Chapter 1

Introduction
CHAPTER I

INTRODUCTION

1.1 CHIT FUNDS

Chit Funds are the oldest indigenous financial institutions in India, and were created and continued as they primarily meet the felt needs of the small communities, to provide a saving as well as a forum of obtaining loans to meet unusual expenditure. With the passage of time, and on account of their popularity, chit funds have recorded substantial growth in their number as well as the volume and turnover of business.

Chit fund is a very unique one wherein members of public, small or big, invest certain sum of money, mostly on monthly instalments, for over a period of time, with the facility of withdrawing the amount of the chit whenever they wish so. This
concept of chit funds is so well known in the southern states. Where, besides organised mutual funds in the form of institutions and the like, a few households join together and run a localised chit fund for the benefit of the residents of a small colony or sometimes within a street. Chit funds are run on mutual trust and honesty not only on the part of persons running the chits but also all the participants.

The promoters of chit groups are known as ‘foremen’. They design and promote various chit groups to appeal to several income groups. Each chit group will have a specified number of months and subscribers. Each subscriber agrees to subscribe a specified amount each month. The total amount of subscription is known as the chit amount or value.

The operation of a chit fund business basically involves three main stages.

They are: enrolment of members; disbursement of bid payable amounts and recovery of monthly chit subscription.

A chit fund scheme involves the following: Pooling of the sums of money contributed by a group of individuals; lending of the pooled amount to a member of the group, and; Continuing the process of collection and distribution of such amount in rotation till all the members receive their contribution.
1.2 Salient Features of Chit Fund

Chit Fund Trade is an indigenous scheme which has been regularised by various draconian provisions and clauses of the Central Chit Funds Act 1982. A very favourable factor in the Indian economy is the high rate of savings. Full benefit of high savings cannot be reaped unless such savings are channelled to productive uses. Chit Funds play a vital role in this regard by bringing together savers and borrowers.

In Chit Funds, the transactions are well guarded by the Act. Before joining chits, intending subscribers think over carefully and base their choice of joining the chit with fair knowledge of character, behaviour integrity, social standing, sincerity and status in the society of directors and office bearers, the tradition and longevity of the company and above all, their capacity and only then extend their applications.¹

Likewise, the chit foremen also verify while admitting membership, the financial status of the proposed subscribers, their capacity of subscribing the chits and whether they are able to furnish tangible security like house property or bank guarantee or personal guarantee of Government or Bank Staff drawing high salary.

This system and its function enables promoters and the subscribers to know about each other and ascertain their repaying capacity, their marketing value, integrity and capacity and helps
1.2. Salient Features of Chit Fund

Chit Fund Trade is an indigenous scheme which has been tightened by various draconian provisions and clauses of the Central Chit Funds Act 1982 by which the status of the chit fund trade has been appreciated by the benefited public.

There are a number of clauses certainly prohibit the erring foreman from doing any mischief of the public money.

In chit funds, the transaction are well guarded by the act. Before joining chits, intending subscribers think over carefully and base their choice of joining the chit with fair knowledge of Character, Behaviour, Integrity, Social standing, Sincerity and Status in the society of Directors and Office Bearers, the tradition and longevity of the company and above all, their capacity and only then extend their applications.¹

Likewise, the chit funds also verify while admitting membership, the Financial status of the proposed subscribers, their capacity of subscribing the chits and whether they are able to furnish tangible security like house property or bank guarantee or personal guarantee of Government or Bank staff drawing fat salary.

This system and its function enables promoters and the subscribers to know about each other and ascertain their repaying capacity, their marketing value, integrity and capacity and helps
to run the business very smoothly with mutual understanding without leading to unnecessary litigation and hurdles.

Until 1961, Chit business in Tamilnadu was free from any kind of legislative control. When some of the abuses of the chit companies came to light, the Government of Madras suggested to the Government of India to undertake the legislation itself as the chit fund companies were mostly confined to the Southern State of Tamilnadu and Kerala and would therefore be a fit subject for State legislation. Accordingly, a Bill was presented to the Madras State Assembly in 1960 and it became an act in June 1961. Though passed in 1961, the Act was brought into force in the districts of Kanyakumari and Tirunelveli from 1964, in the city of Madras with effect from August 1965 and in the remaining parts of the State from December 1969.

The Central Government appointed a Banking Commission with Sri. R.S.*Saraiya as chairman in 1969 to examine whether chit funds are to exist or to be banned. The commission pointed out that the chit funds rendered a social and economic service to the country by cultivating saving habits among those who have no Bank facilities. Then the Banking Commission recommended to the Central Government in 1972 that uniform legislation should be brought throughout the country regulating chit fund. After
this, the Reserve Bank was asked to draft a Model Chit Fund Bill and in 1974 James S. Raj committee was constituted to scrutinise the Model Bill. After eliciting public opinion, a Bill was prepared by the James Raj committee and was introduced in Parliament on 20.11.1980.2

1.3. HISTORY OF CHIT FUNDS

The term 'Chit' in Tamil means a written piece of paper. Although there is no clear evidence to show its exact place of origin and period of establishment, there are ample references in historical records and economic literature to prove its antiquity and usefulness.

Believed to have emerged out of necessity, the Chitty, which was undoubtedly in existence before the establishment of modern banks and the advent of British rule in India, was primarily an arrangement for safe custody of valuables and notably grain.

