Chapter -II

Review of literature
CHAPTER PROFILE

Chit funds have become an integral part of the financial system under the umbrella of Non-Banking Financial companies and moreover served as a significant stream for mobilization of savings for channelization for economic activities. On the other hand these have increasingly become a dominant financial intermediary for enriching the economic life of individuals through the means of cooperative funding. Despite a saga of history across the countries, worth mentioning studies in the direction of chit fund industry is much lacking. But to highlight the place and prominence of the present study and also to identify the research gap some of the studies in the area of chit funds and NBFCs in general have been reviewed for comprehension in the present chapter. The literature review includes in its fold the studies on NBFCs in general and also the chit funds in particular. A journey through the literature clearly shows that the studies so far on the NBFCs in general, on the chit funds in particular are mostly descriptive, role highlighting. Even though some critically analytical studies exist they are confined to the operational aspects and regulatory modalities. In this context, the present study well fits in the research gap of the absence of an exploratory empirical study on the chit funds. The present study is not only exploratory in its analysis but it is also a focus study of the perceptions of chit fund subscriber/members besides the operational/managerial staff of the chit fund companies both registered and unregistered.
LITERATURE REVIEW

The concept of chit funds according to Simcox\(^1\) is originated more than 1000 years ago. And it is mentioned, Dravidian kuri is used for raising money for some special purposes.

Subbarama aiyar\(^2\) has described the working of ‘changati kuri’, where lot decides the person every month to whom the amount is to be paid. The chit fund offers money at a flexible interest rate and the interest rate depends on the demand of the money.

The Travancore Banking Enquiry Commission and Travancore Companies Act\(^3\) recommended that the banks in the state were prohibited from conducting kuri business. But after Independence following the extension of the Indian Companies Act (1913) to Travancore State, the position changed and banks restarted the kuri business with effect from 1\(^{st}\) April 1951.

Banking Companies Act\(^4\) regarded kuries as an agency business which banks could take up and therefore, chit fund business re-emerged as an essential segment of the operations of several banks in South India.

William Logan\(^5\) mentioned the presence of a flourishing Kuri or lottery system existing in the society. He also described the operation of kuri system among friends known as ‘Changaathi Kuri’.

V.Krishnan\(^6\) mentioned the growth, importance, types, features and malpractices of chit funds. The favouring circumstances that fostered the growth of the chit funds were the

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3 The Travancore Banking Enquiry Commission and Travancore Companies Act, (1938).

4 Banking Companies Act, (1949).

lack of organized credit facilities to permit of savings deposits, the accommodation of small capital and the availability of loans on easy terms. The dominant feature of the transaction is that it enables a large number to gradually lay by money to receive their savings in a lump sum, and the scheme in their case is an incentive to thrift.

The chit funds show a great deal of adaptability to the conditions that prevail in the area in which they have to operate. The indebted landlord, the needy trader, the improvident weavers and other artisans, the hard working daily labourers and factory workers and the helpless vegetable vendors all derive benefit from the transaction. There are importantly three types of chits, (1) The Thattu chit, (2) The Auction chit, (3) The Prize or the lottery chit. It is inevitable that there are a variety of malpractices in the system. If such malpractices are only lapses that are bound to exist in any institution then efforts should be taken to bring the working of such institution under rigid control to reduce malpractices to the minimum.

According to S.K. Basu⁷ A Non-Banking Financial Company (NBFC) is a company incorporated under the companies Act, 1956, and conducting the financial business as its principal business. In India, the Non-Banking Financial sector comprises a multiplicity of institutions, which are defined under section 45 I(a) of the Reserve Bank of India Act, 1934.

C.D.Campbell and C.S. Ahn⁸ are documented the existence of kyes in Korea. Korean ROSCA called the kye. Kyes gained popularity after the Korean War. According to Campbell and Ahn, in June 1959, out of 2,691 households sampled, 1,603 were liable for debts. Approximately 8 per cent of the borrowers obtained their loans from banks. The

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bulk of the borrowers obtained their loans from individuals and acquaintances. Campbell and Ahn interpret the last category as referring to loans through kyes.

Ardener\(^9\) explained that the member who defaults in one ROSCA may suffer to such an extent that he may not be accepted as a member of any other. In some communities, the rotating credit institution has become so rooted in the economic and social system that exclusion would be a serious deprivation.

M. S. Joshi\(^10\) explained that, financial intermediaries acquire unique importance in the developing economy as they perform multifarious activities in a development process. Their main function is to purchase primary securities from ultimate borrowers and issue indirect securities to ultimate lenders. Financial intermediaries responsible to some extent for (a) sponsoring or (b) encouraging or (c) discriminating between, various industries whereby sectoral balance is affected.

Srinivas and Higuchi\(^11\) observed that Chit funds have been grouped under the category ‘Mutual Credit Suppliers’, because the demand and supply of credit is mutual—that there is a give and take process involved. Participants typically support each other for credit needs in mutuality. The money supplied or saved by some participants is lent and borrowed by some other participants. Thus the benefits of the operation are mutual to all participants and equally distributed. The central idea of mutual credit suppliers is that they encourage savings from the participants.

Sreedharan Menon\(^12\) presented the position of the Chitty/Kuri business in the state of Kerala and traced out the need for bringing Chitties/Kuries under social control. The

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\(^9\) Ardener, “The Evolution of an Informal Financial Institution: The Rotating Savings and Credit Associations in Cameroon” (1964)


\(^12\) Sreedharan Menon, K.A. Schemes for starting Chitties under State Auspecies, Government of Kerala, (1967), p.16.
necessity for a separate legislation to Chitties/Kuries throughout Kerala has also been emphasized in the study.

According to the information given by **The Banking Commission**\(^{13}\) nine banks in Andhra Pradesh, Kerala, Mysore and Tamil Nadu were conducting chit funds in 1968.

**Dr. C.P.S. Nayar**\(^{14}\) had tried to place the role of Chit Funds in the proper financial perspective. The study emphasized the need to regulate the activities of Chit Funds, and at the same time, perceived their role as active mobilisers of savings of the community and as a useful complement to other financial institutions. The work was an attempt to study all the known types of chit funds, classifying, naming and defining them wherever necessary. The study also attempted to examine the economic aspects of chit funds on an empirical and analytical basis. The analysis covered all the patterns of business of chit funds working throughout the country.

The Author also pointed out that the basic principle underlying a chitty is accumulation of savings. The unique feature of savings in a chitty as against the savings in other types of financial institutions such as commercial bank, the post office savings bank, etc. is that there is a sort of compulsion in effective savings. While examining the history of chit funds, Nayar has also discussed different stages of their evolution. Stated that the original home of chit funds is South India, in the last three decades there has taken place a growth of chit funds in several parts of India. He has mentioned the growth of chit funds in the Union Territory of Delhi and in the state of Maharashtra. He estimated the annual turnover of business of 125 chit companies at ₹217 lakh, in Maharashtra and in Delhi, 109 registered companies with annual turnover of ₹6 Crore, by the end of 1968-69.

\(^{13}\) The Banking Commission (1969)

The Travancore-Cochin Banking Enquiry Commission\textsuperscript{15} stated that more than 166 banks were conducting kuries during the thirties in the erstwhile princely state of Travancore.

