INFORMAL CREDIT MARKETS IN INDIA

By

T.A. Timberg and C.V. Aiyar

The views presented in this paper are solely those of the authors and do not necessarily reflect the official opinions of the World Bank or its affiliates.

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The Public Finance Division has concerned itself with alternative systems of financial intermediation including commercial banks, social insurance funds, and in this instance the Informal Credit Market. A previous study (DFS No. 28) dealt with informal financial markets in Korea and some work by Bhatt and Roe (published as Bank Staff Working Paper No. 338) has suggested a general context for viewing these markets.

The present study represents the findings of a survey of intermediaries and borrowers in several of the important informal, i.e. unregulated, urban credit markets in India. The systems covered are those operated by the Shikarpuri or multani, Gujarati, Rastogi, and Chettiar indigenous bankers and the more modern ones run by finance "companies" and market finance brokers in the cloth and other wholesale markets in various cities.

The results of the surveys of these systems are presented in the context of the Division's and other studies of informal markets and of the discussion of such markets in India and elsewhere.

It is clear that these systems provide a large amount of finance -- at least 50% of that provided by the commercial banks. They serve sectors of the economy or needs that are not served by the banks -- especially support wholesale trade -- and at rates only slightly higher than those charged by the banks. Their transactions costs are normally lower than the banks, and this results in some increase in the total amount of intermediation.

The study reports the number of such intermediaries in the markets studied, the instruments they use and their relative attractiveness to borrowers and lenders, their mode of operations and transactions costs, and the identity of the sectors they serve.

Finally the study uses the evidence marshalled to consider the place of informal markets in the general evolution of financial markets, their effect on the volume of intermediation, and the extent to which they are competitive, complementary or isolated from other financial markets. This last characteristic turns out to be an important explanatory variable for explaining their behavior.

T.A. Timberg
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Abbreviations

EPW -- Economic and Political Weekly (Bombay)
HP -- Hire Purchase
ICM -- Informal Credit Market
ILO -- International Labor Organization
LDC -- Less Developed Country
OCM -- Organized Credit Market
RBI -- Reserve Bank of India
RBIB -- Reserve Bank of India Bulletin (Bombay)
SSE -- Small Scale Enterprise
U.P. -- Uttar Pradesh
I. INTRODUCTION

A. Historical Process

"...One kind of flaw in the system can be the absence of certain markets. The common generic term for the reason why markets are missing is 'transactions costs'. That sounds rather minor, the sort of thing that might go away in due course as accounting and information processing get cheaper. But some of the cases of missing markets really go much deeper."


The process of credit market evolution is characterized by the development of new and different credit instruments to mediate the demands of borrowers and lenders and reduce the transactions costs to the point that more and more intermediation is possible.

Credit markets develop almost in every case where extensive long-range trade or manufacture involving stocks and consumer credit exists. Those with surplus funds lend them to those who need funds to carry on their business -- first for working capital and then for fixed capital assets as well. Soon intermediaries grow up which develop financial instruments -- instruments which serve to reconcile the different terms (length of credit, type of security and so forth) desired by lenders and borrowers. After a period, governments attempt to regulate some of these intermediaries and varieties of instruments in order to protect all market participants -- and often to direct funds preferentially in one direction.
or the other. Other intermediaries and instruments remain outside of the regulatory net in the "informal market". Since the substance of both regulated and unregulated markets is the same mobile lendable funds -- the markets interact -- and funds find their way back and forth between the two markets and go wherever the return is higher. To achieve their purposes of capital channeling, governments often try to repress the informal market, to increase the amount of regulated or channeled funds -- but whether they will be successful or not depends on the external forces which drive the evolution of both markets. To the extent that Informal Credit Markets deal in instruments for which the Formal Credit Markets have no substitute, efforts to suppress the ICM are doomed to failure. In particular, the increases in transaction costs occasioned by artificially channeling funds into the formal market, may cause a net decrease in available funds, and retard economic activity, or repression may fuel "parallel" informal markets.

The raw material here is preeminently Rondo Cameron's volumes on Banking history and Raymond Goldsmith's work on financial development. They actually show some variance. The normal case here was the English, French and German one -- in several cases like Russia and Belgium the state seems rather to have created new regulated institutions to serve the needs which the unorganized market was not meeting.

"Stifling regulation by the Exchange Authorities can be one reason for the establishment of a parallel market. Other reasons are limitations on the minimum transaction or of amounts of each kind of security [instrument] and excessive commissions [transactions costs] charged by brokers on the original market." 1/

The two kinds of markets -- regulated and informal -- may become dis-aggregated and all sorts of irrationalities occur in capital allocation because of the segmentation of what might naturally be a more integrated market.

On the other hand, the repression of informal markets could create space for the growth of a more integrated, rational set of financial institutions.

The pattern of evolution in ICM differs according to whether a market is complementary or competitive with the formal market. 2/ In those complementary cases, like Korea or the extra-bank market in Columbia, we would expect its rates to move in some response to the formal market, and its size to expand along with it. In the Korean case, for example, the banks' appear to be more oriented toward long term, the informal lenders toward working capital. 3/ In addition the ICM's are more willing to serve smaller borrowers. In those cases where the markets are competitive, we would expect an even closer correspondence in rates but an inverse growth in size.


2/ Work in progress by V.V. Bhatt.

India has followed roughly the general pattern outlined here -- old credit markets serving trade and traditional industry remain unregulated -- and co-exist with regulated credit markets serving more modern industry and the state sector. Government policy aimed partially at channeling funds into the regulated financial sector -- and partially at protecting savers and borrowers -- has led to measures of repression which have dis-aggregated this informal market from the regulated one. The questions that arise concern the countervailing gains and losses from such repression and the possibilities for future evolution of the two markets.

B. Definition

For the purpose of this study, informal financial markets are any markets for cash finance (rather than credit in the form of goods) which do not involve directly the regular commercial banks, registered savings institutions, or equity and debentures traded in registered securities markets. The essential characteristic of these markets is that they are far more loosely monitored and regulated than "formal" financial markets. To quote
John Gurley, "If there is anything different about commercial banks [as distinguished from non-bank and in our definition informal intermediaries] in this respect [money creation] it is because they are controlled; they are not controlled because they are different." In this way ICM are similar to the informal sector in industry and trade, now the focus of much concern among development strategists.

The earliest treatment of these financial markets by Bottomley and U Tun Wai in the IMF Staff Papers and elsewhere referred to them as "unorganized markets", because in several cases they seemed highly segmented as compared to the "organized" financial market dominated by the banks. But at least in the Indian case (and the Korean one as well) several of these markets seem large and institutionalized enough to make the term "unorganized" inappropriate. Incidentally, to the extent the markets studied are less


segmented, the very high interest rates reported in studies like U Tun Wai's and Bottomley's seem less characteristic as well. Older Indian literature refers to the "indigenous" market (elsewhere people talk about the bazaar financial market) to differentiate it from the more westernized forms of the regular commercial banks. But the invidious distinction seems hardly appropriate today when all institutions considered are thoroughly Indian.

The present study is not concerned with informal rural credit - except insofar as some of it finances trade and industry. The rural informal sector in India accounted for almost 30 billion rupees of loans, outstanding as of June 30, 1971, lent at rates of 12-25% per annum.¹/ Nor is it concerned with the large market for "black" money financed out of sums not reported to income tax.

This study is also not concerned with the considerable market for consumption credit - especially to support the poorest members of society. This market is probably small in volume, but often characterized by high risks and interest rates.

The rural and consumption credit markets are not always easy to separate from the urban commercial and industrial finance market covered in this survey. Both rural and urban industry sometimes finance themselves out of these rural and consumption markets. Surveys particularly note this in the case of smaller artisans.²/ The Chettiar and Rastogi bankers, and finance

¹/ Indebtedness of Rural Households and Availability of Institutional Finance, All-India Debt and Investment Survey, 1971-72, Bombay, 1977. For general consideration of these markets see Michael Lipton, "Agricultural Finance and Rural Credit in Poor Countries", World Development 4 (July 1976), pp. 543-554.

companies surveyed do considerable household finance—in the latter case especially of consumer durables.

The urban informal financial markets serve both the "organized" and "informal, unorganized" sectors of productive enterprises (in trade, services, and industry). The informal enterprises among these productive enterprises are those whose economic activities are not closely monitored and regulated by the government. In specific, "informal enterprises", refers to those family and proprietary enterprises which do not come under the purview of the company and often the tax and labor laws. In general, less than half of small scale industrial enterprises in India are probably registered as small scale industries with the government, less than 20% have bank credit, and even fewer pay income tax. Thus more than half of all productive enterprises, even in the industrial sector are "informal". But as we shall see, most informal financial sector credit goes to formal sector productive enterprises.

C. Context: Informal Markets Around the World

Informal and non-bank commercial credit markets exist in most market economies. These are markets not subjected to the close customary and legal regulation characteristic of commercial banking and its variants. In the American case, in recent years, commercial banks have bought up many of the major commercial finance companies and factors -- and in one case, Walter Heller, a commercial lender has bought a captive bank. In 1977, the volume of such finance in the U.S. alone was 70 billion dollars. The volume of such lending has doubled since 1970.¹/ The commercial finance companies in the U.S., U.K. and Europe, where they have been growing in popularity, finance primarily businesses -- on a secured basis -- who have been turned

¹/ Source: National Commercial Finance Conference, the figures refer only to secured commercial lending.
down by the commercial banks for unsecured lending.

These non-bank lenders provide working capital, generally at somewhat higher interest rates than the banks for those enterprises whose demands, procedures, and risks are deemed inappropriate by the commercial banks. The differential with the banks rates varies -- though both in the American and Indian case it ranges between 2 and 8 percent. These lenders serve a clientele which includes a disproportionate number of small scale enterprises, whose size and instability make them unattractive to the commercial banks, normally the primary source of working capital.

In the Middle Eastern, South American and East Asian markets (as in Korea surveyed in an earlier study, or in Iran) these non-bank markets are clearly quite extensive. On the other hand, in some recent West African studies sponsored by ILO they seem almost lacking -- and that is clearly an element in the commercial backwardness of these areas.

To understand some of the relative importance of these markets we should perhaps note some comparisons. "In 1978 finance companies accounted for 20% "of short and intermediate term borrowing by non-financial businesses." The proportion in the European countries is probably lower.

The present study makes a rough estimate that the percentage of such non-bank outstanding loans or credit in the Indian urban financial markets is at least 30% of the total (not including 20% accounted for by publicly held deposits with limited companies and call money, or illegal monetary flows).


Commercial bank credit accounts for the bulk of the remaining borrowing by firms. By contrast, in the West Africa studies the proportion of informal finance is under 3%.$^{1/}$

Of course, the economies considered are quite different and at entirely different levels of financial development, but the figures are broadly indicative.

The countries surveyed indicate that there is a considerable span in the size and degree of integration of informal, unregulated credit markets in the countries concerned.

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$^{1/}$ As shown in the van Dijk and Ojo studies.
D. Survey of the Past in India

The existence of this informal "indigenous" credit market has, of course, been no secret to the students of the Indian economy. References to it are made in the oldest Hindu religious classics - the Vedas. The Buddhist Jatakas (7th to 2nd centuries B.C.) report bankers remitting cash and creating credit instruments, receiving deposits, and organized in guilds. Later sources refer to 15-60% rates of interest varying with security and social standing. In the Moghul period (1525-1719), bankers managed the financial affairs of state and financed long-range trade.¹/

Earlier studies of Indian credit markets noted that the bulk of credit moved through this informal market. It was only slowly as the modern sector of the economy grew that financial activity moved under the aegis of the commercial banks and the formal, organized money market. As late as the Second World War - the informal market probably accounted for more activity, even in urban areas than the banks and well over 90% of credit in rural areas. Vigorous development in the modern sector along with government directions to the banks to serve agriculture and SSE have increased the relative role of the formal sector.

The commercial banks in the earlier periods were very much tied into this "informal" credit market. As late as the 1950s they had 100-200 million rupees in Bombay outstanding with Shikarpuri bankers and there and elsewhere often used informal sector brokers ("muccadums") to mediate their dealings with SSE. But these forms of mediation declined as positive missions to lend to "priority" sectors and some perceived RBI displeasure with

¹/ Report of the Study Group on Indigenous Bankers, Banking Commission; Bombay, 1971, pp. 5-14, and bibliography following.
Shikarpuri business wreaked its toll.

Bibliography


There were a large number of provincial sub-enquiries such as:


*The Assam Provincial Banking Enquiry Committee Report (2 Vols.)*, Shillong, 1930.


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II. **THIS STUDY**

A. *Its Method*

The data for this report comes from a series of selected interviews with lenders, borrowers, intermediaries, and associations who are involved in the ICM. Over the course of the study almost one thousand people were interviewed (not always singly) by the three investigators -- and they represent the data base for this study.

Informal Credit Market actors are notoriously shy about publicity and privative about their affairs -- and the task of convincing a number of them to share their knowledge was an arduous diplomatic one -- in which we received extensive assistance from leading figures in the informal markets and other businessmen.

Initially we had planned to concentrate on the traditional bankers alone (those who took deposits and made loans) -- the Shikarpuris, Gujeratis, Rastogis, and Chettiar dealt with here -- but it rapidly became apparent that it was necessary to study brokers, and new institutions like "finance companies" which not only performed parallel functions in many markets, but actually formed part of the same informal market network.
The interviews were spread out in a variety of areas including Bombay, South Gujerat, Delhi, Amritsar, Kanpur, Calcutta, Benares, and Lucknow, and the major centers of South India. They do not represent any work in Central India, with an old banking networks, nor in Eastern India outside of Calcutta. Even in Calcutta, the coverage is far lighter than we would have preferred -- but time was simply not available to establish the connections that would have been necessary for a more thorough study there.