When one examines the history of chit funds, one comes across different stages in its evolution. In stage one, the chitty was confined to a few households situated close to each other in a village and the organiser or foreman was a respectable, trustworthy person in the locality. Foreman was called munnal or munnaalan, meaning person in the front or leader in local language. Mostly the foreman was the karapramani, a person who
commanded respects in the kara or village, by virtue of his family position, wealth, collaterally acquired power and the like. Members from the participating households carried the predetermined measure of paddy or rice to the house of the foreman at each harvest time a year. Member was called Chittal or Chittalan, meaning subscriber to the Chitty. The total contributions of the members at each instalment was then given to a member originally decided by the foreman by using his own judgement regarding the needs of members, or in consultation with all the members either before or on the day the contributions reached his house, and subsequently by a system of lot. The essence of the scheme was the distribution of contributions made by a group of persons over a period of time among themselves by rotation. The foreman received no remuneration. He simply supervised the scheme as a passive, honorary president. The scheme was known as a changathi kuri (changathi means friend) that is a chit for mutual help.³

Since the periodical contribution was the easily available commodity in every house, the chitty became popular among women. Even without the knowledge of the male members, many a housewife participated in chitties by sparing, sometimes “fistful of rice” from each of the cooking times every day. In the early part of the present century, a chitty known as pidiari chitty (Pidi
means fistful and ari or arisi means rice) was popular among the poor people in the erstwhile princely state of Travancore.

The Progenitor of Chit Funds in Tamil Nadu is traced from a socio-economic institution known as “Moyy Murai:”. The term Moyy means Call money pooled and Murai means custom, under this system, a group of persons in a village or locality, known to each other, joined together to pool their resources to meet the need of an individual of the group. There were some well-defined needs such as celebrating marriage, buying of land, building of houses and purchasing of cattle that were prescribed under the system. It was a Sahaya Nidhi, with a strong element of co-operative spirit.

In course of time, the term Moyy was replaced by the term chit or olai (Palm leaf), which was the notice of demand for payment of a members’ contribution to the pool. Later, the names of the members of the group were written on chits or small pieces of paper or palm leaf, rolled up and shuffled to pick out the person to whom the amount of fund was to be given.

The Chit Fund system as it originated was Grain Chit or Dhanya Chittu. In each village, there were different groups contributing different grains. Each group selected its own foreman. In the initial stages the entire periodical collection was given to one member of the group decided by lot or what was known as
kudavolai. On the appointed day, the names of members were written on olai (Palm leaves) and put in a small earthen Kudam(pot), from which one name was pulled out to decide the person to whom the entire collection was to be given. When money came into use, there developed Pana Chittu or Money chits, in which members paid their periodical contribution in money.

There was also the practice among those selling vegetables in village Shandies (fairs) to make a weekly contribution to a trusted individual getting in turn the pool to supply them with capital to buy vegetables they had to sell in the market. In course of time this system spread to various trades. Women in households also started pooling their resources and depositing their savings with an elderly woman of the locality who was generally trusted and respected. As more and more people started joining these chit groups, a system was evolved by which the trustee fixed a particular day for deposits and payments.

As time passed, the menfolk also found this system of mutual co-operation advantageous to meet their casual financial difficulties or invest their cash earnings. The men who joined the scheme were drawn from the locality. The persons who conducted the chits were normally men of known integrity and the people who joined the scheme had implicit faith and confidence in them. Default and delayed payments were very rare.
In the second stage, an active organiser emerged, replacing the previous honorary foreman. The aim of this new foreman was to raise resources for some temporary purpose. The scheme is aptly described by a slogan as follows: "The organiser of the kuri gets a certain number of his friends to subscribe a certain amount of money or of rice husked or unhusked as the case may be. The friends bring their contribution to his house where they are hospitably entertained, and by lot the person is selected to whom similar contributions from all present, including the organiser of the kuri are to be made at a certain date then and there fixed. This individual in turn hospitably entertains his friends when they come (to his house) with their contributions. A third person is then selected, and the same thing comes off at his house. And so it goes on until every one of the original members or his heir has in turn reaped the benefits of the contributions of his friends."

With the above view when Sim Cox wrote. "The Dravidian Kuri is commonly resorted to by anyone desiring to raise a sum of money for some special purpose, such as a daughter's marriage. ...... A feast is always given by the recipient of the lump sum." The organiser did not seem to have realised any fee or commission from the subscriber friends. The subscribers, however, incurred expenditure for the entertainment which was "calculated to cost not more than 10 per cent of one month's
subscription of all the members". Suppose the scheme consists of 20 members including the foreman and the contribution per instalment is 10 measures of rice. Then at the first instalment, the foreman will receive 200 measures of rice out of which about 20 measures will be spent on entertainment, leaving him with a net receipt on 180 measures of rice. The rest of the members also will get the same measures of rice when their turn comes up in any of the subsequent 19 instalments.

Later on, when some of the members who bagged the total contributions in the early period of the scheme failed to make further contributions, the non-receivers approached the organiser for their contributions. Thus he was compelled to take up full responsibility of receipt of contributions and disbursal of total contributions, termed prizes. He has to put in his labour and shoulder risks for which he started collecting remuneration in the form of commission, in addition to taking his prize in the first instalment itself.

With the decline of barter and the emergence of money as the centre of economic activity, the chitty grew to the position of a tiny savings bank with certain restrictions and conditions on withdrawals. The subscribers began to seek money chitties in preference to grain chitties. The pattern of subscribers itself underwent a change. Besides agriculturists, traders, merchants and salary earners also turned to the chitties. This change in the occupational pattern of the clientele was a major turning point in
the evolution of chitties. Whereas the main purpose of the agriculturist subscribers in joining the chitties was accumulation of savings and the primary aim of the traders and merchants was borrowing. Although the principle of lot was an obstacle in the way of taking one's prize at a time when one needed it, one managed the affairs in a round about way. Such members borrowed the necessary amount from local money lenders or others and repaid the debt when they won the lot. Sometimes they borrowed from the foreman himself on the guarantee of the chitty.

To overcome the defects of lot system, the auction system was introduced. This is because many members in a group were in need of money at the same time. The lot system gave the amount to a person who might not necessarily be in need of it. In the auction system, it became possible for needy members to bid for an amount depending upon their urgency. The excess collection, that is the difference between total collection and bid amount was distributed then and there, as dividend or kasar to all members, including the successful bidder. Much later, as the system developed, the excess collection was divided into two parts, not necessarily equal. One part was distributed equally to all the members of the group as Kasar and the other part also equally, but only to the non prized members. The latter was an incentive to those members who joined the group primarily to save.
1.4. STATEMENT OF THE PROBLEM

The credit needs of a vast country like India have to be met in many ways. With every increase in the price level and the consequent reduction of real savings amongst a vast section of the people, the need for monetary accommodation increases. This is one aspect of the situation.

