, even borrowed money against their assets and paid interest similar to present-day mortgages. Siriweera states that,

...currency was deposited in guilds in expectation of a return in interest payment and there were instances of obtaining currency loans on interest (*poli*) by individuals on trust or by mortgage (*ukas*) of movable or immovable property (2004, p. 214).

5.2.2 Ceylon under British rule (1796-1948)

On 2nd March 1815, a convention was held at Kandy between the British governors and the chiefs representing the people of (then) Ceylon. Ceylon acquired a typical colonial export economy supplying the world market with a few primary products and importing consumer goods. British governors revolutionized the economy of Sri Lanka by introducing an export-oriented agriculture-centred economy. Sri Lanka soon became world renowned for producing drinking tea, brand-named Ceylon Tea. Sri Lankan society transformed dramatically embracing Western customs and practices and classes started replacing castes with the power of money and land capital. The next section describes these changes briefly. Between 1885 and 1915 the Ceylon economy had grown rapidly and major contribution was from exports (Jayawardena, 1972). As a result of these capitalist industrial developments, the educated peasant villagers not only got a break from agricultural work but also had an opportunity to break through into the urbanized middle-class pattern of living (Jayawardena, 1972). During this time radical social movements too started raising their heads, apart from moderate national movements and anti-

Christian campaigns. The Donoughmore reforms were implemented and a State Council was elected under universal suffrage in 1931, a political event which marked a significant breakthrough by the Ceylonese middle class into parliamentary politics (Jayawardena, 1972).

5.2.3 Voting rights and Marxist influence

Sri Lanka was the first Asian electorate to enjoy the benefits of universal suffrage just after two years after Britain and 20 years ahead of India (M U De Silva & Wriggins, 1988). Meanwhile, British-educated Marxist political leaders also appeared, challenged the conservative labour organizations and took over the leadership of urban labour in the mid 1930's. They became popular not only among the urban working class but also among the rural farmers who found a similarity between Buddhism and Marxism. This demonstrates a marked difference between Hindu beliefs and Buddhist beliefs because, in India Marxist ideology was rejected by the masses as Max Webber explains:

a religious ordinary peasant who abides by prescribed traditions, never demands over-pay, never deceives as to quality...and as long as the karma doctrine was unshaken, revolutionary ideas or progressivism were inconceivable (Webber, 1958, p. 123).

According to Jayawardena (2000), the economic activity of Sri Lankan capitalists during the 19th century was mildly entrepreneurial. She says that, Sri Lanka like other Third World countries, was neither wholly capitalist nor feudal but comprised features of both because development of capitalism is an “unfinished business”. Therefore, as in many colonies, the Sri Lankan bourgeoisie was a kind of colonial type of capitalist and a class dependent on protection and opportunities provided by the colonial state (Jayawardena, 2000). According to Jayawardena, this double-headed class mostly imitated the ruling British including embracing Christianity but imposed their power on the general public as in the medieval king-ship era and showed willingness to help others by sponsoring social and religious activities which in turn rewarded them by other means such as access to resources without competition and honorary recognitions. She explains this situation as follows:

Sri Lankan bourgeoisie was the product of colonial form of capitalist production it was an appendage of imperialism, a dependent as opposed to an independent class...[their] life styles were imitative of a feudal aristocracy and land owning gentry, and acts of philanthropy and the funding of social and religious causes (which brought rewards...) further enhanced the prestige and status of the class (Jayawardena, 2000, p. ix).

The next section explains the post-colonial socio-economic and political background of Sri Lanka after gaining its independence on 4th February 1948.

5.2.4 Post-colonial administration after independence in 1948

Sri Lanka has doubled its multi-ethnic population to 20 million during the past 50 years after gaining independence, surpassing a population density of 320 persons per square kilometre by 2007 (The Central Intelligence Agency, 2007). The ethnic conflict and the terrorist activities led to migration and the majority of such migrants are Tamils the representation of which is now only 3.9%. There are two principal languages used, Sinhala (75%), and Tamil (25%). Most of the world's great religions are practised with the majority of people being Buddhists (69.1%) and others consisting of Muslim 7.6%, Hindu 7.1%, Christian 6.2%, unspecified 10% (Amnesty International, 1993).

Sri Lanka was awarded its independence in 1948 without much of the bloodshed experienced in India. The governments elected followed mixed economic policies of capitalism (open market system) and socialism (centrally planned system). Beginning with a feudal-capitalist structure (land-owning capitalist structure) in the 1950s, it embraced policies of a planned economy in the 1960s and then it made a revolutionary change to follow market-oriented growth policies in the mid 1970s with restrictions on off-shore capital transfers, and some import taxes. After practising open market economic policies for 29 years, Sri Lanka improved its GNP per capita from US\$250 in 1977 to US\$4,700 in 2006 in spite of a 20-year civil war and a bloody insurrection of "Marxist" youth in the South from 1987-89. On both occasions Sri Lanka lost more than 100,000 lives (Amnesty International, 1993).

The whole Third World including Sri Lanka is struggling to improve their living standards, infrastructure facilities and comfort levels. However, the statistics and analysis below show that most of those countries have not shown satisfactory progress, either in their development activities or their social well-being when compared to that of developed nations. There are various theories which have been presented to explain this situation. This research also attempts to explore the possible root-causes for this social problem with a view to assist the policy-makers of developing countries to find a solution.

5.3 Impact of invasions and transformation

The ancient system in Lanka was such that the king was supreme, and his autocratic power was controlled only by custom and by the fear of assassination (Codrington, 1926). The administration of justice was in the hands of the chiefs and headmen, all of whom had the power of inflicting slight punishments and fines. The king alone had the power of life and death, and the Great Court consisting of the principal chiefs could only impose such punishments as were within the competence of the Adigars (ministers); all important matters were referred to the king.

Traditionally, Sri Lankans with their Buddhist-Hindu culture are scared of wrongdoing and wrong thinking because of their beliefs in *karmic* repercussion either in the present life or even in other lives after death. The primary feature of Sri Lankan culture was a self-sufficient agricultural lifestyle based on non-violence and mutual cooperation (De Silva, 1997). According to (Endagama, 1997) the ancient Sri Lankan people did not have either the habit or the necessity to save money because of their simple lifestyle. However, she says that from the 16th century onwards the political, social, economical and cultural environment started changing because of the arrival of Europeans. When the Portuguese arrived in 1505, the whole island of Sri Lanka had been ruled as a kingdom. This crown-based administration system had been deeply rooted according to the traditional socio-economic values of Sri Lankan culture for 20 centuries, since 483 B.C. The sovereign-authority of the King was a harmless

dictatorship and the people had the faith and expectation that the King would protect their customs and values which were strongly linked to the prevailing unwritten traditions (Codrington, 1926).

5.3.1 Early signs of informal methods

However, changes started appearing in the coastal areas where preferential terms were followed by the rulers towards Europeans and converted Lankans especially under the monopolistic nature of trade by the Portuguese and the Dutch. Also, according to Codrington (1926), the Kandyan Court never observed any treaty obligation. Codrington says that many articles have been published on the iniquities and unjust approaches of the Portuguese. Corruption and discrimination prevailed in all departments of the administration therefore, the Sinhala chose to abide by their own laws at the meeting at Malwana in 1597. Codrington further states that:

Under the old government the chiefs had a wholesome fear of the king, who, if a strong ruler, suffered no tyrant but himself; under the Portuguese every lord of a village, every petty headman, assumed powers which would not have been tolerated before (1926, p. 160).

For example, the cinnamon peelers (the people who extract cinnamon from cinnamon trees) rose against their headmen, but were subdued, punished and deprived of many privileges (Jayawardena, 2000). By a system of rules the Dutch also kept a tight control of all sections of the people in the area. The people needed permission to start their trades and introduction of strict price control of products in addition to moral supervision by the puritanical Dutch rulers (De Silva, 1997) would have paved the way for the people to exploit informal means to carry out their business in more competitive manner.

The grievances of the people in general were many. Fines were imposed for failure of their children to attend school; the cultivation of chenas or low jungle periodically cleared and sown was wrongfully monopolized by the headmen. *Watubadda*, a tax on certain gardens was introduced. The cinnamon peelers complained of unjust treatment by their headmen and of heavy taxation. In this

regard, De Silva quotes from the writings of Franciscan Reverend Trinitade and Jesuit Reverend Kerosé and says that:

The implementation of the orders to maintain the law and order was not successful because the Portuguese bureaucrats at every level had been corrupt to some extent. They neglected the directions from the Portuguese Governor as well as from the provincial King. The people in these areas lost the faith on the Portuguese administration on the matters related to justice, because they had realized that the bureaucrats were out of control. Proper investigation was not carried out for the complaints made by the people against corruption (De Silva, 1997, p. 117-8).

With regard to British mercantilism, according to Jayawardena, trade came under rigid mercantilist control and restricted by “licences”. Codrington says that,

it must be remembered that the worst enemies of the villager often were his own fellow-countrymen; the *Vidanes* were as bad as any Portuguese village lord, and the Lascarins in 1636 actually prayed for Portuguese instead of Sinhala *Mudaliyars* and *Arachchis*, a prayer curiously reminiscent of a similar request by the people at Kandy in 1815 (1926, p. 157).

5.3.2 Development of corruption

This situation created a lot of pressure and unrest among the people in the coastal areas and the evils such as corruption, discrimination and favouritism had gained more recognition than law, order and justice. According to De Silva, (1997) this is a critical factor for the Portuguese in losing the battle against the King with the new arrivals of Dutch. Another factor that worked against Portuguese in winning the hearts of the people was their “by-force” conversion policy imposed on Buddhists and Hindus. Under the Sinhala kingdom system every citizen was entitled to and owned a piece of land. But Portuguese Governors disregarded this rule and confiscated lands and transferred them to affluent people and government bureaucrats (Codrington, 1960).

They rented these lands to ordinary people for cultivation on a crop-sharing basis called the *ande* system (Chandraprema, 1997; M U De Silva & Wriggins,

1988). A system of official shares offered for government service was administered objectively under the Sinhala kingdom system, but this system was abandoned by the Portuguese governors and allowed the official share to pass to the next generation making them official owners of those lands over time. Therefore, a powerful class, irrespective of caste, had been created as land owners without any service to the government or the people. On the other hand De Silva says, quoting from a Portuguese writer Ruberu, that “bureaucrats had the power to deliver even death punishment to an accused without a proper trial” (p. 118) which was the right of only the King before.

Rich people from castes such as *Karawa* (fishermen) and *Salagama* (cinnamon peelers), who are considered as lower castes compared to the castes of farmers and King’s administrators, converted to Catholicism and obtained positions in the administration. Ordinary people shifted their faith from law, order and justice to bribes, favouritism and cronyism. The lifestyles started changing from peasant, non-violent mutual cooperation towards enterprising competition.

An increase of corruption in the state bureaucracy was discussed by several scholars (for example, Liyanage, 1997; Ponnambalam, 1980; Ratnapala, 1986; Srathchandra, 1982)) during the centre-left (socialist-centred) governance of “a curse of seven years” from 1970 to 1977. The perception towards the government was such that, the people elected the exact opposite right-wing (capitalist-centered) United National Party (UNP) government with a historical landslide victory of 80 percent of the seats in the parliament in the 1977 general election. But the criticism is worse for corruption as well as deterioration of the socio-cultural value system (The Central Bank of Sri Lanka, 2008) during the 17 years of right-wing liberal economic governance which was defeated again decisively by the people in 1994 and the impact is such that the UNP has not won a single election for the last 16 years.

5.3.3 Interpretation of traditional methods

However, it is important to recognise methods such as bribes differently from traditional methods of greeting the superiors by way of *dekum* or presents which

were given in public on appointment. The King received these presents also at the New Year, at those festivals the chiefs benefited as well, receiving presents from all the minor headmen whose turn of office only lasted for a year. The system still continues in the Kandyan temples.

5.3.4 Monetary system

There was a popular credit system which prevailed in Sri Lanka known as *Seettu*; pooling of money by a group of people and each takes a turn to enjoy the total amount of money, the order of turn taking was determined by a lottery system. If anyone was in urgent need of money he/she could demand a turn offering a discount which was distributed proportionate to the contribution to the pool. It is similar to zero-coupon bond where the interest is paid up-front.

The first bank in Ceylon was established in 1841 (Andree, 1863). By 2003, Sri Lanka had 22 commercial banks; 11 local and 11 foreign banks. Out of 11 local banks the two state banks dominated the banking industry with a 60 percent market share. Out of nine private commercial banks, four listed banks in the Colombo Stock Exchange accounted for another 34 percent of the banking market. There were nearly 1300 bank branches and offices all over the island with around 500 automated teller machines (ATMs) (The Central Bank of Sri Lanka, 2008). ATMs were introduced as early as 1988. However, according to the Governor of the Central Bank of Sri Lanka, the informal money market still accounted for approximately 30-40% of the total money market operations of Sri Lanka (The Island, 1999).

5.4 Bank supervision regulatory framework in Sri Lanka

The Central Bank of Sri Lanka (CBSL) conforms to international standards in their regulatory framework. The banking regulatory framework consists of the Banking Act No. 30 of 1988 and its amendments, directives, circulars and Guidelines issued by the Bank Supervision department of CBSL based on the standards set by the Basel Agreement to maintain healthy balance sheet for banks. The Bank Supervision Department of the Central Bank of Sri Lanka

monitors compliance with regulatory and statutory requirements in force at any time and attempt further strengthening the regulatory framework to meet the new developments and challenges in the banking sector and the changes in the international regulatory standards. They monitor, on a regular basis, the statutory requirements such as: ownership structure; capital adequacy; single borrower exposure; interest recognition; provisioning for bad loans; corporate governance; and timely publication of Financial Results. The Financial Intelligence Unit of CBSL monitors compliance with requirements arising out of the legislation on Anti Money Laundering, Prevention of Terrorist Financing, and Financial Transaction Reporting Acts.

The regulation and supervision of licensed banks in Sri Lanka are governed by a number of enactments, legislation and supervisory measures. The primary such Acts are listed below:

1. Monetary Law Act No. 58 of 1949;
2. The Banking Act No.30 of 1988 and Banking (Amendment) Act No. 33 of 1995, Banking (Amendment) Act No. 46 of 2006 and No. 15 of 2006;
3. Exchange Control Act No. 24 of 1953 and its amendments;
4. Payment and Settlement Systems Act No. 28 of 2005; and
5. Financial Transactions Reporting Act No. 6 of 2006.

The laws empower the Central Bank to implement the following:

1. Grant approval for the establishing and closing of banks, branches and other business outlets of banks;
2. Issue prudential directions, determinations and orders to banks, under statutes;
3. Conduct off-site and on-site examination of banks; and
4. The enforcement of regulatory actions and the resolution of weak banks.

For these purposes, the Central Bank has requested such banks appoint a suitable senior staff member as a Compliance Officer. However, all banks need

to file Compliance Reports on a monthly and quarterly basis and it is mandatory for the CEO of the bank to sign such Compliance Reports.

Minimum entry capital requirement: In 2005, the Central Bank increased the minimum entry capital requirement for Licensed Commercial Banks to Rs. 2,500 million (from Rs.500 million) and for Licensed Specialised Banks to Rs.1,500 million (from Rs.200 million) (Direction No 2, 2007, The Central Bank of Sri Lanka, 1988-2008).

External auditors: Recently the CBSL warned external auditors of banks not to be too lenient towards compliance requirements and suggested that banks should change their auditors every five years (Circular No. BS/38/90, The Central Bank of Sri Lanka, 1988-2008). There are quite a number of International audit firms present in Sri Lanka including the “big four”: KPMG, Earnest & Young, PriceWaterhouse and Deloitte & Touche. All private banks have auditors with international reputations.

Non-performing loans: Interest income is recognised strictly on a performance basis and if a loan is not serviced for 90 days the interest is credited to a suspense account and the account is transferred to non-performing after 180 days. This complies with the guidelines issued by the director of bank supervision, Central Bank of Sri Lanka. Provisions are made for the net exposure after considering possible recoveries from the forced sale values of collaterals (Direction No. 3 of 2008, The Central Bank of Sri Lanka, 1988-2008).

Capital adequacy: The capital adequacy requirement is 8 percent with Tier 1 capital requirement of 4 percent. Tier 1 capital consists of total shareholders’ funds and preference shares and subordinated instruments such as debentures are classified as part of Tier 2 capital. Assets are weighted according to their risks as stipulated by BASEL agreement in calculating these ratios (Direction No. 9 of 2007, The Central Bank of Sri Lanka, 1988-2008).

Liquidity: The liquid assets requirement is 20 percent of deposit liabilities and reported daily to the Bank Supervision department. Liquid assets include all

sovereign instruments and money market instruments apart from cash in hand. There is a minimum cash maintenance requirement of 2 percent of deposit liabilities (The Central Bank of Sri Lanka, 1988-2008)

Ownership restrictions: The Banking Act allows only 10% of shareholding by a person or persons who are acting in concert (The Banking Act No. 30, 1988). The Security Exchange Act in Sri Lanka restricts holding shares by any single shareholder to 5% in a company listed in the Colombo Stock Exchange (The Securities Exchange Act, 1989). The banking act prohibits lending money to purchase and/or grant advances against its own shares but the loophole exploited by the Seylan Bank board of directors was that, if the beneficiaries are the employees of the bank such purchases are exempt from this requirement (C I Rating, 2007).

The single borrower limit: A single borrower limit restricts banks to lend to a single applicant 30% and for a group of companies 33% of Tier 1 capital of a bank (Direction No. 7, The Central Bank of Sri Lanka, 1988-2008).

The restriction imposed to limit the service period of directors of banks: CBSL introduced new rules concerning age and service periods of a bank Chairperson. The board of directors of the Seylan Bank fought against the CBSL, challenging this regulatory direction which limits the service period of the directors of banks in Sri Lanka to 9 years. The case was lost (Corporate Governance Direction No. 11, The Central Bank of Sri Lanka, 1988-2008).

Corporate governance: A document issued by CBSL specifies, among other matters, the responsibilities of the Board, composition and the criteria to assess the fitness and propriety of directors. The roles of chairman and chief executive officer have been separated and the board is required to have board committees covering Audit, Human Resources and Remuneration and a Nomination Committee and Integrated Risk Management Committee (Corporate Governance Direction No. 11, The Central Bank of Sri Lanka, 1988-2008).

5.5 Accounting profession in Sri Lanka

The Institute of Chartered Accountants of Sri Lanka (ICASL) is the primary accounting body in Sri Lanka. Also, there are other accounting professionals who are members of international accounting bodies such as the Chartered Institute of Management Accountants (CIMA). The ICASL has 3,602 members according to the directory of members and firms 2009. There are 2,651 members in Sri Lanka, mostly employed in large organisations while a few are employed in medium-sized organisations. Another 951 members are overseas scattered through 43 countries (The Institute of Chartered Accountants of Sri Lanka, 2009).

CHAPTER SIX

6 CASE STUDIES; STORIES

6.1 Introduction

This chapter has two main sections. First, it presents the background information to all three case studies considered in this research. This section provides information about the lending institution involved; the bank, its management style and operational aspects. It also provides information on policies and regulations applicable in the banking industry in Sri Lanka supported by an industry outlook as well. The second section deals with the case studies and it provides the background information of borrowers with sections on credit proposals, negotiation processes, decisions and outcomes of the decisions. This presentation style is followed consistently for all three cases.

6.2 Background

There was a terrorist attack in Colombo, the Capital of Sri Lanka, in January 1996. The damage was heavy with a death toll of more than 30 people and casualties of more than 300 people. It caused severe damage to the buildings around, including the office of Mr. Perera who was the Chairperson of Soft Bank, the banking arm of a large group of companies. He was hospitalized with serious injuries to the left eye and eventually he lost the eye.

Mr. Perera (the Chairperson), in his late fifties, was a devoted Catholic, and the most venerable priests came and prayed for him in the hospital. He was told that "...Your duty for this world is not over; therefore the God has saved you to serve the people more."

The University of Sri Lanka recently awarded the Chairperson with a Doctorate for his contribution towards the business development of the country. He was a well recognized business tycoon having more than 100 companies under the

name of Soft Group, and 10 of them had been listed on the Colombo Stock Exchange. A leading business magazine named him as the Personality of the Year in 1997. The Soft Group had more than 10,000 employees, US\$80 million of net assets and US\$2 billion of total assets. The Soft Bank accounted for almost 50% of the assets base and one-third of the workforce of the group.

6.2.1 The Soft Bank

While Mr. Perera was under clinical treatment in London, the General Manager/Chief Executive Officer (CEO) of the Soft Bank had a clash with the Board and he left the Bank together with almost all the members of the senior management team of the Soft Bank in June 1996 and formed a new bank. Further, more than 100 officers left the Soft Bank and joined the new bank in September 1996. The dissidents, in canvassing an already known customer base, also launched adverse propaganda against the Soft Bank. The bank was facing severe problems, losing staff, deposits and customers simultaneously and without a strong management team, in need of strong leadership. As a result the Chairperson had to be involved heavily in the day-to-day operations of the bank and therefore, he suggested to the board that he would have weekly meetings with the senior management of the bank to monitor the progress closely. He also strengthened his power on the board by inviting a few loyal confidants (two lawyers, an accountant and an IT specialist) on to the board of directors of the Soft Bank.

6.2.1.1 The management style of the Soft Bank, pre-1996

Normally the full board meeting was held on the last Friday of the month when all the board members participated and crucial decisions were made. It was evident that the board/Chairperson approved only the proposals (credit, restructuring of large facilities, new recruitments, staff promotions and capital expenditure, etc) recommended by the then management. When there were customer/staff complaints or requests for credit facilities from the Chairperson/directors, they were re-directed to management, and the CEO had

to report on those at the next board meeting. This process was followed to avoid conflicts by giving due respect to the formal hierarchical-authority.