K. Balakrishna\textsuperscript{16} mentioned that the activities of companies conducting prize chits are not clearly prohibited by the existing legislations. The resources of prize chits are used for wasteful spending and hoarding commodities and that these schemes enable certain persons to convert tax-evaded income into accounted money. The persons concerned pay a premium to the promoters in return for the facility. It has also been stated that there are a number of agents who go about contacting persons who are likely to face the problem of saving their income from the tax authorities. The prize chit pass books are issued to them under different names become their passports for traveling from black money territory to the white money area-the easiest and surest way of using ill gotten wealth. Besides, by their misleading names and campaigns the prize chit companies divert private savings into their personal drains, thus disrupting the national economy.

According to R.G. Saraiya\textsuperscript{17} the annual savings mobilization through chit funds is in multiples of 100 crore. Though these savings are less comparing with commercial banks, the number of people benefited by chit funds is quite large. He has bring forth the recommendations of the Banking Commission, which has recommended that the State Governments may consider Starting Chit Funds at strategic places as model foremen with the object of offering effective competition to private chit funds and thus acting as a disciplining factor.

As it is suggested by S. Y. Krishnaswamy, I. C.S\textsuperscript{18} the object of the Chit funds should be to serve the poor and middle class and the average traders. It need not undertake the

\textsuperscript{15} The Travancore-Cochin Banking Enquiry Commission (1974)


\textsuperscript{17} R.G. Saraiya, Chairman’s Address, At the IFMR Seminar on Chit Funds and Finance Corporations, Madras, October 4-5, 1974.

\textsuperscript{18} S.Y.Krishnaswamy, Presidential Address, At the IFMR Seminar on Chit Funds and Finance Corporations, Madras, October 4-5, 1974.
financing of bigger operations by persons who can avail themselves of other credit facilities. He also mentioned that, the major causes of failures and malpractices by chit fund companies are transfer of funds from one place to another.

According to S. Radhakrishnan\textsuperscript{19} Chit funds grew at a time when banking and credit facilities were inadequate and people in general had to rely to a large measure on indigenous sources for their many productive and consumption needs. Despite of the wide expansion of banking and credit facilities and a number of savings media such as postal savings, small-savings schemes, unit-linked insurance, recurring deposits schemes for various needs, chit funds seem to continue to be popular with certain sections of the community. It is also mentioned that people are not fully aware of the risks and costs involved in relying on this financial institution.

Shri K.M. Balavenkataraman\textsuperscript{20} Studied about progenitor Moyy Murai. Moyy means call money pooled and Murai means custom. It was a sahaya-nidhi, with a strong element of co-operative spirit. The principle of chit fund was known to rural India for a fairly long time. For years, women in villages had formed the habit of saving a handful of rice or other grains for a rainy day, and this became very useful to face unexpected guests and unforeseen expenditure. A chit fund is a financial arrangement or institution based on mutual trust and confidence. A chit fund is primarily a mutual benefit society in which some people join to save and others to borrow. A financial intermediary gathers the savings of the people and distributes the funds to numerous borrowers, thus affecting the allocation of real resources. The difference of a financial intermediary and a chit fund is, chit fund collects the savings of the members by periodical subscriptions for a definite period of time, and it connects the borrowing class directly with the lending class and the pooled saving is lent out to the same group of savers.


In so far as the chit funds have no control over the end-use of the funds, the intermediation does not necessarily result in an efficient use of resources. The efficient use of resources takes place only in the case of those members who utilize the prize amount in acquiring income-earning assets, which directly or indirectly promote capital formation. It is therefore; better to consider chit funds as a co-operative endeavor.

The study of Dr. C.P.S.Nayar\(^1\) highlighted that the chit funds is different from other savings and credit institutions in that it is more than a savings bank to the saver and more than a lender to the borrower. The chitty offers many facilities to the borrowers. (1) The loans in most cases are unconditional. (2) They are clean loans. Tangible assets are rarely used as security. (3) They can be rapid in easy installments. (4) The borrower need not keep a margin for the loan. The increasing popularity of chit funds even in those areas where the banking habit of the people is wide spread shows that the scheme is basically sound and cannot be brushed aside as an irrelevant or anachronistic business practice. It becomes easy when the chit funds are operated by disciplined institutions such as the commercial bank, a Government owned company or a public limited company.

Dr. V.T. Mathews\(^2\) strongly argues in favor of commercial banks entering into the chit fund field on the plea that such entry would help safeguard better the interests of small savers and reach out to the wider sections of the society which are important to banks in the present setting. Commercial banks with their reputation for solidity and efficient management will be able to ensure the safety of funds contributed by subscribers. And if banks take up chit funds, they would be arming themselves with an instrument which is capable of meeting the other requirements of the small man.


R.Kalyansundaram\textsuperscript{23} opined that the chit funds have doubtless a positive role in the economy of the country and a separate department for chit funds to control them is an essential need. A commission at Government level is necessary to be set up to go into details of their working, giving chit funds an opportunity to represent their case.

G. Jagadisan\textsuperscript{24} indicated that, some measures of regulation of chit funds. Chit funds like any other non-banking financial institution are treated as Para-banking institution. It has been recognized that chit funds arose at a time when banking facilities had not developed and thus they filled an important credit gap in the economy. Another important aspect is that many companies are coming to rely upon chit funds as a source of finance. The fact that the strength to a chit fund company is the foreman and his reputation for promptness, straightforwardness and honesty. It is very essential that the number of chit companies in each state is reduced over a period of time so that supervision and control become effective. Every chit company should obtain a license before commencing its business. And also the company should be issued the license only if it furnishes the bank guarantee. Government should use the banks as agents to supervise the working of chit funds. Besides it will make the Reserve Bank to exercise some control over chit funds.

As mentioned by M. A. Sreenivas\textsuperscript{25}, in his study on Finance Corporations, Chit funds are conducted by the finance corporations on a large scale to collect funds from the public easily. Being unincorporated bodies, these organizations should not accept public deposits from the public. And he suggested that, before granting them license the Reserve Bank has to investigate the background of these organizations.


S. Narayanaswamy\textsuperscript{26} addressed that chit fund was attractive in so far as it proved a ready-money bank for the subscriber, what time it was equally attractive for the enterprising foreman, who got the feel of the subscriber’s monthly contribution on which he paid no interest, though he was free to earn it himself by sagacious and shrewd investment. The five per cent commission is the wage for his organizing the outfit. Chit fund was born and has stayed to serve the needs of a closely knit community of people living very near each other often in the same village, each of whom was keenly conscious of the rainy day that might call abruptly for a large sum of money. Communications were tenuous or did not exist. Perhaps, the close proximity of all subscribers made for smooth and successful conduct of the chit operations.

Bouman\textsuperscript{27} mentioned that, group of farmers form associations, and the members of the associations make periodical contributions that are pooled in a fund from which loans are made. The total fund is given to each of the members on rotation basis until everyone has had a turn. This is an informal mechanism which has great adoptability to the local conditions and is very successful. These associations are named as rotating savings and credit associations (ROSCAs).

Dale Adams\textsuperscript{28} showed that substantial potential exists for mobilizing savings from rural households in developing countries. Opportunities to save and incentives to save are key factors in developing this potential. He argued that many low-income households in many countries do not save because they do not have opportunities or incentives to entrust their savings to financial institutions.

\textsuperscript{26} S. Narayanaswamy, Presidential Address ‘Model Chit Funds Bill’ edited by S.Radhakrishnan, IFMR, Madras, 1976.


Padmanabha Menon\textsuperscript{29} stressed on the role of kuries and according to him, Kuries developed as a source of finance in Malabar District in the 8\textsuperscript{th} century A.D.

Nayar\textsuperscript{30} attempted a comprehensive study of finance corporations and similar indigenous financial institutions. The study tried to examine their role and operations in rural and urban areas, to identify the factors leading to their growth, and to examine the existing legal framework of regulation and suggest changes if any. The study emphasized the need for strengthening the self-regulatory measures of the corporations and also for introducing some outside controlling measures to make up the deficiencies in self-regulations.