The other aspect is that with the organised banking sector limiting its credit to certain types of business and under conditions of severe security and inelastic repayment much of the credit needs of the country is being met by the non-banking sector of the economy. The impact of this sector on society is much greater as would be evident from the total figures of the transactions. It will be sufficient to show that in the present context of the country's economy, the credit facilities available otherwise than through the banks, is sufficient to nullify the effects of the credit squeeze on price levels. Per Contra, it should be mentioned that without the comparatively easier credit facilities available in this manner, the fall in production and distribution of intermediary and consumption commodities will be greater, with correspondingly deleterious effects on the price level.

The important point is that chit funds arose in response to a felt need of the local communities, at a time when credit facilities were inadequate. Though Co-operative Credit Societies were
started in the early part of the century in many parts of the country, both in rural and urban areas, they could not answer the problem of the immense need for credit. Though there are many irregularities and malpractices of chit funds were pointed out, the confidence of the public in general did not seem to have been shaken in the system of chit funds as such. The growth and popularity of chit funds have to be attributed primarily to the slow growth of banking and credit facilities in several parts of the country. The lending policies of commercial and co-operative banks were also such as to leave scope for the institution of chit funds. Even in areas where there were banks, it was not possible for people in general to borrow either for many of their domestic needs such as marriages, social and religious ceremonies or for their productive purposes. For the people to whom there was no easy access either to commercial or co-operative banks, chit funds along with other indigenous institutions became an important source of credit.

In fact, the two factors, namely, accessibility and relatively easy availability of credit, rather than the cost of such credit seem to explain mainly, the popularity of chit funds. However, the interesting thing is that even with the spectacular growth of banking offices since nationalisation and the increase in flow of credit to the neglected and priority sectors, chit funds have recorded substantial growth in number and volume of business.
Normally chit funds are functioning properly and serves as a very good source of finance for the working capital of the business or for urgent personal needs. Since, it links savings with loan for each members, it boost up self confidence on the borrowers and serves in a more secured way. Loans are given on easy securities and with lesser formalities. The borrower can easily settle the loan through specific small instalments. Effective management of chit funds would lead to the success of the business and the availability of finance to needy people in appropriate time.

Moneylenders, Indigenous Bankers, Nidhis and Chit Funds are natural financial institutions in the country which have been operating for centuries. They have been catering to the needs of millions of small and big borrowers especially in rural areas and in the process have also succeeded in mobilising saving from rural people. They are able to gain the confidence of the rural people, since their service are very informal and personal. They have well founded information about the borrowers. In the process of their functioning they acquired great amount of banking and lending skills through their continued
services. It has been accepted as an indispensable service in rural areas than an exploitation. Even today, with all extension of Banking and Co - Operative Societies in rural areas many rural people prefer these sources because of their informal nature of services.

For a country like India with a large number of villages, the expansion of the organised sector is not sufficient. Hence, the continuation of chit funds is to be accepted as it is. Total prohibition or abolition of this through legal enactment, without providing alternative sources for sufficient credit facilities in rural areas will lead to a problematic situation. Hence, the rural credit structure in India is to remain in the dichotomy with the existence of both banking and non-banking financial institutions.

Not withstanding the expansion of banking and credit facilities and a few instances of malpractices by the chit companies, chit funds seem to continue to be popular in the society.

It has been recognised that chit funds arose at a time when banking facilities had not developed and thus they filled an important credit gap in the economy. It was also believed that when commercial banks developed rapidly, there would be no place for chit funds and that they would die a natural death. On the contrary, what we have witnessed in the last ten or fifteen years is that side by side with the spectacular banking
development, there has taken place a vast expansion of chit funds. This can be explained by the fact that credit needs of the country have grown so much that it is too much to expect the banks to provide all the credit needed by the country. Then, there is also the fact, that despite all the propaganda and claims made by the authorities that credit would be available for all and sundry there are still thousands who throng to chit fund companies, as they do not have access to banks for one reason or another.

After the introduction and implementation of Chit Fund Acts and Rules, it has been a blow to private financial institutions which exploited the weaker sections. Yet many chit funds emerged duly registered and have successfully developed increasing their popularity. In Kanyakumari District also, chit funds play a significant role both registered and unregistered. During the period of 10 years under study, which is from 1990 to 1999, there were 2856 total registration of Chit Funds amounting to Rs.24,49,71,700 showing an increasing trend. Certainly, the unregistered Chit Funds have much more than this amount. Hence, the researcher made an attempt to analyse the Socio-Economic Development of Kanyakumari District Through Chit Funds.

The Process of socio-economic change is an intrinsic part of human civilization. The Primary Objective of the developing countries like India is to achieve rapid, balanced and sustained
rate of economic growth. Economic development if conceived without appropriate social changes becomes stagnated. Therefore even the national planning has become an instrument of socio-economic transformation in developing countries.

One of the Laws of Dynamics of Development tells us, "Economic development is organically related to the impulse of change, reflecting the developmental urge of the society for self-reliance and willingness to observe rigorous discipline. This is a social law which reveals the interdependence of social and economic development." In general, development is essentially a matter of social and economic management. If the social motivation is taken care of, economic development will begin to take care of itself. Hence the researcher has taken social and economic factors as indicators to study the development of chit funds. And so the topic is named as the "Socio - Economic Development of Kanyakumari District Through Chit Funds. - A case study."
1.5. Review of Literature

Literature on Chit Funds are scanty. This study is the first of its kind. No study on this aspect of this topic has been attempted so far. However, there are certain studies undertaken at the individual and institutional levels relating to the management of chit funds, economic liberalization of chit funds and the like. The findings of these studies have enabled the researcher to identify some concepts for the present study. A review of such studies has been presented below.