6.2.1.2 The management style, 1996-1997

The new CEO was a very senior banker, in his late 50s and demonstrated a very democratic and consultative style of management. He had no experience of holding the “hot” seat before and showed laissez-faire type leadership qualities. The Finance Manager, a qualified accountant, was promoted to the position of Chief Financial Officer (CFO), by the new management. In addition to the full Board meeting, the Soft Bank started three more weekly review meetings, on the other three Fridays of the month, for the Marketing, Recoveries and Information Technology functions of the bank. The relevant senior officials were summoned to these meetings whenever necessary, while the CEO and CFO were invited for all three meetings.

It was the practice of the Chairperson to allocate some time to handle customer complaints, plights of potential customers and even requests from the general public. He always exhibited his customer-friendly attitudes and often allowed the customers to confront the bank officers openly, sometimes, causing embarrassment to respective officers.

As the Chairperson of 100-plus companies, he used to give directions over the telephone to the CEOs of those companies for speedy implementations of his decisions. He is so “liked” by his friends and confidants, including his wife, on the Board of Directors that no question is raised against his decisions; all decisions were unanimously approved.

He once approved a proposal forwarded by one of his group companies to buy and implement a computer system for branch banking, priced at US\$40 million, without a proper investment appraisal. The IT chief of the bank later revealed to the researcher (personally) that the project never came up and the bank was left with a few computers, printers and outdated software. The IT chief of the bank, a Washington University PhD, who drew the second highest emoluments in the

bank with foreign trips and other perks, said “Why should we worry? His (the Chairperson’s) car and his petrol, let him drive as far as he can?” This IT expert is now the IT chief of the General Bank of Sri Lanka.

Most of the support services such as catering, security and printing, etc., were diverted to group companies. The catering service was provided by Russel’s Catering Services owned and operated by Mr. Russel who was a relative of the former CEO. Russel’s only customer was the Soft Bank head office. Spotting a slight fault, Russel’s service was discontinued and diverted to a group company by the Chairperson. The justification of firing this small businessman was that infiltrators, especially from the former CEO and the senior officers, could have access to the back-office of the Soft Bank in the uniform of Russel’s Catering. It could be a threat to the Bank.

The Chairperson’s favourites were given rapid promotions, frequent and substantial pay hikes, foreign trips and special bonuses, etc. These developments caused unrest among the staff but nobody dared to speak because it was well known that the intelligence network of the Chairperson was very effective, even conversations were tape-recorded and reported to the Chairperson immediately. The punishments include transferring personnel to areas (called Siberia) where the “suspect” had no expertise. Then they would find faults; create reasons to fire those officers for “incompetence”. It was also common to observe that, if the staff member was influential (or honest but not loyal, or a crony but not honest), he/she is offered substantial compensation for voluntary resignation. Therefore, the staff including the top managerial officers seems very “loyal”, dumb and blind to the Chairperson’s decisions.

6.2.1.3 Compliance with banking regulations/standards

Strict compliance of the single-borrower limit prevented the Soft Bank from lending to sister companies in the Soft Group. The Chairperson was not very happy about this concept since most of the group companies paid significant amounts of interest to other banks on their borrowings and the process was not reciprocal because none of the other banks operated as a part of a group as the

Soft Bank operates. He used to say in a lighter vein that, “the Rugger Ball technique is the best strategy for these regulators. We must do the best for us and let the regulators chase behind us”.

The Soft Bank had obtained special approval from the Central Bank Sri Lanka for direct holding of 18 percent of its equity by the Soft Group. The Banking Act allows only 10 percent of shareholding by a person or persons who are acting in concert. But the Soft Bank had more than 50 percent of its ownership with the Chairperson, his wife and a few companies of the Group, through indirect holdings and employee share ownership schemes, which are allowed by the Banking Act. This loophole is that the special permission granted to purchase shares of a bank by its employees by creating trusts in the name of employees called “Employee Share Ownership Plan” (ESOP) but the ownership is limited to five percent. Under normal circumstances banks cannot lend money to purchase their own shares but ESOPs are exempt of such restrictions. Therefore, the Soft bank created six ESOP trusts and lent money at a concessionary rate of interest to purchase its own shares, and each trust acquired 4.99 percent of ownership adding up to 29.9 percent of ownership in total. The present owners did not inject a single cent as new capital but it was a “smart” way of using others’ money to acquire the controlling power of an institution. The directors of these ESOPs are their most loyal employees (such as relatives and friends) and, in this way the Chairperson feels more powerful because he looks after not only himself but his cronies as well.

Under these circumstances Mr. Perera became the all-powerful Chairperson of the Soft Bank. One rating agency had reported “[T]he Bank’s Chairperson, a promoter shareholder, plays a disproportionately large role in running the Bank and particularly in setting policy. The Group’s track record in managing the Bank has not been good so far”.

6.2.1.4 Financial outlook of the Soft Bank

The Soft Bank was very successful in marketing customer deposits and it had some unique strengths. The bank was young (incorporated in 1989) and had a

young enthusiastic workforce, led by a prominent businessperson in the country, backed by a large group. The advertising and publicity campaign was aggressive and the Soft Bank soon became a household name all over the island. It expanded rapidly, opening 100 branches during the first seven years. The customer deposit base was three times of that of SET Bank, which was also incorporated in 1989. It was the second largest private bank in terms of customer deposits and assets and became the largest private bank in terms of the branches and number of employees by the end of the year 1996.

However, the profitability figures were poor, reporting its Return on Average Assets (ROAA) as less than one percent and Cost to Income (C/I) ratio as more than 70 percent, which was the highest among private banks listed in the Colombo Stock Exchange. The amount of non-performing loans (NPL) had risen to more than 20 percent of the total loans. The Central Bank of Sri Lanka severely warned the management several times and had set time frames to address the issues immediately. The Chairperson was frequently summoned by the Director of Bank Supervision of the CBSL to monitor progress and reassure the commitment of the management to compliance. The Chairperson gradually developed doubts on the efficacy of the systems as well as the personnel of the Bank.

The market price of the Soft Bank stock was also not performing in par with the industry average Price Earning (PE) ratio. Research reports on the Soft Bank, published by most of the stockbrokers were adverse with a recommendation to “sell” or “hold”, because of poor financials when compared to the financials published by the peer banks.

In 1995 the Soft bank had reported US\$3.5 million of after tax profits. The share had been trading with an average PE ratio of seven times, where the industry had performed at 12 times. The Cost to Income ratio worsened from 70 percent in 1995, to 80 percent in 1996. The NPL level was also in the high side with 18 percent in 1995 and 20 percent in 1996, compared to the industry average of 14 percent, while the CAT bank reported the best NPL ratio of seven

percent. The ROAA of the Soft Bank was one percent in 1995, came down to 0.6 percent compared to the two percent of the CAT bank--the international average was reported as two percent.

The Capital Adequacy Ratio was reported as eight percent, just within the regulatory requirement. The Soft Bank was experiencing a hard time with the external auditors and the Bank Supervision Department of the Central Bank of Sri Lanka with regard to the provisions to be made for bad loans. The provision for bad debts, as a percentage of after-tax profits was 50 percent for the Soft Bank whereas the industry average was only 10 percent in 1996. But the deposit growth of the Soft Bank was reported to be the highest in the industry with 35 percent growth, from US\$520 million to US\$703 million during the year 1996, compared to the industry growth of 15 percent. The Soft Bank achieved a remarkable loan growth of more than 54 percent (industry average loan growth was 20 percent) in 1995 and 25 percent (industry average of 20 percent) in 1996 contributing to the total assets base growth of 22 percent compared to the industry average of 15 percent.

The selling pressure on the Soft Bank share was aggravated by the adverse rumors spread by the dissident group, who worked for the new bank. This situation pushed the share price further down.

6.2.1.5 Interest rate changes and the Government Policy

With the change of the Government in 1994 the CBSL cut the REPO rate (Re-Purchase Offer rate similar to the OCR, (Official Cash Rate in New Zealand) and Reverse REPO rate frequently. This situation affected most of the banks (with low Advance to Deposit ratio) which had invested their funds in government securities. The REPO rate, which was at 18 percent at the beginning of the year 1995, was slashed frequently in 1995 and 1996 to remain at 10 percent at the end of the year 1996. The spread between the REPO rate and the Reverse REPO Rate also fell from three percent to two percent.

Sri Lanka had a very peculiar type of interest rate scenario where the Government Securities (GS) carried higher rates of interest than the rate offered by banks to the public for their deposits. Therefore most of the banks followed a very conservative lending policy, comfortably parking their excess funds in risk-free Treasury Bills and/or Treasury Bonds, and made an easy secured spread.

This is because the GS (Treasury Bills/Bonds) were not easily accessible to the general public especially for small customers because there was a minimum amount required for investment. Also the investment and the liquidation procedures were complicated so that ordinary customers conveniently opted for the closest, friendliest branch of a bank and invested their money in deposit products with a lower return.

6.2.1.6 The liquidity position of the Soft Bank

The Soft Bank had about US\$100 million invested in Government Securities. This amount is over and above the statutory liquidity requirement. The Soft Bank was highly liquid with an extraordinary growth in customer deposit base and had reported 34 percent of statutory liquidity ratio as against the regulatory requirement of 20 percent. This situation was reported to the Management by the CFO and pointed out if the bank mobilized funds at the present rate of interest and invest in GS, without investing in loans/lending, the bank would make a negative gross spread (contribution) of three percent on incremental deposit funds. The Chairperson was critical of the lending policy of the Soft Bank and the regulatory requirements such as *Capital Adequacy* and *Single Borrower Limit*, and approved the following two strategies to be implemented immediately:

- To cut the interest rate offered by the Soft Bank for deposits by three percent.
- To introduce attractive loan products for aggressive lending, offering a lower rate of interest.

The CEO and the top management officials were very nervous about reducing the rate of interest for customer deposits, citing that the Soft Bank would not be competitive among the rival banks which were still offering the same rates despite the official rate cut by the CBSL. The CEO warned that there would be a “run on the bank”. The Chairperson queried the tolerable limit of such a “run” and instructed the CFO to monitor the deposit movements daily and report if the liquidity position of the Bank was in jeopardy.

On the other hand, the senior credit officials were severely warned and assigned with a massive task of achieving already increased lending targets. The marketing team was asked to make a presentation on some innovative lending products after working with the advertising agency of the Bank. The budget and the cost-benefit analysis had to be vetted by the CFO and a quick time plan for the launch had to be tabled at the next review meeting.

The Soft Bank lost deposits due to offering the lowest interest rates in the market but the trend was not that alarming to the liquidity position. The marketing team was very critical about the situation and warned, “Once you lose a customer, it is very difficult to win them back.” One of the popular arguments was: “We worked very hard to win this customer base. The cost of regaining them would be much more than the saving that we get from the reduced interest rate.”

However, it was surprising to note that all other banks followed suit and reduced their interest rates for deposits, in six to eight weeks’ time. The growth rate of deposits of the Soft Bank too returned to normal. The average interest rate offered by the banks for one-year fixed deposits as at 30th June 1996, was 12 percent. The Soft Bank reduced that to nine percent in August. In the middle of August the average rate came down to 11 percent, then to 10.5 percent by the end of the month and finally to nine percent by the third week of September 1996.

6.3 Case Study I: Tony Group

6.3.1 Background

One Friday, while the Chairperson was conducting one of the review meetings of the Soft Bank, Mr. Tony, the owner of Tony Group, contacted the Chairperson for an immediate appointment to discuss an urgent matter. The Chairperson immediately made arrangements for a quick meeting showing all the respect due to another business tycoon of the country.

Tony was adjudged the Entrepreneur of the Year in 1995. His group had accounted for a major share of textiles and garments exports, which was the largest foreign exchange earner of the island. The Tony Group expanded very fast, especially during the previous regime of the Republican Government, with huge loan facilities from the government-owned banks, for the setting up of factories in rural areas. The Tony Group had a very good reputation for manufacturing garments for world-renowned brands like Marks & Spencer, GAP, Van Hussein, and a few others. Those buyers also had invested in high-tech equipment and quality-control experts in the Tony Group factories. The Tony Group had been running smoothly. The total export income of Sri Lanka was US\$12,050 million in 1996, and the Textiles & Garments Sector accounted for US\$6,484 million which was more than 53 percent of the total export income of the country. The Tony Group accounted for approximately US\$200 million in the year 1996.

Tony arrived in 30 minutes with his team of professionals including the Finance Director (experienced accountant) Financial Controller (chartered accountant), Chief Operating Officer and three Joint Managing Directors. Tony explained how he developed the group. He stressed the national importance of his business, especially in employment generation and foreign exchange earning.

6.3.2 The proposal

According to Tony, his group had 15,000 permanent employees and another 15,000 contract workers. He tabled the details of his factories with their

capacity and locations. He blamed the newly appointed Labour Government for not allocating an adequate quota for him to work on full capacity and therefore, he complained that his group was running with a negative cash flow due to under-utilization of assets. He was in the midst of a crucial issue, and stated that he had no money to pay the salary bill for the current month. The best employees were leaving the group and he said he had no option other than agreeing to the foreclosure suggested by the banks.

He also pointed out that the new owners of his business would not be able to maintain the same rapport with the international buyers as he did and, the whole episode would end up in a tragedy, pushing 30,000 workers out into the streets. He was pleading to the Chairperson to bail him out, assuring that this credit line would rejuvenate the whole group and the future cash flows would be very healthy with the orders in their hands. He also requested a facility of Letter of Credit (LC) to import the necessary fabrics and accessories.

At the request of the Chairperson he explained his cash-flow situation and borrowing positions. The total borrowings of the Tony Group were more than US\$20 million. This comprised US\$5 million from Bank of Lanka, US\$5 million from SET Bank, US\$2 million from HAT Bank and a syndicated loan of US\$8 million from all three banks. He had borrowed from three private banks and the Bank of Lanka, the largest state-owned bank in Sri Lanka, which had structured a syndicated loan as well. The monthly commitment for servicing these loans was US\$0.7 million. Due to non-servicing of interest, almost all the banks had classified Tony Group as a defaulter and had reported this to the Credit Information Bureau (CIB), which is the central monitoring authority for defaulters.

When evaluating the creditworthiness of a client, the first thing a credit officer has to do is to call for a CIB report of the client. Tony had applied for a facility from the Soft Bank a week ago and the team leader of Corporate Credit Division had declined it on the basis of the CIB report.

Tony was very convincing and very politely explained how the senior officers of the Soft Bank rejected his proposal and praised the Chairperson for his visionary leadership and patriotic attitudes in advance.

6.3.3 The negotiation

The Chairperson showed his grief about the situation and blamed the politicians, regulators and bankers for not identifying the need of the country.

He said, “This is the whole problem with our bankers. They are guided by some stupid rules called banking practices and ruin people like you [Tony]. They will never think beyond that cage of banking practices. Even our state policies do not have provisions to support people like you. Now, you have generated 30,000 jobs. If they lost their jobs and you lose your business, the cost will be much more to the economy in the long run.” Then, in a disappointed tone, he said “I don’t know, when these people will learn these things?... .”

After listening to overjoyed remarks by Tony who too joined the Chairperson to criticize the prevailing systems, the Chairperson suggested “...tell me Tony how much do you want? And what is the collateral you can offer?”

Tony said, “Sir, all my assets have been taken by the banks, I can give my personal guarantee and the secondary mortgage of the assets which have already been mortgaged to the other banks, and Chairman sir, believe me and I will not let you down.”

“Your house?” the Chairperson queried. “That’s in my wife’s name and I am sorry sir, I can’t draw her into this, she will eat me”, Tony answered.

Then the Chairperson asked, “Can you give your wife’s personal guarantee?”

But Tony politely disagreed saying, “I am very sorry sir, but do not worry I will never let you down and I will pay every cent due to your bank on time, and I am not going to deal with any of those other banks in the future, my one and only bank is your bank for the rest of my life”.

The Chairperson smiled and said, “Ok, tell me your requirement, have you got a good accountant? Do you have the cash-flow projections?”

“Yes sir, our cash flow is always positive but not adequate to service the loans because of production hiccups and not performing our factories in their full capacity. If you help we can have enough orders to fill the factories to perform at full capacity then we will have cash surplus of US\$1 million initially and would grow to US\$1.5 million in three months’ time. To do this I need US\$2.5 million advance to pay my salary bill and other statutory dues. And I need a LC facility of US\$1.5 million to finance input materials for uninterrupted production.” (A monthly cash flow projection was tabled and explained it by the Financial Controller and the Chairperson looked convinced).

“Is that all you need? Tell me right now, you will not be facilitated under the normal banking practices by our credit officers in the bank.”

Tony was jubilant and said, “That’s what I wanted your Honor. I do not need a cent more than what is necessary”, and he invited the Chairperson to chair his board: “Why don’t you come and chair our Board meetings as well?”

The Chairperson thanked him for the invitation and said, “I don’t want to interfere with your business, you are the best person to manage your business, but you can give us good publicity.” “Of course, sir”, Tony readily agreed.

The following day the business page of a leading newspaper carried an article entitled, “Soft Bank rescued Tony Group”. The news spread fast and Tony announced that Mr. Perera had helped him. He issued a special circular to the Tony Group employees saying that they all must do banking with the Soft Bank explaining that the Soft Bank was a truly kind bank, while criticizing all other banks for advocating him to sell the factories.

The Chairperson was very happy about the publicity given and the copies of the paper cutting of the news item circulated among the Board members at the next Board meeting. He assured the board that he will bring more and more business

and expressed his regrets that he could have done that before, meaning involving himself more in the day-to-day activities of the bank.

6.3.4 The decision

The Chairperson approved all the facilities amounting to US\$4 million. He was very critical of the bank officers who rejected Tony's proposal purely on the CRIB report and said, "I think we need a good accountant, not a banker, to manage Tony's facilities" and appointed the CFO as the credit officer in charge for the Tony Group. The CFO was instructed to monitor the cash flow position thoroughly and whenever there was a situation which warranted over the limit borrowing, he had to report to the Chairperson.

Tony was jubilant on the quick decision made by the Chairperson and offered him a seat on the main Board of the Tony group with a brand new Mercedes, which was still in the harbour, imported under the permit granted for exporters. The Chairperson politely refused the offer and appointed his CFO as an observer in the Board of the Tony Group. The Chairperson, pointing the CFO, said "He will be my eyes and ears in your Board".

6.3.5 The outcome: what happened to the Tony Group?

Sunil, one of long-time close confidants of Tony, was fired. He was one of Tony's executive directors. It was a known fact among the accountants that, it was very difficult to work with Tony. No financial controller had worked for a long period at the Tony Group and it was not rare to notice vacancy advertisements for the post of Financial Controller for the Tony Group. Senior executives started leaving Tony Group, or were asked to leave. Sunil criticized Tony's financial discipline and always complained about liquidity problems. He complained that Tony did not transfer sales proceeds in full to Sri Lanka. He said that Mr. Tony was very particular about the closed exchange control policy of Sri Lanka, and always had a buffer in overseas. Tony used various tactics to keep a part of his wealth overseas. Once he successfully convinced the Chairperson of the Soft Bank to open a factory in an African country as well.

Tony remitted money for this purpose as a capital investment outside Sri Lanka, under a special permission from CBSL.

The Tony Group's fate is not a unique one. With the cessation of the quota system, the other countries like China and Malaysia could supply the same garments at a lower cost, therefore the buyers naturally shifted their business out of Sri Lanka for better margins. This threat was brought to the knowledge of garment businesspersons, and only a few dynamic enterprisers created their own brands and successfully transformed the threat into an opportunity. But the Tony Group was over-dependent on international brands and lost some of the contracts to Malaysia.

6.3.6 The outcome—Tony Group account at the Soft Bank

Later, the Tony Group account was taken away from the CFO and handed over to the Corporate Banking division. The new credit officer submitted a formal proposal for the Tony Group and the management approved the package recommended and extended a further facility to smooth the cash flow.

After four years of operation, the Soft Bank had to provide for bad debts since the Tony Group could not service the loan. The interest loss was around US\$0.3 million which was in interest in a suspense account, and the capital write off was nearly US\$1 million by the end of 2003. The Tony Group gradually lost their business and started closing down factories under the pressure imposed by the banks. The staff cadre had come down to 10,000 with only 20 factories operating by the end of 2003. The monthly sales of US\$2 million in 1998 had come down to US\$1.5 million in 2003 and were virtually making a negative contribution.

6.4 Case study II; The Lan-Car Ltd.

Similar to Case I presented in the previous chapter, this case-study story follows the same style of presentation starting with the background information of the

borrower followed by the credit proposal, the negotiation process, the decision, a few important events and the outcome of the decision.

6.4.1 Background

The promotion of Foreign Direct Investment (FDI) was the central strategy of the newly formed Republican Government to generate more employment, as they had promised in the election manifesto. However, Sri Lanka continued to experience poor levels of Foreign Direct Investments. Though the government was successful in suspending the war, which had prevailed for more than two decades, the FDI flow did not improved as expected. The FDI was reported as US\$176 million in 2000, and US\$157 million in 1999 against the target of US\$500 million per year (The Central Bank of Sri Lanka, 2003).

The private sector was very critical on inefficient and ineffective government/policies and was demanding a dramatic change in the development strategy. In response, the government decided to stimulate domestic investments by offering more incentives and forming separate decentralized authorities to minimize the effect of the inefficient bureaucracy in the government agencies. The government also invited the well-reputed private sector business personnel to take charge of these authorities and show promising results.

