CHAPTER VI

SUMMARY AND CONCLUSION

Informal credit market is found to be a parallel financial system in an economy. It acts as a catalyst and assists various unprivileged classes in getting credit facilities without much intricate or complex procedures as in the formal system. The unaccounted character of informal credit market poses serious challenge to the implementation of government policies, and at the same time it has been proved as an inevitable part of the system since the formal system cannot meet the financial requirements of all privileged and unprivileged class or business community. Informal credit market is useful and legitimate part of the financial markets. They have been able to develop more or less permanent financial services for the poor in many LDCs while most formal financial system have only provided transitory services to this group.

Focussing on the issues raised by informal credit market the Study is intended to cover important aspects viz., structure, dynamics and intermediation of the urban informal credit market. The first three chapters focussed on introduction with special reference to empirical issues in this area, the profile of informal credit market and the conceptual issues respectively. It needs to be emphasised that the third chapter modified the methodology in defining the informal credit market. The fourth and the fifth chapters dealt with the analysis of primary data relating to the three aspects covered by the study.
6.1 SUMMARY OF THE FINDINGS

Having modified the existing methodology in defining informal credit market, it helped us to find out the minute classification of informal credit market, in Kochi City and its agglomerates. Using this conceptual framework we are able to explain the functioning of different types of informal credit market agents in Kochi. This includes registered and unregistered categories. ICM is more heterogeneous than the formal credit market primarily because of the variety of lender types, the diverse loan and the regionality of credit transactions. The major findings of the study listed below give a clear idea and an overall view about the urban informal credit market.

(1) It is found that full time moneylenders/ entrepreneurs is high among registered chit funds (86.11 per cent) and is followed by registered moneylenders (78.68 per cent). In the case of unregistered category part time moneylenders constitute the major category (64.52 per cent). It implies that businessmen and employees deal in moneylending as their part time activity. But those who run chit funds among them (unregistered) are mostly full timers. According to some experienced foremen, chitties are the most lucrative moneylending activity if it is done with utmost carefulness.

(2) The analysis of the age class of the entrepreneurs shows that most of them (79.68 per cent) are in the 30-60 age group except in the case of entrepreneurs in the unregistered group, where 35.48 per cent are in the prime age group 20-30. The number of entrepreneurs engaged in moneylending in the unregistered category declines as the age group advances.
Another feature of the informal credit markets is that 49.21 per cent of the entrepreneurs were Christians of various castes, followed by various castes in Hindu community 38.28 per cent (49 entrepreneurs). Further analysis shows that Christians constitute the major category under registered moneylender and chit funds category i.e., 59.01 per cent and 55.55 per cent respectively. But in the case of unregistered category Hindus constitute the major category (54.87 per cent).

Considering the educational qualifications, most of the entrepreneurs were having (33.59 per cent) S. S. L. C qualification only. But in the case of unregistered category most of them were (48.38 per cent -15 entrepreneurs) below S. S. L. C. qualification. One notable feature is that Post graduates were in the moneylending activity, along with Professionally and Technically qualified entrepreneurs.

Another finding is that entrepreneurs had mainly nuclear family setup. Of the 128 entrepreneurs 59.37 per cent (76) had nuclear families. This is equally true of all the three categories.

It is found that the line of activity of registered category of ICM and the activity for which licenses have been obtained by them were found different i.e., ICMs do not function according to the licenses they have obtained. Virtually there is no visible difference between the activities of the registered and unregistered categories. This implies that registered moneylenders work in the economy as if they were unregistered moneylenders, since the law enforcing authorities are not able to control these registered categories. Hence they function outside the penumbra of Moneylending and Chit funds Laws. The unregistered moneylenders are found to be unchallenged, since they do not form in any way, part of the legal system. It is found
that they transact crores of rupees unaccountedly and not showing their actual account and not paying taxes according to the volume of business done by them. It is found that the existing laws are found to be inadequate to control and regulate the informal credit markets since there involves confidentiality in their functioning.

(7) Further analysis shows that licenses obtained by moneylenders were used as an authority to do any kind of moneylending/ chit funds business. It was found that moneylending firms who have obtained moneylending license also found to have engaged in chit funds unauthorisedly or in other words they run chitties in guise of having licenses. Similarly, chit fund firms who have obtained chit fund license also run moneylending business unauthorisedly. Thus there were interpenetration of markets between these two categories of firms. It was also found that moneylenders had more inclination towards running chitties because chitty activities were not regulatory in character, performed as per the licenses obtained from outside the states.