Can a Traditional Financial Technology Co-exist with Modern Financial Technologies? The Indian experience. A study conducted by C.P.S. Nayar, with reference to chit funds, Published by the Institute of Financial Management and Research, Madras. His study reveals that the chit funds possess to face the challenge of modern financial technologies are adaptability, flexibility and universality.

The Madras Provincial Banking Enquiry Committee (1930) and The Travancore Enquiry Committee (1930) referred to the useful role played by chit funds in the rural areas of Kerala and Tamil Nadu as an important source of credit to people of moderate means.

The All-India Rural Credit Survey Report (1952) pointed out to the fact that Co-operative credit went to meet the needs mostly of the rich and the middle farmers. For the people to whom
there was no easy access either to commercial or Co-operative banks, chit funds along with other indigenous institutions became an important source of credit.\(^\text{11}\)

Dr. V. Krishnan, in his book Indigenous Banking in south India (The Bombay State Co-operative union, Bombay, 1959), speaks of the remarkable vitality and the high degree of elasticity of chit funds to withstand competition from other organized institutions and their adaptability to changing needs of the people. It is entirely left to the foreman of the chit to devise ingenious ways to attract members to the fund.\(^\text{12}\)

Dr. C.P.S. Nayar in his book chit Finance has given an account of the growth of chit funds in Maharashtra and the Union Territory of Delhi. He estimated the annual turnover of business of 125 chit companies in Maharashtra at Rs.217 lakhs, at the end of 1968. In the Union Territory of Delhi, there were 109 registered chit companies at the end of 1969 with an annual turnover of about Rs.6 crores.\(^\text{13}\)

A study made by Dr. S. Radhakrishnan and others showed that in case of six public limited Companies in Tamil Nadu, the maximum discount at the auctions for various groups varied between 30 and 45 percent in the years 1972 and 1973. The default percentage in case of these companies never exceeded
5% Bad debts were less than 1% of chit amount in the case of 3 companies, 2% in the case of 2 companies and 2.6% in the case of one company.

The Institute for Financial Management and Research, Madras conducted an Opinion Survey in which 118 subscribers to chit funds in the city of Madras were interviewed. They consisted of people in the income range of below Rs.500 p.m. (45 persons or about 39%) between Rs.501 and Rs.1000 p.m. (57 persons or about 49%) and above Rs.1000 p.m. (16 persons or about 12%). 105 persons stated that they had joined chit funds primarily to borrow for purposes such as to repay old debts, to redeem jewels, to meet important expenses, to celebrate marriages or other religious functions and to buy jewellery. Only a small number of persons join to acquire funds to buy property or for their business purposes. Eighty members admitted that they were not aware of the cost of borrowing from chit funds. They approached chit funds mainly because they could not obtain credit from elsewhere. For many of them, chit funds were the only source of credit and they had been members for a long time.

It was reported in the Indian Express (August 3, 1972) that the total number of unauthorized chits in the state as on March 31, 1971 was 19,216 involving Rs.7.55 crores.
In a report published by Central Bureau of Investigation, New Delhi, in 1964, its Director Shri. D.P. Kohhi, observed “quite a number of persons have suffered serious loss on account of the operation of the chit funds, perhaps many more than what is known or generally believe. The worst feature is that the victims are those who belong to the middle income group and who even otherwise, live from hand to month. The evil designs and machinations of the organizers of some of the chit funds lead some of these people to near ruin. In most cases, they have hardly any remedy and even if the perpetrators of the crime are arrested, prosecuted and convicted, the money lost is hardly ever recovered”.

Dr. V.T. Mathew in his paper “Commercial Banks and Chit Funds” presented at the Institute For Financial Management and Research’s seminar put forward a number of points in favour of commercial banks entering the field of chit business. They were:

a. Commercial banks would protect the interests of small savers and bring more people into the fold of organized banking.

b. They would enable banks to extend, through chit funds, loans for non-productive purposes, which they would not be able to provide normally.
c. They would augment the resources of the banks in the form of periodical subscriptions; and

d. They would provide supplementary source of income for banks in the form of fixed commission\textsuperscript{18}.

Shri L. Krishnan, Chairman of the Madura Ltd., pointed out that the main causes for the failure of chit funds were their inadequate capital structure, poor liquidity, dishonesty of management and unsound lending policy. Commercial banks were free from these weaknesses and hence, ideally suited to conduct chit business more efficiently than private foremen. Moreover, commercial banks were careful in enlisting subscribers and because of a good system of collection machinery, kept the arrears of subscription at a minimum\textsuperscript{19}.

A study prepared by Shri. A. Hasib for the Banking Commission expressed concern over the mushroom growth of many non-banking financial intermediaries like loan companies and chit funds and observed that they had either outlived their purpose or did not-contribute to the economic well-being of society\textsuperscript{20}.

Dr. Brahmananda, Professor of Monetary Economics at the University of Bombay conducted a study as regards the end-use of chit fund credit, it was testified that 57 percent of the small-
prize amounts below Rs.1000 and about 20 per cent of the medium prize amounts between Rs.1000 and Rs.5000 were generally spent on unproductive or consumption purposes. It was only in the case of high-prize amount of above Rs. 5000 that about 85 percent were generally used for investment in business and these high-prize chits constituted only a small part of the business of a chit fund.

In a study conducted by Dr. C.P.S. Nayar, the data collected from 100 prize-winners in Kerala, Tamil Nadu and Maharashtra, showed that the shares of the prize money going into productive purposes in the three categories of big, medium and small prize-amounts were roughly 90 percent, 60 per cent and 33 per cent, respectively, of the total prize-amount.