The data contained in the Tables are largely collected by C.V. Aiyar. The Gujerati Shroff data represent pro-forma interviews with 5 of Bombay's larger remitting firms. The Shikarpuri data was supplied at each center by interviews with the Shikarpuri Shroffs Association's officers and selected members -- again responding to standard pro-forma. The Rastogi and Chettiar figures represent the administration of similar pro-forma's in U.P. and Southern India.

The Shikarpuri figures were consistently pursued with groups and individuals at each centre separately. They were verified from brokers, non-member financiers, and borrowers. A firm of chartered accountants managing excess funds of Shikarpuris in Salem, the Chettiar Pawn Brokers and Moneylenders Association in Coimbatore and Madurai, a financier related to a bank employee in Trichy, a Gujerati film financier and a Sindi building financier in Bombay and so forth were all interviewed. Inconsistencies were checked both with market and commercial bank sources when available.

The Shikarpuri data are also confirmed by the four in-depth interviews which Timberg conducted with multanis (three in Bombay and 1 in Madras). In
all Aiyar interviewed 260 bankers (sometimes in groups), 45 finance brokers, and 12 borrowers as well as 50 dealers in illegal credit transactions and knowledgeable bank and academic sources. Timberg interviewed individually:

<table>
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<th>City</th>
<th>Finance Brokers</th>
<th>Lenders</th>
<th>Borrowers</th>
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<tr>
<td>Amritsar</td>
<td>3</td>
<td>1</td>
<td>14</td>
</tr>
<tr>
<td>Kanpur</td>
<td>3</td>
<td>4</td>
<td>4</td>
</tr>
<tr>
<td>Anand, Khera Dist.</td>
<td>7</td>
<td>6</td>
<td></td>
</tr>
<tr>
<td>Calcutta</td>
<td>One financial expert</td>
<td>3</td>
<td>11 plus one group of roughly 20 grain traders.</td>
</tr>
<tr>
<td>Madras</td>
<td>1</td>
<td></td>
<td>5 in group</td>
</tr>
<tr>
<td>Delhi</td>
<td>1</td>
<td></td>
<td>1 trade association</td>
</tr>
<tr>
<td>Bombay</td>
<td>2 Shikarpuri Shroffs, 3 Bank multani loan officers, 3 Shroffs Association groups, 3 finance brokers,</td>
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Most of the informants gave some indication of the size of their own business, the categories of their lending and remittance, and the rough character of their clientele.

B. Types of Agency in the Informal Credit Market

Ethnic Types

The traditional informal credit market intermediaries were organized along lines of ethnic community. Their history can be and is recorded on communal lines.¹/  The Shikarpuris, the Gujeratis, the Chettiars, the Rastogis, and so forth all had separate networks, with separate if similar procedures.

These groups are all a trading caste or a cluster of trading castes from different regions: the Gujeratis from South Gujerat, the Shikarpuris (multanis) from Sind, The Marwaris from North and West Rajasthan, the Rastogis from the Oudh region of U.P. and the Chettiars, appropriately enough, from the Chettinad region of South India. Originally they all accepted deposits, issued and discounted bills of exchange and other commercial paper, provided open lines of credit, insurance and advice to a range of clients in their home regions. Later the Marwaris and Chettiars moved out in India and overseas and served first their owning trading compatriots and later a more cosmopolitan clientele.

Over time the groups evolved differently. The primary activities of the Chettiars were overseas in Sri Lanka and South East Asia. Their banking underwrote trading in that area — and they combined to promote South India's two premier banks — the now nationalized Indian Overseas Bank and the Indian Bank. With the wholesale expulsion of Indians and the heavy restrictions on trade and credit throughout the region during and after World War II, they experienced great losses. A number continue to operate in their home area of South India as pawbrokers, but others have gone into manufacturing and other sorts of activities. The Marwaris moved quite actively into industry and trading positions abandoned by the British and at the same time funded a series of banks — the now nationalized Hindustan Commercial and United Commercial Banks inter alia — and moved actively into the formal financial sector. For a series of reasons, some connected with their high degree of early commercial development, the Gujeratis' maintained a more traditional
banking system in their homeland to a greater degree than the others—though in Bombay the Gujerati bankers divide themselves between a small group (dominated by 6 large firms) who serve as apex remittance centers for up country firms (discounting their real and fictive bills of trade)—and a larger group who either serve primarily as commission agents/financiers or even finance promissory notes as do the Shikarpuris. The Shikarpuris have for the last several decades loaned on relatively small denomination promissory notes (5-10,000 Rs.) to a miscellaneous clientele. Their two primary features are their high liquidity since they rarely lend for longer than 3-5 months and their spreading of risk—as one debt is broken up and shared by many bankers. In Bombay, their major center, these notes are sold through brokers who enable a borrower to get many 100,000’s of rupees if necessary—by selling of the borrowers debts in 5-25,000 Rs. pieces to various different creditors. This is now a common form of finance used in a large variety of areas. The Shikarpuris in South India, where they are now very active, do a lot of direct lending, increasingly on an installment basis and our survey shows that installment lending accounts for 45% of their portfolios in South India. Some business was done across community lines—especially in port cities, and clientele was often gathered from different ethnic communities than that to which the intermediaries belonged. The Chettiar, for example, served almost all economically active groups in South India; the Rastogis served the craftsmen and traders of all communities in the Oudh area of Uttar Pradesh.

In the modern period, there has occurred a considerable blurring of lines—both as to modes of doing business and to business partners—and a melding of the older modes with several non-traditional forms—intercorporate call
money, hire purchase arrangements, finance "companies", etc. The informal intermediaries may now better be classified on functional than ethnic lines. For the purpose of this study we shall find ourselves moving back and forth between the categories -- communal and functional.

Functional Differences

There are four broad types of facilities available in informal credit markets--defined in functional terms--indigenous style bankers, commercial financiers, finance brokers, and commercial paper discounters. None of these are pure types. Agencies of all sorts, for example, discount commercial paper, and perform as brokers for their clients.

A. As the 1972 Banking Commission defined them, "Indigenous Style Bankers" (The Gujaratis, Chettiars and finance companies we surveyed fell into this category) had both to take deposits and make loans. This had to constitute a major part of their business. Though their number has declined somewhat there are still thousands of family firms who continue business of the traditional type. Continuing centuries long banking traditions--most of these firms belong to members of traditional banking ethnic communities. Continuously reorganized, many of these firms have existences going back several hundred years. The Gujarati Shroffs, or indigenous bankers of Western India do almost everything a commercial bank does--accepting deposits, making loans, and providing means of remittance and collection. The Gujarati firms themselves number well over 4,000. There is a continuum among these Gujarati bankers between the Gujarati Shroffs in Gujerat itself, who are often specialized in banking and 90% of whose funds may be based on deposits and the more numerous Marwari and Gujerati firms studied in
Bombay and Calcutta who combine their banking with trade in cloth, grains, and other commodities and whose credit transactions are to a greater or lesser extent ancillary to that trade.

The indigenous style bankers, typically, perform a larger set of services for their clients than simply accepting their funds on deposit and reloaning them. They provide means of remittance (especially "darshani hundis"—sight bills, but can provide checks on out-station banks as well), discount commercial paper and checks, give commercial guidance, and often offer transient accommodation to their out of town clients and associates. Their offices are open both later and earlier than the commercial banks and they are far more flexible in serving their customers. They provide the only banking services in many areas of India and service firms with business interests there. This largely explains the preference of some Bihar and Assam cloth traders in Calcutta for dealing through Marwari indigenous bankers—since there are no commercial banks in the villages with which they trade. In other areas, especially Gujerat, indigenous bankers provide accommodation to "non-priority sector" trades not well financed by the banks—grains, cloth, "biri" tobacco (indigenous style), etc. (see Table XX). For example the overwhelming bulk of indigenous bank finance in Anand in Khera District near Ahmedabad was used in underwriting the "biri" cigarette trade, which the regular banks have found impossible to serve.

Traditionally Gujerati Shroffs did not solicit new clients and restricted themselves to serving a local clientele whom they knew intimately.
There are now a few Gujarati indigenous bankers who have taken a more aggressive pose—and advertise for clients. One such banker has 93 branches and 200 million Rs. deposits.

Though the number of Gujarati Shroffs is relatively high and the range of their services particularly extensive—we found a wide variety of other indigenous style bankers—by the deposit taking and lending definition—among other communities as well. Much of the Chettiar pawnbroking in South India is conducted, for example, on the basis of deposits.

By this deposit taking definition, the indigenous bankers ought to include as well a group of finance "companies" (though they are rarely joint stock companies) who take and solicit deposits and lend them in turn to a commercial clientele.¹/

Many of these "companies" are run by people from a traditional banking background. The companies have flourished since 1960, especially in South India. There were 50-150 of them in the various Southern centers surveyed—though most of our operational data is based on a survey of 20 such firms in Trichy and another group in Karur. One estimate has it that there are 2200 such companies with perhaps 4500 million Rs. of working funds in the

¹/ C.V. Aiyar surveyed two highly successful and reputable firms of this sort. The firm run by Srinivasa Naidu in Coimbatore with 18 million Rs. in deposits (when surveyed)—kept 6 million on fixed deposit at 9% and lent the rest out at 18% against pawned sureties. The depositors are paid 9% per annum. The Gujerat Savings Unit runs a series of very successful savings and prize schemes for small savers. Over a million people are involved in these schemes, and 10,000 agents solicit, at least part-time, for them—the Unit has been especially successful in Andhra. As a matter of policy, fifty percent of the money is invested at the 9% fixed deposit rate and 50% loaned to industry at rates ranging from 18 to 24% per annum. In two other South Indian Centers—Aiyar was able to administer pro-forma's to larger groups of finance "companies" (Karur and Trichy) and it is those survey data which underly the data given in the tables attached to this monograph.
whole country. The twenty surveyed firms in Trichy who were members of the local finance company association had 440 million Rs. in working funds. The largest of these finance companies in the metropolitan centers have several tens of millions of rupees, all of it based on deposits; own capitalization is usually low. Peerless claims more than a billion Rs. in assets, Sugeshan 100 million. In Trichy and Karur, 30% of finance "company" advances went to retail trade and 10% to wholesalers, 8% went to small scale industry and 12% to agriculture. In the largest cities, hire purchase finance of used vehicles seemed most important. In agricultural centers like Kothamangalam, near Ernakulam in Kerala, the credit went to finance trade in cash crops. In the case of Sugeshan in Madras, about half the funds are invested in three month promissory notes and the rest in secured export finance.

The few limited company finance "companies" are mostly involved in the hire purchase finance of vehicles less than three years old and enjoy considerable bank refinance. They had 260 million Rs. of assets when recently surveyed by the RBI.1/ The non-limited "companies", in the larger centers, as we said, specialize in the hire purchase finance of older vehicles, and to some extent of consumer durables. The Hire Purchase Association of India reports that 425 of its 500 members are not limited companies.

The finance "companies" perform many bank functions -- they discount and collect a variety of remittances and commercial paper, maintain deposit accounts, and sometimes provide check-like remittances. The non-limited

company segment of these finance "companies" is almost totally unregulated and some apprehensions are entertained about their soundness. The 1972 Banking Commission treated them in its Working Group on Non-Bank Intermediaries and recommended that the government devise a scheme for their regulation. The RBI has concluded that regulation is impossible, and has introduced a bill in Parliament which would have the effect of banning these companies—as well as restricting a good deal of the rest of the indigenous banking community. No action has been taken as yet on this bill.

A variant on these finance "companies" are the commercially promoted Chit Funds (Kuri), a rotating credit arrangement characteristic of South India. Though not very profitable for those who invest they are very popular. It is estimated that there is an annual turnover of some 2-2.5 billion Rs. in Chit Funds. Chit Funds are often run by traders who find that the funds help meet their working capital needs or by finance "companies"—but the bulk of chit finance is for non-business purposes. A variety of mutual loan funds (Nidhi) and commercial property mortgage firms fill other credit needs—again primarily in South India. As much as a quarter of Chit Fund, Nidhi, and pawnbroking funds go for commercial purposes.

B. Commercial financiers are lenders, who in contrast with indigenous bankers mostly employ their own funds and do not take significant amounts of deposits. In some cases, however, they may serve as intermediaries by discounting (i.e., refinancing) their lendings with commercial banks or others. In this way they are similar to the commercial finance companies in the U.S. or other industrialized companies. The large group of Shikarpuri (sometimes
called Multani) financiers in Bombay and South India are the most widely known of these financiers in India. Originally indigenous bankers of the classic sort, they largely renounced deposits some time ago to rely on bank rediscount of their obligations. In recent years, this refinance has been reduced as a matter of bank policy -- and they now largely rely on their own funds. The amount of bank funds made available to them is less than one tenth what it was in 1960.\(^1\)

There are roughly 600 firms which belong to the various local Shikarpuri Bankers' Association and an equal number who are not. There are 1200 million Rs. of lendable funds in the whole market according to our estimate. The average firm has a capital of roughly a million Rs. -- though two or three firms may often be owned by the same family.

The Shikarpuris traditionally took what were known as "multani hundis", 90 day term notes in amounts like 3-5,000 Rs. (earlier much lower) -- and discounted these notes. With the decline of discount facilities, they have moved toward demand promissory notes (endorsed for a term) and installment finance. Typically, a broker will arrange to break up a large loan into smaller notes which he will sell to a whole group of bankers -- risks are thus spread throughout the Shikarpuri community.

\(^1\) Of course, a certain amount of other bank lending finds its way into informal markets. Lenders report occasional borrowing on the security of shares or fixed deposits -- and those sums may be re-lent. There is certainly some circulation of bank funds from bank borrowers to their business fellows who may be net lenders in informal markets -- but in contrast to the situation in Iran several years ago -- these flows are clearly peripheral. (Benedick, op. cit.).
Financiers of the Shikarpuri sort exist almost everywhere—that is there are in every major market people who make their living by lending their money to businessmen as do the Shikarpuris.\(^1\) They proved the shiest of the informal credit agencies—so in several cases I had to rely on second-hand reports on their activity. In general, the most difficult data to get for this study was that on the identity of lenders.