Further analysis shows that of the 31 firms which had moneylending licenses 83.87 per cent (26 out of 31) firms were proprietorship and, of the 28 firms which had chit fund licenses 67.86 per cent firms were private limited companies. Another interesting finding is that, of the 38 firms which had both moneylending and chit fund licenses, 52.63 per cent (20) firms were partnership firms. Thus the type of business organisation is a major factor while obtaining licenses.

(8) Detailed analysis of the licensed categories and comparing the licenses they have obtained with their actual activities reveal that there is incompatibility between the authority to do a particular moneylending business and their actual operation. For
example the examination of firms which have obtained moneylending licenses portray that these firms did not remain in the gold loan activities. 54.83 per cent (17 firms) diverted their attention to other forms of moneylending. The firms which have obtained chit fund licenses were also found to have diverted their attention from their actual activities. But the percentage of aberration from the licensed activities is low in the case of chit funds activities. In the former case of the 31 firms 17 of them had other forms of moneylending (54.83 per cent) and in the latter case only 42.85 per cent (12) firms diverted from the actual licensed activity.

(9) It is found that of the different categories in the ICM, chit funds constitute the major activity of the informal credit market. Out of the 128 moneylenders 69.53 per cent had chit funds business, followed by 100 day’s loans (64.84 per cent) and gold loan (46.87 per cent). This analysis reestablishes the above fact that chit funds activities constitute the major category among the informal credit market agents in Kochi.

(10) Operational area of moneylenders/ chit funds is found out to be very important in ICMs. Those specialise in moneylending concentrated only on local area, because gold loan is their main form of business and for which gold jewellery/ornaments is used as collateral. They are not ready to advance money to all who bring gold jewellery unless the borrower is introduced by any of his friends. But considering the other activities the lender may not get sufficient borrowers from the local area hence they focus their attention on a larger area. In the case of chit funds, sufficient number of clients is not available from the local area. But the foremen try to woo enough clients from the local area by introducing new and easy methods to pay the subscription amount.
(11) Another aspect to focus is that informal credit market is found to be charging high rate of interest and this can be attributed to various factors. Inelastic demand for informal loans is the prime reason. Exploitative or monopoly factors do not form reason for the high rate of interest charged by the ICM. In its place, risk of default is considered as a factor responsible for the high rate of interest. It was also found that there exists a reference interest rate in the informal credit market and this guides the moneylenders in deciding the rate of interest on the loans they advance. Another interesting feature is that there is no uniform rate of interest for different kinds of loans. It was found that the highest rate of interest charged on monthly loans was 144 per cent per annum. In the case of 100 day’s loans it was 60 per cent. In the case of 50 day’s loans 81.1 per cent is the maximum recorded. The lowest rate of interest was found in the case of gold loans where, 36 per cent per annum is the maximum.

(12) The relation between collateral instruments and the rate of interest is another feature noted in the informal credit market. Except for the short duration loans, collateral instruments form the basis of the determination of rate of interest. The lender demands collateral securities like documents of house/ properties and gold ornaments in the case of gold loans. The lenders also demand in place or in addition to the collateral securities, collateral substitutes like post dated cheques, promissory notes, stamp paper duly signed etc. One reason for the demand of the collateral is that there exists time gap between two payments. But the presence of collateral instruments is absent in the case of daily loans because the payments of which is done daily. In the case of monthly loans, moneylenders charge different rate of interest to different borrowers depending on the type of collateral. Fully marketable
collateral would cost only less rate of interest. Thus there is a negative relation between rate of interest and the value of collateral. It was also found that rates of interest charged also depended on the status of the borrowers. Hence the difference in interest rates which depend on the type of collateral security and the status of borrowers confirms the first hypothesis developed in the study. Other than this information on borrowers was also found to be a major factor while determining the rate of interest.