The study conducted by The Travancore Banking Enquiry Commission, revealed that chit funds have stood as a major portion of strength to the commercial banks. Chit funds are a major growth sector, growing at the rate of 20-25 per cent per annum. The total turnover in 1970 was placed at about Rs.110 crores and in 1975 the turnover was estimated at Rs.200-225 crores. If tapped properly, they can augment the resources and operations of the banking system in a steady and sustained manner.
The finding of an independent study by Dr. P.R. Brahmananda shows that a substantial proportion of the prize amount is used for productive purposes and only a small percentage is devoted for pure consumption. The study also proves that the proportion of funds used for productive purposes increased with the size of the prize amount; larger the prize amount, less the share used for consumption.

It is true that the study Group on Non-Banking Financial companies held the view that “the likelihood of productive use of the prize amount is small. A prospective producer would not depend on the uncertainties involved in a chit fund. The rates of interest generally involved for a prize winner in a chit fund are so high that an inference can be drawn that the prize money is mostly used for consumption or speculative purposes.”

The Organization for Economic Co-operation and Development (OECD) project report by S. Madhur and C.P.S. Nayar gives a break up of credit from chit funds as follows: Trade and business 30%, acquisition of assets and livestock, jewellery and household equipment 17.5%, Building Construction / renovation / repairs and acquisition of landed property 12.8%, personal consumption including social and religious ceremonies 14%, small business, professionals and self-employed 7.5%
cinema theatre and film industry 3.7% Repayment of old debts
4.5% transport including purchase of used vehicles 3% and
unspecified 7%. The figures show that about 41% of credit flows
to direct economic activity, 30% to acquisition of assets while
only 14% flows to personal consumption.26

An opinion Survey of Chit Subscribers in the city of Madras
was conducted by the Institute for Financial Management and
Research in July-August 1974. About 300 Subscribers were
interviewed by the investigators. The important conclusions of
the study were.

1. The subscribers of chits were mainly in the income group
of Rs.200-Rs.1000.

2. People joined chit funds of companies and informal chits
mainly to meet their unproductive expenditure such as celebrating
marriages, redeeming pledged jewels, repaying old debts and
the like. Only a small percentage of the sample expressed the
view that they joined chit funds to meet their productive needs.
Those who joined the traders' prize chits were motivated primarily
to win the prize at the monthly draws.

3. The study indicated that many subscribers to chits feel
that they were conducted fairly and honestly. However, this
conclusions cannot be taken at face value, for the majority of
respondents were subscribing to well-established and reputed chit companies and traders and merchants. There were no complaints generally about informal chits. A few subscribers did complain about several malpractices in the chits.

4. A large number of chit subscribers were not aware of either the cost or risks associated with chits. Even those who were aware of the high costs and risks admitted that they were forced to resort to chit funds, because of their easy accessibility and availability of funds for non-productive purposes.

It was observed by A.G. Chandavarkar, the Informal Financial Sector in Developing Countries, International Monetary Fund, 1986, "The general stance of policy towards the informal financial sector including chit funds in developing countries can be best described as an amalgam of being neglect and even prejudice, which is unwarranted considering that its scope and persistence testify, if any thing, to its basic economic rationale deriving from its capacity to satisfy needs which are not met by the formal sector, Rather it supports the ease for a positive and coherent policy towards the informal financial sector."

Prof. Dale W. Adams of Ohio State University and Delbert A. Fitchett, Senior Economist in the World Bank say "Sustainable financial markets that operate efficiently and equitably are vital
ingredients in rural development. The results of many formal agricultural credit programs in low income countries over the past 30 years have been disappointing, and informal finance appears to be doing a better job of servicing the financial needs of many people in these countries than do these formal efforts." Informal Finance in Low Income Countries, West view Press, Oxford, 1992)29.

A recent five country study on "Informal Finance: some findings from Asia", by the Asian Development Bank and published by the Oxford University Press in 1992, explicitly gives some of the attractions of chit funds to the members as

i) reciprocity or the in-built provision for borrowing at short notice by bidding successfully for the kitty, a sort of access to liquidity guaranteeing function especially important to businessmen.

ii) Being able to save in instalments.

iii) Having to do so compulsorily once the initial decision to join had been made, by deferring other consumption expenditures, if necessary and

iv) Convenience and the absence of formalities".30

As a remedy for the temporary shortage of funds faced by the foremen of chit funds, the OECD project Report by S.
Madhur and C.P.S. Nayar recommend that, “there should be some provision for these institutions to get refinance facilities from Commercial banks fairly, easily but at competitive interest rates and not subsidized, administered rates.”

An Opinion Survey Conducted by the Institute for Financial Management and Research among 105 subscribers to traders' prize chits in the city of Madras showed that more than 70 percent of them were subscribing to more than one chit group or type. The most popular type of chit was in utensils followed by textiles (mostly sarees) and jewellery. Nearly 80 per cent of the subscribers expressed the value that they joined the traders' prize chits primarily to win the prize at the draw.

The Banking Commission had reported in 1981 that indigenous, informal credit channels, including chit funds could account for as much as one-half of all credit to different categories of economic activity.

In the report of a study Commissioned by the Banking commission in 1989, the Asian Development Bank 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 in being so flexible in operation as to
provide a choice in respect of the timing of the borrowing and indirectly the rate of interest as well\textsuperscript{34}.

The Asian Development Bank made a study in 1992 on ‘Informal finance some findings from Asia’. They have highly appreciated the role played by the chit funds and commended that these funds have been meeting the individual requirements without the need for complying with inconvenient and complex formalities\textsuperscript{35}.