C. The typical commercial financier, unlike the typical indigenous banker deals through brokers. But brokers go, as well, to other, non-full time (i.e., non-commercial lender) sources. In the Shikarpuri market, in particular, as the amount of bank funds in the hands of bankers has contracted, the brokers have emerged as an independent force—searching funds from any willing source. There are full and part-time finance brokers in almost every and finance commodity/market—ranging from those who work the inter-corporate call money market (money at 8.5-10% with 1/2% brokerage—500,000 Rs. minimum) in Bombay for tens of millions of rupees at a time, to the kind I interviewed in Kanpur and Amritsar who may carry back and forth as little as 5-25,000 Rs. at a time between traders in the cloth market, or between the grain and jute markets in Calcutta.\(^3\) For certain purposes, it is necessary, however, to differentiate

---

1/ A group of 100 Marwari bankers in Madras were found doing precisely this "multani" business.

2/ One broker gathered funds from 350 different sources in amounts from 10,000 to 100,000 Rs. and re-lent them to 37 larger-sized public companies.

3/ The inter-corporate call market contains 50 to 100 million Rs. of credit outstanding on average terms of 6 months. The company deposits market in which private demand and term depositors are recruited by brokers to help finance joint stock companies in amounts as small as 1,000 Rs. already contained 10 billion Rs. in 1973-74 ("Growth of Deposits with Non-Banking Companies, 1973-74", RBIB (Jan. 1978), pp. 39-54) but it expanded rapidly in the credit crunches after 1974 and is now as high as 35 billion of credit outstanding. A succession of recent regulations limiting the proportion of finance that can be obtained through these deposits has considerably
constrained the growth of this market, and there is a proposal for its total prohibition. One large Bombay firm dealing in the company deposits market reported 500 brokers working for it full time on .6 to 1% commission. (The firm gets 1/4% on the transaction as manager). Another firm handled 50 million Rs. of deposits a year.

Corporate depositors get up to 13.5% in 1978 (the rates are also regulated by the RBI)—though the rate is going down—which is several points higher than the rate on the longest term savings accounts. Their money usually is tied up for a year or less. From the borrowing company’s point of view, however, deposit interest is not fully deductible from tax and the real cost is somewhat higher than the reported face cost.
between the company broker who brokers deposits and call money in the corporate sector (in high volume and at low cost) and the smaller brokers who serve partnership and proprietary firms. The former are often stockbrokers and combine stock brokerage with the brokerage of other financial accommodations.

The brokers used by Shikarpuri financiers (accounting for all of their transactions in Bombay and 75% in Madras, but very little in the smaller centers) often receive as high as 2% commission. There are 85 association member brokers in Madras and three times as many in Bombay—plus many uncertified ones. Some of these brokers—member and non-member—deal with both Shikarpuri and non-Shikarpuri funds sources.

Gujerati indigenous bankers also use brokers, especially in the larger cities, but the brokers' role is less critical than among Shikarpuris and they do not syndicate loans among bankers. Rastogi bankers in Uttar Pradesh are beginning to use more brokers, as they attempt to diversify their portfolio into new fields.

The smaller sort of brokers, providing intermarket or intramarket credit to proprietary firms represent themselves a considerable range. At the top there are those like the Amritsar broker who handled an annual flow of more than 10-20 million Rs. a year for 150 large clients in minimum loan amounts of 50,000 Rs. He was very explicit that he limited himself de-facto to accounts receivable finance, though his lending is nominally unsecured. By contrast a more typical broker surveyed has 15-25 clients and dealt in a minimum unsecured transaction of 5,000 or so in a small cloth or grain market.

D. There is also a considerable business in the discount of commercial paper, checks, post-dated checks, truck receipts, etc. By and large, this financing is done as in the United States and Western Europe—outstanding bills
and accounts receivable are bought without recourse. An important part of the business is the discount of bank checks, current and post-dated. Post-dated check finance was reported in large volume in Bangalore and Benares for hand and powerloom finance and in Madras for financing leather tanneries. Shikarpuri lending, particularly on an installment basis, is now often done through the instrument of a post-dated check. Similar institutions have cropped up elsewhere in the world and post-dated check finance is apparently, for example, common in Colombia in South America. The discounters include a large number of private investors. Numerous firms do this kind of discount in the major centers including indigenous bankers and commercial financiers, but trucking companies, commercial couriers (angaria) and others as well. In one variant, the cotton textile mills find firms to which they can sell their accounts receivable; textile purchasers find firms who will appear as the wholesaler of record in order to finance their transactions. The discounters typically charge what amounts to 18-24% interest on an annual basis.

1/ Lakshmi Narain, "The Parallel Post Office", Business India, March 31-April 3, 1980, pp. 32-33, for a description of the "angaria's".
III DATA ON CREDIT SUBSYSTEMS

A. The Shikarpuris

History

The Multani or Shikarpuri Shroffs, as we mentioned, originate in Sind, now in Pakistan, where they were the local bankers, providing the full range of indigenous banking services. But they have now almost totally transferred their operations to India and narrowed their activities to that of "commercial financiers." At the same time their attached brokers, have broadened their financing activity, and may now be said to function as the important intermediary in this market.

Numbers

Over 100 Multani firms and about 20 Multani brokers were covered by our survey. Including towns not covered, the number of firms who are members of local Shikarpuri associations is about 650 -- and the number of non-member firms roughly as large. In general, the non-member firms, where associations

| Tables I - Number of Shikarpuri Bankers and Brokers in Surveyed Towns | Estimates |
|---|---|---|---|---|
| | Member Bankers | Member Brokers | Non-Member Bankers | Non-Member Brokers |
| Towns | | | | |
| Bombay | 238 | 219 | 350 | 160 |
| Madras | 126 | 86 | 200 | 75 |
| Madurai | 20 | -- | 10 | -- |
| Trichy | 20 | -- | 12 | -- |
| Tanjore | -- | -- | 4 | -- |
| Salem | -- | -- | 40 | -- |
| Coimbatore | 20 | -- | 35 | -- |
| Calicut | 20 | -- | -- | -- |
exist, were more likely to accept deposits, lend to more risky and larger sized borrowers, and thus violate the norms that association members set for themselves.

**Instruments: Types, Rates, Conditions**

Shikarpuri bankers lend for working capital -- and no other purpose. Their preferred instrument is the usance hundi or promissory note, a short term (usually 90 days) credit bill. The funds are loaned to meet trade and production needs, to bridge other finance, or to meet margin requirements for bank finance. Shikarpuris and other informal market intermediaries do not usually provide loans for long term requirements. While in Bombay Shikarpuris only lend on 90 day term notes. In the South funds are also provided on an installment payment basis. Such installments against promissory notes constitute about 45% of the total advances of the southern Shikarpuris. Some of the Shikarpuris also financed transport operators on a hire purchase basis. The usual procedure for charging the Shikarpuris interest is to deduct the interest in advance. Many times, a separate check or cash for the amount of interest is obtained in advance -- and exchanged for the full amount of the principal to simplify record keeping. Shikarpuris do not generally arrange for remittance of funds.

Most of the lending by Shikarpuris who are not members of local associations is done through promissory notes or demand notes supported by post-dated checks. Some of these non-members in fact routinely discount post-

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1/ A Shikarpuri hundi is a demand note which is endorsed for a term and rate on its obverse. As a demand bill, a revenue stamp must be affixed. It is otherwise a usance bill and a promissory note of contract signed by the borrowers.
dated checks issued by leather tanneries in Madras and handloom/powerloom owners and dealers in Bangalore. In Trichy, some of the Shikarpuris also discounted current checks after banking hours or before payment clears at the bank. In addition to post-dated checks the non-member firms obtained sizeable collateral security -- often for as much as 100% of their loans when financing film production.

In Bombay and Madras, the Shikarpuri Bankers' Associations prescribe the normal rates of interest on loans made by their members, but there is considerable variation in the actual rates charged to different classes of borrowers. In general, effective rates of member bankers in all centers cluster around 30% per year.\(^1\)

**Brokers**

Most of the Shikarpuri finance in large towns such as Bombay and Madras is routed through brokers. There are no brokers in the smaller towns. Almost all of the Shikarpuri brokers belong to the same ethnic community as the bankers and are often closely related to them. Brokers, however, are typically not tied to any one banker--and deal with them on the basis of business convenience. Brokers typically deal with a large group of bankers. The broker is supposed to have a good knowledge of the market and is judged by the kind of borrower he can produce. Normally, however, each borrower deals with only one broker -- and any attempt to compete for a borrower's business is felt to be unethical.

The Shikarpuri broker is in fact an intermediary himself. Most

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\(^1\) In Bombay, the Shikarpuri Association has pegged the rate at Rs. 1.70 per month -- about 21% per year. If we include the brokerage and incidental charges, and take account of the fact that interest is paid in advance -- the rate could go up to 30%, though the mode seems to be between 24 and 27%. In Madras, the prescribed rate is 2.3% per month -- and the cost to the borrower may reach 37%. The rate varies from 1.75 to 2.25 in the smaller towns in South India, where no brokers are present.
Shikarpuri bankers do not have any direct contact with their borrowers. One aggressive broker in Madras explained that if a Shikarpuri banker were to contact his borrowers directly it could affect the relation between the broker and the banker.

Most Shikarpuri brokers command resources from sources other than Shikarpuri bankers to meet their borrower-client needs. They sell notes to investors like film artists and distributors, as well as the general public. They supply credit directly to the corporate sector -- and are now the most important actors in the Shikarpuri market.

**Modus Operandi**

While appraising a proposal, the Shikarpuris first obtain market reports about the borrower, his integrity, means and business transactions -- through brokers where they exist -- and direct inquiries with the trade when they do not. They satisfy themselves about the purposes of the loan and often call for Wealth Tax and Income Tax returns. In Bombay and Salem, some Shikarpuris lend only to Income Tax assessees. Income Tax assessees can be presumed to have at least the income declared for income tax purposes, and are somewhat less likely to be involved in black market transactions -- i.e., they have some significant non-black market business. The Shikarpuris normally have a notional limit fixed for each borrower. Generally they will not lend any party more than 25% of his net worth.

**Deposits**

Multani bankers take very little in the way of deposits, but traditionally have refinanced their lending by discounting their hundis with commercial banks. As this facility has declined, some of the non-member firms have sought deposits. And the brokers have gone to sources outside the community for funds that they could reloan.
Bad Debts

Our survey estimates that the total bad debts which are required to be written off in a year, average about 5% of a firm's gross annual profits. In terms of turnover, the bad debt write-off is about 5% of turnover. In some of the smaller towns the bad debt figures are somewhat larger -- around 7-10% of gross profits.

Establishment and Expenses

Usually a Shikarpuri firm is a simple establishment often located in a rental shop premises with a floor mattress spread in the room for sitting. Besides a telephone, an office normally includes 2 to 4 persons on regular employment, depending of course on the size of the business. Many of these items are for the use of several allied family firms. Our study estimates that an average firm's expenses would easily total to about Rs. 30 - 35,000/ per year. In a few cases where accommodation rentals are high, average annual expenses may work out to as high as Rs. 45,000. The table below indicates the prime costs of funds and the net return before tax for an average Shikarpuri banker with sizeable dependence on bank refinance. 1/

The net returns of a Shikarpuri banker should easily approximate between 9 and 10% of their working funds. In certain categories of advances,

1/ One large firm reported a payroll of 19,000-27,000 Rs. depending on the size of bonus, for one manager, one cashier and one peon (roughly an office boy-messenger). The same respondent paid 1,200 Rs. a year for rent (he must have had rent controlled accommodation) -- and had considerable expense for travel to look at his interests in South India, telephone charges and charity -- that might easily have totalled 20,000-30,000 Rs. more. His legal costs were 500 Rs. a year, dues to the Shikarpuri Association Rs. 100, and brokerage on bank discount .07% of the business he did with the banks. If he used his 500,000 average credits with various banks, by turning them over four times a year brokerage would cost him 14,000 Rs. The expenses cited are in fact spread over three firms with assets totalling two to three million rupees. In the main firm one million is his and 500,000 is typically due to bank discounts.
Table II: Expense As Percentage of Working Funds of Shikarpuris (Aiyar)

<table>
<thead>
<tr>
<th>Costs</th>
<th>Without Brokers</th>
<th>Returns</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Interest payment on bank funds or</td>
<td>15.0</td>
<td>1. Earnings by interest charges on advance</td>
</tr>
<tr>
<td>opportunity cost</td>
<td>15.0</td>
<td>30.0</td>
</tr>
<tr>
<td>2. Payment of brokerage and incidental</td>
<td>0.5</td>
<td>2. Other incidental charges of stamp fee and</td>
</tr>
<tr>
<td>expenses.</td>
<td>0.0</td>
<td>charity.</td>
</tr>
<tr>
<td>3. Cost of idle funds</td>
<td>0.5</td>
<td>3. Total</td>
</tr>
<tr>
<td>4. Risk of default</td>
<td>1.0</td>
<td>Add brokerage</td>
</tr>
<tr>
<td>5. Administrative expenses</td>
<td>4.0</td>
<td>1.0</td>
</tr>
<tr>
<td></td>
<td>3.5</td>
<td></td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>20.5</strong></td>
<td><strong>20.0</strong></td>
</tr>
</tbody>
</table>

The other expense ratios estimated in the survey are:

1) Wages and salaries as % to Total expenditure - 25%
2) Rentals as % to Total expenditure - 20%
3) Other expenses as % to Total expenditure - 55%
4) Total expenditure as % to Total income - 30%
5) Total expenditure as % to Total turnover - 2%
6) Total bad debts as % to Total income - 5%
their interest charges are as high as 33 to 37%. In other cases, when they operate on their own funds only, their effective rate of return is higher, though the turnover is less. Generally the ratio of their own funds to borrowed funds at present is 1:1 to 1:5; and their turnover runs to at least 4 cycles per year.