Mr. Perera (the Chairperson of the Soft Bank) was appointed as the head of Western Province Economic Development Authority (WEDA), one of the five authorities set up under the new government policy. The other four zones were based in the North, East, South and the Central provinces. Mr. Perera publicly canvassed for stimulating domestic investments and minimizing foreign investment dependence. The domestic investment as a percentage of GDP was reported as 25.1 percent in 1998 and 27.3 percent 1999 as compared to the target of 35 percent per annum.

The Chairperson was very enthusiastic about the new role and started his duties with a “big road show”. He set up a fund from his own companies and full-page advertisements appeared in the newspapers for the grand opening of his office

as the President of WEDA. His wife started a reservoir project and named it Dora—her own name. He reserved Mondays for his new venture and Sunday newspapers used to carry huge advertisements on the investment promotional activities in the Western Province.

At the board meetings of the Soft Bank, as well as at the Soft Group companies, he used to mention that he was bringing more business to those companies.

The Television programme he started became a trumpet for Mr. Perera and his group. The participants appeared as entrepreneurs praised the Chairperson for his support; some of them almost worshiped him for rescuing them from debt traps. The Chairperson initially used TV Channel One, then extended to Channel Two and telecast a few advertisements during the Tele-programme sponsored by the Soft Bank on Channel Three, to advertise his contribution in promoting local investors—big or small.

6.4.2 The proposal

Lan-Car Ltd., an automobile manufacturing company located in the Central Province, was the second automobile manufacturing company in Sri Lanka. The first was in operation in the 1970s and that was closed soon after the open market economic policies were introduced in 1978. Lan-Car Ltd. manufactured two models (a car and a van) and branded them as “Lancar” (the car) and “Lakvan” (the van). Except for the engine and a few parts, imported from Italy and China, all other parts of the car were made and assembled in their factory in Sri Lanka. But these vehicles had been refused registration by the authorities on the grounds of a lack of conformity to safety and not being roadworthy, etc.

The owner of Lan-Car Ltd. Mr. Yousef, and his management team approached the former Hon. Minister of Lands to obtain a piece of land to establish their plant and sought assistance to expand production that was running at a rate of eight cars per month. They waited for more than a year for a favourable response from the Hon. Minister, but were disappointed. Eventually, they sought favours from the Chairperson, who was holding a series of investor

seminars in 2000 to promote economic activities in the region under his purview.

Yousef and the team attended one of the seminars and realized that they could find solution with the Chairperson. They came up to the next forum equipped with the best car and van they had made. Throughout the oral presentation, that lasted barely 15 minutes, the Chairperson appeared convinced and said that he was going to extend maximum support to them. He expressed his displeasure about the oligopoly type of vehicle market in Sri Lanka, dominated by a few countries, mainly for dumping their used vehicles, and draining away the country's foreign exchange resources. After inspecting the vehicles and having a test-run as well, the Chairperson immediately decided to provide them with suitable land to set up their new factory, and he requested them to identify a suitable piece of land in the Western Province.

The Chairperson used to host lunches for the participants of the investment forum, at a tourist hotel restaurant (sponsored by the Soft Group) and discussed the financial matters related to financing their projects. There was no one from the Soft Bank to point out prudent lending terms to the Chairperson; instead Soft Bank officials only answered his questions, mostly endorsing the Chairperson's view. The prospective investors, politicians, if any, and the top officials of WEDA often participated in these discussions.

6.4.3 The negotiation

Yousef and the team did their homework well and returned with the details of a few suitable pieces of land. The most preferred land already had an almost complete factory building which they could use. Apparently, it had been vested with another investor, by the WEDA for an ill-fated project that had been abandoned for some time without any action as per the terms of bestowal. The President of WEDA (the Chairperson) had full powers to transfer the land to another prospective investor. But Yousef volunteered to negotiate with the former investor for a fair compensation. They praised the President for his

support in finding a suitable piece of crown land through WEDA, for their project.

Yousef boasted that he was unable to cater for the demand for vehicles. Because of lack of machine-capacity and factory-space, he proposed to install new machinery to increase the production. They were already incurring losses, as production was insufficient to meet the fixed costs, so they appealed to the Chairperson to save them from total ruin.

The Chairperson was convinced about the feasibility of the project. He asked Yousef to consult a professional accounting firm to prepare a project report.

The Chairperson promised market-support as well, placing an order for 200 Mobile Banking Vehicles for the proposed Soft Bank branches in rural areas that were not covered within the branch network. Lan-Car's prospects were significant, and they should make 200 such banking vehicles in the next year commencing with 10 vehicles for 2000. Table 6-1 below shows the projections presented by the accountants of Lan-Car Ltd.

Table 6-1: Production and financial projections of Lan-Car Ltd.

<i>Year</i>	<i>2001</i>	<i>2002</i>	<i>2003</i>	<i>2004</i>	<i>2005</i>	<i>2006</i>
Sales (Units)	20	30	50	100	200	900
Sales	\$ 50,000	75,000	125,000	250,000	500,000	2, 250,000
Loan (31Dec.)	\$ 500,000	700,000	1.2M	1.2M	1M	NIL
Interest thereon	\$ 60,000	84,000	130,000	130,000	100,000	60,000
Cash flow	\$ (30,000)	(39,000)	(68,000)	(30,000)	100,000	840,000

Fixed cost proportion is negligible. Break-even point is US\$325,000 (130 cars) and Contribution Margin Ratio is 60% in 2001, 2002, 50% in 2003 and 40% afterwards as no price increase.

6.4.4 The decision

The Chairperson was keen on promoting investments by Sri Lankans and used his powers as the President of WEDA to sort out various problems of investors within his authority area, without hesitation. He used to quote Professor Yunus from Bangladesh to justify certain credit decisions he made in favour of certain small/poor self-employed enterprisers. But these accommodations were perceived by bank officers as tactics for publicity.

Yousef presented the project report with positive financial projections professionally prepared by qualified accountants. Based on the cash flow budget and profitability forecast, Chairperson immediately approved a loan of US\$500,000. The bank officers endorsed the Chairperson's decision without any hesitation as the decision was justified by the feasibility figures on paper. No one raised the question of roadworthiness and refusal of registration by the Registrar of Motor Vehicles. He approved a further facility of US\$200,000 in 2001 and US\$500,000 in 2002 to accelerate production.

6.4.5 A few important events

Though the facilities were provided continuously, Lan-Car Ltd. could not perform as expected due to various obstacles. Some problems identified and reported by Yousef were as follows:

- Red tape at the Sri Lankan Customs to import the factory fittings and machinery items.
- Production capacity was still not at the contributory level, and running at cash-flow deficit, therefore, the bank facilities were escalated.
- Registrars of Motor Vehicles refused to register the vehicles, according to Yousef, mainly due to absence of methodology to check the safety measures of the vehicle.

The morale of Yousef and his team was also depleted and Lan-Car was in jeopardy; even the cars released to company employees had been run using

temporary numbers. The Chairperson, constantly briefed on the progress of the projects, decided to take a Lan-car personally to the Registrar of Motor Vehicles and got it duly registered using his social status and influence, and this opened the gateway for the Lan-car to the roads.

6.4.6 The Outcome—what happened to Lan-Car Ltd.?

Though Yousef is still struggling to organize his factory to meet the demand, his loan is in the active category due to the continuous support extended and the interest would have been paid by new loans.

Finally, Yousef abandoned the manufacturing project, but converted the resources to assemble a different automobile by importing all the parts. The car manufacturing plant was established in 2001. By the end of 2006 the factory had 19,500 square metres of land, 7,500 square metres under roof and 1,500 metre of test track. However, the plan was to have 1300 cars by 2006 and to make a positive cash flow of US\$850,000 after paying all the loans in full. The loans had increased to US\$2 million by 2006 and some of the interests were in a suspense account. In 2006, a company spokesperson said there are about 500 cars on the roads in Sri Lanka but these cars were not manufactured as planned but assembled in his factory with all foreign parts for which huge import duties are levied. Therefore, the cars did not contribute 40-50 percent as projected and break-even was never achieved; cash flow was negative.

The bank had earned handsome interest, maybe through its own loan. The project was a failure. The loans are now serviced from a different project which is assembling automobiles. No credit officer would have considered this automobile manufacturing business as a feasible project purely because the product cannot be marketed in Sri Lanka; there is a refusal of registration due to problems of roadworthiness. Though it was registered by the Chairperson, informally, using his powers, doubts on safety hindered the demand and on the other hand, Yousef never achieved the expected production. The Soft Bank will have to write off some capital with interest overdue.

6.5 Case study III; Superclean Services

Similar to the previous two cases this case-study story follows the same style of presentation starting with the background information of the borrower, followed by the credit proposal, the negotiation process, the decision, a few important events and the outcome of the decision.

6.5.1 Background

Superclean Services was a sole proprietorship of Mr. Silva of Dehiwela. He started this janitorial service business in 1991. His first client was the Dehiwela branch of the Soft Bank, which was the first branch of the bank. His service was very satisfactory so that he was contracted with all janitorial services of the bank. As the bank expanded its branch network rapidly Superclean's business boomed, becoming the sole janitorial service provider to the bank.

Mr. Fernando, the manager of Dehiwela branch (BM) handled the Superclean account very systematically, financing its initial capital investment requirements to serve the newly opening branches. The recovery process was streamlined by directing the payments from the Soft Bank to the loan account of the Superclean. Superclean was exceptionally good at meeting the needs of "finishing up" at branch openings, mostly at short notice, sometimes at concurrent branch openings. Further, he did these services all free of charge for the opening day polish-ups, strengthening the relationship with the Bank. The

business is small scale and neither Mr. Fernando nor Mr. Silva worried about hiring qualified accountants to manage the accounts and finances of Superclean.

Silva had accumulated a considerable amount of assets in his business, and always had substantial payments due from the bank, against which he had facilities including an overdraft. His ambition was to cater to big institutions like the parliament, airport, embassies, etc. For that purpose he invested more in the business, which created a liquidity problem. Fernando was worried about continuing requests for additional facilities and/or overdue loans and Silva's argument was that there was money overdue from the bank. But he did not have the accounting expertise to prove his claim.

Silva used to send a team to polish the house floors of bank officers, who did him even the slightest favour, at Christmas or at New Year. Such personal favours to the bank officers gradually became as dues and his inability to cope with the requests made by down-the-line staff (in addition to the managers) caused irritation amongst staff circles. The staff made it a point to complain that the Superclean services were not up to standard and branch managers started cutting payments for the slightest lapse or error of Superclean staff. Further, branch managers sought permission from the CEO of the bank to look after their own janitorial needs and started recruiting Superclean employees on a contract basis.

Meanwhile, Mr. Nath, who was in-charge of janitorial services at ABC Ltd., which was an established large company in the same business, approached the Soft Bank through the Personal Assistant (PA) to the CEO. Finally, the PA, who was a classmate of Mr. Nath, became in full charge of the bank's janitorial services and started to divide branch janitorial work between the two contenders, ABC and Superclean. Still, it was expected that Superclean should attend to the opening day's work of new branch openings, which was offered free, and thereafter it was the PA who decided "to give which branch to whom".

6.5.2 Action taken against Silva as a defaulter

Fernando, manager of the Dehiwela Branch, was promoted and transferred to head office and the credit officer of the branch, where Silva had his account, became powerful in the branch. The credit officer, who was not on very good terms with Silva over some misunderstanding, started treating Superclean account in the strictest sense of discipline, ignoring delays in receiving bank's payments thereto and thus depriving him from business expansion. The PA's intervention aggravated the issue. Silva was experiencing a very severe liquidity crunch, lost business gradually because the Soft Bank:

- Did not issue any performance bonds for Superclean to canvass new clients.
- Returned all cheques if without fund and no arrangements made.
- Did not extend advances against payments from the bank and did not allow withdrawals from his account until "overdues" are cleared (despite payments to him from the bank being still overdue for months).

It was later revealed that the branch has over-recovered (charged) interest, substantial enough to recover half the term loan. The Superclean was too small to afford qualified or experienced accountants and totally relied on the bank statements.

Soft Bank classified the Superclean account as non-performing and transferred the file to the recoveries department for closely monitored recovery action, failing which, the Soft Bank could serve a Letter of Demand proceeding towards legal action.

6.5.3 Negotiations at the recoveries department

After careful examination of the account, realizing that the bank had overcharged interest and pushed the client to the present condition, Manager-Recoveries (M-R) comprehended Silva's plight in all aspects, i.e:

- Overcharging of Interest.

- The non-recovery of capital whilst funds actually being available (due from the bank) causing a loss situation to the client.
- The deprivation of business expansion was “criminal” negligence in banking sense.

By this time, Silva had lost all his credibility and business integrity and was unable to pursue tender bids without performance bonds. The only business that Superclean had at this time were a few branches in the conflict areas (the North and East) where ABC was reluctant to serve.

The Manager-Recoveries called for explanations from the new branch-manager of the Dehiwela branch on the overcharged interest. A bank officer said that, “This action probably may not have been taken to take action against the errant staff but may be to build up a case and find an avenue to help the victim of errant action of the bank”.

6.5.4 The first decision

The Manager-Recoveries was a professional experienced banker and was working with Soft Bank from the beginning. He had authority to re-structure loans for the purpose of recovery/settlement and if new facilities were required, he had to recommend them to the CEO for approval. He had no authority to approve new facilities. But realizing the lapse on the bank’s part, and identifying the need of resurrecting Superclean, Manager-Recoveries made the following decisions.

- Set-off of overcharged interest against capital outstanding;
- Re-scheduling the Term Loan; and
- Appropriation of money due from the bank for the services rendered to bank branches.

The Manager-Recoveries, going beyond his authority, further approved the following facilities for reasons unknown:

- Performance bond facility to secure future contracts;
- A small overdraft; and,
- Additional facilities as and when he successfully negotiates business on assignment of payments direct to the bank.

Mr. Silva started building up his business outside the bank and was able to secure a few lucrative contracts in outstations. Some friends helped him because he deserved it but with the blemish created by the bank's unreasonable action, he lost a few good contracts. However, he was gradually coming out of his commitments but was rejected again by a higher officer who strictly followed "banking rules".

6.5.5 The outcome

The Manager-Recoveries lost his job for approving facilities (including Superclean), without authority. The succeeding Chief Manager-Recoveries (CM—R), a retired senior banker assigned on contract for special recovery jobs declined the credit applications of Superclean for new facilities on grounds that Silva should settle a substantial part of the existing commitments for him to recommend a new facility and/or did provide a positive cash flow projection to convince the decision-maker.

Silva is now in a pathetic situation, struggling to save his house which was mortgaged to Soft Bank, and looking for an opportunity to present his case to the Chairperson. However, he did not have the necessary social network to reach the Chairperson as Tony did nor had an appealing project to present at an investor promotion forum as Yousef did. He had a certain amount of wealth, different networks and a customer base although he was not in the affluent class such as Tony or Yousef. He is small and powerless.

CHAPTER SEVEN

7 CASE STUDIES - ANALYSIS

7.1 Background

This chapter analyses the case study stories and present additional empirical data on possible influencing factors on the behaviours of lenders, borrowers and credit mechanisms. These analyses provide the foundation for theoretical discussion of research findings in the next chapter based on Marxian critical interpretations. These analyses are developed around four basic aspects of bank-lending processes described in the case-study stories:

- a) The approach and method used by the borrower for credit applications.
- b) The approach and method used by the lender to accommodate or reject credit applications.
- c) The influencing factors of decision-making.
- d) The decision-making.

This discussion is staged case-by-case for all three cases. A combined analysis is also presented for the first two medium-sized credit applications as they share common features, and therefore, repetitions can be avoided. This analysis provides the necessary foundation for the theorization of the research outcome presented in the next chapter.

7.2 Discussion and analysis of Case Study I

As explained in the data analysis section in the Research Method chapter, the analysis is developed through a series of questions and logical presentation of probable explanations. The common questions are: Why did the borrower approach the Chairperson directly? Why did the bank accommodate the borrower informally? How was the negotiation carried out? And what are the influencing factors and the decision?

7.2.1 Why did Tony approach the Chairperson of the Soft Bank directly?

For credit applications, the usual practice in Sri Lanka is that, if the customer knows an officer in a higher rank, he/she always gets that officer to introduce himself/herself to the credit officer. As discussed in Chapter five in detail, in Sri Lanka, the perception is that, if one doesn't know somebody in the institution concerned, the expected service is either delayed or never made available. On the other hand, Tony was a powerful businessman and it was not that awkward to contact another businessman for a business deal. Tony had the access to the Chairperson of the Soft Bank, because they were in the same social network and had been known to each other for some time. Furthermore, Tony Group had tried the formal path but had been rejected by the credit officers of the Soft Bank. Therefore, Tony had contacted the Chairperson directly for a credit facility, which can be considered as an informal personal approach.

7.2.2 Why did the Soft Bank accommodate Tony informally?

To uncover "Why did the Chairperson decide to lend to the Tony Group", following possible arguments are considered.

- a) Was the decision made because of the prevailing excess liquidity position causing a negative spread to the bank?
- b) Was the decision made for business development purpose because of the misleading influence of Tony and his accountants?
- c) Was it for personal gratification?
- d) Was it on sympathetic/patriotic/nationalistic grounds and/or based on social responsibility?
- e) Was it because of a personal relationship?
- f) Was the decision influenced by the ego of the Chairperson?
- g) Did the organization structure force the chairperson to make such decisions?

These possible arguments are discussed and analyzed in detail below.

7.2.2.1 Was the decision made because of the prevailing excess liquidity position causing a negative spread to the bank?

The bank was desperate to shift their funds from low interest bearing gilt-edged Government Securities to commercial lending for higher return in June 1996. But the bank lost their additional liquidity position later, because of the strategic decision made to cut the interest rates offered for customer deposits. The Soft Bank was comfortably canvassing deposits at lower cost in the level playing field, because the competitors also had reduced the interest rates by September 1996. The Chairperson was fully aware of the situation because, the CFO was reporting the position daily. Therefore the Chairperson's decision to extend the credit facility could not be persuasively related to the excess liquidity position or the prevailing negative return position.

7.2.2.2 Was the decision made for business development purposes because of the misleading picture shown by Tony with his accounting projections?

In previous instances the Chairperson referred such requests to the Management of the Bank for due recommendation after proper credit evaluation.

The Chairperson would have thought of getting all the banking business of Tony by bailing him out in this crucial situation. He would have been carried away by the positive cash flows projected by Tony's accountants; US\$1 million per month which is over and above the required commitment of US\$0.7 million to the banks. The service cost of the Soft Bank credit was around US\$0.07 per month, the annual effective rate of interest (AER) charged from Tony Group was in the range of 17 to 22 percent as they had not been sufficiently backed by collateral. But why he did not do that previous occasions for other applications?

The Chairman was well aware of the already committed liabilities of Tony to other banks. The single-borrower limit would not allow the Soft Bank to acquire the banking business of the Tony Group with other banks by settling Tony's debts to other banks because such an exposure would be too much for a bank like the Soft Bank where the Capital Adequacy was only just at the stipulated level. Capital adequacy of a bank is calculated by weighing the assets

(including loans) according to the risk of realization at a point of bankruptcy. Loans are weighed according to their collateral. The Basel Agreement, which was reached by the leading banks in the world in Basel, Switzerland, is to weigh the loans, backed by commercial properties by 50 percent assuming that they are at risk of price fluctuations. The Chairperson was of the view that developing countries never experience downward price fluctuations for properties. However, the volume of business that the Tony Group had offered to the Soft Bank was significant.

7.2.2.3 Was it for personal gratification?

The Chairperson refused the Mercedes Benz car offered by Tony. He had the control of over US\$2 billion assets. The Chairperson rejected the offer of being the Chairperson of the Tony Group as well. Therefore, this decision could not be treated as one that was influenced by immediate personal gratification.

7.2.2.4 Was the decision made on sympathetic/patriotic/nationalistic grounds and/or based on social responsibility?

The Chairperson might have been sympathetic to the workforce of 30,000 of the Tony Group, and especially with the remarks made by the priests that “..the God has saved you to serve the people”. There was not sufficient evidence to conclude that he made this decision purely on sympathetic grounds. Then, his move might have been influenced by patriotic attitudes, if we recall his criticism, quoted in the previous chapter, on banking practices and government policies towards SME development in Sri Lanka:

...this is the whole problem with our bankers. They are guided by some stupid rules called banking practices and ruin people like you. They will never think beyond that cage of banking practices. Even our state policies do not have a proper system to support people like you. Now, you have generated 30,000 jobs. If they lost their jobs and you lose your business, the cost will be worth much more to the economy in the long run... ...I don't know, when these people will learn these things?

On the other hand, the Chairperson, being the head of more than 100 companies, was fully aware of the grievances of the 9,000 small individual shareholders and 1.5 million deposit customers. But one of the colleagues argued saying that, “The fate of the 30,000 employees of the Tony Group was critical and warranted an immediate remedy, therefore, the Chairperson may have acted rationally to address first things first”. However, this argument looks like eyewash to the public because the Chairman’s justification to the board of directors of the Soft Bank for accommodating The Tony Group was “bringing more business to the Soft Bank”. Therefore, this patriotic or social responsibility claim cannot be justified in a business sense. Also, accommodating a client who had been blacklisted in CIB is a clear indication of disregarding state intervention to protect public deposits from potential risk of default. Also it is an act of working in the opposite direction to maximizing shareholders’ wealth which is the primary goal of a firm. On the other hand one could argue this act was a socially irresponsible decision with regard to public depositors, unethical in the interest of minority shareholders and totally unprofessional.