A socio-economic study of the unorganised sc/st (dalit) workers in Rural areas with special reference to Tirunelveli District in Tamil Nadu. The study reveals that fifty years of independence have gone by, but the socio-economic conditions of the Dalits are deplorable. Therefore, it is the responsibility of the government to raise the standard of living of the dalits by launching various employment schemes providing alternative avenues of employment and by making them earn income throughout the year.\textsuperscript{36}

Impact of Bank lending to weaker sections of the society at Pudukottai Block in Chidambaranar District - an empirical study carried by S. Caroline. The study is an attempt to highlight the socio-economic impact of bank credit on weaker sections of the society. The study reveals that out of 100 sample borrowers, 87
have satisfactory level of improvement in their economic position. All the 100 sample borrowers have satisfactory level of improvement in their social life. Hence, it is concluded that there is an improvement in socio-economic conditions of the weaker sections of the society because of bank loan at Pudukottai Block of Chidambaranar District.\textsuperscript{37}

A study of Financial Performance of the Kerala State Financial Enterprises Limited. The researcher concluded that KSFE Ltd., as a public sector enterprise discharges its social responsibility, if it creates healthy surplus with which it can both grow itself and enable the state, by giving fair return on investment to propagate its economic activity and social welfare.\textsuperscript{38}
1.6. Objectives of the Study:

The objectives of the present study may be stated as follows.

1.6.1. To evaluate the significance of chit funds in the structure of Indian Financial System.

1.6.2. To examine critically the development of chit funds in Kanyakumari District.

1.6.3. To find out the repayment performance of the chit subscribers.

1.6.4. To analyse the socio-economic development of chit subscribers through chit funds.

1.6.5. To analyse the socio-economic development of chit foremen through chit funds.

1.6.6. To discuss the cost implications of chit funds and

1.6.7. To offer suggestions based on the findings for further development.

1.7. Hypotheses of the Study

Hypotheses are framed to test the following matters.

1.7.1. To know the structural changes of Chit Funds in Kanyakumari District during the 10 year period under study.
1.7.2. To Know the factors which significantly affect the repayment performance of chit subscribers.

1.7.3. To bring out the social and economic factors which influence the socio-economic development of chit subscribers of Kanyakumari District through chit funds.

1.7.4. To bring out the social and economic factors which influence the socio economic development of chit foremen of Kanyakumari District through chit funds.

1.7.5. To highlight the reasons for the success of the chit business.

Supportive hypotheses have also been framed to substantiate the above mentioned major hypotheses.

1.8. Scope of the study:

The present study highlights the development of socio-economic status of the various subscribers and foremen of chit business. There are two ways of studying the problem. One is from the point of view of the subscribers and the other is from the point of view of the foremen. The present study takes into account both the aspects, however confining only to the Kanyakumari District of Tamilnadu.
1.9. Operational Definitions of Concepts Chit

**Chit:**

Chit means a transaction whether called chit, chit fund, chitty, kuri or by any other name or under which a person enters into an agreement with a specified number of persons that every one of them shall subscribe a certain sum of money (or a certain quantity of grain) instead by way of periodical instalments over a definite period and that each such subscriber shall, in his turn, as determined by lot or by auction or by tender or in such other manner as may be specified in the chit agreement, be entitled to the prize amount.

**Chit Agreement:**

It means the document containing the articles of agreement between the foreman and the subscribers relating to the chit.

**Chit Amount:**

It means sum-total of the subscriptions payable by all the subscribers for any instalment of a chit without any deduction of discount or otherwise.

**Chit Business:**

It means the business of conducting a chit.

**Default:**

Failure to fulfil an obligation especially to repay the loan.
**Defaulting Subscriber:**

It means a subscriber who has defaulted in the payment of subscriptions due in accordance with the terms of the chit agreement.

**Discount:**

It means the sum of money or the quantity of grain which a prized subscriber is under the terms of chit agreement, required to forego and which is set apart under the said agreement meet the expenses of running the chit or for distribution among the subscribers or for both.

**Dividend:**

It means the share of the subscriber in the amount of discount available under the chit agreement for reteable distribution among the subscribers at each instalment of the chit.

**Draw:**

It means the manner specified in the chit agreement for the purpose of ascertaining the prized subscriber at any instalment of the chit.
**FOREMAN:**

It means the person who under the chit agreement is responsible for the conduct of the chit and included any person discharging the functions of the foreman.

**PRIZE AMOUNT:**

It means the difference between the chit amount and the discount, and in the case of a fraction of a ticket means the difference between the chit amount and the discount proportionate to the fraction of the ticket, and when the prize amount is payable otherwise than in cash, the value of the prize amount shall be the value at the time when it becomes payable.

**PRIZED SUBSCRIBER:**

A subscriber who has either received or is entitled to be received the prize amount.

**NON-PRIZED SUBSCRIBER:**

It does not include a defaulting subscriber.

**SUBSCRIBER:**

Includes a person who holds a fraction of a ticket and also a transferee of a ticket or fraction thereof by assignment in writing or by operation of law.
**Ticket:**

It means the share of a subscriber in a chit.

**State Government:**

It is in relation to a Union Territory, means the administrator of the Union Territory appointed by the President under article 239 of the Constitution.

**Registrar:**

It means the Registrar of chits appointed under section 61 and includes an Additional, a Joint, Deputy or an Assistant Registrar appointed under that section.

**Investor - Member:**

If the prize-money received by a member exceeds his total net subscription, he is deemed to be an investor-member, and the excess of his prize-money over his total net subscriptions constitutes the interest received by him.

**Borrower-Member:**

If the prize-money received by a member falls short of his total net subscriptions, he is regarded as a borrower-member, and the excess of his total net subscriptions over the prize-money represents the interest paid by him.
**Authorised Agent:**

It means a person duly authorized by a power of attorney executed and authenticated in the manner specified in section 33 of the Registration Act, 1908 or a person authorized by a duly stamped power of attorney or a letter of authorization specified in Form XX by the person concerned.\(^1\)

**Special Resolution:**

It means a resolution which is passed at a meeting specially convened for the purpose of the general body of subscribers by a majority of not less than two-thirds of the subscribers present at the meeting in person or by proxy.

**Variola:**

It means the discounting containing the articles of agreement between the foreman and the subscribers relating to the chitty.