(13) The evidence gathered from the study proves that informal credit market depends on various sources of funds for capital. Their chief source of funds are mainly public deposits, funds from relatives, own capital etc. Of the 128 firms only 10.15 per cent (13) firms fully depended on own capital and among them unregistered group occupies the largest number. It was found that most of the moneylenders mobilised public deposits unauthorisedly. And not a single firm was found to be using/depending on public deposits fully. Public deposits are the single largest category in the capital of the moneylenders. 103 moneylenders (80.47 per cent) depended on public deposits. Realising that informal credit market cannot give guarantee to the deposits they mobilised, Reserve Bank of India has amended the existing law banning/restricting the informal credit market from accepting public deposits. But the restriction remained only on cards. ICM continued to mobilise deposits from the public by offering high rate of interest. It is interesting to note that the public is unconcerned about the security of their deposits and they continued to rely on informal credit market. It was found that most of the deposits are black money and this cannot be deposited with formal banks.
Registered moneylenders mobilised an average of 28.29 per cent of public deposits in the total capital. This is low compared to registered chit funds (28.43 per cent) and unregistered category has the highest average i.e., 25.55 per cent. Comparing the three categories it is found that registered moneylenders are more stable in regard to deposit mobilisation. (Coefficient of Variation (C.V) – 31.77 per cent). The deposit mobilisation is more variable in the case of registered chit funds.

Analysing the rate of interest charged on deposits unregistered category offered the high rate of interest and it is clear from the analysis of average. This category has the highest of averages (31.77 per cent). The lowest average is in the case of registered chit funds (19.37 per cent). The rate of interest offered is more variable in the case of registered moneylenders and less variable in the case of unregistered category. On an average 70.29 per cent of the total capital is used as own capital by the registered moneylender group. But unregistered category has the highest average 78.62 per cent. The C.V is highest in the case of chit funds. (34.23). And it is more stable in the case of unregistered category (19.03).

Registered chit funds holds the highest average (27.5 per cent) with regard to the funds from relatives and their use of funds from the relatives is more stable than others (14.60 per cent). But it is more variable in the case of registered moneylenders (36.88 per cent).

It is further established that there is a relation between formal credit market and informal credit market. Number of previous studies proved that informal credit market depended on formal credit market and formal credit market in turn used the funds from the informal credit market. There are mainly four types of relations with
the formal sector, viz., ordinary relation, safekeeping, repledging and availing loans. 60.15 per cent (77) firms were found to have ordinary relationship with the formal credit markets. In the registered moneylending category 42.62 per cent (26) firms had depended on formal banks for safekeeping valuables (jewellery) and repledging in order to meet the illiquidity resulting from the shortage of sufficient funds. Chit funds used overdraft facilities from the formal banks in times of financial difficulty while paying the prize amounts to the clients. Some firms also availed of loans in order to relend. It was found that informal credit market depended on formal credit market for funds. Thus there exists only a vertical upward integration between the two sectors. But no downward integration is found to exist. Hence the second hypothesis developed in the study is partially valid in the context of Kerala. Further analysis show that entrepreneurs who are businessmen in the past had intimate relationship with the banking community.

Further analysis shows that informal credit market in urban areas has availed of overdraft facilities from the formal banks compared to firms in the suburban areas. This is because most of the chit funds are concentrated in urban areas. Firms which had obtained only the moneylender license were found to have safekeeping and repledging relation with the formal banks (19 out of 31 firms-61.28 per cent). It is clear that one of the their main moneylending activities is gold loan. It is further established that firms, which had concentrated on local area, were found to have more safekeeping and repledging relation with formal banks. It reestablishes the fact that firms, which deal in gold loan mostly, concentrate on local area. Out of the 60 firms, which had concentrated on local area, 21 firms (35 per cent) had safekeeping
and repledging relation. But in the beyond local area category only 8 firms out of 55 firms (14.54 per cent) had safekeeping and repledging relation. It is because most of the firms in the beyond local area category were chit funds firms. Coming to the large area category not a single firm had safekeeping and repledging relation with formal banks but in place of that 4 out of 13 firms (30.76 per cent) had availed overdraft facilities from the formal banks. This is because the firms, which have concentrated on a large area, are mostly conducting big chitties and sometimes they are in dire need of liquid cash to payoff the prize amounts.