7.2.2.5 Was the decision made due to a personal relationship?

The Chairperson had great respect for Tony who is a successful premier businessperson in the country. On the other hand, most of the people who approached the Chairperson were privileged to obtain a favorable decision from him. Most cases so referred were defaulters to other banks and the Chairperson used to accommodate them with generous concessions. However, The Chairperson was very lenient in applying due diligence and acted significantly on “trust” and “gut-feeling”. Therefore, this decision can be interpreted as an extending of a “favour” and getting another fellow capitalist, who is also a powerful individual (as an award-winning leading foreign exchange earner in Sri Lanka), hooked into his social network.

7.2.2.6 Was the decision influenced by motives such as ego or prestige of the Chairperson?

This could be a contributory factor since he had achieved the highest level of social status. The Chairperson was very keen on making popular decisions, followed by a good propaganda campaign. The Chairperson asked for publicity, which he got promptly from Tony.

Though the Chairperson's name Mr. Perera was a household name, he was known as only a businessperson. With the narrow escape from the bomb, now he may have thought of developing his image as a patriotic businessperson and win the hearts of the people in the latter stage of his life. He did not have any child to hand over his business and always used to say that his employees are his children. He started his own newspaper and a one-hour TV programme which showed negotiations with the clients/customers of his group. That propaganda was to convince the public that this was how generous he was in helping small entrepreneurs in Sri Lanka. All the clients who participated in that TV programme praised the Chairperson for the generous support he extended to their business, especially during the hard times.

The Chairperson was convinced that he could boost his image as a patriotic businessperson with the publicity promised. Therefore, it is more realistic to assert that he would have made this decision to fulfill his egoistic motives under the pretence of patriotism or social responsibility.

7.2.2.7 Did the organization structure force the Chairperson to make this decision?

The organizational structure was very conducive for him to make such decisions. It is evident that he had legitimate authority under a poor management support and weak organization structure. Also, he had no faith on the formal credit approval and monitoring systems. He always criticized the formal systems. He had very little confidence in the credit officers of the bank and appointed CFO, who was a non-banker, to monitor the Tony Group account. However, it was not expected of him to make such decisions at the

highest level of authority and it was not the practice of the banking industry. Therefore, it is also believable that the organization structure was conducive to making such decisions especially as the decision-maker was vested with enormous power.

7.2.3 What were the influencing factors?

What could be inferred from the above analysis is that the arbitrary/informal decision was made under the enormous power entrusted to the Chairperson in a weak organizational structure with a poor management support. The decisions may have been influenced by patriotic attitudes and egoistic motives especially when the decision-maker is from the top slot of the bank. However, further analysis is necessary to discover the roots for such attitudes and/or to find more convincing reasons. This issue is further discussed in the next chapter: Theoretical Discussion.

7.2.4 How was the decision made?

Tony was very impressive and convincing on his marketing capabilities and “filling the factories with orders” for uninterrupted production if materials are supplied. The Chairperson made a quick assessment of Tony’s integrity and the risk and return of the credit involved based on the cash flows presented by the team of accountants, including chartered accountants. He did not want to consult credit experts in the bank, as he had no faith or confidence in any of them. He had the power and he was confident that the Board would not decline what he recommended. Therefore, he approved this incomplete credit application and granted US\$4 million over the table. Table 7-1 below provides the summary of this case study.

Table 7-1: Summary of the description and analysis of Case Study I

ITEM	Credit Applicant: Tony—Tony Group	Credit Decision-Maker: Chairperson Mr. Perera
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Background	Tony is in the garment manufacturing business. He accounted for the largest single share of country's exports and 30,000 workers. Tony's credit application had been rejected by the credit officer of the Soft Bank based on an official credit-default investigation report. He had won several awards for his contribution to the country.	Mr. Perera became the all-powerful chairperson of the Soft Bank with his loyalists as board members and weak Management. The Chairperson was in a business development drive as he had no faith in the bank's Management especially the credit officers. This powerful businessperson had become a fame seeker after a "near death" experience.
Approach	Tony and Mr. Perera knew each other as leading businesspersons in Sri Lanka. Tony's request for an appointment with Mr. Perera was accommodated promptly even though the Chairperson was at a meeting at that time. The approach was casual and formal rules were bypassed.	
Influencing factors	The business that Tony brought was lucrative and significant. The credit decision was justified by the positive cash and profit forecast by professional accountants. The Chairperson was not aiming at any personal gratification but showed some "patriotic" feelings and "sympathy" over the workforce who were without wages facing redundancy because of the foreclosure of factories called by the other banks to recover their debts. The state policies on such issues were not helpful to borrowers or to lenders. The Chairperson had an egoistic motive to boost his image and wanted to strengthen his social power base by getting another powerful businessperson tactfully hooked into his social network. Tony promised the publicity warranted by this ego-maniac Chairperson.	
Decision-making	Tony was very impressive. The Chairperson got a quick assessment of Tony's integrity and the risk and return of the credit involved. The Chairperson had the power and he was confident that the Board would not decline what he recommended. Therefore, he instantly granted US\$4 million. This casual decision was made under the enormous power entrusted to the Chairperson in a weak organizational structure with a poor management support. The decisions were defended under the façade of "patriotic" attitudes and influenced by egoistic motives especially when the decision-maker is from the top echelon of the bank and more importantly backed by projected cash flows presented by accountants.	
Post-decision events	Tony's accountant complained about not bringing all the sale proceeds to Sri Lanka. This situation had caused liquidity problems therefore, Tony frequently demanded enhancement of credit. The workforce had been reduced to 15,000 and monthly sales had reduced by 25% and were making a negative contribution by 2003.	Further credits were granted but later the loan was classified as bad and provisions were made to comply with the prudence principle of accounting and regulatory requirements. The interest loss was around US\$0.3 million and the capital loss too was significant.

7.3 Discussion of Case Study II

Similar to Case I, this discussion too developed through a series of questions and logical presentation of probable explanations. The common questions are: Why did the borrower approach the Chairperson directly? Why did the bank accommodate the borrower informally? How was the negotiation carried out? And what are the influencing factors and the decision?

7.3.1 Why did Yousef approach the Chairperson of the Soft Bank directly?

Mr. Yousef, unlike Tony, contacted Mr. Perera not as the Chairperson of the Soft Bank or as a known personality but as a business promoter authorized by the government. They had seen on TV programmes how Mr. Perera, who was also the Chairperson of the Soft Bank, provided solace to those in financial difficulties. They were desperately exploring possibilities for launching their products: Lan-Car and Lak-Van. They had tried one of the Government Ministers as well, the usual way that Sri Lankans were used to getting things done, but without success. The Management of Lan-Car Ltd. was aware of the way that the Chairperson made decisions at the investment forum headed by the Chairperson. The patriotic speeches by the Chairperson, encouraging domestic investments, would have created an optimistic perception in the minds of the local car manufacturers. But for the greater part, it was their desperation that brought them all the way to the Western Province business development forum from their own Central Province.

7.3.2 Why did the Soft Bank accommodate Lan-Car Ltd. informally?

When this question was posed, a colleague said that, “He [the Chairperson] wished that his bank should support the majority who were left out by those formal banking practices.” To prove his [the Chairperson’s] point he used to quote from his personal experiences where his diamond project was declined by the banks, on the basis of those formal banking practices, but he had taken that diamond project to its maximum heights by generating 500 employment opportunities and declaring huge dividends to the shareholders, continuously.

Therefore, it is evident that he had no faith in the formal credit evaluation systems of the banks, especially with regard to new ventures.

The Chairperson was also critical of some of the regulations, especially the way they were interpreted by the Department of Bank Supervision of the Central Bank of Sri Lanka. He was critical of the Capital Adequacy ratio, which was an outcome of the Basel Agreement, saying that the concept of “Capital Adequacy” was irrelevant for developing countries like Sri Lanka. He was critical of the conditions imposed by the World Bank and the IMF towards developing countries, and basically he wanted to show that his bank was different and he would go out of his way to help Sri Lankan entrepreneurs.

The following question was posed to a research participant who accompanied the Chairperson to the investors’ forum, in order to ascertain the perception of the officers behind him. “Why did the Chairperson accommodate Mr. Yousef and Lan-Car without following formal banking practices?” The officer said, “It was not that the Chairperson totally disregards caution, reason, peril; nor that he was acting on his dreams and fantasies, and made these unsystematic decisions. In fact, he added value to the abandoned factory premises and took the total picture into account, to approve the loan. It was informal, because normal systematic banking could not accommodate this loan.” Responding to the same question, he further added, “Though the decision was informal, it was a deserving case, not only to an emerging national venture but also to a prospective client to the bank.”

The bank officer, who was working closely with the Chairperson argued by cross-questioning, “was it fair to penalize a prospective business venture because of the prevailing systems which are not advanced enough to cater for new concepts?” He also said “Let us accommodate them till the relevant authorities develop necessary systems to cater for them and allow the “James Watts” in Sri Lanka to advance our lives and theirs.” On the other hand the Chairperson justified import protection saying that dumping used vehicles would drain away the foreign exchange from Sri Lanka. A colleague of the

researcher responded to this claim saying that “How can a small country like Sri Lanka manufacture automobiles?” He further said that “Even New Zealand tried such ventures such as automobiles and electronics like TVs etc., but failed.”

7.3.3 The influencing factors

The Chairperson had taken over a significant part of the business development function of the Bank, with his new appointment as the President of WEDA which was one of the business development agents of the government. On the other hand, the government and the public are watching how Mr. Perera performs as the President of WEDA.

Therefore, it is sensible to deduce that the Chairperson accommodated Yousef because he had the power to disregard prevailing systems; wanted to show his performance using nationalism/patriotism as a smokescreen supported by rosy financials prepared by accountants. Table 7-2 below provides the summary of this case study.

Table 7-2: Summary of the description and analysis of Case Study II

ITEM	Credit Applicant: Yousef—Lan-Car Ltd.	Credit Decision-Maker: Chairperson Mr. Perera
Back-ground	Yousef was in the automobile manufacturing business. His automobiles were made with fibreglass bodies and imported engines and parts. He had produced a few sample vehicles—a car and a van and was desperate for financial assistance. The barriers include the prevailing state policies on credit, Customs red-tape and vehicle registration regulations.	Mr. Perera was appointed as the President of Western Economic Development Authority (WEDA) by the government. He inaugurated the new task with a “big-show” and all of his “quick” decisions were given wide media coverage and the cost was born by his companies including the Soft Bank. He was the all-powerful chairperson with all the board members with “Yes, Sir” attitudes and weak Management.

Approach The wide publicity enjoyed by Mr. Perera as the President of WEDA attracted Yousef to one of his weekly investment promotion forums. Yousef came up with his new car and was able to convince the Chairperson that he could facilitate an “import substitution” to the automobile market in Sri Lanka and said, “We will save Foreign Exchange for our country.” Mr. Perera criticized the automobile market for using Sri Lanka as a dumping yard and immediately decided to help Yousef, again under the label of “nationalism” promoting domestic investments as against FDIs.

Influencing factors Lan-Car Ltd. was very appealing as a venture of import substitution. Mr. Perera had no faith in the formal credit evaluation systems especially for new ventures. According to Yousef, he could not cater to the demand for his vehicles due to capacity limitations. The Chairperson had become front runner of marketing credit in his bank and, on the other hand, the government and the public were watching how Mr. Perera performed as the President of WEDA. The Chairperson had the power to disregard prevailing systems, wanted to show his colours in investment promotion and affection to “nationalism/patriotism”. The Chairperson had an egoistic motive to show that he is different (disregard the IMF, the World Bank, the Basel banking standards or regulatory issues) and he was well convinced by the cash flow projections certified by accountants.

Decision-making The Chairperson had the power and he was confident that the Board of Directors of the Bank is always behind him. Therefore, he instantly granted US\$0.5 million. The Chairperson also promised market support. This casual decision was made under the enormous power entrusted to the Chairperson in a weak organizational structure and weak management. The decisions were defended using the mask of “nationalism”, influenced by egoistic motives and, justified by very positive cash flow projections certified by professional accountants.

Post-decision events Lan-Car could not perform as projected. Customs delays and registration problems frustrated Yousef. The project resources finally converted for assembling of vehicles which had very low contribution margin and still struggled to achieve the break-even point. The Chairperson had to interfere personally to get the automobile approved using his power. Further credits of US\$0.7 million were granted and the loan was in the performing category because interest was serviced by further loans by 2004.

7.4 Combined conclusions for Cases I and II

In the final analysis, it can be concluded that no bank would consider Lan-Car Ltd. as a prospective client purely because of the product that cannot be marketed (Lan-car could not be registered) in Sri Lanka. With regard to Case I, the Tony Group had no alternative other than approaching the Soft Bank, since

the banking sector was well aware of its default situation and listing in the CRIB.

On the other hand, in Sri Lankan culture people believe that an informal approach is an easy way out to get things done quickly. The perception of the general public is that, one must know someone in the institution concerned to receive a positive response. This problem is severe with regard to the public service where customer service is not considered to be an important element. Even though some of the banks are private, the belief is such that to get a credit facility, one must know someone.

It is very common that customers who enjoy credit facilities always deliver bulky hampers to the officers/branch managers of the banks in festival seasons. One senior officer of a bank revealed that he got a refrigerator full of food and beverages as a New Year hamper. Lunches are frequently organized, either by the customers or by the bank officers. Issuing letters by members of the parliament, requesting senior officers of various institutions to accommodate their supporters is very common in Sri Lanka.

Therefore, these decisions could be related to the enormous power enjoyed by the Chairperson within a weak organizational structure, enthused by egoistic or any other motive and appealing cash flow projections by accountants. This claim is further discussed in the next chapter which theorizes the research findings.

7.5 Discussion and analysis: Case III

The discussion and analysis of this case is developed in a similar manner as the previous two cases but poses different questions according to the circumstances. Initially a banker (Manager–Dehiwela Branch, Mr. Fernando) was instrumental in building up Superclean. Then a few other bankers tried to bring him down as they had personal grudges. Again another middle-level officer informally helped Superclean to rebuild, ultimately another upper-middle level manager

decided to recover the money due to the bank, and declined new facilities, pushing Mr. Silva to a desperate situation.

“Why do so many contradictory views and judgments exist within the formal banking systems?”

The research participant, who was well aware of this case, answered in an appealing tone saying, “Study of an enterprising person, taking a calculated risk in deciding to finance the young entrepreneur, who, of course, was providing a service to his bank was all to the credit of the banker [Manager–Dehiwela Branch] who had been looking to support entrepreneurs. It is a lack of exposure and dispositions with conventional-type attitudes of the officers that make such a big difference among their views and judgments. It would be an uphill task to identify true entrepreneurial skills.”

He further said, “When there is a new entrepreneur, it is important to be close to him, correct him and back him as necessary such as the support Mr. Silva received from the first Manager–Dehiwela Branch and the Manager–Recoveries.”

Mr. Silva had following complaints against the bank:

- Misuse of his free service for opening ceremonies of new branches but not rewarded with contracts for continuous service.
- Deprivation of business expansion by not extending required facilities.
- Interest overcharged.
- Dishonouring cheques, at the same time as the bank is defaulting payments to him, damaging his image.
- Robbing of his workers which also deprived him of the ability to fulfill his contractual performance.
- Cutting payments by exaggerating lapses and errors of Superclean staff.

Explaining the situation, the bank officer said, “The overcharging of interest from Superclean shows not only how shortfalls in simple checks and balances were overlooked, but also how much personal animosity against a client on narrow personal issues, could kill simple obligations in banking.” To the contrary, according to this bank officer, Mr. Silva showed gratitude to the Manager-Recoveries who had re-adopted a comprehensive customer-rehabilitating approach even going beyond his authority and succeeding in reaping results for his ingenuity and customer care.

7.5.1 How and why did Manager-Recoveries approve facilities informally?

The performance of Manager-Recoveries was measured by the amount of recoveries he made and the extent of reduction he achieved in the non-performing loans under his purview as against the targets set. The measuring system was such that the comparing was not carried out taking each and every client/account, but taking the net outstanding in bad loans (Brought Forward Balance less Recoveries less Restructured and Transferred to the branch). New bad loans transferred from branches to the recoveries department were shown separately. This formula encourages re-structuring which is somewhat more practical than squeezing the client against the wall.

All the bad loans, which were restructured by the recoveries department, were transferred back to the respective branches for close monitoring and rehabilitation. The Manager-Recoveries had a practice of restructuring and transferring such loans with new facilities beyond his authority so that he could recover part of the interest, which was in the interest in suspense account (capitalizing the interest by adding them to the loan capital). This process showed an extraordinary improvement in the level of non-performing loans under his purview. By doing this he could convince the Management and so managed to secure handsome raises, bonuses and rapid promotions as well. When he was fired he had been promoted twice to the level of Chief Manager.

7.5.2 Why did the credit officer and the Branch Manager carry out instructions of an unauthorized officer?

A bank officer answered to this question saying: “The credit officer might have been under threat of disciplinary action for the negligence/errors he committed in calculating the interest receivable from Silva.” The gravity of the offence depended on the level of severity that the Manager–Recoveries would attach in reporting them to Management. Therefore, the credit officer might have followed instructions of the Manager–Recoveries with the blessing of the Branch Manager, who also benefited with the improved branch performance in terms of lower levels of bad loans and higher interest income.

7.5.3 Why didn’t the new Chief Manager–Recoveries accommodate Superclean?

Chief Manager–Recoveries was a senior banker recruited on a contract basis and was following orthodox banking practices to the letter. He discovered that Superclean was not accommodated under the normal banking rules and reported that the practices followed in the recoveries department were not regular. Also Silva did not have qualified accountants to provide “convincing” financial projections about his business prospects. He was new to the bank and maybe he was trying to impress the CEO with some “good” work.

7.5.4 Why did the Soft Bank accommodate a new service provider?

What would be the reasons to obtain the services of another service provider especially when the bank was happy with the services of Superclean? The Personal Assistant to the CEO would have extended favours to his classmate and would have been influenced by potential personal gratifications as well. On the other hand it is also sensible to argue that the Management of the Soft Bank would have made some strategic move to obtain the services of a competitor for better services from both parties and avoid any over-dependence on a single service provider. Therefore, it is evident that the credit decisions have mostly been made on other grounds rather than the potential, skills and capabilities of the applicant.

7.5.5 How was the decision made?

The Manager–Recoveries abused his authority and just made decisions because the staff down the line (Branch Manager and the credit officer at the branch) who carry out the orders were under obligation (or threat) because of their mistakes and negligence. The Manager–Recoveries was further encouraged because the senior management ratified those decisions indirectly by recognizing and appreciating his work through rewards and promotions. Therefore, the Manager–Recoveries restructured this loan too by himself and implemented it without due approval. Finally he lost his job because of such decisions. The Chief Manager–Recoveries, on the other hand, followed the rules and denied credit with proper approvals.

It is noteworthy that the research participants agreed with the researcher that, if Mr. Silva was powerful or had come from the same social network, the Manager–Recoveries would have got another reward instead of losing his job. They said, “It is not rare that directions coming from the top to treat customers differently, when they were denied and had the power of reaching the top to complain about that”. The grapevine works this way but no one dares to speak being scared of being exposed and reported. Table 7-3 below provides a summary of this case study.

Table 7-3: Summary of the description and analysis of Case Study III

ITEM	Credit Applicant:	Credit Decision-Maker:
	Silva—Superclean Ltd	Recoveries Department
Back-ground	The threats to Silva’s janitorial business include: the new entrant who was a friend of the then top Management, harassment by the credit officer due to a personal grudge. Silva lost business to the newcomer and was facing liquidity problems and financial barriers for business development and got into the bad books as his loans were not serviced.	Fernando, the branch manager who nurtured Silva and his business Superclean, was promoted and transferred (Decision 1). The Superclean account was classified as non-performing and transferred to the recoveries department. First it was positively handled by the M–R and then negatively by the Chief M–R.

Approach **Decision 1.** Under normal banking practices

Decision 2. M–R comprehended Silva’s plight by extending several bank facilities outside the normal credit rules. M–R discovered some errors of the branch staff and blamed them but did not report to the Management rather used it to intimidate the branch staff. Silva was happy with M–R and had praised him with research participants.

Decision 3. CM–R applied the set credit rules strictly and stopped all the facilities extended by M–R and requested Silva to settle existing outstanding immediately for him to consider further facilities.

Silva searched for avenues to approach the Chairperson as advised by people who are aware of the Chairperson’s approach and, as Mr. Perera was boasting of helping small businesspeople via his TV shows, but without success because he was not influential and not in as powerful circle as Tony or did not have such an appealing project as Yousef had.

Influencing factors **Decision 1.** Under normal banking practices

Decision 2. M–R’s performance was measured by the reduction shown in the bad loans handled by him. He could transfer restructured bad loans back to branches as performing loans and that process enhanced M–R’s performance for which he was rewarded. But M–R did not have the necessary authority to approve such new credit facilities. Even the staff at the branch at the mercy of M–R due to their blunder committed for interest calculation had no alternative but to carry out M–R’s unauthorized orders.

Decision 3. CM–R was an orthodox banker and he strictly applied the rules and tried to impress the Management about his “good work”. Silva could not afford get the services of professional accountants to project his prospects convincingly.

Decision-making **Decision 1.** Under normal banking practices

Decision 2. M–R abused his authority and was at an advantage that the branch staff was under obligation. M–R was promoted and encouraged by the Management for his performance though the decisions were not duly approved.