Ligeti sandor\textsuperscript{31} revealed that, the rotating savings and credit associations (ROSCAs) have versatile role in the developing countries.

Nayar\textsuperscript{32} pointed out that Chit Funds have come to stay as a unique non-banking financial intermediary in India especially in South India. He also pointed out that the rationale of an auction Chitty or Business Chitty is that the borrowers and lenders meet to fix the rate of interest and since there is more than one borrower competing for the same amount, a competitive rate of interest is offered. Only the members enjoy the benefits of the scheme. The study highlighted the fact that for the subscribers, the return on subscriptions was not the only consideration. The possibility of getting a lump-sum on easy terms at short notice was a great inducement. Hence, it is advisable to retain these within the framework of non-banking financial institutions controlled under chit funds act 1982, by the state government.

\textsuperscript{29} Padmanabha Menon, K.P. History of Kerala, (Ed.) Asian Educational Services, New Delhi, Vol.1.(1982)


\textsuperscript{31} Ligeti sandor, “Rural Savings and Agricultural Credit” Savings and Development: Proceedings of a Colloquium, Paris (1984), P.87

According to Nayar\(^{33}\) the Indian ROSCA is commonly known as chit fund or chitty. The chitty was very popular among women, who saved a handful of rice from each daily meal to contribute to their rice bank. They invested the proceeds of chitty in gold ornaments, household utensils or small livestock. The Indian money ROSCA knows three basic variations of the rotation principle. The first is the lottery type, in which lots are drawn to decide whose turn it is to receive the fund. The second is the lottery with discount; a small sum is deducted from the fund and distributed among the members. The third type is the auction ROSCA in which members bid for the fund. The fund goes to the bidder offering the highest amount of discount.

Mohandas\(^{34}\) Attempted to evaluate the Central Chit Funds Act 1982 as a regulatory measure for chit business. And also deal with the features of Chit finance, conceptual issues involved in chit fund regulation and also with the economic implications of the major provisions of the Act. The study suggested a graduated ceiling on discount ranging from thirty to fifty per cent for chits of different durations. To eliminate unnecessary competitive bidding, the study recommended restriction on open bidding up to twenty five or thirty per cent of the chit amount and allow further bidding up to fifty or sixty per cent only on the production of cash deposits above the initial limit. The study also analyzed the economic gain to the saver and cost of borrowing in terms of effective annual interest yield and effective annual interest cost.

F. J. A Bouman\(^{35}\) explains most of the countries in the Third Word have experimented with designing financial systems to service the weaker sections of the rural economy. Cooperatives, commercial banks, and specialized farm credit institutions have been encouraged to dispense low-priced credit among rural borrowers and to compete with informal financial intermediaries for the clientele of the poor. And it is mentioned by


him, that despite the huge subsidies and easy access to public funds, most systems proved not viable as the costs were higher than revenues. The rural masses in less developed countries still rely predominantly on the financial services of informal lenders. Informal lending has a number of favorable features. The most important one is that it has been part of the rural economy for centuries. Informal lenders have adapted their systems to rural conditions and culture. They operate with minimum cost without costly buildings, staff, and paperwork. Because of proximity, they have knowledge of the creditworthiness of the borrower. While formal credit systems are weak and unable to adopt the rural conditions.

Mauri et al.\textsuperscript{36} observed in Ethiopia, “Equb” is a ROSCA which is mainly concentrated in the urban conglomeration. What makes Equb distinct from formal sector financing is that it caters to the less privileged strata of the Ethiopian society-weavers, potters, carpenters, shoeshine boys, “tela”, an “tej” traders(local drinks made of barely and honey respectively) etc. This ROSCA is thinly spread in the rural hinterland. In a situation where not just a few but all farmers have an urgent credit need at the same time to meet planting and harvesting expenditures, it becomes difficult to meet the credit needs of all farm households simultaneously. Moreover, in a setting which is basically subsistence, the irregularity and low per capita income precludes the effective functioning of ROSCAs in rural areas. The most common form of Equb is the one where payment is effected in monetary terms. However, contributions can also be arranged in kind.

F.J.A. Bouman\textsuperscript{37} discussed the financial intermediation, formal and informal financial sectors and rural finance. Financial institutions can play an important role in the growth and development of an economy by channeling funds from surplus sectors (savers) to deficit sectors (investors).


The third world countries are particularly committed to rural development, and majority of rural households is dependent on informal intermediaries for their daily financial needs. Financial markets contain a formal and an informal sector. The formal sector is institutional and officially monitored and regulated, comprising the banks, co-operatives and special public credit institutions and projects. The informal financial sector is known by many other names: unregulated or unorganized markets, informal finance or indigenous financial market. It is usually believed that the volume of rural informal finance in Asia exceeds that of formal finance, because of the widespread absence of banking institutions in the countryside. Representatives of developing nations now seldom express the view that to advocate support of ROSCAs is tantamount to efforts to keep their country from entering the era of modern finance.

**Dasgupta**\(^{38}\) who made four case studies of money-lenders in rural India, explains that default is only 23 per cent of the interest rate charged.

**World Development Report**\(^{39}\) Has presented Rotating Savings and Credit Association (ROSCA) as a popular form of informal finance in a number of countries, which intermediate in the most basic way. The money collected (the fund) is given in rotation to each member of the group. The popularity of ROSCAs among low and middle-income groups shows that people like to save even under trying circumstances.

**The Asian Development Bank**\(^{40}\) Lauded chit funds as the only system for both saving and borrowing effected under mutual help with dignity, scoring over other savings, credit and investment options being so flexible in operation. Their strengths, weaknesses and potential therefore deserve serious study on par with the rest of the more conspicuous denizens of the financial domain.

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Shanmugan\textsuperscript{41} observed in the French speaking African countries, the common use of the word “Tontine” for ROSCA, derived from the Italian count Tonti, has prompted speculations that the ROSCA originated in Europe about 1653. Annuity shared by subscribers to loan, the shares increasing as subscribers die till last survivor gets all. Particularly that “Last survivor gets all” has inspired many exciting tales of greed, murder and horror by fiction writers. Shanmugan, having consulting the Encyclopedia Italiana, shows a more conservative Tonti, a Neapolitan banker whose “device was more of an insurance scheme involving State Participation.

Aleem\textsuperscript{42}, found that, the median rate of default across money-lenders in Pakistan is just 2 per cent. The cost of capital for the money-lenders was 32.5 per cent in a year when banks were only paying 10 per cent for their deposits.

Itoop M.L.\textsuperscript{43} has identified the factors leading to the growth of Chit Funds in Kerala especially in the 1980’s. He also examined its utility as a saving instrument and supplier of easy credit and thus employment potential. The findings of the research revealed that Kuries help industry, agriculture and even house construction. The only unproductive expenditure related to the money spent on marriages and on durable consumer goods. The study also found that the cost of credit is cheaper compared to the cost of credit with reference to the commercial banks other financial institutions.

A case study conducted by Jose KG\textsuperscript{44} with reference to three panchayats in Kerala revealed that in all three Panchayats, namely thazhava, Pananchery and Muttil, 191

\begin{thebibliography}{99}
\bibitem{44} Jose, K. G. “Rural Transformation in Kerala: A Case Study with Reference to Three Panchayats”, Ph.D Dissertation, Cochin University of Science and Technology, Cochin, (1990).
\end{thebibliography}
persons out of 228 (84%) surveyed had savings in the form of Kuri. The Kuri amount when obtained was generally utilized for house construction, purchase of land, marriage, etc.