(15) Analysing the occupational mobility, it was found that most of the entrepreneurs came from business community (37.5 per cent), especially among registered chit funds. Of the 48 entrepreneurs migrated to the moneylending activity, 56.25 per cent (27) were full time moneylenders. Of the 29 entrepreneurs who were agriculturists in the past, 65.5 per cent (19) were migrated to the moneylending activity as full timers. But the number of full time moneylenders who have migrated from any occupation is high in the case of employment. In this case, of the 22 entrepreneurs, 77.27 per cent (17) were full time moneylenders. Of the 38 part timers 50 per cent (10) were businessmen in the past. Thus we conclude that business community represents the highest class in regard to part time moneylenders.

(16) In the urban informal credit market in Kochi it was found that there were only thirty migrated entrepreneurs out of the total 128 entrepreneurs. (23.43 per cent). Out of this 66.7per cent (20) belong to the registered category and out of these 83.3 per cent belonged to the urban areas. Further analysis shows that 56.6 per cent (17) of the
migrants were part timers, and among them 70.58 per cent were business people and the rest were employees.

(17) Informal credit market is found to be helpful to those which are rationed out of the formal financial sector especially small scale borrowers and informal enterprises. Further analysis shows that 56 per cent of the borrowers who borrowed money from the registered moneylenders constitute small-scale firms. In the unregistered category of the total 77 per cent firms were small-scale borrowers. In the case of registered chit funds 52 per cent of the firms were small-scale firms. It was found that out of the 105 firms of small scale 76.19 per cent (80) have borrowed from the informal credit markets. And among them 50 (62.50 per cent) firms depended on informal sector only and the rest of the firms depended on both formal and informal sector. It was found that only 14 firms out of the sample 105, fully depended only on formal credit markets. Trading firms constitute the highest category among the borrowers i.e., 45 out of 80 firms (56.25 per cent). Hence, there is horizontal integration between informal credit market and informal sector. Thus the third hypothesis developed for the study is found valid in the context of Kerala.

(18) Traders in the informal sector also depended on formal credit market for fixed capital requirements and working capital requirements. Analysing the relation between informal sector and informal credit market traders depended on informal credit market to meet working capital needs. But in the case of personal service category, most of the firms depended on informal credit market for household loans. It was also found that manufacturing firms depended on registered moneylenders. Trading firms more or less depended on both registered and unregistered
moneylenders. In the informal sector there are firms with temporary and permanent structure. Within the informal credit markets some lenders do not like to lend to firms having temporary structure. These lenders are fairly big moneylenders with handsome trade volume. But unregistered moneylenders like to lend to firms having temporary structure. This is also because unregistered moneylenders mostly deal in small amount of money.

6.2 POLICY IMPLICATIONS

1) Policies of the government may affect the constituents of informal credit market in different levels. The constituents in the study affected by the regulations at present are those firms which are coming under the purview of the Kerala Chitty Act, 1975 and Kerala Moneylenders Act, 1958. But except the firms coming under Kerala Chitty Act, 1975, (Chitties run according to this only) all the other firms are not adequately controlled by the government departments. The chitty firms, which are said to be registered with Commercial Establishment Act in the other States, are totally out of control of any Government or Banking authorities.

Of late, Government has evolved policies to regulate the non-banking financial intermediaries especially with regard to the acceptance of deposit mainly as an adjunct to Monetary and Credit Policy. But this sector had been included in the formal sector (See Conceptual Framework) except the chit fund companies. Regulating this sector does not ensure the control of informal credit market.

In the case of firms coming under the Kerala Moneylenders Act, 1958 RBI has announced certain control to regulate this sector. But in the real world any attempts
credit market find other ways and means to function. The sheer restriction on deposits taking activities of ICM could not deter the ICM to accept deposits through unaccounted means or the savers who need high rate of interest deposit money with ICM.

In fact, ICM accepts deposits in order to lend money. If there is restriction on acceptance on deposits from the public ICM may find other ways to accept deposits. So their source of funds and deployment of fund is totally unknown to the authorities. If the government permits the constituents (registered firms) to lend a specified sum of money and accept a certain specified sum as deposits, and fix a fee for this category it would result in more regulation of the ICM than the present level. It should be thoroughly checked that moneylenders show it in their books of accounts. And laws should be amended in order to cancel the licenses of those firms which do not comply with the laws and also those firms which are not able to deal in the volume of money sanctioned by the authority or in other words if the firms could not deal in the ceiling fixed by the authorities, there should be a system to cancel the licenses of the concerned moneylender. Thus giving them more freedom of action to deal in moneylending may bring sufficient regulation and at the same time more income to the government in the form of taxes. Suppression or regulation of moneylending business may bring substantial increase in the volume of business through unaccounted means. This policy is suggested in view of the finding made in the study that, big volume of business is done by those firms who have taken either moneylending or chit fund licenses. Since the moneylending business involves enormous amounts of black money, the policy needs strong implementation and
vigilance. And it is better to give authority to the RBI to control and regulate all the moneylending business coming under the present Kerala Moneylender Act, 1958 framework.