According to our quick estimates, the transaction costs as a percentage of working funds would be as high as 5% in the case of Shikarpuris. In the case of non-member firms the transaction costs would be as high as even 8 to 10% of working funds partially because of the high risks entailed.

Clientele

Among all the indigenous bankers, the Shikarpuris had the most varied clientele. Except for agriculture every other sector of the economy and every kind of commodity market have been touched by the Shikarpuri banker. Though a considerable amount of their finance goes to trade and industry, other types of activities are also covered. The sectoral distribution of Shikarpuri credit is reported by the Shikarpuri Associations of Bombay and Madras and our estimates based on the discussions with brokers and small town multani bankers are as follows.
Table III

**Percentage of Total Shikarpuris' Credit Extended to Different Sectors (Aiyar)**

<table>
<thead>
<tr>
<th>Category</th>
<th>Shroff Associations Estimate</th>
<th>Our Estimate</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>1970* 1978</td>
<td>1978</td>
</tr>
<tr>
<td>1) Wholesale Traders</td>
<td>7 7</td>
<td>6</td>
</tr>
<tr>
<td>2) Retail Traders</td>
<td>21 25</td>
<td>22</td>
</tr>
<tr>
<td>3) Small Scale Industries</td>
<td>27 25</td>
<td>16</td>
</tr>
<tr>
<td>4) Miscellaneous Small Business Enterprises</td>
<td>5 5</td>
<td>3</td>
</tr>
<tr>
<td>5) Transport Operators</td>
<td>5 5</td>
<td>7</td>
</tr>
<tr>
<td>6) Exporters</td>
<td>7 21</td>
<td>20</td>
</tr>
<tr>
<td>7) Hoteliers &amp; Tourist Agencies</td>
<td>4 1</td>
<td>1</td>
</tr>
<tr>
<td>8) Film Industry</td>
<td>- 1</td>
<td>8</td>
</tr>
<tr>
<td>9) Construction Activities</td>
<td>- 3</td>
<td>3</td>
</tr>
<tr>
<td>10) Contractors</td>
<td>9 1</td>
<td>1</td>
</tr>
<tr>
<td>11) Marketing &amp; Clearing Agencies</td>
<td>12 4</td>
<td>4</td>
</tr>
<tr>
<td>12) Large Industries</td>
<td>- -</td>
<td>7</td>
</tr>
<tr>
<td>13) Others</td>
<td>3 2</td>
<td>2</td>
</tr>
<tr>
<td></td>
<td>100 100</td>
<td>100</td>
</tr>
</tbody>
</table>

The Shikarpuris Association's estimates indicate a considerable shift in their portfolio towards the "priority sectors" (as defined by government credit policy) especially in serving exports, and towards retail trade. While there has been

*As returned to the Banking Commission of 1972.*
a marginal decline in credits to the manufacturing sector, the fall is sharpest in the services sector. Obviously the estimates of the Shikarpuri Associations have the limitation that they relate only to the member shroffs and brokers and mostly concern their pattern of operations in Bombay or Madras. However, our estimates are more broad-based including non-member shroffs and brokers as well as smaller town bankers surveyed in this study. From our estimates, the shifts in the credit flows of the multani market also seems clear. The traditional trade sector although it is still consuming the bulk of their credit seems to stagnate at its 1970 level. A distinct trend has been the substantial flows to the export sector as well as large scale industries and films.

**Average Assets**

According to our survey estimates, the average assets or capital of middle size member firms in the Bombay and Madras metropolitan cities is well over Rs. 500,000, perhaps 1 million Rs. Over 70% of the member firms come under this category. The remaining large sized member firms average worth is about 1.5 million Rs. In terms of annual turnover the smaller member firms in the two cities would not be worth less than 500,000 whereas the large majority of middle sized firms would have an average annual turnover of about 2.5-3.5 million Rs. In the smaller towns of South India, the average assets of member firms would be about Rs. 2-300,000 with an annual average turnover of about 1-1 1/2 million Rs. The disparity in the asset holding structure of member firms in smaller towns was not found to be as wide as in the metropolitan cities.
Total Credit

It is relevant here to consider at least a broad estimate of the size of the multani informal market. Although short of a total survey it can only be a wide approximation. Our Survey covered most of the important multani money markets on the basis of which we shall attempt an estimate of the total multani credit market in India.

Table IV. Annual Credit Turnover of Shikarpuri Bankers in/Millions of Rs. (Aiyar)

<table>
<thead>
<tr>
<th>Centers</th>
<th>Members</th>
<th>Non-Members</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bombay</td>
<td>94</td>
<td>132</td>
<td>226</td>
</tr>
<tr>
<td>Madras</td>
<td>60</td>
<td>65</td>
<td>125</td>
</tr>
<tr>
<td>Madurai</td>
<td>12</td>
<td>0</td>
<td>12</td>
</tr>
<tr>
<td>Trichy</td>
<td>3</td>
<td>0</td>
<td>3</td>
</tr>
<tr>
<td>Tanjore</td>
<td>0</td>
<td>24</td>
<td>24</td>
</tr>
<tr>
<td>Salem</td>
<td>0</td>
<td>20</td>
<td>20</td>
</tr>
<tr>
<td>Coimbatore</td>
<td>12</td>
<td>16</td>
<td>28</td>
</tr>
<tr>
<td>Calicut</td>
<td>8</td>
<td>0</td>
<td>8</td>
</tr>
<tr>
<td>Bangalore</td>
<td>18</td>
<td>22</td>
<td>40</td>
</tr>
<tr>
<td>Hyderabad</td>
<td>12</td>
<td>18</td>
<td>30</td>
</tr>
<tr>
<td>Vijaywada</td>
<td>4</td>
<td>0</td>
<td>4</td>
</tr>
</tbody>
</table>

Tens of 222 297 520

Out of a total turnover of Rs. 5200 million, the total loanable funds would work out to roughly Rs. 1300 million on the basis of average 4 turnover cycles per year. The table below indicates the estimate of funds employed in business by the Shikarpuris and the average assets per firm separately for member and non-members.
### Table V: Assets Employed in Business by Shikarpuris (Aiyar)

#### Member firms

<table>
<thead>
<tr>
<th>Classification of firm size by annual turnover</th>
<th>% of firms</th>
<th>No. of firms</th>
<th>Annual credit turnover in tens of millions of rupees</th>
<th>No. of turnover cycles per year in each size</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs. 8 - 1.2 million</td>
<td>10%</td>
<td>60</td>
<td>6</td>
<td>3</td>
</tr>
<tr>
<td>Rs. 2.5 - 3.5 million</td>
<td>60%</td>
<td>360</td>
<td>108</td>
<td>5</td>
</tr>
<tr>
<td>Rs. 5.5 - 6.5 million</td>
<td>30%</td>
<td>180</td>
<td>108</td>
<td>4</td>
</tr>
<tr>
<td></td>
<td></td>
<td>600</td>
<td>222</td>
<td>Average 4 cycle</td>
</tr>
</tbody>
</table>

Estimated of total funds employed in business: 

\[
\frac{222}{4} = \text{Rs. } 555 \text{ million}
\]

Total available refinance from banks: 

\[
\text{Rs. } 375 \text{ million}
\]

Estimated (at 15%) deposits from friends and relatives: 

\[
\text{Rs. } 75 \text{ million}
\]

Estimate of total own funds employed in business: 

\[
\text{Rs. } 442.5 \text{ million}
\]

Average own funds employed per Shikarpuri firms: 

\[
\frac{\text{Rs. } 40 \text{ million}}{650} = \text{Rs. } 730,000
\]

#### Non-member firms

<table>
<thead>
<tr>
<th>Classification of firm size by annual turnover</th>
<th>% of firms</th>
<th>No. of firms</th>
<th>Annual credit turnover in Rs.</th>
<th>No. of turnover cycles per year</th>
</tr>
</thead>
<tbody>
<tr>
<td>Rs. 2.5 million</td>
<td>60%</td>
<td>420</td>
<td>1260 million</td>
<td>4 1/2</td>
</tr>
<tr>
<td>Rs. 5.5 million and above</td>
<td>40%</td>
<td>280</td>
<td>1500 million</td>
<td>3 1/2</td>
</tr>
<tr>
<td></td>
<td></td>
<td>700</td>
<td>2750 million</td>
<td>Average 4 cycles.</td>
</tr>
</tbody>
</table>
Estimates of total working funds employed in business $\frac{2760}{4} = 690$ million

Estimated (@ 20%) deposits of friends and relatives $130$ million

Estimate of total own funds employed in business $Rs. 560$ million

Average own funds employed per Shikarpuri firm $\frac{560 \text{ million}}{700} = Rs. 800,000$ approx.

Estimated total working funds employed by all Shikarpuri firms $Rs. 1300$ million approx.

The estimates of the size of the multani market are by themselves conservative since they do not include the funds canalised and deployed by brokers. For instance, a Madras Shikarpuri broker reported that he had a monthly turnover figure of nearly Rs. 30 million and most of his financing was managed from out of his own funds, and deposits from the public. If we therefore add the contribution by brokers to the total multani credit market, the size of the available funds and the annual credit turnover may well be estimated to go up to over Rs. 2500 million and Rs. 10000 million respectively. Some of this figure for non-member firms—may be accounted for by funds that properly belong in the black market, for funds not reported for income tax purposes.

Change in Finance Sources

The effect of the commercial bank refinance drying up on the Shikarpuri market has been many sided. Firstly, the broker has gained importance because of his commanding position over resources, as a result his leading role in arranging large sized loans has become a common feature of the present Shikarpuri market. Secondly, bank refinance has been increasingly substituted
by market refinance sources partly against rediscount of hundis (what used to be called selling 'purjas' but is no longer for fear of tax officials who dislike this transaction). Thirdly, since the traditional hundis now have little refinance value with the banks, they have begun to disappear and been substituted by promissory or demand notes.\footnote{In Salem, Coimbatore, Calicut, and Trichy, Shikarpuris reported that over 60\% of their advances are demand note advances. One Shikarpuri banker pointed out that the practice of obtaining promissory-notes was becoming more common. Instalment due dates along with the pro-notes was becoming more common. A Salem banker confirmed that post-dated checks were the only insurance against the risk of large advances which are more in demand than hundi loans.}

Fourthly with reduction in multani hundi loans, instalment credit or multiple-due date credits have become possible and seem more suited to the needs of businessmen in the South. However, in Bombay, the multani hundi is still in use to evidence that borrowing is not done on a promissory note but on a negotiable instrument and thereby avoids the effect of the Bombay Money Lending Act. Finally with the traditional multani principle of small lending in hundis of Rs. 5000 values rapidly shrinking, one distinction between members and non-members among Shikarpuri bankers begins to fade.

B. Gujerati Shroffs

Among the most ancient of the various forms of indigenous banking we surveyed are the Gujerati shroffs. They are well organized indigenous style bankers operating as family firms and continuing centuries old traditions of banking. They have an extensive network covering all districts of Gujerat and Bombay city. In many places, they provide the only banking services. The Gujerati shroffs have, as well, branches in all the major commercial centers of India, wherever Gujerati traders are found.
Number and Type

The Gujerati Shroffs are of two types: (i) those who are pure bankers and (ii) those who combine banking with trade as commission agents. Our Survey showed that there were only 6 major pure shroffs in Bombay City, each with several branches in Gujerat. Most of the pure shroffs are in Gujerat and may well number over 1500 there. Shroffs combining commission agency and banking are more numerous and may number one thousand in Bombay alone.

Instruments: Types, Rates, Conditions

The Gujerati Shroffs perform a variety of functions for their clients:
(a) they accept deposits on current and fixed accounts from the public;
(b) they make loans on call and for fixed periods with or without security or on personal credit and
(c) they arrange to remit funds by issuing hundis and also undertake collection of hundis.

Those who also act as commission agents dealing in textiles, cotton, machinery, spices, bullion etc. offer finance for the purchase of goods or against goods received for sale. By this process their credit percolates from cities to urban and then to rural areas. It also provides a link in the distribution of goods from ports to consuming centers and vice versa. The shroffs provide means of remittance especially by issuing darshani hundis (sight bills) and checks on outstation banks, discount commercial paper, provide valuable guidance regarding prospects of trade lines, and other incidental services.
The shroffs do lend both with and without security for working capital and mostly to traders. There are no term loans made for the acquisition of fixed assets. The usual lending rates are 18% per annum on advances. About 30% to 40% of their commercial financing is made by way of direct advances either by cash or account payee check. Such advances are usually channelised through brokers in Bombay. In smaller centers the advances are made directly to the borrower. Where clients or borrowers operate current accounts, advances were made to the credit of their accounts and withdrawals against them permitted in cash. The shroffs do fix limits for each party within which they can borrow. In the normal run of business, the average size of advances (made by the 5 surveyed pure Bombay shroffs) ranged from Rs. 50,000 to Rs. 100,000 per borrower. Normally there is no system among Gujerati shroffs for syndicating loans as among the Shikarpuris. Generally a borrower borrows from only one shroff.

The bulk of the shroff's business (that not accounted for by cash advances) -- almost 60-70% -- is comprised of commercial financing through hundis (indigenous style means of remittance). The shroffs issue hundis to parties against payment of cash or on clean credit enabling a transfer of funds from one center to another for deposit or for payment for goods. They also

1/ Although there are various types and local usages among darshani hundis, there are some common features. There are generally four parties to the darshani hundi i.e. drawer, drawee, payee, and the presentor, as well as a number of endorsees (average number of endorsements were 7 according to our survey). The darshani hundi is recorded in the books of accounts of several parties to it (a point which makes it less than ideal as an instrument for handling black money (unaccounted for income tax)---unless, of course, it is a specifically black hundi, recorded in their black books.) While the seller of goods in India can realize payment of an out of station check after an average lapse of 15-20 days, the payment of a hundi is normally realized on the very day of its presentation.
finance their customers for purchase of goods through sight hundis drawn on
their firms or on shroffs at other centers, honor hundis drawn on them by
third parties for the goods supplied to their clients against their advice, and
collect or discount out-station bank checks/drafts for their clients. Our study
of 5 leading Bombay shroffs revealed that the daily average turnover of
hundis/drafts/bills business was of the order of Rs. 4 millions, each
or as high Rs. 20 millions for the 5 shroffs. A rough
estimate of the total annual turnover of the Gujerati hundi business in Bombay
alone is of the order of Rs. 16 billion (of which a Rs. 10 billion is accounted
for by the 6 pure city shroffs themselves).