**Veethapalisa:**

It means the share of a subscriber in the discount available under the variola for rateable distribution among the subscribers at each instalment of the Chitty.\(^2\)

**Act:**

Act means the Chit Funds Act, 1982 (central Act 40 of 1982)
ADVERTISEMENT

It means any matter published on behalf of the company in a newspaper and any other written or printed matter published in the form of a notice, prospectus, circular or other document or any other material or text appearing on posters, bill boards and hoardings and includes any matter appearing on lantern slides or exposed cinematograph films.

FREE RESERVES:

It shall include all sums shown or published in the balance sheet or in the profit and loss account of the company as being retained for any general or unspecified purpose and any statutory development rebate reserve created under sub-section (2) of section 10 of the Income tax Act, 1922 or sub-section (3) of section 34 of the Income-tax Act, 1961 or any reserve for development allowance created under sub-section (3) of section 33A of the Income-tax Act, 1961 or under any other law which is for the time being in force but shall not include depreciation and renewal reserves or other receives which may be earmarked or declared by the company to be earmarked for any specified purpose.
**Depositor:**

It includes any person who has given a loan.

**Main Occupation:**

In this study, main occupation means the routine business which is undertaken by the subscriber or foremen at the time of joining or running the chit business.

**Subsidiary Occupation:**

Subsidiary Occupation means the occupation of the subscriber or foremen other than the main occupation.

**Economic Impact:**

In this study economic impact means the improvements in income, expenditure, savings, Personal Investment and Business Investment of the chit subscribers after joining the chit and foremen after starting the chit business.

**Social Impact:**

In this study, social impact refers to improvement in 20 aspects. They are improvement in friendship, improvement in contact which relations, improvement in charity outlook, membership in various association, development in leadership quality, increase in status of life, increase in skill and knowledge, involvement in social service, interest in religious
activities, involvement in recreation, participation in various activities, social welfare services, change in the living lifestyles, change in the behaving lifestyles, cultural change, change in the ethical values, social control, social mobility, change in the social attitude and social change due to technology.

**COMPANY:**

It means any body corporate and includes a firm or other association of individuals.

**DIRECTOR:**

Director in relation to a firm means a partner in the firm.

**1.10. PERIOD OF THE STUDY:**

The present study covers a period of 10 year from 1990 to 1999. The socio-economic survey was conducted from June 1999 to April 2000 with the help of Interview Schedules.

**1.11. METHODOLOGY:**

The present study is mainly empirical based on survey method. The primary data of the study were mainly pertaining to the socio-economic impact of the chit subscribers and chit foremen. For collecting the primary data, a field survey with the help of Interview Schedule (Appendix A) to the chit subscribers and Interview Schedule (Appendix B) to the chit foremen were administered.
The required secondary data have been collected from the records of the registrar offices of Nagercoil and Marthandam, Government Statistical Department, Nagercoil, RBI Bulletins, Monthly magazine Chittu Murasu, the book Chit Fund, a few articles of Dr. C.P.S. Nayar, Prof. Radhakrishnan, Souvenir of Economic Liberalisation and Chit Funds and the compilation of the seminar papers on the Management of Chit Funds and the like. The researcher has personally interviewed the officers and chit inspectors of Registrar Offices to get additional information regarding the performance of chit funds.

1.1.1 Sample Design:

For conducting the survey, the researcher selected 200 chit subscribers and 70 chit foremen by adopting simple random sampling and convenience sample respectively.

1.1.2 Tools for Collection of Data:

Two Interview Schedules have been prepared to collect information for the present study. One is for the chit subscribers and the other is for the chit foremen. Both the schedules have been prepared keeping in mind various factors which directly and indirectly affect the functioning and performance of chit business and also the impact of the same on the socio-economic development of the people who involved in it. Variables to be studied have been identified by the researcher by going through various literature directly and indirectly connected with the study.
1.11.3 Framework of Analysis

The main aim of the study is to analyse the socio-economic development of chit fund subscribers and chit foremen in Kanyakumari District.

To find the development of the chit fund in Kanyakumari District, straight line trend has been applied with the help of the Method of least Square by $Y = a + bx$ equation. Simple Correlation and correlation by grouped data have been applied to find out the relationship between various items. The structural changes of the Chit registration of Kanyakumari District in two Registrar Offices over 10 years have been calculated with the help of the significant of correlation analysis, by applying the following formula.

$$t = \frac{\sqrt{n-2}}{\sqrt{\Sigma x^2 \cdot \Sigma y^2}}$$

where $r = \frac{\Sigma xy}{\sqrt{\Sigma x^2 \cdot \Sigma y^2}}$

$n$ = number of items

The items taken for comparison were the chit registration by men, women, chit amount, arbitration amount, registration as Individual, Partnership Firm, Company, number of chit registration number of arbitration cases filed and the number of persons filed the arbitration cases. These factors were compared with the period of 10 years.
To analyse the extent of repayment performance of the chit subscribers, a non parametric test, chi-square is used. The $\chi^2$ test described the magnitude of the discrepancy between theory and observation. The observations are based on the identified 10 influencing factors. They are sex, age, caste, occupation, size of the family, education, amount of chit, purpose of joining the chit, utilization of chit amount and the motivation they got from the foremen to join in the chit. The formula for $\chi^2$ test is

$$\chi^2 = \frac{\Sigma (O-E)^2}{E}$$

Where $O$ = Observed frequencies

$E$ = Expected frequencies

The expected frequency for any frequency can be calculated by adopting the formula.

$$E = \frac{RT \times CT}{N}$$

Where

$RT$ = The row total for the row containing the cell

$CT$ = The column total for the column containing the cell

$N$ = The total number of observations

Since the cell frequency happens to be less than 5, in observations, Yates' Correction is applied for continuity\textsuperscript{45}. The
formula used for this purpose is

$$\chi^2 = \frac{(O - E - .5)^2}{E}$$

At the time of analyzing the extent of socio-economic development and the factors influencing the development, certain statistical methods such as Mean, Standard Deviation, Coefficient of Variation, Chi-square, Two-way Analysis of variance and Association of Attributes have been used. With a view to test the hypotheses, a scale has been constructed for measuring the dependent variable of the study.