2) Chit business is found out to be the most important business among the informal credit market. The volume of business done is running to crores and crores of rupees. Another fact is that most of the firms in the ICM run chitties according to the rules of the other states where no chitty law is in effect (especially Jammu and Kashmir). So these firms are outside the control of the Kerala Government authorities. Policies should be framed in order to restrict the activities of these chit funds. Government should enact laws to control these firms and should direct all these firms to obtain a license from the State government authorities. Along with that Reserve Bank of India should take measures to regulate the chit fund companies irrespective of their type of organisation just like they govern the constituents in the Non-banking Financial Companies. But it is alleged that by the implementation of Kerala Chitty Act, 1975, many firms could not conduct chitties in Kerala, as the ceiling for private chit fund was restricted at prize amount Rs.25,000. If the Government raises this ceiling the Government may get lakhs of rupees as taxes from these private companies. Thus the government can control their unauthorised chitty activities.

3) One merit of the ICMs is that they accept all kinds of collateral securities and collateral substitutes like post dated cheques, promissory notes, blank stamp paper duly signed by the borrower etc. Measures should be taken by the Formal Banking authorities to accept all kind of securities mentioned above and should advance
money on the basis of the financial standing of the borrower, and keeping a close watch on the borrower by employing marketing executives/agents to collect the repayment promptly.

The formal sector banks by insisting only on fully marketable collateral make poor borrowers to depend on the informal credit market. The informal banks lend money on simple terms and conditions and they demand high rate of interest. The Government should start programs to help poor borrowers/ informal sector enterprises depending on their performance and area of business. It is found that most of the loans in the informal credit market are daily payment loans and repayments of most of the loans are fully paid, because it is paid back in easy and small installments to the informal credit market. The formal banks deal in big sums of money backed by fully marketable collateral but most of the repayments are resulted in failure.

4) It can be suggested that if the banks start small branches to help poor with decentralised management system i.e., by employing collection agents sans malpractice there would be more or less good repayment rate and for these loans the government should charge a low rate of interest compared to the one charged by the informal credit market.

5) Informal sector needs working capital and not fixed capital. The policy package should give room for improving the credit deployment of the formal sector to informal sector enterprises. For the purpose there should be opened local branches to cater to the needs of the sector locally. Just like some informal credit market the formal banks should give small amounts first and the banks should give a little more
on successful repayment of the loans and so on. Thus making a close connection between the banker and the customer, what is being done by the informal credit market. Close interaction with the customer may bring more information about the defaulting borrower and the banker should stop paying to that customer further, after receiving the previous money. Thus a decentralised banking system is essential for the formal banking sector to support the ill-effects of the informal credit market with regard to the charging of high rate of interest.

6.3 FURTHER RESEARCH ISSUES

The present study has identified a number of issues for further research. The important issues among them are listed below.

1) Just like in the urban sector rural sector also witnesses the presence of informal credit market. Although some sort of studies were conducted in rural areas more analytical study has to be performed using a more advanced conceptual framework in order to find out the different constituents in the rural informal credit market and its working.

2) A comparison between rural and informal credit market can be investigated.

3) Future research can also be carried out to improve the methodology in identifying the true informal credit market so as to use in a national wide perspective.
6.4 CONCLUSION

To conclude it can be argued that with its low acceptability in the legal system informal credit market continues to grow at a faster pace scaling new heights posing a real challenge to the formal banking system and Monetary and Credit Policies. The need of the hour is to deregulate the working of the informal credit market in view of their services to the society especially, the way in which they deploy credit to the needy.

Without much systematic or accounted features they survive the currents of recession by deploying their credit to the needy and the honest borrowers and thus making their working more noteworthy in the present environment. Formal sector can adopt many of the virtues of informal credit market in order to serve the society in a better fashion and also to save the poor and needy borrowers from the clutches of the thirsty moneylenders and ensure a more systematic growth of the economy.