According to Dimitri Germidis\textsuperscript{45} the ensemble of financial circuits in the developing countries is composed of the formal and informal sectors together. Three basic types of informal financial operators can generally be distinguished: individual moneylenders; groups of individuals organized mutually; partnership firms. The informal financial activity by Group of individuals generally organized mutually and subject to the rules and regulations of functioning which they themselves have lay down and agreed upon. The two main types of informal associations, which also assume a function of social protection, are: savings arrangements only (fixed-fund associations, savings clubs); combined savings and credit arrangements where regular participation in the savings accumulation process entitles a member to loan facilities with or without interest from the group.(mutual aid associations and ROSCAs.)

Prabhu Ghate\textsuperscript{46} examined the role of informal finance in most Asian countries. The form of informal finance that makes the greatest contribution to additive savings (that is savings that would not have been mobilized anyway by the formal sector in the absence of the informal) is mutual finance. The study noted the possibility also of an indirect effect on savings through the higher productivity of investment stemming from increased allocative efficiency because of the higher volume of intermediation made possible by the informal sector.

Joseph M A\textsuperscript{47} evaluated various savings / investment schemes available in comparison to the chit schemes. It showed that chit schemes can be treated as the best investment alternative available. The rate of return on chit was calculated by dividing the annual

\textsuperscript{45} Dimitri Germidis, Interlinking the Formal and Informal Financial sectors in Developing Countries, Savings and Development-No.1-(1990)-XIV, pp.5-22.


dividend by the annual net subscription. The study showed that the rate of return calculated for a chit was much more than the rate of return applicable to the various investment alternatives. It also presented the various characteristics of chit schemes and concluded that unauthorized chit business was in the ruins due to hard and stringent provisions of the enactments and KSFE was far away from the reach of the common people.

**Nayar**\(^48\) Describes four major types of informal finance in India and identifies their strengths. It is argued that informal finance is often conducted more efficiently than formal finance in terms of loan processing, the ability to make small and short term loans, and effective loan recovery.

**Otto Hospes**\(^49\) is of the view that Financial and quasi financial services in low-income countries that are used by poor people on a large scale, are those provided by merchants, pawnbrokers, loan brokers, landlords, friends and relatives, money guards, ROSCAs and ASCRAs. The most appealing one among all the above is ROSCA (Rotating savings and credit Association). The pressure on scarce money resources due to lack of dependency of the banking system and illiquidity preferences refer to savings practices that constitute a socially acceptable argument to deny claims for financial assistance from people belonging to the same social or socio-spatial unit. The most sophisticated and widespread examples of such a savings practice are the ROSCA and ASCRA (Accumulating Savings and Credit Associations).

**Baby Soosy**\(^50\) found out that the most accepted form of saving for the respondent households was chitties (28.2%). Deposits with banks formed 18.64% of the savings,

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Provident Fund and LIC accounted for 7.76 per cent and 6.64 per cent respectively. The study also showed that of the types of chits, monthly chits seemed to be more popular.

**Timothy Besley, Stephen Coate, and Glenn Loury**\(^{51}\) studied the economic role and performance of ROSCAs (Rotating savings and credit associations), which is an informal financial institution prevalent in developing countries and also used by immigrant groups in United States of America. They studied two important types of ROSCAs, Random ROSCAs and Bidding ROSCAs. Each type of ROSCA allows individuals without access to credit markets to improve their welfare. They have assumed on preferences, random allocation is preferred when individuals have identical tastes. This conclusion need not hold when individuals are heterogeneous. And they have also discussed the sustainability of ROSCAs given the possibility of default. ROSCAs provide a means of making joint savings work.

**Besley et.al.,**\(^{52}\) states that the ROSCAs use pre-existing social connections between individuals to help circumvent problems of imperfect information and enforceability. And also they argued that, on average, ROSCAs allowed members to enjoy the benefit of the pot earlier than if they were saving at home.

**Nancy Horn**\(^{53}\) observed in Zimbabwe the involvement of entrepreneurs in savings clubs appears to have grown time to time. The per cent of Zimbabwean vendors belonging to some kind of savings club is as high as 64 per cent.

**Besley T. Coate, S. & Loury, G.**\(^{54}\) examines the allocative performance of rotating savings and credit associations (ROSCAs), a financial institution which is observed


world-wide. A model is developed in which individuals save for an indivisible good and study ROSCAs which distribute funds using random allocation and bidding. The allocations achieved by the two types of ROSCAs namely, random ROSCA and bidding ROSCA are compared with that achieved by a credit market and with efficient allocations more generally. A random ROSCA may sometimes yield a higher level of ex ante expected utility to prospective participants than would a credit market.

**Manjeshwar Ananth Pai** argued that chit funds can be considered as mutual benefit associations. Accordingly income derived from such association has been exempted from income tax on the ground of mutuality. Since the basic proposition in the context of taxation is that no one can make a profit out of himself and this proposition still holds good when a number of individuals join together and contribute to a common fund in pursuance of a scheme for their mutual benefit having no dealings or relations with any outside body.

**S. Radhakrishnan** argued that Chit Funds and Nidhis have not received the attention they deserved in the scheme of reforms. The paper included certain measures of reforms to enable Chit Funds to grow on sound and healthy lines, including the introduction of credit rating for all incorporated Chit Fund companies.

**Indira Rajaraman** tried to explain Rotating Savings and Credit Associations and their similarities with Chit Funds in India. The article showed that these associations are functional in various parts of the world including highly developed countries. Random ROSCAs are similar to Prize chits in India, while bidding ROSCAs are similar to our Auction chits.

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According to Bouman, F.J.A.⁵⁸ Financial self help groups in low-income countries consist of two basic types, Rotating and Accumulating Savings and Credit Associations, or ROSCAs and ASCRAs. In ASCRA, funds are not immediately withdrawn but are left to grow for loan making.

F.J.A. Bouman⁵⁹ explained ROSCA stands for Rotating Savings and Credit Association. The logic of collective action and mutual aid in a rotation of resources has made the ROSCA a universal phenomenon, occurring all over the world. Bouman in this article presented the origin and development of ROSCA system all over the world. ROSCAs existed long before the introduction of money into an economy, when the means of payment consisted of rice, cowries, and bronze rings of strips of raffia cloth. The ancient Indian “Chit fund”, already in existence before the advent of British rule, originally consisted of grain-contributions and only later changed into a monetary “Chitty”. In Japan, the earliest records of ROSCA-with contributions in money-date back as far as 1275. In Korea, the “kye” (Korean ROSCA) may even go back to the 9th century. In Africa, ROSCA (called as “esusu”) appeared in the economy somewhere around the mid 19th century. ROSCA originated in Europe about 1653.

S. Krishnamurthi⁶⁰ critically presented the recommendations of Banking Commission in 1974 that it is essential to have uniform chit fund legislation applicable to the whole country. A central legislation besides enduring uniformity in the provisions applicable to chit fund institutions throughout the country would also prevent such institutions from any state to exploit the benefit of any lacuna or relaxation in any other state law by extending their activities in such States.

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⁵⁹ F.J.A. Bouman, ROSCA: On the Origin of the Species, Savings and Development-No.2-(1995)-XIX.