Decision 3. CM–R followed normal banking practices, did not believe Silva’s appeal about his business prospects and declined further credits. He was contemplating serving a letter of demand threatening legal action against Silva and his house which was mortgaged to the Bank.

Post-decision events Research participants were of the view that if Silva had enough power or adequate influence to reach the Chairperson with the backing of accounting expertise, he could have got the necessary facilities and M–R would have got another promotion instead of losing his job. Unfortunately Silva was not from that class and social network and could not afford professional or experienced accountants.

7.6 Latest developments

In December 2008, Mr. Perera (the Chairperson) had been questioned by the Criminal Investigation Department (CID) of Sri Lanka and they filed a case against him and other directors for an alleged scam of US\$250 million which happened in one of his group companies which had accepted money-deposits without a Finance Licence. The Soft Bank nearly crashed following a “run” due to loss of confidence (in the group) but the Central Bank of Sri Lanka (CBSL) intervened and saved it by giving an “assurance”, yet depositors are not allowed to withdraw money prematurely.

The Board of Directors of the Soft Bank, including the Chairperson, was dissolved by the CBSL. The management has been handed over to the Bank of Sri Lanka, the largest State bank in Sri Lanka and a new Chairman and three directors have been appointed by the CBSL.

Repeated requests from the solicitors of the Chairperson to bail him out were rejected by the Colombo High Court and the Chairperson and other directors were further remanded in March 2009. The CID has sought assistance of the Interpol to arrest Dora—the wife of the Chairperson who has been avoiding the courts forwarding medicals from overseas. The magistrate blamed the police for not acting promptly and allowing her to leave the country.

7.7 Summary of the analysis of case studies

The nature of the credit applications, approach, issues, negotiation process and decision-making processes of all three case studies are summarized in Table 7-4 below. The explanations/justifications section of this table provides the necessary background for the theoretical interpretations discussed in the next chapter.

4: Summary of the analysis of case studies data

	<i>Case Study I</i>	<i>Case Study II</i>	<i>Case Study III</i>
	Medium-scale credit for a garment manufacturing company struggling with lack of orders and liquidity problems.	Medium-scale credit for a car manufacturing company in Sri Lanka, struggling with regulatory authorities and financing problems.	Small-scale credit, an upcoming service enterprise struggling with business and with financing problems.
h	Casual, informal and personal. Both the credit decision-maker and the client are socially powerful businesspersons.	Social, outside the bank at an investment forum, both the credit decision-maker and the client are socially powerful. Informal credit application and accommodation.	Formal, within the normal banking and credit rules. Then followed methods by the credit decision-maker.
	Client was under threat of foreclosure and redundancy. The client was the highest single foreign exchange earner in Sri Lanka.	Import protection? Protect foreign reserves. These automobiles were refused registration on road worthiness and safety issues. Investment promotion mechanism.	A big competitor penetrating into the Soured relationship between bank of the client. Businessman without social network.
ion	Friendly. Accountants helped. Quick.	Enterprise promotion oriented. Accountants helped. Quick.	Formal. No qualified accountants. Dragged.
	Without formal evaluation. Granted, over the table.	Without formal evaluation. Granted, over the table.	Decision one: Formal. Granted Decision two: Informal. Granted three: Formal. Denied.
tion/ tion	Sympathetic/patriotic grounds. Prevailing systems are not good.	Patriotic/nationalistic grounds. Prevailing systems are not good.	Decision one: Normal practice. De Personal benefits, error rectifying three: Rigid application of rules.

CHAPTER EIGHT

8 THEORETICAL DISCUSSION

8.1 Introduction

This chapter further discusses the case study research data described, discussed and analyzed in the previous two chapters from theoretical perspectives. Theorization (or conceptual framing) is the “value-added” of qualitative academic research (Llewellyn, 2003) and, according to Coffey and Atkinson, “theorizing is integral to analysis; they are not separate stages in the research process” (1996, p. 139). The findings of this research are theorized in three steams. First, interpretation of various types of credit decisions observed in the case studies and framing them conceptually into a matrix. Then an attempt to strengthen the Marxian critique that accounting plays a significant role as a technology in credit mechanisms and exploitation mechanisms. Finally, there is an argument to establish a relationship between bank lending, the socio-economic power of credit decision-makers and income/wealth inequality in the Sri Lankan society. A common theoretical analysis was carried out for Cases I and II, because of the similarity of their backgrounds, identical pattern of decision-making processes and types of decisions to avoid repetition, and for a cogent argument for theorization. Final conclusions were drawn from the interpretations of all three cases.

As explained in Chapter four; Research Methods, much interpretation are primarily based on inductive generalization where the researcher provides empirical evidence to prove “*how*” it happened and “*why*”. However, some interpretations are drawn based on abductive inferencing/reasoning where the researcher argues that “*something might be the reason*” especially for “*why*” questions. Therefore, interpretations are generally subjective and they are presented by analyzing the research data with the support of Marxian critical themes and other reliability and validation checks. Most of the “*how*” questions,

for example “*How can influential credit applicants get easy access to top level credit decision-makers?*” were interpreted with straight explanations such as: “*...these lenders and borrowers are friends and/or in the same social network...*”.

This chapter consists of five sections. First, it attempts to analyze the various decision-making personalities observed in the case study stories. Second, it argues to strengthen the Marxian critical claim on the importance of the role of accounting in credit mechanisms and exploitation mechanisms using the empirical evidence provided by the case studies. The third section answers the research questions by providing empirical and theoretical evidence and further develops them into a macro-level theorization of the research findings. Fourthly, it provides a model for informal decision-making to summarize the factors discussed in the previous two sections. Finally, it further investigates theoretically to find the motives behind the decision-makers’ decisions (why) and what methods they used (how).

8.2 Nature of decision-making

It is revealed that there are four basic types of decisions that have been made by the credit decision-makers in these case studies according to the situation. It is observed that some credit decisions are made following formal rules and some are not. On the other hand, some credit decisions seem logical but some do not exhibit any business sense but rather appear to be ridiculous. The nature of decision-making is analyzed below.

8.2.1 The Chairperson: Case studies I and II

The Chairperson is an undisputed leader of 100-plus companies including seven listed companies in the Colombo Stock Market. He is a socially and economically powerful individual. He is also influential because of his position as the President of a Government authority, WEDA. He is closely associated with the government and political elites. It is argued that businesspersons in the long run, to maintain their position of power, may accept certain responsibility

to the whole of society (Davis, 1967). One of the researcher's colleagues argues that the Chairperson's decisions in Cases I and II are rational because they were intended to rescue 30,000 workers of the Tony Group and save foreign currency by promoting an import substitution project, Lan-Car Ltd. He interprets this as a reflection of the Chairperson's perceived responsibility to the whole society. On the other hand, it is argued that the social power holder might show his willingness and ability to help others to feel powerful might not bother about formalities in decision-making (Peay & Dyer Jr, 1989). However, this "*willingness to help others*" is only a mere intention and does not make any business sense therefore cannot be treated as rational.

Further, when this proposition was posed to a research participant regarding the Chairperson's credit decisions in Cases I and II, he argued, "Although the Chairperson's credit decision in the case of the Tony Group created a loss to the Soft Bank after three–four years it was a relief to the workforce of nearly 20,000 of the Tony Group to have adequate time to find alternative occupations..." and, he said "...but the decision to help Lan-Car was a winner and Lan-Car is marching forward because of the Chairperson, giving an expected return to the bank as well." But his views on Lan-Car Ltd. were proved incorrect as the CEO of Lan-Car is still struggling to manufacture the number of cars he promised and had still not reached the break-even point even in 2005. It was also revealed that even Tony had closed a few factories and the workforce was reduced to 15,000 by 2005.

The two medium-sized credit applications; Tony Group and Lan-Car Ltd., would not have been accommodated if a solid organizational structure (formal) and professional management culture (rational) were in place in the Soft Bank. The Bank was run as an autocracy. The Chairperson was all-powerful and no Board member or officer had the courage to oppose the decisions of the Chairperson. But the bureaucracy was also challenged by the Chairperson overruling the decisions of the credit officers of the Soft Bank in the case of the Tony Group. Therefore, those clients who could approach him could bypass the normal lending procedures that were rigid and not conducive for the new

concepts to grow. Although the theory of autocracy explains “*how*” the decision was made it is not helpful in explaining “*why*” the Chairperson made decisions which are not rational in a business sense. The concept of bureaucracy does not support the motives of the decision-maker but it is helpful to explain why the borrowers tend to resort to informal methods when they seek credit from banks. Therefore, the question “*why*” remains still unanswered.

However, another colleague points out the extent of publicity the Chairperson was aiming at and argued that ego-boosting also would have had significant influence over Mr. Perera, the Chairperson, to make such irrational decisions. To the extent that the decisions are informal, radical and irrational they attract more publicity. The Chairperson, as an esteemed individual, was leading his group of companies, to which the Soft Bank belongs, towards the largest group of companies in Sri Lanka. Therefore, it could be argued that the Chairperson would have been influenced by such attitudes but the motives are not clear and decisions seem not rational.

8.2.2 Branch manager (BM): Case III

The concepts such as ego, self esteem, social power or even social responsibility have little relevance in Case III since the decision-makers and credit applicant involved were not socially powerful individuals or from a social network with powerful backgrounds. They were in the middle management of the Bank. Mr. Silva of Superclean believed that his major client (the Soft Bank) was doing a favour to him and used to reward the bank officers informally as Sri Lankans normally do. In the South-eastern culture traditional gifts differ from corruption (Alatas, 1986 cited in Jayawickrama, 2001) and Mr. Silva’s free services at Christmas and New Year time were treated as gifts.

Branch Manager (BM) Mr. Fernando was instrumental in building up Superclean. Fernando, the branch manager who nurtured Silva and his business Superclean, was promoted and transferred to head office. The formal rational banking practice is studying on enterprising person, taking a calculated risk and deciding on the nature and amount of credit entrepreneurs who in turn bring

business to the bank. In this sense BM Mr. Fernando has managed Silva's account as a true banker.

8.2.2.1 Manager-recoveries (M-R): Case III

Mr. Silva pays gratitude to the Manager-Recoveries (M-R) who had re-adopted a comprehensive customer-rehabilitating approach even going beyond his authority (informal) and reaping the results of his ingenuity and customer care (rational). The M-R had a practice of re-structuring and transferring such loans with new facilities beyond his authority to show very impressive performance and managed to secure raises and rapid promotions as well. Though the credit decisions made by the M-R in favour of Silva seem rational according to the research participants the decisions were made informally without proper authority. There was no substantial evidence available for major personal gratifications offered by Mr. Silva to M-R. The most probable reason for the informal decisions by the M-R could be that the intention of impressing the management on his performance for rewards. This shows a kind of "petty corruption" that prevails in the system and whenever the opportunities arise, bank officers and the customers are very well prepared to resort to informal methods.

8.2.3 The Credit Officer (CO) and the CM-R: Case III

The Credit Officer (CO), who was in charge of Silva's account after Fernando's transfer, had a personal grudge with Silva and acted irrationally (overcharging interest and delaying payments, etc.). He pretended that he was applying formal banking rules and declined credit to Silva while harassing him for "irregularities".

Chief Manager-Recoveries (CM-R) was a senior banker and he too seems to be following banking practices to the letter. He quickly discovered that former officer had accommodated Silva without proper authority. He was yet to impress the Management on his skills and performance. CM-R did not believe Silva's appeal about his business prospects, maybe due to adverse comments by

the CO of the branch, and declined further credits. Also Silva did not have qualified accountants to provide “convincing” financial projections about his business prospects. CM–R was contemplating to serve a letter of demand threatening legal action against Silva and his house which was mortgaged to the Bank. The Management agreed with CM–R’s recommendations and Silva was helpless.

8.2.4 Credit-decision classification

It is manifested that there is diversity in decision-making in the Soft Bank and this might be common in Sri Lanka as a cultural phenomenon. These decisions on credit mechanisms depend basically on the authority entrusted to the decision-maker, the ability and the willingness in breaking or following rules of credit policy. These decisions can be classified meaningfully using two variables namely method used (formal or informal) and manifested sense (rational and irrational). Therefore, four decision types are identified: Formal–irrational (the type followed by CO and CM–R); Informal–rational (the type followed by M–R); Formal–rational (the type followed by B–M) and Informal–irrational (the type followed by the Chairperson). CO and CM–R strictly followed rules therefore, formalities were adhered to but did not care about the consequences are therefore, looked irrational. M–R made decisions which were beneficial to both the decision-maker and the credit applicant, therefore they looked rational but he had to follow informal methods since formal rules prevent making such decisions. B–M managed within the formal system to support credit applicants as well as develop business therefore, those credit decisions looked rational. The Chairperson made informal decisions because he was powerful with legitimate authority to break the rules but he provided “solace” to the “needy”, to people who were “close” to him and therefore, looked irrational in the business sense. These decision-makers are summarized in Table 8-1 below with characteristics and attributes discussed.

Table 8-1: Matrix of Credit Decision-Making

<i>Variable</i>	<i>Manifested sense</i>	
	Rational	Irrational
<i>Method used</i>	Formal	CO/CM-R
	Informal	The Chairperson

Source: Compiled by the author

8.2.5 Rule-breakers are treated differently based on their access to power

This type of informal decision-making was possible because of a lack of strict application of set systems and procedures within the bank. Although banks have very well written policy and procedure manuals for most of the processes especially in outlining the delegated authority levels, the Soft Bank culture was influenced by the informal methods used by the Management and it was known that rule-breakers were not punished properly due to favoritisms. Mere documentation of guidelines to follow the set of rules will not serve the actual purpose of setting up systems. The people involved in the systems should make sure that delivery of quality output is what is most important to achieve the corporate goal of the organization.

This was clearly evident in Case III as the research participants were of the view that M-R would not have been punished if he and/or the client were from a powerful social class. On the other hand, when the formal credit evaluation procedures applied, Silva's credit application was rejected; because there was no backing from the client to influence the higher authority in the bank, because he is not a privileged powerful individual, and because his financial projections were not vetted by accountants. This phenomenon is further discussed below using Marxian critical lenses.

8.3 Role of accounting as a Marxian general-intellect

The accounting system is capable of recording the “affairs of the most unscrupulous money-lender or crooked businessman” (Yamey, 2005, p. 81). Hooper and Kearins (2008) stress the importance of the role of accounting as a key technology in facilitating the exploitation mechanism. They point out that accounting is a means of serving the owners of capital in accumulating wealth. Both credit decisions in Cases I and II provide evidence to show exploitative use of deposit funds in the Soft Bank based on accounting projections without following proper banking procedures. The borrowers used cash flow projections to prove their business prospects; on the other hand the Chairperson used those cash budgets to convince the board of directors to ratify his casual decisions. The role played by accounting in these two cases helped the borrowers to exploit credit facilities for non-feasible projects while helping the Chairperson to boost his image. Hence, this research strengthens the Marxian critical claim that, the accounting function plays a significant role in the concentration of wealth through the exploitation and credit mechanisms. This process in turn results in sustaining or even increasing the gap in wealth between those who are powerful/influential and those who are powerless.

The relationship between accounting and exploitation go beyond the technical level of facilitating to justify the exploitation mechanism hence the owners of capital are protected (Chiapello, 2007). The claim: “even when badly kept and useless as a decision aid, accounting contributes to the legitimacy of practices originally considered illegitimate” (2007, p. 264) is well endorsed by the Chairperson’s behaviour in Cases II and III where he got his illegitimate decision converted into a legitimate one by ratification using cash budgets—a tool of accounting.

Identifying the problem is a major intellectual responsibility and exposing the roots of exploitation is a precondition for liberation; Dillard and Tinker (1996) insist that bringing structural contradictions into consciousness and to develop them to the highest level of instability is one purpose of critical accounting

research. The evidence provided by this research further strengthens this claim. Further Case III, where the credit applicant was rejected brings such discriminating deeds and the increasing importance of intellectual systems such as accounting in exploitation mechanisms into consciousness.

In a macro point of view, when productivity motives become secondary to political ones such as in Cases I and II, the accounting reports were rarely discussed or used for accountability and accounting systems were seem to be maintained only as a regulatory requirement to legitimate events to external bodies and the populace (Wickramasinghe & Hopper, 2003).

8.3.1 Addressing the research questions

As De Brunhoff (2003) suggests financial activity should be taken out of the hands of the rich owners of money capital and regulated by the state so that some deserving powerless individuals like Mr. Silva in Case III can not only develop their businesses but also save their houses. This case provides evidence for De Brunhoff's claim that entrepreneurs and workers should not be dependent upon the interests of owners of capital and should not be at the mercy of bureaucratic banking officers.

But De Brunhoff (2003) suggests that "it is necessary to understand more fully the complex relationship between financial and industrial capital, and the respective roles of financiers and entrepreneurs in capital accumulation. Therefore, lack of support from the government in developing business enterprises appears to have a detrimental impact on the formal banking systems. That is, in the absence of regulatory policies and a conducive economic-political environment, the contribution of individual characteristics of credit decision-makers may be fostered and amplified.

The central research question in this research is "*Do credit mechanisms and income/wealth inequality create a mutually reinforcing cycle in Sri Lankan society?*" The supportive other research questions are:

- *Are credit decisions made in favour of influential businesspeople?*

- *Are certain demographic groups at a disadvantage in obtaining credit?*
- *As a result of favourable credit decisions, could influential groups of people get richer and more influential?*
- *Are “ability to obtain credit” and “becoming more influential” mutually reinforcing?*

To build up arguments to the central question it is useful to address the above four supportive questions first.

8.3.2 Social power and access to credit

Are credit decisions made in favour of influential businesspeople? And Are certain demographic groups at a disadvantage in obtaining credit? All three case studies provide evidence to substantiate the claims of certain researchers discussed in the preliminary literature review presented in chapter one. For example, the Governor of the Bank of England claims that the access to start-up or early-stage finance for disadvantaged groups in poor neighbourhoods is a problem. Silva in Case III is from a “disadvantaged group” in a “poor-neighbourhood” and access to capital through credit was truly a problem for him.

Another argument was that “budding entrepreneurs from different demographic groups do not have similar opportunities in accessing finance; some groups have less access while other groups have more access to finance capital”. With the evidence provided in this research, this argument can be restated as “certain poor entrepreneurs have less access while powerful businesspersons have more access to credit”.

Another claim is that a growing body of evidence suggests that owners of small businesses from some demographic groups may have less access to institutional financing (Bates, 1973; 1991; Cavalluzzo & Cavalluzzo, 1998). This research has added further proof to this growing body of evidence to strengthen the argument that there is discrimination in lending based on social status and economic power. This means poor/powerless groups are discriminated against

in provision of credit because they lack certain qualities and factors such as money, inclusion and networks, etc. which are prerequisites for obtaining credit.

The criticism of banks for their dominating role in providing finance to SMEs because there are very few lenders who facilitate them (Whincop, 2001) is also substantiated by the case study stories in this research. Banks, when run under autocratic leadership, especially when systems are disregarded and management is weak put SME credit applicants such as Silva in Case III on the receiving end.

Therefore, the claim of Marx and Engels that the capitalist class, who own the means of social production, control society and construct values and social relationships in their own interests is further substantiated by the evidence provided in this research. Further, in the contemporary context capitalism promotes separation of the poor from the whole environment (James (2008). This is the Marxian concept of “alienation”; with regard to workers, but now it is apparent in almost every field where every-day life is commodified (Dominelli & Hoogvelt, 1996; Tinker, 1999). Case study III provides verification for such alienation where agents discriminate or deny the rights of one group of people to protect and/or strengthen another group in society. It is argued that “people are poor today because of the failure of the financial institutions to support them in the past. Like the right to food, clothing, shelter, education and health, credit should also be recognized as a fundamental human right” (Yunus, 2007, p. 2). But this right was denied to Silva who was desperate to save his business and house. Silva had proof of his business acumen and enterprising skills. The only lapse on his part seems to be “overtrading” especially without a “cordial relationship” with his bankers. But what Silva did not have is the social power or membership of a powerful social network to support him in finance capital when he was in need.

8.3.3 Access to credit and social power are mutually reinforcing

The other two supportive questions are: *As a result of favourable credit decisions, could influential groups of people get richer and more influential?*

And Are “ability to obtain credit” and “becoming more influential” mutually reinforcing?

According to case studies I and II, the credit facilities were granted casually on a personal basis without following the policies and procedures of the bank. These favourable credit decisions helped the borrowers to remain in the market doing “trial and error” businesses masquerading as “successful” businesspersons and enjoying government concessions on business development programmes such as long-term leased lands, export promotions and tax advantages, etc. This situation enables the industrial capitalists to accumulate their wealth even though they and their loans are classified as bad by banks. The loans are serviced with further borrowings. On the other hand, in particular, these accounting treatments facilitated the financial capitalist (the Soft Bank) to declare some unearned profits and artificially push the non-performing loans down to dress up the financial statements.

Therefore this capitalist credit mechanism is required for financing new industrial investments, and it also centralizes the money of all social classes. Owners of small savings are passively involved in the process, while the ownership of financial assets is highly concentrated in the hands of a few wealthy people, including some industrial capitalists. This concept of extreme extraction of value from a group of people in the society, is termed as exploitation in Marxism.

Marxian critical theorists argue that, in the final stage of capitalism bankers and industrialists set the ground rules in distributing the benefits with ultimate power balancing between capital and labour. Their studies investigate how capitalist forces influence decision-making/lending processes by weakening state power (economic–political environment) and ignoring the role of people’s abilities, and the skills of bank professionals and at the same time enhancing the social power of a few “real” decision-makers in the sector. It is evident, in these case-study stories, that most individual, social-cultural and economic-political factors are collectively directed towards protecting the social power of an

advantaged class of the capitalist society. Social power, privilege and inclusion in various activities are intertwined with possession of money in capitalist society, meaning that the economic power afforded by money eventually leads to social power. Therefore, social power becomes the fundamental driving force for decision-making based on preferred social norms in the state and private institutions, particularly in the finance sector.