In recent years, the shroffs have increased their business of
discounting and collecting bank checks whose number varied between 50 and 500 among the
5 shroffs depending upon their size of operations. The corresponding daily
inflow of hundis varied between 40 and 350 among the shroffs surveyed.
Similarly the daily outflow of checks and hundis issued varied between 30 and
50 and 15 and 30 respectively. Discounting hundis or advances made by way of
hundis carried an interest of 18% on an annualized basis. On cash paid hundis for
transfer payments, the shroffs charged various rates of commission ranging
from Rs. 7 to Rs. 15 per Rs. 100,000 of hundis.

Most of the Bombay shroffs are not pure shroffs and combine
commission agency business with banking business. In many cases the hundi business
is undertaken only to the extent that it supports their non-banking business.
The business consists of purchasing goods on a party's account and sending them
on credit. Sometimes they extend a line of credit to their customers. For
all such credit interest charged is between 15% to 18% per annum. A
commission charge of 1/2% to 3/4% of the value of the goods supplied is also levied as commission in addition to freight and handling charges.

**Deposits**

The pure shroffs accept deposits from the general public both on current account and for fixed periods. Their demand liabilities constitute, generally, over 70% of their total deposits. Interest is paid on demand deposits at a rate of from 6 to 9% per year. Time liabilities up to one year carry an interest of about 9 to 10% per year. Interest is either paid regularly or credited by the shroff to the account.

The five leading shroffs of Bombay and the rural shroffs surveyed maintained a minimum capital/deposit ratio of 1:12. The total deposits with the 5 surveyed city pure shroffs are roughly 60 million Rs. whereas their own capital was roughly 4 million Rs. Informed observers estimated that the capital/deposit ratio of the commission agent shroffs in Bombay would be around 1:15.

**Bad Debts**

The average bad debts of the Gujerati Shroff do not exceed 5% of their gross income.

**Establishment and Expenses**

The basic unit of a Gujerati Shroff is the branch -- most firms have one, but the largest surveyed had 93 branches and 200 million Rupees deposits. The branch is headed by a manager paid Rs. 600-1,000 a month. The pure shroffs of Bombay generally employ about 12-15 persons. The Gujerati firms are often larger, but not necessarily so, than the Shikarpuris and have as well messengers and sweepers since they do a considerable business in
collecting bills around town and often house their visiting clients. 1/
The office of a Bombay Gujerati Shroff has a mattress spread on the floor of the shop premises with pillows around for back rests. Sometimes the employees writing the ledgers are provided with low-lying desks. The only other fixture is normally a receipts counter for payments, a telephone, and perhaps a fan or two. In Anand, however, in small town Gujerat, some of the shroffs now set up their offices like those of commercial banks with stand up counters and chairs. Since most of the Bombay offices were established years ago they are all in rent controlled (extremely cheap) accommodations.

The expenses entailed by these establishments varied little among the pure shroffs. A shroff with an annual turnover of over 800 million Rs. had only 100,000 Rs. of expenses a year, whereas a second with a turnover of 3.6 billion Rs. only had 150,000 Rs. of expenditures. (These are both three year averages for the last three years before the survey). The bulk of the shroffs' expenses (55%) went for wages and salaries. 2/

1/ One large small town firm had more than 10 employees, one manager, one cashier, 9 clerks, and 2 messengers. The largest surveyed firms had 18 employees in a branch office, the smallest 2. The clerks are usually not college educated and start at salaries of 150-200 Rs. a month plus an annual bonus of one month's salaries. The clerks are recruited on recommendation from friends of the banker, and experience a low turnover. Overheads of the small town surveyed firm were roughly 2% of its net worth or roughly 400,000 Rs. a year.

2/ One large Gujerati firm reported the following workload allocation for a clientele who maintained 2000 current accounts, 500 borrowing accounts and 100 time deposit accounts. The firm handled the following daily flows:

<table>
<thead>
<tr>
<th>Inflow</th>
<th>Outflow</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bills (Nos.)</td>
<td>200</td>
</tr>
<tr>
<td>Hundis (Nos)</td>
<td>300</td>
</tr>
<tr>
<td>Checks/drafts (Nos.)</td>
<td>450</td>
</tr>
<tr>
<td>Cash (average in Rupees)</td>
<td>3 million</td>
</tr>
</tbody>
</table>

---

1/ One large small town firm had more than 10 employees, one manager, one cashier, 9 clerks, and 2 messengers. The largest surveyed firms had 18 employees in a branch office, the smallest 2. The clerks are usually not college educated and start at salaries of 150-200 Rs. a month plus an annual bonus of one month's salaries. The clerks are recruited on recommendation from friends of the banker, and experience a low turnover. Overheads of the small town surveyed firm were roughly 2% of its net worth or roughly 400,000 Rs. a year.

2/ One large Gujerati firm reported the following workload allocation for a clientele who maintained 2000 current accounts, 500 borrowing accounts and 100 time deposit accounts. The firm handled the following daily flows:
### Distribution of Man Hours Among Functions in a Gujarati Firm

<table>
<thead>
<tr>
<th>Function</th>
<th>No. of Persons</th>
<th>No. of hours per workday</th>
<th>Total hours of work</th>
</tr>
</thead>
<tbody>
<tr>
<td>Bookkeeping</td>
<td>12</td>
<td>@8 hrs/person</td>
<td>96</td>
</tr>
<tr>
<td>Dealing with public</td>
<td>2</td>
<td>@2-1/2 hrs/person</td>
<td>5</td>
</tr>
<tr>
<td>Remittances</td>
<td>1</td>
<td>@1 hr./person</td>
<td>1</td>
</tr>
<tr>
<td>Bills collection and purchase</td>
<td>2</td>
<td>@3hrs/person</td>
<td>6</td>
</tr>
<tr>
<td>Cash payment and receipt</td>
<td>2</td>
<td>@8hrs/person</td>
<td>16</td>
</tr>
<tr>
<td>Advances</td>
<td>2</td>
<td>@4hrs/person</td>
<td>8</td>
</tr>
</tbody>
</table>

132 hours a day
The table below indicates the prime cost of funds and the net returns for an average shroff.

Table VI: Costs and Earnings as Percentage of Pure Gujerati Shroff Firms

<table>
<thead>
<tr>
<th>Costs</th>
<th>Earnings</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Interest liabilities on deposits from public</td>
<td>1. Interest earnings on advances and hundis</td>
</tr>
<tr>
<td>2. Cost of inter-shroff and market borrowing including brokerage, etc.</td>
<td>2. Interest earnings on call funds and inter-shroff advances</td>
</tr>
<tr>
<td>3. Cost of idle funds</td>
<td>3. Commissions on hundis/drafts issued</td>
</tr>
<tr>
<td>4. Provision for defaults</td>
<td></td>
</tr>
<tr>
<td>5. All administrative expenses</td>
<td></td>
</tr>
<tr>
<td>Total 11.5%</td>
<td>Total 20.0%</td>
</tr>
</tbody>
</table>

This data is relevant only to the Bombay shroffs and is based on the actual working of the 5 shroffs surveyed. In fact, the cost of funds are even less than proposed since there are such frequent fluctuations in the amount of demand deposits especially between the slack and busy season transactions that the effective interest paid on deposits comes down to 5% of the working funds. Similarly, administrative expenses do not exceed 2.0%. Since almost 70% to 80% of shroff funds are demand deposits and 50% of their funds are deployed on very short periods including call, the earnings on these are just 12% to 15% per annum - almost 20% to 25% of their funds are deposited in commercial banks both on current account and fixed deposits earning an average yield of 6% per
annum. 1/ Very few funds are deployed on risky advances with yield of 24% to 27% per annum. The effective interest earned could probably be reduced to only 15%. For the table estimates, we have taken good business years when both deposits and deployment are high so that we can estimate the maximum cost of funds position. Therefore, the effective net returns would scarcely exceed 8% of their working funds.

Our estimates show that the transactions costs as a percentage of working funds for the Gujerati Shroff is within the range of 3.0% to 3.5%. If we relate the administrative cost to the annual turnover, the ratio is negligible. Some of the other important indicators of their operations may be observed from the following expense ratios estimated in the survey of the Bombay City pure shroffs.

1/ Their reserves are held both in cash and deposits both with commercial banks and with other shroffs. Two leading shroffs of Bombay kept as high as 30% of their resources as reserves in the bank - about 10% in cash and 20% in fixed deposits against which they enjoyed large overdrafts. The average credit deployment never exceeded 75% of his resources in the peak periods. Significantly, their daily cash balances on hand was about Rs. 30 millions on an average. However, the small sized shroffs only maintain 5% of their resources as reserves including cash on hand. The shroffs doing commission agency work were not so particular about reserves—although most of the time they did keep large credit balances with a number of their upcountry traders for long intervals and thus restricted voluntarily their loanable resources in the process of trade.
Size of Clientele

The Gujerati firms interviewed had a wide range in the number of their clients. The smaller firms in Anand limited themselves to 200-300 accounts and an average working funds of 2.5 million Rs. The largest one had over 2000 accounts and 20,000,000 Rs. The larger firms in Bombay were even larger. The following is the data from five big pure shroff firms in Bombay:

- Number of borrowing accounts — total 1100, average 220, largest 500
- Number of current accounts — total 4100, average 800, highest 2000.
- Credit limits Average range 10-50,000 Rs., 3 under 20,000 Rs.
  - Maxima Range 1 million to 25,000, 3 under 50,000
- Average size of time deposits Range 40-7,500 Rs. Three were under 10,000 Rs. Total credit extended — not counting portfolio of unredeemed hundis ranged from over 30 million Rs. to 600,000 Rs. The clientele of the Gujerati shroffs are mostly traders but include large scale exporters. 1/

Total Credit

Although our sample survey covered only Bombay, Madras and Calicut in respect of the Gujerati shroffs, yet a very conservative estimate of the size of the Gujerati shroff market is attempted here. The table below indicates the estimates of the number of pure shroffs, their own capital and deposits.

1/ In the small town center of Anand, the typical firm surveyed had 200-300 depositors in amounts ranging from 1,000 to 100,000 rupees. Demand deposits got 7-14% as contrasted to 6% in Bombay, three-month deposits got 9%, and one-year deposits got 12%. More than half the total was in these one-year deposits. The one larger firm had well over 1,000 depositors. Though depositors are primarily businessmen who often borrow as well, they include agriculturalists and professionals as well. The Bombay shroffs had roughly the same number of depositors each — but the deposit amounts were much larger and the bulk of the depositors were in current account, but were still traders.
Table VII: EXPENSE RATIOS FOR PURE GUJERATI SHROFFS IN BOMBAY
(Aiyar)

1) % of Wages and salaries to total expenditure 45%
2) % of Rentals to total expenditure 20%
3) % of Other expenses to total expenditure 35%
4) % of Total expenditure to total income 15%
5) % of Total expenditure to total turnover 0.01 to 0.5%
6) % of Total bad debts to total income 3%

Table VIII: TOTAL CREDIT EXTENDED BY GUJERATI SHROFFS
(estimates) (Aiyar)

A. Estimates of Pure Shroffs

<table>
<thead>
<tr>
<th>Classification according to size of deposits</th>
<th>Number</th>
<th>Own Capital</th>
<th>Deposits</th>
<th>Total Working Funds Rs.</th>
</tr>
</thead>
<tbody>
<tr>
<td>Above Rs. 6.5 million</td>
<td>250</td>
<td>@ 800,000/firm 20.00</td>
<td>2 billion</td>
<td>220 billion</td>
</tr>
<tr>
<td>Between Rs. 2.5 million - 6.5 million</td>
<td>675</td>
<td>@ 600,000/firm 40.50</td>
<td>3.02 billion</td>
<td>3.43 billion</td>
</tr>
<tr>
<td>Up to Rs. 2.5 million</td>
<td>1075</td>
<td>@ 500,000/firm</td>
<td>1.3 billion</td>
<td>1.84 billion</td>
</tr>
<tr>
<td></td>
<td>2000</td>
<td>1.4 billion</td>
<td>6.32 billion</td>
<td>7.46 billion</td>
</tr>
</tbody>
</table>

Clientele

The Gujerati Shroff market serves Gujerati traders. In the Bombay urban market, the bulk of their funds flow to Gujerati traders—small and big—covering all the commodity markets.
C. Chettiar

History

Chettiar is an honorific derivation of the word "chetti" which denotes 'a trading and business community among the Hindus.' By tradition, the Chettiar were principally money lenders against security and largely financed foreign trade, or at least commodities destined to flow in foreign trade. In Malaysia, they financed rubber, tea, silk and cloth and in Sri Lanka they financed coconuts. The unsettled political conditions after the Second World War in many of the countries in which they traded forced many of them to return to India, and abandon much of their wealth. For instance, out of the 3 million acres of paddy land owned by the Chettiar in Burma, they were only able to bring back the proceeds of 2 million acres (80%) -- an amount of 750 million Rs. They repatriated 250 million Rs. from Malaysia and 100 million Rs. from Sri Lanka.