Klonner, S.\(^{61}\) observed that aggregate factors like seasonality in agriculture and harvest failures are reflected by ROSCA auction outcomes and that bidding in ROSCAs with a big contribution is substantially different from bidding in ROSCAs with small contributions. And also if a ROSCAs group can adopt less aggressive bidding, social gains can be realized. So groups of experienced organizers bid less aggressively than groups of new comer-organizers. Moreover groups which have operated more than one ROSCA before bid less aggressively than ROSCAs groups with no or only a short history. When the bidder has a pecuniary emergency like the marriage of a daughter or the need to repair his house and this information is revealed before the auction, auction outcomes are more favourable for the winner. This indicates certain degree of mutual cooperation among the participants, when information is public.

According to S. Krishnamurthi\(^{62}\), Financial intermediation is the process through which the differing needs of ultimate savers and ultimate investors and consumers are reconciled. The financial intermediaries perform the function of transferring funds from persons with excess of money to persons who require extra funds to fulfill their expenditure or investment plans. They are responsible for channeling savings to investment and consumption purposes and without them many of the funds in the economy would remain idle. With the inadequacy of the public financial institutions and the services provided by them companies were set up in the private sector under the Companies Act whose main business was to do non-banking financial business. These non-banking financial companies in the private sector have created a major impact for innovation during the last four decades in the post independence era.

Besley and Levenson\(^{63}\) documented the existence of ROSCAs in Taiwan called the hui. Levenson, A.R. & Besley, T\(^{64}\) analyzes participation in rotating savings and credit

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associations using a national household survey from Taiwan. They found that participation is highest among high-income households. There is some evidence that income stability may play a role as well. Life cycle differences suggest a role in funding durable purchases. Their evidence indicates that ROSCAAs may be an alternative savings device to the formal financial sector.

W.N.Shahin\textsuperscript{65} opined that the presence of informal loan markets leads to a different sequence of results due to the increase in the cost of working capital caused by contractionary monetary policy. Credit rationing in the formal sector forces many firms to seek informal loans. This behavior causes an increase in the informal loan rate and thus, the cost of working capital.

Rajendran\textsuperscript{66} attempted to provide a brief resume of the evolution of credit in Kerala, the different practices and the institutions concerned, since the beginning of the 19\textsuperscript{th} century. The role of chitties in terms of their number, extent and volume of operation up to 1936 has been included in the study. The study pointed out that the vital links between the pre-institutional and the institutional phases were provided by Chit Funds which gradually emerged into banking institutions.

Otto Hospes\textsuperscript{67} focused that the most elaborate technique of mutual aid is the ROSCA with a marriage ceremony. The nearest kin and closest friends of the bridal couple assemble at the house where the ceremony is to take place. They are expected to help decorate the place, to cook the rice, prepare the other food and drinks and serve the guests. Guests to the party make contributions in kind, that may range from a bag of


\textsuperscript{65} W.N.Shahin, Financial Liberalization and Informal Finance, Savings and Development-No. 1-(1996)-XX, pp.105-115.

\textsuperscript{66} Rajendran, G.K. Rural Credit Market: Anmol Publication, New Delhi, (1997).

\textsuperscript{67} Otto Hospes, New Studies on Informal Finance: Exploring the State- of- the art and the Art of the State, Savings and Development, No.1-(1997)-XXI, pp.5-17.
paddy, a chicken, a piece of cloth or any other household item. The wedding ROSCA combining labor, kind and money contributions is still popular in today’s Indonesia.

**Van der Brink, R. & Chavas, J.P.**\(^{68}\) analyzed from a micro perspective a particular variant of financial intermediation that remains popular in many parts of the world, even where formal credit markets exist and are relatively well developed. ROSCAs are a type of credit associations playing the role of an alternative credit institution to the formal financial sector. These ROSCAs are commonly found in the rural and urban economies of much of sub-Saharan Africa and are popularly known as ‘njangeh.’

**Mark Schreiner and Geetha Nagarajan**\(^{69}\) examined that, Accumulating Savings and Credit Associations (ASCRAs) reach poorer borrowers than do Rotating Savings and Credit Associations (ROSCAs). They have mentioned that all these informal finance institutions work on five basic virtues: slashed transaction costs, supply of savings as well as loans, substitution of confidence for collateral, socially enforced and/or self enforced contracts, and sequence of repeated interactions. It is also stated that the publicly observable characteristics help predict credit worthiness. Informal lenders are good judges of creditworthiness. And they consider females to be more creditworthy. Second, the ASCRAs and ROSCAs reach borrowers of similar levels of poverty. Publicly observable characteristics do not help predict the matching of borrowers with an ASCRA rather than with a ROSCA.

According to **Colomiris and Rajaraman**\(^{70}\) ROSCAs do exist that fulfill durable financing and insurance needs. ROSCAs may be viewed as a substitute to insurance, especially in developing countries where markets for insurance either do not exist or do

\(^{68}\) Van der Brink, R. & Chavas, J.P (1997)


not function well. This applies only to bidding ROSCAs. Some bidding ROSCAs in India contains insurance components.

Harper, A.\textsuperscript{71} stated that using groups as forums through which to provide savings facilities and as channels for delivering credit is widely accepted as a successful way of overcoming many of the problems associated with providing microfinance services to the poor. It differentiates between the well-known Grameen Bank model and an alternative model based on larger and more flexible groups, in which a lender ‘wholesales’ a loan to a group, which is then left collectively responsible for on-lending smaller loans to the individual members. The potential advantages of this model over the ‘Grameen’ model are considerable lender support is required, and is likely to consist of training, advice services and monitoring, balanced with a flexibility which allows groups to develop their own systems to meet the particular needs and demands of their members.

The study of Handa and Kirton\textsuperscript{72} pointed out that the key in success of ROSCAs is the social collateral that ensures sustainability. It has been discussed that defaulters would not only be sanctioned socially but also prevented from further ROSCA participation.

As mentioned by Leonard TeRuindjo\textsuperscript{73} the Rotating Savings and Credit Associations in Cameroon showed that the Rotating Savings and Credit Associations (ROSCAs) mobilize resources, which would have been hoarded otherwise. The study revealed that ROSCAs accelerated the speed of circulation of money. The study also showed that the proliferation of these ROSCAs can be explained by their easy adaptability to the economic and social transformation of each epoch and by the inability of the formal financial system to integrate the local realities in its relationship with its customers.


Kimuyu, P.K.\textsuperscript{74} suggests that rotating savings and credit associations (ROSCAs) improve welfare by reducing the utility cost of saving for a consumer durable. The study in East Africa reveal major differences in the incidence of ROSCAs participation arising, conjecturally, from differences in the relative depths of market penetration and perceptions about the efficacy of alternative strategies for compensating for failures in the financial markets. Participation in ROSCAs in these communities is partly driven by the need to raise school fees, meet medical expenses and buy food. ROSCAs funds are also used to start or promote small businesses and acquire assets, including livestock. Households owning smaller landholdings and those enjoying higher expenditures are more likely to participate in ROSCAs funds while contributions and value of receipts are determined by total expenditures and frequency of turns respectively.

Kovsted, J. & Lyk-Jensen, P\textsuperscript{75} observed the performance and efficiency of random and bidding rotating savings and credit associations (ROSCAs) are compared within a game theoretic model. Information about individuals return from investing the ROSCA pool is assumed to be asymmetric and imperfect, and ROSCAs members are allowed to use funds raised outside the ROSCA to supplement the funds raised in the ROSCA. The conclusion is that although both types of ROSCAs can improve individual welfare, the bidding ROSCA is preferred to the random ROSCAs expect when credit from other sources is costly and types of ROSCA members are not widely dispersed.