And, in societies where commodity exchange is widespread, the economic power afforded by money naturally leads to social power. “Money is the monopolist of the ability to buy, or in Marxist terminology the ‘universal equivalent’”, (Lapavistas, 2003, p. 70-71). Cases I and II provide evidence to strengthen this argument and therefore, it is evident that, as a result of favourable credit decisions, ‘influential’ groups of people could get richer and more influential—“ability to obtain credit” and “becoming more influential” seem mutually reinforcing.

Based on the above analysis, the central research question is addressed below with a macro-level discussion using Marxian critical theories.

8.3.4 Discussion of the central question

Do credit mechanisms and income/wealth inequalities create a mutually reinforcing cycle in Sri Lankan society?”

According to Marxian analysis, the distribution of profits between entrepreneurs and finance providers is awkward, but this accumulation of capital needs both of them. The credit system transforms idle money into loans that can earn interest for their owners and redirects it back to accumulation. This loanable money capital, Marx says, “no longer passive but active, usurious, [and] proliferating capital” (1978, p. 569 cited in Lapavistas, 2003, p. 70). Case-studies I and II provide facts to strengthen the Marxian claim that, the credit system is a serious weapon in the battle of competition and forms a significant social mechanism for the centralization of capital. Also, Case III provides proof that a lack of money translates into powerlessness, deprivation and exclusion

from several social activities for the majority of the poor under capitalism. In capitalist society, successful participation in social affairs depends less on a person's abilities and skills and more on possession of money.

Inequality is a global phenomenon. Some researchers argue that economic development that was basically conceived in terms of industrialization and that liberal democracy did not bring marked change to the problems of the Third World countries (Schuurman, 1993). The external pressures, including privatization and import liberalization, eventually create more opportunities for accumulation of wealth to the group of influential capitalists, making them more socially powerful. Hence, the issue of income/wealth inequality in a country cannot be separated from that of the widening gap between rich and poor countries through globalization of business and through propaganda for privatization to weaken State power especially in developing countries.

The Marxist interpretation is that inequality is a structural component of capitalist accumulation in a world economy. The ultimate result of these influences from international capitalist forces is a continuous widening of the gap between rich and poor nations further increasing inter-country inequality. The major tool used for this purpose is the heavily conditional hold of financial capital controlling the access to it by the poor countries. Despite the huge differences among development studies scholars, they all agree on one fact: that economic development in the developing countries will continue to be hindered by continuous structural roadblocks—including access to credit.

Kuznets's (1955) assumptions, inferences and even "facts" such as the economic development of a country would trickle down the benefits to the poor and would reduce the gap between the rich and poor, have been proven false by the history. For example, the share of national income enjoyed by the poor has been continuously reducing in Sri Lanka and was reported as 1.08 percent in 2003 (The Central Bank of Sri Lanka, 2008).

There seems to be a barrier between ordinary people's potential (through abilities, ideas and skills) and access to money capital in the capitalist society. In the meantime, people (with or without abilities, ideas and skills) who possess money could gain the potential and reap the benefits. More seriously, when access to money capital is coupled with true potential with ideas, abilities and skills, it could have an undue advantage over moneyless people and on exponential effect in accumulating wealth.

Based on the evidence discussed above, it could be theoretically argued that there is a tendency to make credit decisions based on preferential measures when the credit applicant is socially and economically powerful and the lending decisions are made by abusing legitimate authority overruling the normal banking practices for credit evaluation. Exploring from a Marxian critical theory perspective, Lapavistas (2003) explains the motives behind such arbitrary lending decisions as follows:

Social power, privilege and inclusion in various activities are intertwined with possession of money in capitalist society. In capitalist society, successful participation in social affairs depends less on a person's abilities and skills, and more on possession of money (p. 64).

Therefore, all individual, social-cultural and economic-political factors are collectively directed towards protecting and strengthening the social power of an affluent class within the capitalist or feudal society. The economic power afforded by money eventually leads to social power and in turn, social power becomes the fundamental driving force of arbitrary/informal decision-making in the banking/finance industry in Sri Lanka. Then, because the powerless are ignored, the poor class is neglected. Equally, lack of money translates into powerlessness, deprivation and exclusion from several social activities for the majority of the poor under capitalism.

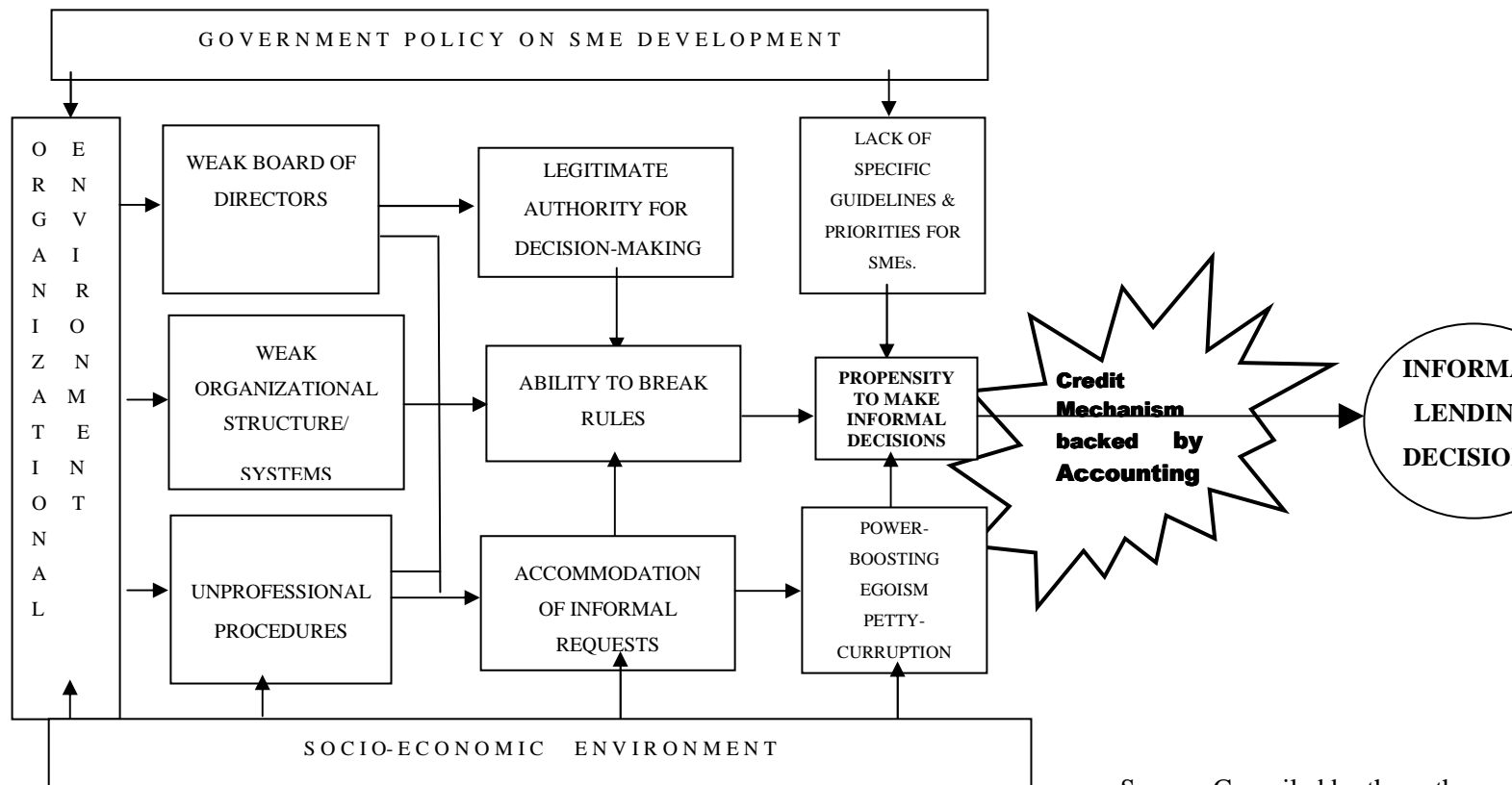
The next section elaborates this discussion further by investigating the possible reasons and motives behind these irrational and informal credit decisions which are made differing to preferential social norms.

8.4 Informal decision-making model

When the informal decisions involved the decision-makers at the highest level in the bank, it is more likely that the decision-maker was influenced by the motives of power-boosting through the credit and exploitation mechanisms backed by accounting technology coupled with the need to achieve esteem needs. But when the informal decision involves the decision-makers at the middle level of the hierarchy of the bank, it is more likely that the decision makers are influenced by genuine banking spirit or motivated by rewards expectancy. The powerful decision-makers disregard systems and abuse their authority to accommodate socially powerful credit applicants. The credit applicants from the disadvantaged group of people are declined through strict application of banking rules.

For the decision-maker, the ability to break the rules is intensified by the presence of a weak board of directors, weak organizational structure and unprofessional procedures. It is also promoted with the cultural and egoistic motives of accommodating informal requests backed by “legitimate” decision-making authority.

Lack of support from the government in developing the SME sector seems to be having a significant impact on the formal banking systems with regard to financing SMEs, both formally and systematically. These forces collectively increase the propensity for creating on informal decision-making process especially when the organizational structure is weak. These factors are summarized and presented below in a model illustrated in Figure 8-1: Arbitrary Credit Decision-Making Model.



Source: Compiled by the author

Figure 8-1: Arbitrary Decision-Making Model: Combined Influence of Individual, Organizational, Political and Environmental Factors on Informal Decision-Making in Formal Banking System in Sri Lanka

8.5 How and why are credit decisions made informally and differently?

Case studies I and II show that informal lending takes place, when the decision maker: (a) has unchallenged authority and; (b) was influenced by motives such as ego, self-esteem or favouritism. The case studies data analysis in chapter seven also revealed that this informal lending will not occur just for reasons of;

- a) benefits to the institution (bank) and/or decision-maker; or
- b) the personal relationships or gratifications; or
- c) technical issues such as the extra liquidity position of the lender; or
- d) patriotism/nationalism or social responsibility. But these factors may have had an impact in influencing the decision-makers.

The case studies show that, when the decisions were made at the highest level, the informal lending decision might have been made as a result of a combination of social attributes such as social power, influence, inclusion and prestige, individual traits such as self-esteem, ego, and individual aspirations. Marxian analysis argues that these individual traits are super-structural. As discussed in the literature review chapter, structure plays a vital role in shaping one's motives. The structure under review is class-based capitalism and therefore, capitalists 'favour' their fellow capitalists to strengthen their social network and boost their power, as is evident in this research. Also, the findings of this research support Goulet's (2002) notion on the interconnectivity of vested interest and disproportionate political power of privileged classes and show how these essential attributes of bank capitalists in Sri Lanka contribute to enhancement of their social power which, in turn, boosts the capacity of decision-making within the credit mechanism.

8.5.1 Petty Bourgeois

With regard to the justification of lending to an automobile manufacturing company in Sri Lanka, Allahar's (2004) theory of "petty bourgeois nationalism" partly but convincingly explains the possible motives of the finance provider who is a traditional business individual, because the petty bourgeois is more traditionally in favor of protectionism according to class-bound nationalism. They are unable to compete internationally, use masks such as nationalism and patriotism to promote and protect their specific, locally produced goods and services. This powerful class places their egoistic interests and symbolic gains before the economic interests at large. These traditional businesspeople, who could not completely alienate themselves from the feudal paradigm as the capitalist class did in the industrialized countries, are not sophisticated enough to compete internationally and their business is restricted to the local market. They use masks such as nationalism and patriotism to promote and protect their specific spheres of operation: local industry, local manufacturing, and the exchange of locally produced goods and services (Allahar, 2004). In the case of Lan-Car Ltd., this exchange of goods and services is clearly evident where the Soft Bank Chairperson provided 'market support' by promising to buy automobiles from them in addition to provision of financial capital. What the Chairperson was primarily targeting was the publicity which is an essential requirement to boosting his popularity and therefore to enhance his social power base.

Further, as Munck (1986, cited in Allahar, 2004) stressed, nationalism matters because people die for it but the motive is not clear. Therefore, analyzing and interpreting the behaviour of such petty-bourgeois are useful endeavours and important in discovering the motives of such irrational decision-makers.

8.5.2 Four birds in one shot

The Chairperson made credit decisions to disburse loans and blew his own trumpet to the board of directors of the bank about his 'business development' drive while showing off to the general public about his 'patriotism' to the

country. The Chairperson was aiming at four birds with one shot, i.e., fulfilling egoistic motive, strengthening his position as the Chairperson of the Soft Bank, becoming more powerful as the President of a state authority and boosting popularity among the general public. The more devious and “smart” these performances of these types of individuals are the more they achieve their personal goals at the cost of public funds, customer deposits and minority shareholders. This argument is built on the claim of Hooper and Karin (2008) on the wealth confiscation through the Marxian concept of an Exploitation Mechanism.

8.5.3 Exploitation of minority shareholders

On the other hand, even small shareholders are affected by such decisions which hamper the institution’s profitability, returns and therefore distribution of dividends. Moreover, publicity given for such risky lending decisions creates a negative image for the lending institution among the business and investment community and sends adverse signals to research units of stockbrokers and other companies with large investment portfolios. The invariable result is circulation of unfavourable research reports on the target institution by those researchers and, the natural consequences are increased selling pressure and depleted demand to the shares of such institutions and ultimately the inadvertent crashing of the share price. This scenario has little, or no effect at all, on the managing owners since they do not expect genuine business returns such as dividends or capital gains but numerous other returns such as fringe benefits, other perks and fulfilling their other motives such as “feeling powerful”. The ultimate sufferers are the small shareholders of such companies and sometimes its employees. But in the worst case scenario, this type of loss of confidence can infiltrate into the general public and could result in a “run” on deposits and finally could be exposed to a collapse as was evident in the case of Soft Bank in 2008.

Due to resulting low share prices, these institutions are not exposed even for take-overs, hostile or otherwise, because the present owners have the controlling

power with more than 50 percent shareholdings. This accumulation of share ownership has been carried out by making use of the loopholes in the regulatory policies and procedures regarding ownership restrictions. It is interesting to note that, the share price fell by 50 percent from LKR28 to LKR14 during the ‘run’ in December 2008 and, when the CBSL had to intervene and changed the management by appointing a new Chairperson and a board of directors, the market quickly responded by bouncing back the share price to LKR24 and since then it has improved gradually, and touched LKR35 closing the gap with the industry PE ratio in January 2009.

It is quite interesting to conjecture why bank capitalists would take such exorbitant risks in lending money especially when the prevailing risk-free government securities carry rates of interest higher than the average rate of interest offered on deposits. Banks are in a very comfortable position to make their margins which are moderately thin but steady and secured. Such irrational behaviour by owners of financial capital has very little justification.

8.5.4 Importance of State intervention

Lack of state support could result in detrimental impacts on financing enterprises, forcing certain decision-makers to make uninformed, informal and sometimes illogical decisions in their own interests. But if the credit mechanism is completely regulated and monitored by the state as Marxian theory advocates, there would be momentous changes in the whole structure of the capitalist accumulation of wealth. Therefore, De Brunhoff (2004) suggests that “it is necessary to understand more fully the complex relationship between financial and industrial capital, and the respective roles of financiers and entrepreneurs in capital accumulation.

It has been revealed by surveys of small businesses (for example, in Sri Lanka and Tanzania, see section 2.5.2) that State support is vital in developing business enterprises. The suggestion to strip the powers of rich owners of money capital because the entrepreneurs should not be dependent upon the interest of such decision-makers is further supported by this research. Had there

been a proper SME development programme in Sri Lanka, the three credit applicants considered in this research would have been in a better position. Tony and Yusoof would have been advised appropriately and been guided straight to viable projects. Yusoof realized the Lan-car was not up to standard lately, collaborated with Korean manufacturers and abandoned the original project. Silva may have been offered financial back-up and business strategy assistance. The Marxian perspective is that state intervention is part and parcel of capitalist development though the promotion of capitalism did not mention that explicitly. These cases confirm Isbister's (2001) argument that "It is a serious misunderstanding of capitalism to think that it consists of a private sector alone or that it stands in opposition to government" (p. 38). It is evident that capitalists while opposed to certain government policies, widely depend on governments but without proper guidance from the government these petty bourgeois "nationalists" just go on gut feeling influenced by personal motives such as those seen in case-studies I and II. Moore's (1997) criticism of Smithian/neo-liberal arguments about governments as obstacles to capitalism in the contemporary Third World are analogues is proved valid. It is worth noting that Saad-Filho's (2003) claim that

"...developed markets arise only through state intervention. The state establishes the institutional and regulatory framework for market transactions, including property rights and law enforcement. It regulates the provision of infrastructure, ensures that a healthy, trained and pliant workforce is available, and controls social conflict. The state establishes and regulates professional qualifications and the accounting conventions... (2003, p. 9).

8.5.5 Credit mechanism is a terrible social mechanism

The credit system transforms idle money into active money capital and, in society at large, the economic power afforded by money naturally leads to social power.

The discovery in case-study III is that, when the informal decision-making was involved at the middle and lower management levels, decisions might have been

made as a result of rewards expectancy on performance and/or reciprocation expectancy from the parties involved. On the other hand it was observed that Mr. Silva is powerless—he lacks the social network to reach the top management of the bank. Also note that Superclean is a small enterprise and therefore it was ignored.

One discovery in cases I and II is that the capitalists from the finance and industrial sectors act together in exploitation and as a result they get richer and more powerful. The implications vary from lost opportunities to waste of resources. The important elements of this reasoning are identified as the credit mechanism and the role of accounting as a technology for smooth functioning of the exploitation mechanism. Certain capitalists often use masks such as “nationalism/patriotism”, or “social responsibility” to maintain the capitalistic socio-cultural structure which, in Marxian analysis, is detrimental to economic development as well as to the equal distribution of income/wealth of a country, among its people. Also the impact of such systems goes beyond the boundaries of countries through “globalization” and contributes towards widening inter-country differences as well in terms of economic development.

8.5.6 Structure over ideology and institutions over individuals

Arbitrary/informal decision-making is encouraged when standard systems and procedures are not effectively implemented in an organization. Especially, financial institutions are supposed to have, and they generally do have, well written policy and procedure manuals in accordance with the regulatory requirements. Although industry standards of the Sri Lankan banking sector are comparable and on par with international standards by rating agencies, the banking culture, as discussed in detail in the chapters five, six and seven, is highly contaminated with traditional arbitrary methods.

Therefore, it is not only the need for individual power that generates arbitrary decision-making but also the systemic stimulants induced by the institution and the social network as a whole, because, as the Marxian critique suggests, power is held by capital and exercised on its behalf.

CHAPTER NINE

9 CONCLUSIONS

9.1 Introduction

This research on the credit mechanism in Sri Lanka is pioneering. The previous research elsewhere provides evidence for the existence of the discriminatory nature of financing, and the subsequent neglect of disadvantaged groups in society. This research takes that premise further by an empirical investigation and attempts to link it theoretically to the country's income/wealth inequality.

The central research question, "*Do the credit mechanisms and income/wealth inequalities create a mutually reinforcing cycle in Sri Lankan society?*" is answered by combining the arguments developed from all three case studies. This research provides empirical and theoretical evidence to argue that there is a possibility of a relationship between the credit mechanism and income/wealth inequality in Sri Lankan society and, this relationship seems mutually reinforcing. Further, the research findings strengthen the Marxian critique that accounting plays a significant role as a technology in the credit and exploitation mechanisms. The findings of this research are useful in optimizing understanding of the credit mechanism and some behavioural aspects of credit decision-makers in the Sri Lankan banking industry.

The conclusions are helpful in formulating policies for more productive financial capital mobility systems in Sri Lanka and other similar countries. This research reveals that the implementation of proper policies and systems with regard to credit mechanisms warrants state intervention. The Soft Bank crisis showed that crony capitalism, which facilitates the exploitation mechanism at its extreme and enables the credit mechanism to work mainly for the rich, is not sustainable. Such credit mechanisms waste resources and ignore the need for nurturing potential projects, which in turn create roadblocks for employment

generation and economic development, and help to keep the poor frustrated, finally resulting in maintaining income/wealth inequality.

9.2 Summary of the three cases

Case study I: Tony Group: a garment manufacturing business, was the highest single foreign exchange earner in Sri Lanka but was struggling with a lack of orders and liquidity problems and the consequences were dire with huge probable redundancies. Tony had a close relationship with the Chairperson of the Soft Bank as both are powerful businesspersons. He was privileged to get a quick meeting with the Chairperson. After a short, friendly negotiation, with the help of accountants, Tony secured a US\$4 million credit line over the table, without formal credit evaluation. The Chairperson justified his decision on sympathetic (social responsibility/patriotism) grounds and cash flow projections provided by the accountants.

Case study II: Yousef: a car manufacturer in Sri Lanka, was struggling with regulatory authorities and financing problems. The owner, Yousef, of Lan-Car Ltd. was powerful enough to contact the Chairperson of the Soft Bank directly, and was privileged to get an instant credit line without formal credit evaluation. However, the company's automobiles had been refused registration because of roadworthiness and safety issues. The Chairperson's justification was under the mask of patriotism, to save foreign exchange, etc., and was supported by positive cash flow projections made by accountants. These informal credit decisions were unjustified as demonstrated.