Chettiar is an honorific derivation of the word "chetti" which denotes 'a trading and business community among the Hindus.' By tradition, the Chettiar first migrated from Vedaranyam and Kaveri-pun-pattinam (the capital of the 3rd century B.C. Chola Kings) -- where they had started as salt merchants trading with the Fiji Islands -- into Chettinad where they are distributed among 78 villages in the two districts of Ramnad and Pudukottai. Even today they have the custom of giving a bag of salt together with the dowry in their marriages. Their total number is estimated to be over 100,000. Later, they emigrated to such countries as Burma, Sri Lanka, Singapore, Malaysia, etc. where they established themselves as prosperous businessmen during the last 150 years. In Tamil Nadu today, besides Chettinad they are scattered in small towns throughout the state.

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Number and Type

Out of about a 100,000 Chettiar families, over 25,000 continue their hereditary occupation of money lending against security or pawn broking. A large number of these money lenders also do banking business i.e., accept deposits and finance transactions. On the other hand, a good number of the affluent repatriates have become industrialists while some others have ventured into plantations, films, transport, and stock broking.

Among the Chettiar pawnbrokers numbering over 25,000 according to the estimate of their association, over 2,500 are also in the banking business and members of local banking associations. There are about 1,500 non-member moneylenders. Important places where banking is carried on by Chettis are Pudukottai, Tanjore, Coimbatore, Trichy, Madurai, Karaikudy, Virudhnagar, and Salem. In Tanjore district, there are 1,200 licensed pawnbrokers, 300 licensed moneylenders who are members of the moneylenders association and over 1,500 licensed non-members.

Instruments, Rates, Deposits

Chettiar bankers accept deposits and do commercial financing. Although many of them also do pawnbroking -- a distinctive feature of indigenous banking in South India. They also finance businessmen on the strength of hundis, promissory notes and hire purchase agreements. But the Chettis always require securities -- in contrast to the other indigenous bankers we surveyed. The Chettis are far more reluctant to accept deposits than the Gujeratis and largely trade on their own funds. Again in contrast to the Gujeratis, Chettis usually accept term deposits of 3 months and more, though they usually actually permit withdrawal on demand. Depositors are paid annual interest of 12-15%.
The interest rate charged on hundis or promissory notes or on usance hundis is normally Rs. 1.8% per month and in any case not less than 18% per annum. Loans repayable in installments were charged at rates that amounted to 30% per annum. Other short-term advances were typically made at rates close to 24% per annum. In the case of loans paid off in daily installments, the maximum tenure was 200 days and the interest rate was normally 24% per annum.

**Bad Debts**

The Chettiars were not forthcoming about their bad debt experience, but appear to have a somewhat worse record than their confreres elsewhere. Many of the Chettiars were very critical about the series of recent measures by the government which provide relief to small debtors at their expense. Since many of the Chettiars' clients belong to the more moderate income classes, their overdue portfolio would be expected to be higher in any case, than those of other indigenous bankers. These measures simply worsened their situation. The Chettiars did estimate that their bad debts averaged 10% of their profits -- which would compare favorably with the commercial bank experience for the class of client served.

**Establishment**

The Chettiars conduct a low overhead business. Their premises are simple and many times did not even include a well spread mattress. The Chettiar sits on a small mattress or a small chair and the staff sits on a plain mat and operate on a floor desk. The business of money lending alone normally requires only two persons to assist the Chettiar. If pawn-broking is also carried on, then one more person, who could also be an appraiser is employed. The Chettiars usually appointed persons of their own community especially as cashier accounts keepers and appraisers.
Often they employed a Brahmin who may be hereditarily associated with their Chettiar family as an accountant. The salary scales of the clerical assistants range between Rs. 150 and Rs. 250 per month. They also pay their staff an annual bonus equal to a month's salary. Their expenses on rentals is very low and in a large number of cases the business premises is located in a portion of their own houses. A telephone is the only piece of equipment in the Chettiar's establishment. The total establishment expenses may not exceed Rs. 15,000 a year on the average.

The Chettiar's usually keep 5-10% of their assets as reserves with commercial banks or other Chettiar's.

Transactions Costs

According to some Chettiar's, the returns on money lending have been rapidly declining. Our estimates on their cost of funds and earnings based on our survey return are reflected in the tables below but are 2-3 years out of date.

<table>
<thead>
<tr>
<th>Costs</th>
<th>Earnings</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Interest liabilities</td>
<td>1. Interest earnings on</td>
</tr>
<tr>
<td>on deposits</td>
<td>advances</td>
</tr>
<tr>
<td>9.0%</td>
<td>24.0%</td>
</tr>
<tr>
<td>2. Cost of inter-</td>
<td>2. Commissions and</td>
</tr>
<tr>
<td>Chettiar borrowing</td>
<td>Service charges</td>
</tr>
<tr>
<td>0.0</td>
<td>0.5%</td>
</tr>
<tr>
<td>3. Cost of idle funds</td>
<td></td>
</tr>
<tr>
<td>0.1%</td>
<td></td>
</tr>
<tr>
<td>4. Provision for defaults</td>
<td></td>
</tr>
<tr>
<td>1.5%</td>
<td></td>
</tr>
<tr>
<td>5. All administrative</td>
<td></td>
</tr>
<tr>
<td>expenses</td>
<td></td>
</tr>
<tr>
<td>3.0%</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>Total</td>
</tr>
<tr>
<td>13.6%</td>
<td>24.5%</td>
</tr>
</tbody>
</table>
During the last two years the Chettiars have reduced their credit deployment to minimal levels. Their prime costs of funds have increased while their earnings have gone down considerably. Previously the Chettiars had obtained a net return of at least 10% of their working funds. In pockets like Karaikudy where interest rates were not less than 27% per annum their returns were higher. The interest spread works out to about 15% of working funds. The transaction costs thus work out to 6% of the working funds. Some of the other important expense ratios are as follows:

<table>
<thead>
<tr>
<th>Table X: Expense Ratios of Chettiar Firms (Aiyar)</th>
</tr>
</thead>
<tbody>
<tr>
<td>(i) % Wages and salaries to Total expenditure</td>
</tr>
<tr>
<td>(ii) % Rentals to Total expenditure</td>
</tr>
<tr>
<td>(iii) % Other expenses to Total expenditure</td>
</tr>
<tr>
<td>(iv) % Total expenditure to Total income</td>
</tr>
<tr>
<td>(v) % Total expenditure to Total turnover</td>
</tr>
<tr>
<td>(vi) % Total bad debts to Total income</td>
</tr>
</tbody>
</table>

It will be observed that their transaction costs are relatively higher than the Gujerati Shroffs because their deposit capital ratio is much less on an average. The capital deposit rate in pawn-brokings is reported to be 2:3.

**Clientele**

The bulk of Chettiar financing is concentrated in the industrial belt of Coimbatore and Salem. It was estimated for me that the Chettiars of Coimbatore District (about 250 of them) had over 1 billion Rs. of advances out with different industries in the district. In other centers, most of the advances are for trade and commerce and about 10% of them are made to agriculturalists. In Madras City, some advances are made to cover
traders working capital needs, but others finance speculation on the stock market or film production. Many Chettiars have turned to hire purchase finance of motor vehicles and consumer durables.

**Average Assets and Total Credit**

The various interviewees estimated that the total outstanding Chettiar credit is probably of the order of Rs. 3.8 billion. According to one estimate, the small pawn-broking businesses of Chettiars have an average own capital of Rs. 100,000 per firm or a total of about Rs. 250 million for the 2500 pawn-broking firms doing money lending. In Pudukkottai the average own capital of money lenders was Rs. 1 million per firm, in Coimbatore Rs. 3 million, Karaikudy 500,000, and Tanjore only 200,000 Rs. (estimates by local associations).

We may therefore take the general average as Rs. 1 million per firm which works out to Rs. 1.5 billion for the 1500 money lenders bankers. Thus the total own capital used by the 4000 Chettiar indigenous bankers may add up to Rs. 1.75 billion and the total deposits may be estimated at Rs. 2.5 billion. The total working funds of the Chettiar bankers would thus be of the order of Rs. 4.25 billion.

**D. Rastogis**

**History**

Many castes include the Agarwals, Khatris, Kayasthas do money lending business in Uttar Pradesh. But most prominent among the castes of financiers in U.P. are the Rastogis. The Rastogi financial operations have considerably declined particularly with the enactment of the Uttar Pradesh Money Lending Regulations Act of 1976. Important among the centers where
Rastogis still operate are Lucknow, Benares, Farukhabad and Moradabad. Rastogis are bankers in the sense they accept deposits and make advances.

**Number**

According to our survey observations, over 500 Rastogi families are engaged in banking business in the Lucknow region alone.

**Instruments and Rates, Brokers**

Rastogi bankers provide three types of credit:

(a) direct advances and loans
(b) hire purchase credit and
(c) pawn-brokings

Advances are made directly to borrowers in trade and in artisan industries at interest rates not less than 24% per annum. Many such loans were made without any tangible security. Usually such loans were given to traders who in turn provide credit to the artisan borrowers. All direct lending to small borrowers in urban and rural areas was in the form of pawn-brokings in which borrowers pledge their ornaments or jewels as security. Such small loans with or without security were often realised over a period of a year. Such loans are called 'Ugahi' - *realisation over 1 year*. Since the U.P. Moneylenders Lending Regulation Act 1976 has almost entirely curbed their pawn-brokings loans, direct small borrowers loans against security have completely ceased. The Rastogis have now limited their operations to the urban areas and diversified their portfolio increasingly to hire purchase financing of transport vehicles. A flat rate of 18% per annum is charged on all such HP finance.

Brokers number only about 10 in number in Lucknow and about a dozen in Benares. They are important particularly since the Rastogi bankers now have to diversify their portfolio from pawn-brokings to HP and
other direct loans in the urban areas.

**Deposits**

The Rastogis accept deposits, mainly time liabilities for fixed periods, up to 1 year, 3 years and 5 years. Interestingly, demand deposits are not at all significant. Time deposits carry interest rates between 12% and 15% per annum. Among depositors were larger traders and businessmen who had surplus funds. Deposits were of small amounts usually from Rs. 5,000 to Rs. 15,000. In case of the larger reputed families of Rastogi bankers, the depositors were generally bigger businessmen and investors.

In recent years, a couple of brokers have also been canvassing for deposits for some of these Rastogi bankers. Earlier such brokers would directly link depositors with borrowers, and this practice is still very much in vogue in Benares. The banker issues a receipt called 'SARKAT' to the depositor for the amount received from him. The Sarkat is an indigenous form of receipt, analogous to a commercial bank fixed deposit receipt and specifies the date of receipt of the deposit, the depositor's name and address, the amount of deposit, the period of deposit, the form in which the deposit was received (cash/check number) and the name of the broker through whom the deposit was received. The interest rate is not mentioned. Traditionally, the practice is to affix four revenue stamps (now of 20 paisa each) but this has no legal significance. An important feature which varies between Lucknow and Benares informal money markets is that deposit interest rates in Benares are higher (almost Rs. 1.15 to Rs. 1.75 per Rs. 100 per annum) i.e., 14% to 20% per annum as compared to Lucknow rates of 12% to 15% per annum. The reason for such difference is mainly the intermediation cost—in Benares, the depositor contacts the
borrower directly through a broker whereas in the usual Rastogi indigenous banking the depositor invests with the Rastogi banker who in turn does the lending.

**Bad Debts**

Before the regulations, Rastogis reported that the extent of bad debts were as high as 10% to 15% of their gross profits. Although this may not be significant in comparison to the bad debts of the formal agencies, yet it is high as compared to other informal agencies.

**Clientele**

Rastogis direct the bulk of their finances to artisan industries like embroidery, brassware and handicrafts. A significant feature of their financing is that they were primarily rural financiers although they operated from urban centers and are today only lending in the urban areas.

**Establishment and Expenses**

The large size firms usually employed about 8 persons but the smaller financiers employed not more than two persons. The establishment expenses of a small Rastogi banker scarcely exceed Rs. 15,000 a year. The larger firms reported that their establishment expenses amounted to Rs. 40,000 annually.¹/

¹/ The one private banker in Kanpur (interviewed by our survey) had two clerks (paid 300-500 Rs. a month), 15 collectors (Taqqadgirs) paid 150 Rs. a month plus a .01-.02% commission on collections--totalling a probable monthly payroll of 3-4,000 Rs. The firm also pays rent on a one-room office in Kanpur and another in Farrukhabad and retains a full-time lawyer. The total worth of the firm is 2-3,000,000 Rs. and it costs should not be more than 3-4% of its outstanding credit. But even then a good deal of the collection expense is probably connected with the small scale consumer lending the firm does, rather than its commercial finance.
The position may appear more clearly if we can estimate the cost of funds and returns of a Rastogi banker as below:

**Transactions Costs**

Table XI: **Rastogi Costs and Earnings as Percentage of Working Funds**  
*(Aiyar)*

<table>
<thead>
<tr>
<th>Cost</th>
<th>Earnings</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Interest paid on deposit liabilities</td>
<td>9.0%</td>
</tr>
<tr>
<td>2. Inter market borrowings.</td>
<td>0.0%</td>
</tr>
<tr>
<td>3. Cost of idle funds</td>
<td>0.5%</td>
</tr>
<tr>
<td>5. All administrative expenses</td>
<td>3.0%</td>
</tr>
<tr>
<td><strong>Total</strong></td>
<td><strong>14.0%</strong></td>
</tr>
</tbody>
</table>

There is a comfortable interest spread of about 11% and a net return of about 6.5% on working funds. Since the turnover is much less on small loans, the returns on working funds would be relatively lower. The large sized Rastogi banker may have net returns as high as 10% to 11%. The transaction cost however would be the same for all sized financiers at about 5% of the working funds. According to our Survey, some of the expense ratios of Rastogi bankers are as reflected below:

Table XII: **Cost Ratios of Rastogi Bankers**  
*(Aiyar)*

1. % Wages and salaries to Total expenditure 35%
2. % Rentals to Total expenditure 25%
3. % Other expenses to Total expenditure 40%
4. Total expenditure to Total income 25%
5. Total bad debts to Total income 12%
Average Assets and Total Credit

About 6% of the 500 Rastogis near Lucknow are large-sized firms whose resources exceed Rs. 6 million. Nearly 30% of the 500 firms would fall in the resource range of Rs. 2.5 - 3.5 million and the rest are below Rs. 1.5 million. Thus, the total resources of the 500 financiers would be about Rs. 1.11 billion. The capital deposit ratio varied widely among the three categories of financiers ranging from 1:4 among the large financiers to 1:1 among the small size financiers. The estimated own capital of all the three categories of financiers works out to about Rs. 450 million.