Stuart Rutherford\textsuperscript{76} states, that the lack of access to reliable savings accounts appears common to the poor everywhere. The poor use many strategies to deal with this problem. They form savings clubs where each person makes sure that the others save. Self-Help Groups (SHGs), popular in India and Indonesia are saving clubs which also make loans to their members out of the accumulated savings. Rotating Savings and Credit


Associations (ROSCAs) allow people to lend their savings to each other on a rotating basis.

According to Binu Domnic\textsuperscript{77} chit funds in the formal sector also conduct informal business. The informal credit institutions play important role in mobilizing savings to different categories of people in the society.

Olubiyo, S.O. & Hill, G.P\textsuperscript{78} vehemently stated that a large proportion of economic activities in many developing economies are not serviced by credit from formal institutional credit markets. The operations of such markets are selective in their choice of enterprise to finance and in most cases the peasants, small scale and micro enterprises are not usually favoured. Hence, a large number of active entrepreneurs must use the informal credit market to finance their business activities. However, the extent to which the informal credit market can effectively meet demand is limited. This paper examined the operation of one of the predominant types of organized informal credit providers in Nigeria, namely cooperative savings and credit associations.

Mahmoud S. Mohieldin and Peter W. Wright\textsuperscript{79} showed that for the Egyptian villages surveyed, the informal financial sector is more active than the formal sector, although the loans obtained are generally smaller. And it is also found that the most common form of informal finance is occasional lending through participation in ROSCAs.

All India Debt and Investment Survey\textsuperscript{80} indicates that Andhra Pradesh, the state with highest concentration of self-help groups (SHGs), microfinance institutions (MFIs) and banks, reported 73 per cent of rural non-institutional debt and 57 per cent of rural moneylenders’ debt, the highest among all the states in India.


\textsuperscript{80} All India Debt and Investment Survey (2002)
The survey conducted by Emily Chamlee-Wright\(^{81}\) in Harare, Zimbabwe revealed that 51% of the traders interviewed started their business either in part or entirely from personal savings. The source of savings could be wages from a formal or informal sector job. Most traders rely on informal structures for their daily, weekly, monthly, and even annual saving needs. In the current study, 76% of traders interviewed engage in some form of ma-rounds (literally “the rounds”), in which members of a group save a particular amount over a specific time frame and give the accumulated lump sum to each member in turn. Women generally belong to several different clubs at the same time, each with a different structure. Most clubs require daily or weekly contributions, though some clubs require monthly contributions, of a higher amount. The average daily club has 10 members and require a contribution of approximately Z$50 per day. The average weekly round has seven members and require a contribution of Z$450 per week.

Bala Subramanian. V\(^{82}\) stated that the latest amendments in the Central Chit Fund Act will go a long way in making the ancient and India’s own financial institution of Chit industry more vibrant and a healthy business. The article showed that Chit firms were having better cash flows now due to the reduction in security deposit and higher discount limit on the prize money. This will also bring high return to the subscribers by way of more dividends. This article also cited the peculiar case in Kerala where the State Government itself is a big operator in the field. It also showed that most of the chit funds from Kerala are said to be operating out of Chandigarh, Faridabad and Jammu and Kashmir.

Anderson, S. and Baland, et.al.\(^{83}\) have investigated into individual motives to participate in rotating savings and credit associations (ROSCAs in a Kenyan slum


(Nairobi). It suggests that most ROSCAs are predominantly composed of women, particularly those living in a couple and earning an independent income. Participation in ROSCA is a strategy a wife employs to protect her savings against claims by her husband for immediate consumption.

**Hoque, Hafiz Al Asad Bin et.al.** opined that like many other developing countries, in Bangladesh, informal finance plays a positive role in savings mobilization, capital formation, and investment. ROSCAs and ASCRAs are the popular sources of informal finance in developing countries. These informal organizations continue to flourish even in urban areas where density of formal financial and strong quasi-formal institutions is high. The case studies revealed the underlying reasons for existence of ROSCAs and ASCRAs in Dhaka. The studies revealed that restricted production technology of formal credit market, high demand for credit, limited types of formal loan products, high transaction cost of saving with formal banks, need for consumption or lumpy expenditure contributed to existence of ROSCAs and ASCRAs in the urban areas. The age, marital status, family monthly income level, occupation and education level have significant effect on memberships of ROSCAs versus ASCRAs. Small businessmen tend to prefer ASCRAs for continuous flow of finance, while individuals with need for lumpy expenditures prefer ROSCAs.

It is mentioned by **Stefan Klonner** that in India, ROSCAs emerged mostly in the southern parts of the country and are known throughout the country as ‘chit funds’ or chits. ROSCAs can offer insurance for homogenous, risk averse individuals who have stochastic, privately observed incomes and no access to credit. Bidding ROSCA enables participants to obtain funds when they observe a particularly profitable investment project. Homogeneous individuals prefer a bidding ROSCA because it can allocate funds to the participant with most urgent current need, and facilitates risk sharing among risk adverse individuals.

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Ambec, S. & Treich, N\textsuperscript{86} presented that in developing countries, traditional social obligations often press rich individuals to share their income. People can sign binding financial agreements amongst themselves, thereby forming coalitions. These financial agreements may help them to alleviate their social obligations with respect to income sharing. It is showed that there exists a stable structure of coalitions in which people form associations called rotating savings and credit associations (ROSCAs) which are most prevalent and puzzling financial institutions.

Aredo, D\textsuperscript{87} described that Informal Savings and Credit Associations (ROSCAs) have remained popular in many developing countries for over a long period of time. In fact in some countries, such as Ethiopia, they have become increasingly popular among almost all sections of society. However, their emerging features and flexibility are little understood by those interested in savings mobilization and credit provision in developing countries. Existing economic models of ROSCAs are based on the experience of a limited number of countries and thus, have failed to fully explain the distinct characteristics and dynamism of this fascinating financial intermediary. Using the evidence from Ethiopia and other developing countries, this paper identifies the distinct characteristics of ROSCAs and discusses how they minimize risk arising from problems of adverse selection and of moral hazards. The findings of the study have generated interesting policy implications for the promotion of informal finance in developing countries.

Banerjee and Duflo\textsuperscript{88} indicates that the credit from informal sources tends to be expensive. These high interest rates seem to occur as a result of the high costs of contract enforcement. While delay in repayment of informal loans is frequent, default is actually rare.


\textsuperscript{88} Banerjee and Duflo “Growth Theory through the Lens of Development Economics” Handbook of Economic Growth, Volume 1A, (2005) P473-552
Robert Deckle\textsuperscript{89} states that the development of an important informal financial intermediary in Japan, the rotating savings and credit association (ROSCA) called the mujin-ko or tanomoshi-ko. The mujin have survived from the pre modern period until the post World War II period. The mujin is a Japanese form of a rotating saving and credit association, which has much in common with ROSCAs in other countries. The mujin originated from Buddhist traditions and came to Japan from India, China, and Korea. Mujin provided financing without collateral and without interest payments. When commercial lenders did not provide sufficient lending to the poor, these ROSCAs were considered to be helpful. In 1915, the MOF and Bank of Japan evaluated the advantages and disadvantages of mujin. According to the MOF, 831 mujin were then in operation with a total capital of 20.3 million yen. Of these, over 80\% were incorporated as joint-stock companies.