Case study III: Silva was a powerless janitorial-service enterpriser struggling with a loss of business and financing problems. Silva prospered fast at the beginning and he assigned his success to the Branch Manager (BM; credit decisions were formal and rational). Then, Silva had to deal with the Credit Officer of the branch but was not comfortable because of some personal grudges (CO; credit decisions were formal and rigid). But Silva recovered with the help of Manager-Recoveries (M-R; credit decisions were informal and

rational) who went beyond his authority to grant credit to Silva. Finally, Silva ended up with the Chief Manager– Recoveries (CM–R; credit decision was formal and rigid) who applied the rules strictly and Silva lost his house and was imprisoned. M–R was fired.

Based on the above case analyses, the outcome of the discussion of the other four research questions is that there are credit decisions made in favour of influential businesspeople and therefore, certain demographic groups are at a disadvantage in obtaining credit. As a result of such favorable credit decisions, certain influential groups of people become richer and more influential, therefore, it is inferred that, the “ability to obtain credit” and “becoming more influential” are mutually reinforcing.

9.2.1 Post-research events

Post-research events enhance the credibility of the data collected in this research and are useful in verifications and validations of claims and arguments and therefore, increase the dependability of the outcome of this research.

The instant credit extended to the garment manufacturer in Case I and the car manufacturer in Case II directly by the Chairperson proved futile. Both the credit facilities were classified as non-performing loans (NPL) later. By 2006, the Soft Bank’s NPL levels, at 12 percent of total loans, was the highest among the banks. The Soft Bank rating outlook was downgraded to negative by rating agencies based on weak solvency, slow NPL resolution, insufficient internal capital formation and challenges faced in raising fresh equity capital. The level of profitability of return on assets of 0.7 percent, coupled with its high dividend payout ratio of 42 percent of profits after tax, together with bad debts prevented internal capital formation to improve solvency.

The middle-level recovery manager, M–R was fired for unauthorized decisions which included granting credit facilities to Silva. However, the research participants were of the view that M–R would not have been punished if he/clients were powerful/rich/influential. M–R is still respected among his peers

for his knowledge and skills. Silva's credit application was declined based on formal credit evaluation. Silva is not influential, he is not a powerful individual, and therefore the bank proceeded with legal action including selling his house to recover his debts. Also, Silva was jailed for non-payment of employee provident fund contributions.

Soft Bank faced a 'run' in late December 2008 due to a loss of public confidence in the Chairperson. The Central Bank of Sri Lanka (CBSL) intervened and rescued the Bank. The Board of Directors of the Soft Bank, including the Chairperson, was removed by the CBSL. The management was handed over to another stable bank in Sri Lanka. A threefold increase in provisions for NPLs, which were largely extended to the group companies by the new management, substantiates the claim that credit had been provided to connected parties on preferential norms without proper evaluation.

9.3 Research conclusions and contribution to knowledge

Five individual credit decision-makers and their four decision types were investigated in relation to the credit mechanism, the unit of analysis of this research. The case studies focused on the behaviour of decision-makers, the organization structure, the management style of the Soft Bank and the credit culture in Sri Lanka at large. The discussion centred around the links between accounting technology, social mechanisms and income/wealth inequality as a global phenomenon. Therefore, this research is a study on both the micro level (individual or institutional level) and a macro level (income/wealth inequality, accounting and the credit culture in Sri Lanka). Two theoretical models are proposed for *Informal Credit Decision-Making* (Figure 8.1) and on increasing income/wealth inequality. These models were developed by combining empirical evidence and theoretical interpretation of the research questions and answers. The core findings of this research are presented below as empirical findings: Marxian theoretical confirmations, methodological derivatives and combined conclusion.

9.3.1 Empirical findings

Credit applicants Tony and Yousef, who were sufficiently powerful and/or privileged to reach the ultimate decision-making authority, were at an advantage and were successful in obtaining necessary finance for their projects. Conversely, the credit applicant, Silva, lacking social power or any other influence, could not obtain the necessary finance and, therefore, failed.

The social power involved was such an influential factor it could even reverse regulators' decisions, so that Yousef's unroadworthy automobiles were declared to be road-worthy. But this power or influence was not available to the poor enterpriser to turn around his small and viable cleaning business during hard times.

All three credit applicants had failed formal credit evaluation. In fact Tony had been reported to the Credit Investigation Bureau for default by four other banks and Yousef's fibreglass automobile had been rejected by authorities on regulatory grounds, lack of road-worthiness and safety. But Tony and Yousef were successful in obtaining credit while Silva was discriminated against.

All three case studies provide empirical evidence to the claim that the application of credit rules had become a negative device in this particular banking environment. These credit rules are meant to be superseded by the decision-makers to provide credit to all businesses: small, medium or large. But encouraging poor clients can have a negative effect on decision-makers' prospects as is evident in the Silva case where the M-R was fired for "abusing authority" by superseding rules and providing credit to Silva, a deserving credit applicant.

Both Tony and Yousef had qualified accountants working for them. They had the capacity to provide professional project reports, feasibility studies with convincing cash-flow projections and profit forecasts to justify their credit requirements. But Silva was a small businessman who lacked the power of

accounting technology to convince the credit decision-makers and to pass the credit rules' requirements and therefore was not successful in obtaining credit.

In the decision-making process, it is evident that accounting tools such as profit planning and cash-flow projections play significant roles in justifying credit decisions. The credit applicants supported by qualified accountants have an advantage in obtaining favorable credit decisions. The small credit applicant who cannot afford qualified accountants and without "professionally prepared cash flows" etc., failed to convince credit decision-makers.

This research revealed that the credit culture in Sri Lanka is contaminated with informal methods. The informal nature in this decision-making is known but not in its entirety to all the role players in the mechanism. Yet it plays an important role in financing businesses, especially to the advantaged groups of society. Informal methods were apparent on all fronts in the process, from both credit applicants as well as credit providers, at all levels from small to large clients and from the junior credit officers to the top-level decision-makers. These informal methods are more effective when it involves powerful individuals rather than ordinary persons.

It was also evident empirically that the state policies and systems on entrepreneurial development and business financing are weak or not in place at all. The inconvenient process and the difficulties experienced by Yousef is an example showing that there was no proper system in place to evaluate the viability of such projects, especially when they are in the national interest, involved economic policy issues and required large resources. Also it was revealed that businesspersons lack confidence in existing systems and regulatory frameworks. On the one hand Yousef did not agree with the regulators on the non-viability of his automobile project while the Chairperson viewed the regulators as obstacles.

Much diversity was observed in credit decision-making in Sri Lanka during this study. The credit decisions are largely dependent on the extent of authority

entrusted to the decision-maker and his/her ability and willingness to break or follow the rules of the credit policies and credit administrative procedures. There is empirical evidence to claim that the Chairperson was steered to informal credit decisions largely by his desire to strengthen his network, show his powers and to project himself as a saviour of “helpless entrepreneurs” and he used masks such as patriotism to justify his decisions.

It was empirically revealed that import protectionism is promoted with ulterior motives. This might be due to a lack of proper policy, systems and institutions to identify and nurture potential entrepreneurial projects. The petty-bourgeoisie is more traditionally in favour of import protectionism. The traditional businesspeople, who are not sophisticated enough to compete internationally and whose business is restricted to the local market, use masks such as patriotism to promote and protect their specific spheres of operation: local industry, local manufacturing, and the exchange of locally produced goods and services. This exchange of goods and services is clearly evident where the bank Chairperson provided market support by placing an order in advance to buy automobiles from the borrower in addition to granting him financial capital. It was also revealed that state sponsorship in assessing, evaluating and developing projects is not encouraging or not in place at all. This situation has led to making credit decisions which are naïve and by taking an uncalculated risk, or on a trial and error basis. Therefore, resources are wasted, potential projects/entrepreneurs are neglected and economic development is hampered.

9.3.2 Marxian theoretical confirmations

The importance of the role of accounting as a key technology in facilitating the credit mechanism and exploitation mechanism is manifested in this research too. Both Cases I and II provide evidence to show the exploitative use of deposit funds in the Soft Bank without following proper evaluating procedures but on professional accounting projections. The borrowers used cash-flow projections to ‘prove’ their business prospects. On the other hand the Chairperson used accountants and accounting reports to convince the board of

directors and to justify his decisions. Hence, it is evident that accounting functions play a significant role in the exploitation and concentration of wealth through the credit mechanism. Therefore, accounting is a strong persuasive technology which serves the wealthy and sustains inequality.

Nationalism in the guise of import substitution serves to preserve class differences between the owners of capital and the working class. According to Marxian analysis, the distribution of profits between entrepreneurs and finance providers is awkward, but this accumulation of capital needs both of them. The credit provided under the mask of nationalism activates the credit mechanism, transforms idle money into loans that can earn interest for their owners, and redirects it back to accumulation, thereby increasing the class difference.

Individual traits are super-structural. Structure plays a vital role in shaping one's motives. According to Marx, the structure is class-based and the Chairperson, a powerful capitalist, tactfully hooked other socially powerful individuals into his social network which in turn boosted his own socio-economic power base. Socially powerful decision-makers in this research seemed to place their egoistic interests and symbolic gains before the country's economic interests, under the façade of popular theories such as nationalism, patriotism and social responsibility.

The major shareholders did not inject a single cent as new capital but they smartly used others' money to acquire and retain the controlling power of the Bank using certain loopholes in the system and by forming employee share ownership programmes (ESOPs). The directors of the ESOPs are their most loyal employees and include relatives and family friends. In this way the Chairperson established his powers to extend credit to connected parties outside the credit rules and feels more powerful because he looks after not only himself but his cronies as well. This is a clear exploitation of public deposit funds for the benefit of the "owners" of finance capital. The negative publicity was such that the Soft Bank faced a 'run' and lost 10 percent of its deposits. The regulators had to intervene by removing the board of directors including the

Chairperson and assign the management of the bank with another stable, state-owned bank.

On the other hand, small shareholders are exploited through bad credit decisions which hamper the bank's profitability. This resulted in circulation of unfavourable research reports on the bank, the fall of its share price and the ultimate consequence of reducing the shareholders' wealth. This scenario has little, or no effect at all on the controlling major shareholders since they do not expect genuine business returns such as dividends or capital gains, but numerous other advantages such as fringe benefits, other perks and/or fulfilling their motives such as "feeling powerful". The ultimate sufferers are the minority shareholders, its employees, customers and in the worst case scenario, the public.

Marxian critique suggests that power is held by capital and exercised on its behalf. Equally, lack of money translates into powerlessness, deprivation and exclusion from social activities for the majority of the poor under capitalism. As argued in this thesis, successful participation in social affairs depends less on a person's abilities and skills and more on possession of money and power. Money, whether through credit or other sources, is the possessor's essential powers. According to Marx, one's individuality is secondary to possession of money. Any wicked, dishonest, unscrupulous and stupid individual is respected because money is respected. Money is the highest good, and consequently by association, its owner is also good. There seems to be a barrier between ordinary people's potential (through abilities, ideas and skills) and access to money capital in capitalist society. In the meantime, people (with or without abilities, ideas and skills) who possess money gain potential advantages and multiply them. Moreover, when access to capital is coupled with true potential or ideas, abilities and skills, it may have an undue advantage over moneyless people and an exponential effect in accumulating wealth.

It is argued that the culture of using informal methods in Sri Lanka is an outcome of lengthy colonization where business was possible only with

government support such as issuing various licences to trade and manufacture. The implementation of successful transactions requires bureaucratic approval but a large number of the bureaucrats are corrupted by people with connections. The introduction of strict price controls of products would have also influenced people to exploit informal means to carry out their business in a more competitive manner. This situation is a vicious cycle where economic power is instrumental in encouraging informal methods and the ‘job’ is done by using or abusing power, which in turn boosts the social power of the power holder and, further encourages using informal methods in the society.

There are four types of credit decisions observed during the interpretation of research data. This classification of decisions was done based on decision-makers’ approach towards application of credit rules and rationality of the decisions. There are some credit decisions which were made according to credit rules and seem rational. Conversely there are some decisions which were made superseding rules but still seem rational. Also there are some credit decisions which are made by strict application of credit rules but look irrational while some other decisions which are made informally, without following rules and look irrational.

9.3.3 Methodological derivatives

Many researchers feel a need to position themselves as a particular type of researcher and identify themselves with a defined way of knowing. Each research situation and research question is unique, and assumptions can be as varied as the situations. The researcher has taken a strategic position in designing the research methodology of this research.

The past experiences of a few senior bank officers were reconstructed for building understanding and to expose the existing credit systems in Sri Lanka. Then they were substantially backed by evidence obtained through secondary sources. Some real-world experiences were iteratively filtered through analyses, interpretation and theorization and then articulated as knowledge in this thesis.

This case study research also supports the claim that case studies are not really a methodology, but rather, are an approach to research. The case study research data was collected through different sub-methods such as questionnaires, interviews, exchange of e-mails and internet chats, etc. The research data were analyzed using narrative methods and posing *how* and *why* questions repeatedly. The theoretical guidance provided by Marxian critical theory played a significant role in presenting, analyzing, interpreting and theorizing the outcome of this research. In designing this case study research, the integration of carefully articulated research assumptions/questions/propositions based on the preliminary investigation backed by the researcher's exposure to the relevant field of study were useful to maintain the focus of the study.

9.3.4 Combined conclusion: Credit Mechanisms create roadblocks for economic development and play a role in sustaining wealth inequality

This thesis argues that all individual, social-cultural and economic-political factors are collectively directed towards protecting and strengthening the social power of an affluent class within capitalist society. The economic power afforded by money eventually leads to social power and in turn, social power becomes a significant driving force of arbitrary/informal decision-making in the banking/finance industry in Sri Lanka. Then, because the powerless are ignored, the poorer classes are neglected. Equally, a lack of money translates into powerlessness, deprivation and exclusion from social activities for the majority of the poor under capitalism. Therefore, opportunities are lost to the society/country as a whole, and the poor remain poor.

On the other hand, because the powerful classes acquires more power through such informal decisions, it can be concluded that inequality in the society and preferential/informal bank lendings are mutually reinforcing. And therefore, the socially powerful rich classes get richer and richer while the powerless poor classes remain stagnant.

Preferential credit decisions are made to accommodate fellow socially powerful credit-applicants, while the arbitrary strict application of rules is apparent to reject some other credit applications. The application of rules has become a negative device and they are meant to be superseded if prospective business projects are to be financed through bank loans. But such encouragement of small, poor clients can have a negative effect on a manager's prospects. The mutually reinforcing cycle is that certain credit decisions, which are made through abusing authority, supply money to the influential individuals in the society and, such economic power enhances the social powerbase of those individuals, which in turn reinforces the propensity to make preferential credit decisions. On the other hand when credit is declined by applying the rules strictly because the credit applicants are not influential or do not have informal access to credit decision-makers, the powerless poor class is ignored and opportunities are lost to disadvantaged social groups. This mechanism makes rich people richer while poor people remain poor if not poorer.

The Soft Bank crisis showed that the extreme use of the exploitation mechanism and credit mechanism for capital accumulation is not sustainable. Also, these power-driven discriminatory decision-making systems not only restrict the availability of financial capital for feasible projects, but also blatantly deny credit applications of potential enterprises. Further, wasting resources for unfeasible projects, while ignoring the need for nurturing potential viable projects, are a double blow to the efforts towards employment generation and economic development and therefore, detrimental to the economic well-being of the general population. This situation frustrates the poor. These findings provide insight for policy formulators in developing policies for more productive financial capital mobility systems in Sri Lanka. The conclusions of this research emphasize the need for radical changes in the financial mobility system through state intervention for SME development. It is suggested that proper state intervention in regulating SME financing could remove such credit-related obstacles to economic development, and work towards a fair distribution of economic benefits to the people in Sri Lanka and beyond.

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Appendix 1: Questionnaire (1)

1. Please identify and provide details; credit amount, project description and application process (you are free to use fictitious names) for a credit applicant you are well aware of the credit application process followed.
2. Was it successful?
3. Did credit applicant attempt to approach higher authority to influence the loan officers who were doing formal credit process? How, what methods, did the credit applicant use to approach the decision-makers?
4. How and to what extent that the credit applicant has been accommodated by the decision-makers and what methods were followed?
5. Please describe the the project proposal in detail in relation to the general economic environment in Sri Lanka?
6. Please describe the loans negotiation processes in a form of dialog if you can recall them?
7. How and what methods were used to present those projects to the decision-makers?
8. What methods did the borrower use to convince the decision-makers? Please indicate as you believe, why did the bank decision-makers accommodate it? (If you feel comfortable to answer?)
9. What were the immediate results of the credit decision?
10. Please describe the present situation of the enterprise? Does it service the loan/s?

Appendix 2: Participation Information Sheet



1. Date Information Sheet Produced:

03rd July 2006

2. Project Title

Role of bank lending in sustaining income/wealth inequality in Sri Lanka.

3. Invitation

You are cordially invited to participate in this research because the findings would be helpful for economic development of Sri Lanka and to minimize unequal distribution of income/wealth among people. Participation is entirely voluntary.

4. What is the purpose of this research?

This research is for the researcher's doctoral studies and a thesis will be produced on the findings of the research.

5. How are people chosen to be asked to be part of this research?

You will be asked to be part of this research by emails and/or over the telephone. You have been chosen because you have worked for local banks in Sri Lanka for more than 20 years.

6. What happens in this research?

You will be interviewed by secured emails during which you will be invited to describe a series of events that you observed and your perception of the effect of these on lending decisions of banks in Sri Lanka where you work or worked.

7. What are the discomforts and risks?

There may be some ethical risk or discomfort to you even though informal/arbitrary methods including bank lending decisions are very common in Sri Lanka and the public is aware of these cases. However, very careful control measures are suggested to alleviate these risks as described below.

8. How will these discomforts and risks be alleviated?

There will not be any clue to identify you as your identity will be kept strictly confidential. You are not expected to reveal anything which will embarrass you or make yourselves uncomfortable. Only two participants would be interviewed out of large number of bank employees and only three cases will be selected for the purpose of this research. As there are a number of people involved in managing each credit per client from the point of accepting the applications, processing, negotiating, recommending, approving to monitoring, the probabilities of tracing them is very remote.

You will be advised to use email accounts outside the banks, so that you cannot be identified by the bank by tracing employees' email accounts. I will advise you to use my Hotmail or Gmail accounts as my email box is accessible to the IT staff of AUT university.

The e mails will be destroyed immediately permanently after making printouts which will be stored in locked cabinets in the supervising professor's office for six years and then will be destroyed permanently.

If you experience any imotional or other discomfort, you will be able to use the AUT online counselling service, if you consider it necessary.

9. What are the benefits?

The research findings would be helpful for the economic development of Sri Lanka and to minimize unequal distribution of income/wealth among people. The knowledge could be applicable beyond Sri Lanka for other developing countries with similar backgrounds. The thesis might earn the researcher a PhD.

10. What compensation is available for injury or negligence?

N/A

11. How will my privacy be protected?

Your identity will be known only to the researcher and to the supervising professor. Your identity will be kept strictly confidential.

12. What are the costs of participating in this research?

Only some of your time. This could be up to 4 - 8 hours.

13. What opportunity do I have to consider this invitation?

You are invited to respond, if you wish to take part, within one month.

14. How do I agree to participate in this research?

You will be able to agree to participate by providing the signed Consent Form that is e mailed to you with this information sheet.

15. Will I receive feedback on the results of this research?

Yes, you will be sent the draft documentation of your interviews for verification and the articles written on the research findings will be sent to you.

16. What do I do if I have concerns about this research?

Any concerns regarding the nature of this project should be notified in the first instance to the Project Supervisor, Prof. Keith Hooper, keith.hooper@aut.ac.nz telephone +64 9 921 9999 extension 5758.

Concerns regarding the conduct of the research should be notified to the Executive Secretary, AUTEK, Madeline Banda, madeline.banda@aut.ac.nz, 921 9999 ext 8044.

17. Who do I contact for further information about this research?

18. Researcher Contact Details:

C A Saliya, saliya.ca@gmail.com

19. Project Supervisor Contact Details:

Prof. Keith Hooper, keith.hooper@aut.ac.nz, Telephone +64 9 921 9999 extension 5758

**Approved by the Auckland University of Technology Ethics Committee on
29 May 2006 AUTEK Reference number 06/40**

Appendix 3: Questionnaire (2); Analytical questions

a) The approach and methods used by the borrower

Why did the credit applicant approach the chairperson direct?

- Was it because he is powerful?
- Was it because he is rich?
- Was it because he had the access or had the network?
- Has the applicant tried the formal methods before?

What was the outcome of such approaches?

In the case of denying the credit, did the credit applicant attempt to approach the decision-makers informally? Was it successful? If not, why?

b) The approach and the methods used by the lender

Why did the bank accommodate the credit applicant informally?

- The project is financially feasible?
- Because of the technical reasons such as excess liquidity?
- Because the decision-maker was deceptively guided by the capable credit applicants?
- Was it for personal gratification?
- Was it on sympathetic/patriotic/nationalistic grounds and/or based on social responsibility?
- Was it because of personal relationship?
- Was the decision influenced by the ego of the decision-maker?
- Did the organization structure force the decision-maker to make such decisions?
- Has the SME financing schemes of the government any impact on this decision?

c) The influencing factors

Please comment on the following factors in contributing or acting as roadblocks towards the decision-making process of this decision:

- Organization structure
- Poor management skills of the relevant bank officers
- Nationalistic or patriotic attitudes
- Egoistic motives
- Government policies on entrepreneurship development
- Government policies in SME financing

d) The decision-making process

Please critically analyze the decision-making process and comment on the following questions:

- Was it quick?
- Was it after following proper banking policies and procedures?
- Was it based on cash flows and proper credit evaluations?
- Were decision-makers rewarded as a result of those decisions?

e) Concluding remarks

Please feel free to express your views on this credit application with regards to the social network and economic and social power of individuals involved.