E. Finance Companies

History

In recent years, there has been a mushroom growth of finance companies particularly in Tamil Nadu, Andhra Pradesh, Kerala, Karnataka and of late in Punjab, Gujarat and Madhya Pradesh. Such corporations are non-banking financial intermediaries carrying on the business of unregulated banking. They are not incorporated or registered under the Companies Act nor covered by the provisions of the Reserve Bank of India Act 1934. The oldest of these institutions emerged in the early 1960s. They are generally unlimited liability partnership firms with a capital investment of less than Rs. 100,000 and with several partners. Our survey of a few companies in Karur in Tamil Nadu indicated that as many as 200 firms operating there were into this business. The individual firms were small since the provisions of Chapter III-B of the Reserve Bank of India Act 1934 relating to non-banking institutions receiving deposits were applicable only to firms with a subscribed capital exceeding Rs. 100,000.

Our survey covered finance corporations in Trichy, Karur, Madras,
Coimbatore, Salem in Tamil Nadu and Kothamangalam, Muvattapuzha and Calicut in Kerala.

Many finance companies especially those in smaller towns and rural areas carried names akin to established scheduled banks such as 'Dena Finance Corporation', 'United Commercial Corporation', 'New India Bank' etc. Probably this was a method to attract the public on the strength of reputation of the established banks. Sometimes, some of the limited companies promote or link up with such corporations to attract deposits and avoid the restrictions of the Reserve Bank directives on acceptance of deposits by limited companies. In such cases, finance corporations are like holding companies used to raise funds for investment in the parent company.

Number

According to our Survey, there are about 20 partnership firms which are members of an Association of Finance Companies and 40 non-member firms in Trichy. The non-member firms are both proprietary and partnerships and are engaged in both banking and chit business. Similarly in Karur there are 150 partnership firms and about 50 individual /doing banking business. In Kothamangalam, a rural center in Ernakulam district of Kerala, there were about 40 such private finance 'companies'. In one study conducted by the Institute of Financial Management and Research, Madras, the number of such 'companies' were over 100 in Bangalore City. Data on other centers were not readily available.

Instruments and Rates

A notable feature of these corporations is that they perform many functions of a bank. They collect dividends for their customers, discount
hundis, negotiate lorry receipts and discount post-dated checks. The rate of discount in Madras was normally 24% and in any case it was not less than 20%. Usually the interest is recovered in advance but some of the corporations recover at periodic intervals. Many "corporations" also run chit funds.

Since these corporations function like banks, they do maintain both current and fixed deposit accounts with commercial banks, they maintain minimum cash balances with the banks to meet their liquidity needs. Some reserve funds are kept as fixed deposits.

In recent years, these companies also arrange for remittance facilities or have discounting facilities with commercial banks. They have been attracting large amounts of deposits in Kerala especially remittances from Indian nationals abroad. Many Madras based corporations have branches in Kerala and the impression gathered in the survey was that substantial funds flow through these corporations from Kerala to Madras City.

Some of these corporations under a variety of non-financial services especially in Madras, Bombay and Ahmedabad such as providing agency and advisory services -- free advice on income tax, legal and financial problems, investment in shares and securities to their valuable clients. Some of them have gone as far as working as trustees and executors. They have, therefore, to employ qualified persons as well as incur other overhead expenses.

The most popular type of credit is the 90 day credit by means of a usance hundi. It is less rigid than the multani hundi in the sense that it is more easily renewed and thus credit is rolled over. The corporations reported that the rate of interest charged on advances was Rs. 1.75% per month or 21% at term. But many small borrowers said that loans were rarely
available at less than 24% per annum. At some times of year, some "corporations" charge as much as 36% per annum. The corporations reported that the maximum size of their advances would normally not exceed Rs. 10,000 although they have also at times gone up to Rs. 150,000. In Madras, where hire purchase finance was predominant the maximum size of a loan would reach Rs. 300,000.

**Deposits**

Our survey revealed that the capital deposit ratio of these firms was not less than 1:4. The 20 member firms of Trichy had over Rs. 440 million of working funds. The number of depositors ranged from 50 to 2500 and the size of individual deposits ranged from Rs. 100 to Rs. 100,000. There were various types of deposits like savings, cumulative, seasonal, call, lucky, trust, fixed and life deposits. Most of their deposits were for fixed periods up to 3 years. Their deposit clientele mainly came from the middle class officials, traders, shop keepers, self employed, salaried people, and even agriculturalists. These corporations offered attractive interest rates on deposits - 12% per annum on 1 year deposits, 9% per annum on call money and 15% on deposits over 1 year. Further women and charitable institutions were offered slightly higher rates. Door to-door collections of tiny deposit amounts are also made. The drive for deposits considerably declined during the Emergency (1975-77) when the deposit levels were sharply reduced. This does provide a clear indication that a substantial amount of their deposits may have been 'No. 2' moneys, unaccounted for income tax, which may have declined because of stricter enforcement during the emergency. The position has now more or less stabilized at the post Emergency levels (Capital deposit ratio of 1:6) since investment opportunities are gradually improving.
Payment of interest on deposits is done variously—some times half yearly, in others quarterly. Larger size deposits are paid monthly interest. Instances of default in payment of interest are very few. Generally deposits cannot be withdrawn before the maturity period.

Some important features of these corporations are their innovative schemes for attracting deposits. Some of these schemes have also been later introduced by some scheduled banks. Besides attractive interest rates, a prize element was also tied to some deposit schemes.1/

Bad Debts

Bad debts appeared to be 1% of working funds.

Establishment

The small size corporations employed about 5 persons on an average. The large size corporations employed as many as 15 persons. Some of them have moved into their own commercial buildings and others have acquired spacious accommodations in such buildings. But in the smaller towns of Trichy and Karur or Kothamangalam these corporations or banks are located in small unostentatious premises on a rental basis.

1/ For instance, in one scheme, depositors were classified into 3 or 4 groups according to the size of monthly deposit made by them and a few prizes were awarded to depositors in each group. In another scheme, depositors paid a stipulated amount per month for a fixed period, and every month 3 beneficiaries were chosen for fixed prizes. At the end of the period all the depositors would get back their entire amount together with a bonus. In yet another scheme, a depositor pays Rs. 100 per month for 75 months at the end of which he is entitled to a payment of Rs. 10,000 inclusive of interest or can receive Rs. 100 a month for life. Some corporations introduced 6 year cash certificates of various denominations like Rs. 500, Rs. 1,000 and Rs. 5,000. At the end of six years the certificate holders would get back double the amount of deposit, besides facilities for discounting the certificates if needed before the 6 year period. Some corporations had a provision for personal accident insurance up to Rs. 10,000 at no extra cost to the depositor. Others provided incentives of interest free loans up to 10% of the amount of deposits for short periods up to 15 days. Many corporations collected funds from the public by conducting chits.
In Trichy, the corporations surveyed explained that advances were made only to those who were personally known to the partners. Proposals for credit were decided on the basis of the personal knowledge of partners regarding the standing of the parties. Proposals were sanctioned by the managing boards or special sub-committees of the boards of these corporations. Market reports and tax returns are also considered in assessing loan applications. Lists of credit worthy borrowers are drawn up on the strength of market reports, records of borrowers repayments and personal knowledge of borrowers' transactions and these are referred to in assessing proposals. Confidence and informality are very significant and decisions are taken within a week. Loans are secured by promissory notes or hundis.

Transactions Costs

Table XIII: Costs and Earnings of Finance Companies as Percentage of Working Funds (Aiyar)

<table>
<thead>
<tr>
<th>Costs</th>
<th>Returns</th>
</tr>
</thead>
<tbody>
<tr>
<td>1. Interest paid on deposits</td>
<td>1. Interest earnings on advances</td>
</tr>
<tr>
<td>10.0%</td>
<td>24.0%</td>
</tr>
<tr>
<td>2. Additional incentives and prizes to depositors</td>
<td>2. Discount and other commission charges</td>
</tr>
<tr>
<td>1.0%</td>
<td>2.0%</td>
</tr>
<tr>
<td>3. Cost of idle funds</td>
<td>3. Interest earnings on deposits with commercial banks.</td>
</tr>
<tr>
<td>0.0%</td>
<td>0.5%</td>
</tr>
<tr>
<td>4. Provision for default</td>
<td></td>
</tr>
<tr>
<td>1.0%</td>
<td></td>
</tr>
<tr>
<td>5. All administrative expenses</td>
<td></td>
</tr>
<tr>
<td>3.0%</td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>Total 26.5%</td>
</tr>
<tr>
<td>15.0%</td>
<td></td>
</tr>
</tbody>
</table>

There is a minimum net return of 11% on working funds looking at interest earnings on advances. In fact, if their portfolio consists of more discounting business, the returns are even higher. The interest spread was itself 14%. One reason for these corporations to offer attractive interest
on deposits are their high earnings. In fact, one finance corporation informally mentioned that the attraction of promoting large numbers of such corporations was that net returns in this business are as high as 12% to 18% on working funds, and without any regulatory burden under the Companies Act or Reserve Bank of India Act.

**Clientele**

The bulk of the advances of these corporations were made to that trading community in which the partners had interests or specialized knowledge. Purposewise lending of these corporations in Trichy and Karur areas were as follows:

Table XIV: **Allocation of Finance Company Advances by Sector** *(Aiyar)*

<table>
<thead>
<tr>
<th>Purposes</th>
<th>Percentage of Their Advance Portfolio</th>
</tr>
</thead>
<tbody>
<tr>
<td>Wholesale Trade</td>
<td>10%</td>
</tr>
<tr>
<td>Retail Trade</td>
<td>30%</td>
</tr>
<tr>
<td>Small Scale Industries</td>
<td>8%</td>
</tr>
<tr>
<td>Small Business Enterprises</td>
<td>5%</td>
</tr>
<tr>
<td>Road Transport Operations</td>
<td>2%</td>
</tr>
<tr>
<td>Self Employed</td>
<td>5%</td>
</tr>
<tr>
<td>Agriculture</td>
<td>12%</td>
</tr>
<tr>
<td>Cinema</td>
<td>1%</td>
</tr>
<tr>
<td>Construction Contractors</td>
<td>2%</td>
</tr>
<tr>
<td>Hotels</td>
<td>2%</td>
</tr>
<tr>
<td>Exports</td>
<td>-</td>
</tr>
<tr>
<td>Consumer Credit</td>
<td>5%</td>
</tr>
<tr>
<td>Other</td>
<td>18%</td>
</tr>
<tr>
<td></td>
<td>100%</td>
</tr>
</tbody>
</table>
In metropolitan cities like Madras, Hire Purchase finance to the transport sector was predominant. Whereas in rural producing centers like Kothaman-galam, financing of cash crops was very significant. Again financing consumer durables such as scooters, refrigerators, T.V. etc., in metropolitan cities were significant. These corporations assisted their trade clientele with facilities like bridging loans or in meeting short term urgent credit needs. Often, corporations also finance traders dealing with sensitive commodities covered under selective credit controls.
F. Some Financial Markets

It may be useful for the moment to look at how these informal credit systems impinge on certain geographically defined markets—for this purpose we will look at the metropolis of Bombay and the small town of Anand in Gujerat.

Bombay

Both Shikarpuri and Gujerati bankers are active in the Bombay financial market. We estimate that 1.2 billion Rs. of working funds are accounted for by all elements of the Shikarpuri market and finance a wide variety of enterprises—235 millions of these are controlled by Shikarpuri bankers who are members of the Shikarpuri Shroffs Association. The pure Gujerati Shroffs in Bombay account for less than 100 million Rs. of lendable funds—the commission agent shroffs for a great deal more, almost all of it going to finance wholesale trade. The amounts of intermarket credit and other sorts of informal finance—intercorporate call money, company deposits, "badla" finance of stock market speculation, etc.—should be far higher. Much of the informal finance is lent to traders, but it is important for a whole range of industries as well. Commercial banks had 21 billion Rs. of advances in Bombay—5.4 billion to wholesale trade outstanding in December 1977.¹/

Bombay is the center of a metropolitan region which includes an important suburban industrial zone in the Thana-Bellapur area—but the major trading centers are in the city. Bombay has always had an extensive coastal trade with South India and the Middle East—and with the rise of the oil

¹/ Communication from Credit Planning Call, RBI, Bombay, April 15, 1980.
producing regions of the Persian Gulf, this has enabled a rapid expansion of its export and service functions and has made it to some extent an important financial center for the region.

Bombay has a population of over 5 million. It is one of the three new cities (the others are Calcutta and Madras) which the British made their headquarters in India in the eighteenth century. Gradually the West Coast trade was transferred there from ports at the mouth of Gujerat's rivers to the North, like Surat, Cambay and Broach. The wholesale export markets in the nineteenth century gave birth to a number of industrial establishments especially for cotton textiles (which accounted for 83 of 166 factories in Bombay in 1908). Factory employees already numbered 138,000 in 1908. The industrial development accelerated after independence in 1947 and Bombay may have 40,000 or more industrial establishments today, over 5,000 of them full scale factories. These establishments employ over 500,000 workers. A third of the total factory employment is still in the large cotton textile mills, but there are large scale chemical, metal working and other industries as well. Almost as many people appear to be employed in commercial establishments in Bombay, though the number of such establishments is roughly twice as great. Of these trading establishments, roughly 11,000 are wholesale units according to the census, though this seems far too low, even allowing for the fact that pure brokers may have no fixed establishments and thus be unlisted.