Mark Schreiner\textsuperscript{90} viewed that in most parts of the world, most ROSCAs in Argentina are informal. Unlike in most parts of the world, Argentina also has some formal ROSCAs run by car dealers and banks. The members do not know each other and never meet. In the absence of social capital among the members of the group, the government of Argentina regulates formal ROSCAs to protect the deposits of net savers. Formal ROSCAs can have bigger pots since the bank bears default risk and since the bank has the net worth and diversification to accept more risk. Members make payments at a bank branch during the first week of each month. The bank after deducting its fee sends the rest to the management of the formal ROSCA. On the tenth day of the month, the manager draws one winner by lot. Before collecting the pot, the winner makes a standard loan application and offer guarantee to the bank. Finally formal ROSCAs impose lower transaction costs on members than informal ROSCAs, since social capital requires maintenance.


\textsuperscript{90} Mark Schreiner(2005),
The study of Huppi, M. & Gershon F.\textsuperscript{91} brings out that successful group lending schemes work well with groups that are homogeneous and jointly liable for defaults. The practice of denying credit to all group members in case of default is the most effective and least costly way of enforcing joint liability. Another way to encourage members to repay is to require mandatory deposits that are reimbursed only when all borrowers repay their loans. The article points out those credit cooperatives that mobilize savings deposits are less dependent on external sources and increase the borrowers’ incentive to repay. The success of credit cooperatives requires training of members as well as management. Experience suggests that credit cooperative should not expand their activities beyond financial intermediation until they develop strong institutional and managerial capabilities.

Gingrich, C.D.\textsuperscript{92} explained that Savings and Credit Cooperatives provide a variety of microfinance services to households in three of Nepal’s distinct regions—the Hills, Terai, and Kathmandu valley. Nearly all Nepali savings and credit cooperatives are self-funded using member savings and equity. Most Nepali savings and credit cooperatives are also profitable, including those located in poor, remote areas of the hills region. Key reasons for the savings and credit cooperatives strong financial performance include reliance on member savings and control of administration costs.

Geertz\textsuperscript{93} reports that the other types of social and ceremonial ROSCAs apart from labor and economic ROSCAs come from all over the world. In the “paketan kawinan” (“pakat”, to agree upon; “kawinan”, “marriage ceremony”) in Indonesia, meetings are held only irregularly, occurring only when a member has a ceremonial need—an offspring’s wedding, circumcision, etc.—which he uses the pool to finance. Such associations are very long term affairs, with positions being inherited as members die.


As reflected by Owoeye, T. & Adenuga, D.S.\textsuperscript{94} rural informal savings and credit associations persist and remain extremely popular among the very poor in the society. This is because they are able to resolve the problems of asymmetry information, transaction costs, adverse selection, moral hazards and other related risk, that are associated with formal financial sector. The impressive capability of traditional savings and credit associations in coping with the above problems reveals a strong character trait of such association. The study conducted in Ado Local Government area of Ekiti State, Nigeria in 2004, shows that these associations appear to cope well with the risks associated with formal financial sector by exploring social relationships, using collateral substitutes and reducing the imbalance in information between the lenders and the borrowers. The study also investigates that more than proportionate participation of women in such associations and reveals that this may be due to the fact; they are more likely to be shut-out of the formal financial sector because of social and economic factors.

While explaining the risk involved in investment V.A.Avadhani\textsuperscript{95} has mentioned that gold, silver, real estate; Nidhis and chitfunds are the other avenues of investment for average Householder, of middle and lower income groups. If the investor desired to have a real rate of return which is substantially higher than the inflation rate he has to invest in relatively more risky areas of investment like shares and debentures of companies or bonds of Government and semi Government agencies or deposits with companies and firms. Investment in Chit funds, Nidhis, company deposits and in private limited companies has the highest risk. Among the categories of investments popular with semi-urban and rural areas, there are various types of deposits kept with non-banking finance companies like hire purchase, investment and finance companies, housing finance companies, mutual benefit funds, chit funds and Nidhis. Investors have to weigh pros and cons of making investments in such agencies. The deposits with these companies are

\textsuperscript{94} Owoeye, T. & Adenuga, D.S. “Economic and Social Issues in Rural Informal Savings and Credit Association: Lessons for Reform in Rural Credit Schemes in Nigeria”, (Available online: June 18, 2005).

unsecured debt and hence the investors should be careful in taking this risk of investment in deposits in the chits and Nidhis.

According to Duflo, Kremer, and Robinson\textsuperscript{96} the main challenge for the poor who try to save is to find safety and a reasonable return. Stashing cash inside the pillow or elsewhere at home is neither safe nor well-protected from inflation. In addition, that the poor, like everyone else, have problems resisting the temptation of spending money that they have at hand.

Rogers, C.\textsuperscript{97} Observed, the inability to obtain sufficient capital to finance the start up or operation of a small enterprise is often a constraining factor limiting engagement in income generating activities by residents of less developed countries where formal sources of credit are unavailable, inadequate, or unpopular due to rigid collateral requirements. In this paper it is described that the recent adoption of a bidding form of rotating savings and credit association (ROSCA) by villagers from the Nyishangte community in the Manang region of Nepal and analyzes the community’s remarkably successful use of bidding ROSCAs to finance local business ventures. The proliferation of bidding ROSCAs in Manang since 1999 has effectively created a local market for capital where credit can be accessed at a price directly reflecting the local demand. By reducing the risk and raising the returns associated with investing capital and by lowering the trouble of accessing credit, the use of bidding ROSCAs has greatly facilitated the pooling of finance capital in Manang and made credit available to a large portion of the community, enabling widespread involvement in entrepreneurial ventures.

Anyango, E.\textsuperscript{98} described the Village Savings and Loan Associations (VSLA) as a time bound-accumulating savings and credit associations (ASCA). In it, 15 to 30 people save regularly and borrow from the group fund. On a date chosen by the members, usually


after about a year, all the financial assets are divided amongst the members in proportion to each one’s savings. This payout is called the action audit. The groups normally reform immediately and start a new cycle of savings and lending. The VSLA methodology proposes that once mature, groups can function with no external support. Its proponents suggest that in the best programmes, 95% of the groups continue to function after two years and that the model reaches deeper into rural areas and serves poorer people than other microfinance models.

Allen, H.99 The Village Savings and Loan (VSLA) model is a savings-based approach that has proven on a significant scale that it can substantially fill the gap between the needs of the poor for financial services and the ability of banks and MFIs to provide these services. It provides sustainable and profitable savings, insurance and credit services to people who live in places where banks and MFIs do not have a presence such as rural areas and urban slums. CARE is tackling these difficulties by encouraging the formation of village loan funds entirely composed of member’s savings. The VSLA programme of CARE in Zimbabwe, where very high rates of inflation existed are rated as posing a challenge to any microfinance programmes.

Preethi Rao100 suggested that chit funds are good financial sources to small businesses, which has been suffered from the money lenders with their high cost of loans and banks with their stringent procedures. They can save the money with chit funds and when in any emergency need of capital they can take loan out of the money saved. The Author has mentioned the reasons of failures of chit funds, like the regulatory hurdles due to the stringent rules proposed by the Government and the increased costs of operations for the registered companies are the setbacks of the industry. Because of these reasons, the registered companies are shifting their operations to unregistered companies.

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Prof. Mudit Kapoor\textsuperscript{101} opined strongly that the chit funds are an important source of finance for small businesses and low-income households in India. Registered chit funds are away from low value chit schemes due to increased operational costs and strict rules imposed by Government. Chit funds are very safe mode of financing and saving. They offer loans at lower interest rates than money lenders and sometimes than banks also. The size of the unregistered chit funds is stated about 67 times of the registered industry in Delhi and 3.2 times in Chennai. On an average 50\% of chit fund clients are poor households and most of them save for particular target events like marriage, education etc., and also they value the flexible provision of credit. Customers feel comfortable with the bidding process and 96\% of them perceiving registered chit industry as safe or very safe. Most funds have moved away from smaller chit schemes due to strict regulatory norms imposed by the Government and increasing wealth levels in India.