Also you can express your views on the impact of such credit decisions to economic development and addressing poverty problems in Sri Lanka.

Appendix 4: Linking exercise of evidence; from data to story- The background and Case I

Evidence Type	Evidence Content (Pl. refer sections indicated within brackets)
News Papers/direct observation	<p>Bomb blast in Colombo (7.2):</p> <p>There was a terrorist attack in Colombo, the Capital of Sri Lanka, in January 1996. The damage was heavy with a death toll of more than 30 people, casualties of more than 300 people. It caused severe damage to the buildings around, including the office of Mr. Perera who was the Chairperson of Soft Bank, the banking arm of a large Group of companies. He was hospitalized with serious injuries to the left eye and eventually he lost the eye. Mr. Perera (the Chairperson), in his late fifties, was a devoted Catholic, and the most venerable priests came and prayed for him in the hospital. He was told that "...Your duty for this world is not over; therefore the God has saved you to serve the people more".</p>
Newspapers	<p>Doctorate to the Chairperson (7.2):</p> <p>The University of Sri Lanka recently awarded the Chairperson with a Doctorate, for his contribution towards the business development of the country. He was a well recognized business tycoon having more than one hundred companies under the name of Soft Group, and ten of them had been listed in the Colombo stock exchange. A leading business magazine named him as the Personality of the 10,000 thousand employees, US\$80 million of net assets and US\$2 billion of total assets.</p>
Annual reports/Press-releases/ Direct observations reconstructed	<p>Management style and change (7.2.1)</p> <p>General Manager/Chief Executive Officer (CEO) of the Soft Bank had a clash with the Board and he left the Bank together with almost all the members of the senior management team of the Soft Bank in June 1996 and formed a new bank. Further, more than 100 officers left the Soft Bank and joined the new bank in September 1996. The dissidents, in canvassing an already known customer base, also launched adverse propaganda against the Soft Bank. The Bank was facing severe problems, losing staff and customers at the same time and without a</p>

<p>Regulatory directives issued by the CBSL Rating</p>	<p>strong management team, in need of a strong leadership. As a result the Chairperson had to be involved heavily in day-to-day operations of the bank and therefore he suggested to the Board that he would have weekly meetings with the senior management of the bank to monitor the progress closely. He also strengthened his power in the board by inviting a few loyal confidants (two lawyers, an accountant and an IT specialist) onto the board of directors of the Soft Bank.</p> <p>Normally the full board meeting was held on the last Friday of the month where all the board members participated and crucial decisions were made. It was evident that Board/Chairperson approved only the proposals (credit, re-structuring of large facilities, new recruitments, promotions and capital expenditure, etc) recommended by the then management. When there were customer/staff complaints or requests for credit facilities from the Chairperson/Directors, they were re-directed to the management, and the CEO had to report on those at the next Board meeting. This process was followed to avoid conflicts by giving due respect to the formal hierarchical-authority.</p> <p>The new CEO was a senior banker, in his late fifties and demonstrated a democratic and consultative type of a management style. He had no experience of holding the hot seat before and showed laissez-faire type leadership qualities. The Finance Manager, a qualified accountant, was promoted to the position of CFO by the new management. In addition to the full Board meeting, the Soft Bank started three more weekly review meetings, on the other three Fridays of the month, for the Marketing, Recoveries and Information Technology functions of the bank. The relevant senior officials were summoned to these meetings whenever necessary, while the CEO and Chief Financial Officer (CFO) were invited for all three meetings. It was the practice of the Chairperson to allocate some time to handle the complaints made by customers, potential customers and even by the general public. He was very customer oriented and often allowed the customers to confront the bank officers openly, sometimes causing embarrassment to such officers.</p> <p>Basel Agreement, Capital Adequacy, Single Borrower Limit, Liquidity Ratio, Ownership restrictions (7.2.1):</p>
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<p>reports/Internal circulars/ Direct observations reconstructed through the Questionnaire Two, Question (c)</p>	<p>Strict compliance of the Single Borrower Limit prevented the Soft Bank from lending to sister companies in the Soft Group. The Chairperson was not very happy about this concept since most of the group companies paid significant amount of interest to other banks on their borrowings and the process was not reciprocal because none of the other banks operated as a part of a group as the Soft Bank operated. He used to say in a lighter vein that, “the Rugged Ball technique is the best strategy for these regulators. We must do the best for the Bank and let the regulators chase behind us”.</p>
<p>Rating reports/ Interviews with colleagues/ direct observations</p>	<p>“The Chairperson plays disproportionately large role” (7.2.1):</p> <p>The Soft Bank had obtained a special approval from the Central Bank Sri Lanka for direct holding of 18% of its equity by the Soft Group. The Banking Act allows only 10% of shareholding by a person or persons who are acting in concert. But the Soft Bank had more than 50% of its ownership with the Chairperson, his wife and few companies of the Group, through indirect holdings and employee share ownership schemes, which are allowed by the Banking Act. One rating agency had reported “[T]he Bank’s Chairperson, a promoter shareholder, plays a disproportionately large role in running the Bank and particularly in setting policy. The Group’s track record in managing the Bank has not been good so far”.</p> <p>This loophole is that the special permission granted to purchase shares of a bank by its employees by creating trusts in the name of employees called a “Employee Share Ownership Plan” but the ownership is limited to five percent. Under normal circumstances banks cannot lend money to purchase their own shares but the exception is ESOP. Therefore, the Soft bank created six ESOP trusts and lent money at a concessionary rate of interest to purchase its own shares, and each trust acquired 4.99% of ownership summing up to 29.9% of ownership in total. The present owners did not inject a single cent as new capital but it was a ‘smart’ way of using others’ money to acquire the controlling power of an institution. The directors of these ESOPs are their most loyal employees such as relatives and family friends and, in this way, the Chairperson feels more powerful because he looks after not only himself but his cronies as well.</p>

<p>Annual reports/Press-releases</p>	<p>Financials of the Soft Group and the bank (7.2.1)</p> <p>The customer deposit base was three times of that of SET Bank, which was also incorporated in 1989. It was the second largest private bank in terms of customer deposits and assets and became the largest private bank in terms of the branches and number of employees by the end of the year 1996.</p> <p>However, the profitability figures were poor, reporting its Return on Average Assets (ROAA) as less than 1% and Cost to Income ratio as more than 70%, which was the highest among private banks listed on the Colombo Stock Exchange. The amount of non-performing loans (NPL) had risen to more than 20% of total loans. The Central Bank of Sri Lanka severely warned the management several times and had set time frames to address the issue immediately. The Chairperson was worried about this situation and raised doubts on the efficacy of the systems as well as the personnel of the Bank. The market price of the Soft Bank stock was also not performing in par with the industry average Price Earning (PE) ratio. Research reports on the Soft Bank, published by most of the stockbrokers were adverse with a recommendation to 'sell' or 'hold', and because of poor financials when compared to the financials published by the peer banks.</p> <p>In 1995 the Soft Bank had reported US\$3.5 million of after-tax profits. The shares had been trading with an average PE ratio of seven times, where the industry had performed at twelve times. The Cost to Income ratio worsened from 70% in 1995, to 80% in 1996. The NPL level was also on the high side with 18% in 1995 and 20% in 1996, compared to the industry average of 14%, while the CAT bank reported the best NPL ratio of 7%. The ROAA of the Soft Bank was 1% in 1995 came down to 0.6% compared to the 2% of the CAT bank and the international average was reported as 2%.</p> <p>The Capital Adequacy Ratio was reported as 8% just within the regulatory requirement of 8%. The Soft Bank was experiencing a very hard time with the external auditors and the Bank Supervision Dept. of the Central Bank of Sri Lanka with regards to the provisions to be made for bad loans. The provisions for bad debts, as a percentage of after-tax profits, was 50% for the Soft Bank whereas the industry average was only 10% in 1996. But</p>
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	<p>the deposit growth of the Soft Bank was reported as the highest in the industry with 35% growth, from US\$520 million to US\$703 million during the year 1996, compared to the industry growth of 15%. The Soft Bank achieved a remarkable loan growth of more than 54% (industry loan growth was 20%) in 1995 and 25% (Industry 20%) in 1996 contributing to the total assets base growth of 22% compared to industry average of 15%.</p>
<p>Inter-rater reliability checks</p>	<p>“Mr. Perera became all powerful” (7.2.1) Under these circumstances Mr. Perera became the all-powerful Chairperson of the Soft Bank.</p>
<p>Research reports of Stock Brokers</p>	<p>Soft Bank shares were recommended to ‘sell’ or ‘hold’ (7.2.1) The selling pressure on the Soft Bank share was aggravated by the adverse rumours spread by the dissident group, who worked for the new bank, pushing the share price further down.</p>
<p>Treasury reports – Internal</p>	<p>The Soft Bank was making a negative contribution (7.2.1) The Soft Bank had about US\$100 million invested in GS over and above the required amount for the statutory liquidity requirement. The Soft Bank was highly liquid with an extraordinary growth in customer deposit base and had reported 34% of Statutory Liquidity Ratio as against the regulatory requirement of 20%. This situation was reported to the Management by the CFO and pointed out if the bank mobilizes funds at the present rate of interest and invest in GS, without lending, the bank will make a negative gross spread (contribution) of 3% on incremental deposit funds.</p>
<p>Reconstructed direct observations Internal circulars Direct observations</p>	<p>New strategies for interest rates and lending, warning the Bank officials and comments of the officers, etc. (7.2.1) Chairperson was critical on the lending policy of the Soft Bank and the regulatory requirements such as Capital Adequacy and Single Borrower Limit, and approved the following two strategies to be implemented immediately.</p> <ul style="list-style-type: none"> • To cut the interest rate offered by the Soft Bank for deposits by 3%.

<p>Research reports</p>	<ul style="list-style-type: none"> • To introduce attractive loan products for aggressive lending, offering a lower rate of interest. <p>The CEO and the top officials of the management were very nervous about reducing the rate of interest for customer deposits, citing that the Soft Bank would not be competitive among the rival banks which were still offering the same rates. The CEO warned that there would be a ‘run on the Bank’. Chairperson queried the tolerable limit of such a ‘run’ and instructed the CFO to monitor the deposit movements daily and report if the liquidity position of the Bank was in jeopardy.</p> <p>On the other hand, the senior credit officials were severely warned and, given a massive task of achieving already increased lending targets. Marketing team was asked to make a presentation on some innovative lending products after working with the advertising agency of the Bank. The budget and the cost-benefit analysis had to be vetted by the CFO and a quick-time plan for the launch had to be tabled at the next review meeting.</p> <p>The Soft Bank lost deposits due to the lowest interest rates offered in the market but the trend was not that alarming to the liquidity position. Marketing team was very critical about the situation and warned, “Once you lose a customer, it is very difficult to win them back”. One of the popular arguments was “We worked very hard to win this customer base. The cost of regaining them, would be much more than the saving that—we get from the reduced interest rate”.</p> <p>However, it was surprising to note that all other banks followed suit and reduced their interest rates for deposits, in six to eight weeks’ time. The growth rate of deposits of the Soft Bank too returned to normal. The average interest rate offered by the banks for one year fixed deposits as at 30th June 1996, was 12%. The Soft Bank reduced that to 9% in August. In the middle of August the average rate came down to 11%, then to 10.5% by the end of the month and finally to 9% by the third week of September 1996.</p>
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<p>Central Bank Annual Reports/ Bulletins</p>	<p>Gilt edged instruments offer higher returns than bank deposits (7.2.1)</p> <p>With the change of the Government in 1994 the CBSL cut the REPO rate (Re-Purchase Offer rate; similar to the cash rate in New Zealand) and Reverse REPO rate frequently. This situation affected most of the banks with low Advance to Deposit ratio, and which had invested their funds in government securities. The REPO rate, which was at 18% at the beginning of the year 1995, was slashed frequently in 1995 and 1996 to remain at the 10% level at the end of the year 1996. The spread between the REPO rate and the Reverse REPO Rate also reduced from 3% to 2%.</p> <p>Sri Lanka had a very peculiar type of interest rate scenario where the Government Securities (GS) carried higher rates of interest than the rate offered by banks to the public for their deposits. Therefore most of the banks followed a very conservative lending policy, comfortably parking their excess funds in risk-free Treasury Bills and/or Treasury Bonds, and made an easy spread.</p> <p>This is because the GS (Treasury Bills/Bonds) were not easily accessible to the general public specially for small timers where there was a minimum amount required for investment. Also the investment and the liquidation procedures were complicated so that ordinary depositors conveniently opt for the closest, friendliest branch of a bank and invest their money in deposit products with a lower return.</p>
<p>Newspapers/ CBSL reports</p>	<p>Import-Export statistics (7.3.1)</p> <p>The total export income of Sri Lanka was US\$12,050 million in 1996, and Textiles & Garments Sector accounted for US\$6,484 million which was more than 53% of the total export income of the country and the Tony Group accounted for approximately US\$200 million in the year 1996.</p>
<p>Reconstruction of observations through the Questionnaire (1) Questionnaire (2)</p>	<p>The meeting with Tony (7.3.1)</p> <p>One Friday, while the Chairperson was conducting one of the review meetings of the Soft Bank, Mr. Tony, the owner of Tony Group, contacted the Chairperson for an immediate appointment to discuss an urgent matter. The</p>

<p>Questionnaire (1)</p>	<p>Chairperson immediately made arrangements for a quick meeting showing all the respect to another business tycoon of the country.</p> <p>Tony was adjudged the Entrepreneur of the Year in 1995. His group had accounted for a major share of textiles and garments exports, which was the largest foreign exchange earner of the island. The Tony Group expanded very fast, especially during the previous regime of Republican Government, with huge loan facilities from the government owned banks, for the setting up of factories in the rural areas. Tony Group had a very good reputation for manufacturing garments for world-renowned brands like Marks & Spencer, GAP, Van Hussein, and few others. Those buyers also had invested in high-tech equipment and quality experts in the Tony Group factories.</p>
<p>Questionnaire (2)</p>	<p>The credit proposal of Tony (7.3.2)</p> <p>He tabled the details of his factories with their capacity and locations. He blamed the newly appointed Labour government for not allocating on adequate quota for him to work on full capacity and therefore, he complained that his group was running with a negative cash flow due to under-utilization of assets. He was in the midst of a crucial issue, he said that he had no funds to pay the salary bill of the current month. The best employees were leaving the group and he said he had no option other than agreeing to the foreclosure suggested by the banks.</p> <p>He also pointed out that the new owners would not be able to maintain the same rapport with the international buyers and the whole episode would end up in tragedy, pushing 30,000 workers to the streets. He was pleading to the Chairperson to bail him out, assuring that this credit line would rejuvenate the whole group and the future cash flows would be very healthy with the orders in their hands. He also requested for a facility of Letter of Credit (LC) to import the necessary fabrics and accessories.</p> <p>On the request of the Chairperson he explained his cash flow situation and borrowing positions. The total borrowings of the Tony Group were more than US\$20 million. It comprised US\$5 million from the Bank of Lanka, US\$5 million from SET Bank, US\$2 million from</p>

<p>Questionnaire (2)</p>	<p>HAT Bank and a syndicated loan of US\$8 million from all three banks. He had borrowed from all private banks and Bank of Lanka, the State owned largest bank in Sri Lanka, which had structured a syndicated loan as well. Due to non-servicing of interest, almost all the banks had classified Tony Group as a defaulter and had reported to the Credit Information Bureau (CRIB), which is the central monitoring authority for defaulters.</p> <p>When evaluating the creditworthiness of a client, the first thing a credit officer has to do is to call for a CRIB report of the client. Tony had applied for a facility from the Soft Bank a week ago and the team leader of the Corporate Credit Division had declined it on the basis of the CRIB report.</p> <p>Tony was very convincing and very politely explained how the senior officers of the Soft Bank rejected his proposal and praised the Chairperson for his visionary leadership and patriotic attitudes in advance.</p> <p>The negotiation (7.3.3)</p> <p>The Chairperson was very upset about the situation and blamed the politicians, regulators and bankers for not identifying the needs of the country. He said, "...this is the whole problem with our bankers. They are guided by some stupid rules called banking practices and ruin people like you [Tony]. They will never think beyond that cage of banking practices. Even our State policies do not provide proper support to people like you. Now, you have generated 30,000 employments. If they lost their jobs and you lose your business, the cost will be much more to the economy in the long run, I don't know, when these people will learn these things?..." And the Chairperson said "...tell me Tony how much do you want? And what is the collateral you can offer?" Tony said, "Sir, all my assets have been taken by the banks, I can give my personal guarantee and the secondary mortgage of the assets which have already been mortgaged to the other banks, and Chairman sir, believe me and I will not let you down". "Your house?" the Chairperson queried. "That's in my wife's name and I am sorry sir, I can't draw her into this, she will eat me", Tony answered.</p> <p>Then the Chairperson asked, "Can you give your wife's</p>
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	<p>personal guarantee?” But Tony politely disagreed saying, “I am very sorry sir, but do not worry I will never let you down and I will pay every cent due to your bank on time, and I am not going to deal with any of those other banks in the future, my one and only bank is your bank for the rest of my life.”</p> <p>The Chairperson smiled and said, “Ok, tell me your requirement, have you got a good accountant? Do you have the cash flow projections?” “Yes sir, this is how we are going to manage, I need US\$2.5 million advance to pay my salary bill and other statutory dues. And I need a LC facility of US\$ 1.5 million to finance input materials for uninterrupted production.”</p> <p>“Is that all you need? Tell me right now, you will not be facilitated under the normal banking practices by our credit officers in the Bank.” Tony was jubilant and said, “That’s what I wanted Your Honor. I do not need a cent more than what is necessary.” and he invited the Chairperson to chair his board; “Why don’t you come and chair our Board meetings as well?” The Chairperson thanked him for the invitation and said, “I don’t want to interfere with your business, you are the best person to manage your business, but you can give us a good publicity.” “Of course, sir,” Tony readily agreed.</p> <p>The following day the business page of a leading newspaper carried an article saying, “Soft Bank rescues Tony Group”. The news spread fast and Tony was announcing openly that Mr. Perera helped him. He issued a special circular to the Tony Group employees saying that they all must do banking with the Soft Bank explaining that the Soft Bank was a true kind bank, while criticizing all other banks for advocating him to sell the factories.</p> <p>The Chairperson was very happy about the publicity given and the copies of the paper cutting of the news item circulated among the Board members at the next Board meeting. He assured the board that he will bring more and more business and expressed his regrets that he could have done that before; means involving more in day-to-day activities of the bank.</p>
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Questionnaire (2)	<p>The decision (7.3.4)</p> <p>The Chairperson approved all the facilities amounting to US\$4 million. He was very critical of the bank officers who rejected Tony's proposal purely on the CRIB report and said, "I think we need a good finance person, not a banker, to manage Tony's facilities," and appointed CFO as the credit officer in charge for the Tony Group. The CFO was instructed to monitor the cash flow position thoroughly and whenever there was a situation which warranted over-the-limit borrowing, he had to report to the Chairperson.</p> <p>Tony was jubilant on the quick decision made by the Chairperson and offered him a seat on the main Board of the Tony group with a brand new Mercedes, which was in the harbour, imported under the permit granted for exporters. The Chairperson politely refused the offer and appointed his CFO as an observer in the Board of the Tony group.</p> <p>The outcome (7.3.5 and 7.3.6)</p> <p>Sunil, one of long-time close confidants of Tony, was fired. He was one of Tony's joint-Managing Directors, and was in charge of the finance function. It was a known fact among the accountants that it was very difficult to work with Tony. No financial controller had worked very long periods at the Tony Group and it was not rare to notice vacancy advertisements for the post of Financial Controller for the Tony Group. Senior executives started leaving Tony Group, or were asked to leave. Sunil criticized Tony's financial discipline and always complained about liquidity problems. He complained that Tony did not transfer sales proceeds in full to Sri Lanka. Mr. Tony was very particular about the closed exchange control policy of Sri Lanka, and always had a buffer overseas. He used various tactics to keep a part of his wealth overseas and was successful in convincing the Chairperson of the Soft Bank to open a factory in an African country as well. Tony remitted money for this purpose as a capital investment outside Sri Lanka, under a special permission from CBSL.</p> <p>The Tony Group's fate is not a unique one. With the cessation of the quota system, the other countries like China and Malaysia could supply the same garments at a lower cost, therefore the buyers naturally shift their</p>
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	<p>business out of Sri Lanka for better margins. This threat was brought to the knowledge of garment businessmen, and few dynamic businessmen created their own brands and successfully transformed the threat into an opportunity. But the Tony Group was over-dependent on international brands and lost some of the contracts to Malaysia.</p> <p>After few months, the Tony Group account was taken away from the CFO and handed over to the Corporate Banking division. The new credit officer submitted a formal proposal for the Tony Group and the management approved the package recommended and extended a further facility to smoothen the cash flow.</p> <p>After four years of operation, the Soft Bank had to provide for bad debts since the Tony Group couldn't service the loan. The interest loss was around US\$0.3 million which was in interest in suspense account, and the capital write-off was nearly US\$1 million by the end of 2003. The Tony Group gradually lost their business and started to close down factories under the pressure imposed by the banks. The staff cadre had come down to 10,000 and running only 20 factories by the end of 2003. The monthly sales of US\$2 million in 1998 had come down to US\$1.5 million in 2003 and was virtually making a negative contribution.</p>
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