The dependent variables are the social factors and economic factors. The researcher has identified five economic components namely income, expenditure, savings, Personal investment and business investment. The 20 factors selected for social improvement are improvement in friendship, improvement in contact with relations, improvement in charity outlook, membership in various association, development in leadership quality, increase in status of life, increase in skill and knowledge, involvement in social service, interest in religious activities, involvement in recreation, participation in various activities, social welfare services, change in the living lifestyles, change in the behaving lifestyles, cultural change, change in ethical values, social control, social mobility, change in the social attitude and social change due to technology.
As there is no readymade scale to measure the impact levels, two scales namely ‘Economic Impact Scale’ and ‘Social Impact Scale’ have been developed and scores have been awarded to the components.

The economic impact scale has been constructed with the help of 100 scores. These total scores are equally distributed among all the five components that is 20 scores for each component. It has been measured in terms of percentage calculated for all the five components. The % has been calculated on the basis of data collected for two periods, that is period before getting chit and after getting chit. The 20 scores are distributed on the basis of % for the five components by applying the following formula.

\[
\text{Economic Impact Score} = \frac{\text{Change in the components from the before chit level to the after chit level} \times 100}{\text{Value of the component before chit}}
\]

Like this, economic impact score is calculated for each and every respondent of chit subscribers and chit foremen.

The social impact scale has been computed with the help of 20 components. For each component, 5 statements have been prepared. Altogether there are 100 statements. For every statement, two point scale ‘yes’ or ‘No’ has been applied and for ‘Yes’ response ‘One’ score and for no response ‘Zero’ score have been given. Thus the scores secured by the sample respondents
varies from 0 to 100. Like this, the social impact score is calculated for each and every respondent.

On the basis of the scores obtained for economic impact, the respondents were classified into three categories namely high (Mean (\(\bar{X}\)) + Standard deviation (s)), medium (\(\bar{X} \pm s\)) and low (\(\bar{X} - s\)). Similarly on the basis of scores secured for social impact, the respondents were classified into three categories namely high, medium and low. This classification was used as the basis for further statistical analysis. The following formula were used for this purpose

\[
\bar{X} = \frac{\sum X}{n} \quad \sigma = \frac{\sqrt{\sum X^2}}{n}
\]

To find the extent of variation between levels, the Coefficient of variation\(^46\) has been applied with the help of the following formula.

\[
C.V = \frac{\sigma}{\bar{X}} \times 100
\]

To analyse the economic and social impact of the Chit subscribers, 3 main factors namely chit amount, Instalment amount and the Period of chit have been taken into consideration. With regards to the influencing factors, income, education, occupation, type of family and age were taken for social impact and age and occupation for economic impact.
The social and economic impact of the sample chit foremen have been analysed with the help of the main factors like chit amount, number of chits conducted and their experience in chit business. The influencing factors are age, size of the family, occupation, education, the purpose of running the chit business, sex and type of family for social impact. And age, occupation, size of family, type of family, utilization of chit amount, number of defaulters and the purpose for which they are running chit business for economic impact.

To find the success of the sample chit foremen, income has been compared with the factors of monetary motivation, non-monetary motivation, selection of prized subscribers, nature of contacting the subscribers, form of chit registration and the number of assistants they have for collection of chit money. Their extent of association have been calculated with the help of the following formula\(^ {47} \)

\[
C = \sqrt{\frac{\chi^2}{N}} \\
\text{Where} \quad \chi^2 = \frac{\sum (O - E - .5)^2}{E}
\]

\( N = \text{Total number of observations} \)

To test the hypotheses, \( \chi^2 \) test and Two-way Analysis of Variance test have been applied by presenting the data in the following table.\(^ {18} \)
TWO WAY ANOVA

<table>
<thead>
<tr>
<th>Source of Variation</th>
<th>Total sum of squares</th>
<th>Degree of freedom</th>
<th>Mean Sum of Squares</th>
<th>F ratio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Between Columns</td>
<td>SSC</td>
<td>C-1</td>
<td>MSC</td>
<td>MSC/MSE</td>
</tr>
<tr>
<td>Between Rows</td>
<td>SSR</td>
<td>r-1</td>
<td>MSR</td>
<td>MSR/MSE</td>
</tr>
<tr>
<td>Residuals</td>
<td>SSE</td>
<td>(c-1)(r-1)</td>
<td>MSE</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>SST</td>
<td>N-1</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

1.12. LIMITATIONS:

1. Economic and social impact of the chit subscribers and chit foremen are the only two aspects studied. Hence, for want of time, cultural and political aspects have been deliberately omitted.

2. Most of the respondents do not have the habit of maintaining records and the financial data are obtained from their memory. Every attempt is made to elicit accurate information at the time of interview to overcome these limitations.

3. The researcher has taken into Consideration only the registered chit funds of Kanyuakumari District. But there are a number of persons who are running chit business without registration and almost all the people of Kanyakumari District are having chits apart from other savings.

4. The study has been limited to a period of 10 years.
1.13. **Chapter Scheme**

The study has been divided into seven chapters.

The first chapter deals with introduction and design of the study. It includes introduction, history of chit funds, statement of the problem, objectives of the study, operational definitions, review of literature, period of the study, methodology, sample design, tools for collection of data, collection of primary data, processing of data, framework of analysis, hypotheses and limitations of the study.

The second chapter deals with the role of chit funds in the Structure of Indian Financial System.

The third chapter presents an overview of the progress of chit funds in Kanyakumari District.

The fourth chapter analyses the factors influencing the repayment performance of the chit subscribers, the levels of social and economic impact and the factors influencing the same.

The fifth chapter analyses the levels of social and economic impact of the chit foremen and the factors influencing the same. It also analyses the factors determining the success of the sample chit foremen.

The sixth chapter discusses the cost implications of chit funds in detail.

The seventh chapter gives the summary of findings suggestions and conclusions of the study.
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