The study of Abhijit V. Banerjee and Esther Duflo\textsuperscript{102} concludes that the poor save little because they lack a safe place and infrastructure to put their savings. Very few of the poor households get loans from formal lending sources. Especially in towns, only about two-thirds of the poor had a loan. Of these loans, 23 per cent are from a relative, 18 per cent from a moneylender, 37 per cent from a shop keeper, and only 6.4 per cent from a formal source. ROSCAs may be viewed as a commitment device which helps people to cope with their own self-control problems. People want to avoid spending too much money in the future purchase of a superfluous good, and to avoid this is to commit in advance to contribute a fixed amount at regular dates.

Antoinette Schoar\textsuperscript{103} opined that many people who use chits have no access to banks and other forms of finance, thus chits provide a good local solution that helps them pool


\textsuperscript{103} Antoinette Schoar, Professor of Entrepreneurial finance, Massachusetts Institute of Technology, Sloan school of Management. “Chit Funds as an Innovative Access to Finance for Low-income Households”, Institute for Financial Management and Research, Chennai (India), (2007).
savings and provide funding to businesses and individuals. People are smart enough to comparing the effective interest rates between chits, banks and money lenders.

**Stefan Ambec et.al**\(^{104}\) examines a third justification based on a limited self-control hypothesis. It argues that the specific characteristics of ROSCAs help people to cope with their self-control problems. Self control problems might be caused by social pressure from relatives or community members. People in developing countries are involved in networks of relations with strong norms and obligations enforced by social pressure. People tend to purchase some specific goods like gifts, alcohol, food etc. during some social events.

The study of **Mary Kay Gugerty**\(^{105}\) contributed to the literature on ROSCAs and commitment by providing evidence on ROSCA participation and design from a sample of 70 ROSCAs and 1,066 ROSCA participants in rural Kenya. The evidence gathered with ROSCA participants suggests that making a public commitment to saving is a key reason for joining a ROSCA for many participants. The answers to the questions, why individuals joined a ROSCA are, it was difficult to save alone, that they got strength to save by sitting with each other. And it is difficult to save at home because money got used up in small household needs. And another reason they joined ROSCA as a response to household conflict, fear of theft, or demand by kin. A ROSCA makes one look harder for money to save.

**Arjun sengupta, K.P.Kannan, G.Raveendran**\(^{106}\) mentioned that more than three-fourths of Indians are poor and vulnerable with a level of consumption not more than

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\(^{104}\) **Stefan Ambec et.al.**, “Roscas as financial agreements to cope with self-control problems” Journal of Development Economics 82 (2007) pp.120-137


twice the official poverty line. These people are known as common people, and the inequality is widening between the common people and the better-off sections of society.

The RBI reports in *Trend and Progress of Banking in India*\(^\text{107}\) indicates that even after the four decades of banks’ nationalization, country’s 41 per cent adult population remained outside the banking system but are surmised to be covered by the NBFCs wise Chit Funds’.

**Dr. Jafor Ali Akhan**\(^\text{108}\) stated that the Non-Banking Financial Companies (NBFCs) have been playing a very significant role in the present day rigorous money-market conditions. They are serving the nation by supporting the economic reconstruction and giving a booster to industrial production. They are engaged into the business of providing loans and advances of small amounts for a short-period to small borrowers. The Non-Banking Financial Companies (NBFCs) play an important role in channelizing these savings into investment. They have supplemented the role played by the banks.

**Prof. Mudit Kapoor**\(^\text{109}\) found that the chit funds are safe investment instruments for low-income groups whom it is very difficult to get loans from commercial banks. It develops a kind of financial discipline among the common people. It is very safe to invest in registered chit fund companies, and the saver gets more interest than banks. It fulfills the urgent needs of the common people and acts like an insurance scheme in emergency. Most of the people are away from the chit funds because of lack of awareness of the industry.

According to **Siwan Anderson et. al.**\(^\text{110}\) who studied on Rotating Savings and Credit Associations (ROSCAs), ROSCAs constitute one of the most commonly found informal

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financial institutions in the developing world. The importance of these institutions is the participation is voluntary and the groups do not and cannot rely on external enforcements. ROSCAs are formed by a relatively small group of individuals who live in the same area, it is generally assumed that the prospect of participating in future cycles of the ROSCA as well as the threat of social sanctions (giving a bad reputation, retaliating at the work place, or damaging personal property) by the other members of the group are enough to deter opportunistic defection. In the Kenyan survey conducted by the author, 57.2 per cent of households have at least one individual who belongs to a ROSCA. The average monthly contribution to a ROSCA group is equal to 20.3 per cent of individual income.

According to Y. Bala Bharathi and Sanjoy De\textsuperscript{111} NBFCs are financial entities that provide banking services without meeting the legal definition of a bank. They are typically not allowed to take deposits from general public and hence have to seek other means of funding. These NBFCs have matured a lot and even withstood the recent deadly crisis with a lot of resilience. NBFCs can reach the unorganized segments of society with their ability to provide innovative financial services. These entities play a critical role in disbursing credit to the rural sector, thus preventing the concentration of credit risk in banks. In urban areas too, NBFCs focus on non-salaried individuals, traders, transporters and stock brokers who are neglected by banks.

Namrata Acharya\textsuperscript{112} mentioned that chit funds are looking down in terms of number and are growing in terms of value. The registered chit funds find it less lucrative to fund the poor due to the rising operating costs. According to AIACF, running chit funds is no longer viable. Though the money circulated has increased, the number is going down. It may come down further in the years to come. On the other hand, unregistered chit funds have found a utility in evading tax and access to large deposits. The clout of unregistered chit funds is tremendous. The number of unregistered companies is almost 100 times than the registered companies.


\textsuperscript{112} Namrata Acharya, “Unregistered Chit Funds having a field day” an article published in Business Standard, Kolkata, July 25, (2010)


Dr. Amrit Patel and Dr. Gopal Kalkoti\textsuperscript{113} mentioned that according to RBI, the major reason for increase in overall household debt and increase in the share of rural household indebtedness to non-institutional sources was a significant increase in the current farm expenditure and household expenditure for which households found it difficult to obtain loans from banks. In addition to that the cumbersome procedure of submitting various documents with loan applications and documentation process led to an average of 33 weeks taken by commercial banks to approve loans. And this scenario is the niche for chit fund like entities under the banner of NBFCs.

Dr. Jatinder Kaur\textsuperscript{114} reveals that, despite the phenomenal growth of banking sector, the extent of rural indebtedness in India has been on a continuous rise. About one-third of the rural credit requirements are still met by non-institutional sources, like moneylenders. The favoring factor of moneylenders is that banks will not sanction loans for consumption purposes and default of repayment of previous loan makes it ineligible for further assistance from banks.

Usha Thorat\textsuperscript{115} states that non-banking entities can be either non-banking non financial entities or non-banking financial entities. In case of non-banking financial entities, there are deposit taking and non-deposit taking financial companies is there. Considering the difficulties in ensuring the effective supervision of large number of small deposit-taking entities, fresh approvals to NBFCs for accepting deposits are not considered.

\textsuperscript{113} Dr. Amrit Patel and Dr. Gopal Kalkoti, “Rural Credit: How to Take Forward?”, The Indian Banker Vol V No.2, February 2010, PP 20-25.

\textsuperscript{114} Dr. Jatinder Kaur, “Rural Indebtedness Causes and Cures”, The Indian Banker Vol V No.2, February 2010, PP 36-39