These wholesale establishments constitute the major wholesale markets for Western India--first in cloth, grain, cotton and oil seeds, but in iron and steel, chemical goods, gems, bullion and silver and securities

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1/ S.M. Edwardes, *Gazetteer of Bombay City and Island*, Bombay, 1908.
as well. 1/ But "perhaps the most influential of all Bombay markets was the traditional money market". By the 1920's, there were 250 Gujerati shroffs in Bombay clearing 30-40,000 Rs. a year each from hundi discount. In harvest season, money would be remitted upcountry to pay cultivators and in slack season to Bombay to pay for cloth, taxes and other purchases. In addition to the professional shroffs, a large amount of money was lent inside the wholesale market, often through full and part time brokers. "The indigenous money market was not, in fact, closely linked to the modern money market in terms of interest rates and links between shroffs and joint stock banks were tenuous, the shroffs lending from within their own pool of finance." 2/

The Gujerati banking firms today are divided between a small group of large firms (6 account for the bulk of the business and 5 were surveyed intensively)—who specialize in remittance to a chain of correspondents in Gujerat—and a large number of firms who serve primarily as wholesale commission agents—and only incidentally issue their own means of remittance or advance funds to independent operating firms. The proportion of firms who are primarily shroffs, bankers, is far higher in Gujerat. The Bombay remittance firms do have large funds with them in the slack season in Gujerat and are major financiers of a whole range of Bombay traders.

With the development of Indian-owned commercial banks in the early twentieth century some began to serve segments of wholesale trade—as do the somewhat more recent Urban Cooperative Banks. But a considerable role remained for shroffs and as recent credit policies have again cut down the


2/ Gordon, op. cit.
amount of credit the banks can extend to traders, so they must turn again to traditional sources like market broker and Gujerati shroff finance.

The share market has its own type of credit system (called badla) operated by the share brokers under which 14-15% money often with 100% margin is provided on the security of shares (with 1.2% brokerage).

In addition, to these entirely traditional systems there exist several largely informal markets which serve the corporate sector—primarily in industry. These markets have expanded considerably in recent years in partial response to credit stringencies enforced by the commercial banks. There is a call money market between larger firms, and a more general market in corporate deposits—usually in denominations of several thousands and vigorously sold by stock brokerage firms to a wide range of the middle class. In the case of the call money, the money is slightly cheaper than available from the banks and enables more efficient cash management for lenders. The deposit money is more expensive, but overcomes bank credit constraints. Recent government regulations have severely limited the extent to which joint stock companies can rely on these forms of finance.

A group of Shikarpuri bankers from Sind have also operated in Bombay for years and were augmented by a large number of others who fled from Karachi after the partition of the subcontinent between India and Pakistan in 1947. These Shikarpuri bankers lent to a more cosmopolitan clientele, including industrialists and exporters. They were heavily dependent on discounting their bills with the Imperial Bank, later the State Bank of India, and other commercial banks.
Bank accommodation for these Shikarpuri bankers was reduced throughout the 1960's and is now less than 1/10 of its former amount and their own lending has declined accordingly. But the Shikarpuri brokers, who formerly served as agents for these bankers have gone in search of new purchasers for their credit notes and may even have increased the volume of lending they handle. We estimate here that the Shikarpuri brokers were responsible altogether for 1.2 billion Rs. of outstanding credit in 1979.

Data on intermarket lending is scattered. The Hindustan Chamber of Commerce which has 1300 members, mostly Marwaris in the textile and Kirana (spices, lentils, etc.) trade supervises a considerable system of intermarket lending. Lendings are made within the range of 15-21% per annum on the basis of a promissory note. Similar rates were characteristic of other wholesale market credit systems.

One rough estimate is that total informal credit in the Bombay grain trade may be 9 billion Rs.; in iron and steel, 800 million Rs.; with lesser amounts in other markets such as the 100-120 million Rs. in the dried fruit business; possible 50-40 million Rs. in the Bombay jute market, etc. The amount of money in corporate deposits is reported to be 35 billion Rs. by the Reserve Bank of India.
Anand

The role of indigenous bankers is easier to trace in a small town in Gujerat, which is a more typical locus for Gujerati Shroffs. Anand (population 70,000) is a small market town in the center of the Charottar "good land" 1/ region of Kaira (Khera) District in Gujerat. The region is one of India's richest agricultural areas. Famous as the cradle of the nationalist movement (the home of Sardar Patel), as the home of Indian emigrants to East Africa, and most recently for the Amul Dairy Project which has succeeded in the modern commercial production of milk in India--the region is especially characterized by the growing of the indigenous style of tobacco, that is used in the "biri" cigarettes, so popular with traditional Indians. As early as 1903, 24 square miles were planted in tobacco, 2% of the total and by 1960, 12% of the total area of Kaira district was in tobacco, producing 44,000 tons of tobacco a year.

The Kaira area is also a grain surplus area and considerable grain is exported. There is a small amount of medium sized industry (358 units in 1961) in the district and a large number of small household units (more than 3000 in 1961), and again in 1961--more than 6000 people belonged to 115 industrial cooperative societies. Most of these small units serve a local market--processing oil seeds, making and repairing clothes and utensils, but there are some who send out their products such as the snuff industry in Anand town. Despite the presence of tobacco--only 1-2 factories for biri exist in the district.

The town of Anand, commercial headquarters of one of the districts subdivisions, is fairly close to the major industrial center of Ahmedabad and several hundred miles from Bombay. It has been the center of vigorous trading and financing firms for several centuries. Kaira and Anand firms are found throughout India and East Africa.

The local Shroffs, and there are several hundred in Kaira district and 20 in the town of Anand provide the bulk (possibly 80-90% of their working funds, estimated to be 250,000,000 Rs. a year) to the merchants who buy the "biri" tobacco, store it for a year while it ages and send it, especially to Calcutta, where it is rolled into cigarettes. These tobacco merchants are typically paid themselves 1½ to 2 years after the tobacco is harvested and require enormous capital to carry the necessary stocks and trade credit.

One large village based commission agent (of peasant origin--the six family members have 125 acres of land of their own) purchased 15 million Rs. of tobacco in 1978 and had a current stock of 2.8 million Rs. He charges interest on his trade credit to manufacturers--1 year after delivery at 9% and is totally dependent on shroff credit and what he gets from cultivators--whom he typically pays four months after delivery. In addition--he gets brokerage and a commission. Another big merchant (150 acres of own land) also buys from 10-15 million Rs. of tobacco a year. He has credit limits of 2.5 million Rs. with two nationalized banks in his village in addition to shroff credit.

Shroffs also fund the bulk of the grain trade, wholesale cloth, and a variety of smaller enterprises including sporadic industries, building contractors, and even doctors' surgeries usually on the basis that the
borrowers are related to their other clientele. While shroff capital in Kaira district was placed at 250,000,000 Rs. (in August 1970)—commercial banks there had 488 million Rs. outstanding advances in Dec. 1977—25 million of that to traders 1/. The shroffs offices in Anand are located throughout the main markets and several of them look and cooperate like commercial banks. They have abandoned the white padded mats of the traditional Indian "gaddi" and have broad clienteles of businessmen and must have a minimum of 6,000 account holders in the Anand Taluk area—around 2% of the total population.

G. Intermarket Finance and Brokers

In North India, and to a lesser extent elsewhere, the central institution in various local informal financial markets turned out to be brokers who carried finance in the form of term loans from surplus to deficit units. These markets were studied in Amritsar and Kanpur by interviewing a selected group of brokers and borrowers.

Both Amritsar (pop. 1971—430,000) and Kanpur (pop. 1971—1,300,000) are major industrial and market centers and both the location of regional cloth and wholesale markets (for cloth in Kanpur, the Generalganj market and in Amritsar, the Katra Ahluwalia). In Amritsar’s case the market serves the Punjab and in Kanpur, Eastern and Central Uttar Pradesh. Total was outstanding credit of commercial banks/1 billion Rs. in Kanpur (district) (125 million to trade) and 662 million in Amritsar (79 million to trade) in Dec. 1977, so trade finance has largely to come from non-bank services.

In these cloth markets, mill made cloth is sold to authorized "stockists" on 1-3 month credit (no interest) and they in turn sell it to

1/ Communications from Credit Planning Cell, RBI, Bombay, April 15, 1980.
larger dealers and commission agents who distribute the cloth directly or through brokers to retail shops throughout the region. But there is no sharp differentiation of wholesale and retail dealers. Most of the higher level dealers will also sell to final consumers and there is no uniform series of wholesaler and retailer discounts. Each member of the chain, typically, sells on longer terms than he receives, and thus needs finance to support his share of trade debts as well as to bridge his cash flows. Relatively little bank credit is provided to the cloth trade, as a matter of policy. So the cloth wholesalers or larger dealers (200 in Kanpur, 500 with many semi-wholesalers in Amritsar), borrow extensively (up to fifty percent of their working capital in peak season) through brokers (who number 10 in Kanpur, 15 in Amritsar). Brokers are generally felt to facilitate lending, though lending, including most lending on open current account, is done directly. The normal instrument is a 3-4 month promissory note, a face demand note, endorsed for a term on the back. Since it is a demand note in form, it avoids stamp duty. The notes are issued at 12-18% interest per annum plus .5-1% per annum brokerage and occasionally a couple of "points"--called "Shigriti", literally "speed money." The smaller notes are normally not less than 5,000 Rs.--though there is considerable variation. The ruling rate in 1978 seemed to be at the top of the range. The notes are unsecured.

The sources of funds on whom the brokers draw are various, but most are traders within the cloth or adjoining commodity markets, a few are full time moneylenders. The lenders include, especially in Amritsar, some wealthy farmers.
The whole of this credit operates in an ingrown world of winding narrow streets of the cloth market where brokers, lenders, and borrowers are in intimate contact. Defaults are few, about 1-2% of lendings or less—usually compromised, and rarely collected through the courts.

Industrial units in Amritsar borrow in roughly the same form. Again the borrowers are larger size firms—with over 500,000 Rs. net worth. Both in Kanpur and Amritsar, about 5-10% of the peak season working capital needs of powerloom owners was estimated to be met by such borrowings. These loans are in addition to bank credit, and made at rates close to 18%. There are 12,000 art silk powerlooms, 1200 wool cloth powerlooms and 3700 wool handlooms in Amritsar.

Though the powerloom clientele is more dispersed than those in the cloth market, brokers insist on long records of association and intimate knowledge.

Smaller units do not have access to this kind of finance—but may get their yarn at 24% per annum from financiers and dealers.

The pattern is duplicated in many other wholesale markets and industrial fields. In Calcutta, for example, the leading grain traders (188 members of the association, 50-60 non-members) estimate that for an annual turnover of 2 billion Rs., they need 300-400 million Rs. of capital during the peak season, of which 250 or so is borrowed through brokers on promissory notes (nominally demand notes, but actually term notes) at 18% per annum plus 1.2% brokerage. Most of the funds come from within the market but at least 50,000,000 Rs. comes in from jute traders during peak season.
IV. SUMMARY OF CHARACTERISTICS
Table XV: INDIGENOUS CREDIT SYSTEMS AND THEIR CREDIT EXTENDED  
(1979, AIYAR)  
(All rates are approximate - the interest rates and numbers of firms are firmer than the estimates of credit extended)

<table>
<thead>
<tr>
<th>Number of Firms</th>
<th>Credit Extended in Millions of Rs. (i.e. Working Funds in Use at Point of Survey)</th>
<th>Rates of Interest Charged in % Per Annum</th>
</tr>
</thead>
<tbody>
<tr>
<td>(1) Shikarpuri or Multani Bankers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Members of Local Associations</td>
<td>550</td>
<td>600*</td>
</tr>
<tr>
<td>Non-members</td>
<td>650</td>
<td>650</td>
</tr>
<tr>
<td>Brokers</td>
<td>550</td>
<td>1250</td>
</tr>
<tr>
<td>SHIKARPURI SUBMARKETS</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Bombay members</td>
<td>238</td>
<td>240</td>
</tr>
<tr>
<td>Bombay non-members</td>
<td>350</td>
<td>330</td>
</tr>
<tr>
<td>Madras members</td>
<td>126</td>
<td>150</td>
</tr>
<tr>
<td>Madras non-members</td>
<td>200</td>
<td>160</td>
</tr>
<tr>
<td>South Indian Cities</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Madurai members</td>
<td>20</td>
<td>30</td>
</tr>
<tr>
<td>Madurai non-members</td>
<td>10</td>
<td>N.A.</td>
</tr>
<tr>
<td>Trichy members</td>
<td>30</td>
<td>8</td>
</tr>
<tr>
<td>Trichy non-members</td>
<td>12</td>
<td>N.A.</td>
</tr>
<tr>
<td>Tanjore</td>
<td>4</td>
<td>6</td>
</tr>
<tr>
<td>Salem</td>
<td>40</td>
<td>50</td>
</tr>
<tr>
<td>Calicut</td>
<td>20</td>
<td>10</td>
</tr>
<tr>
<td>Coimbatore members</td>
<td>20</td>
<td>30</td>
</tr>
<tr>
<td>Coimbatore non-members</td>
<td>35</td>
<td>N.A.</td>
</tr>
<tr>
<td>Bangalore members</td>
<td>N.A.</td>
<td>45</td>
</tr>
<tr>
<td>Bangalore non-members</td>
<td>N.A.</td>
<td>55</td>
</tr>
<tr>
<td>Hyderabad members</td>
<td>N.A.</td>
<td>30</td>
</tr>
<tr>
<td>Hyderabad non-members</td>
<td>N.A.</td>
<td>45</td>
</tr>
<tr>
<td>Vijayawada</td>
<td>N.A.</td>
<td>10</td>
</tr>
<tr>
<td>Marwaris in Madras doing similar business</td>
<td>100</td>
<td>104</td>
</tr>
<tr>
<td>(Multanis receive 30-60 million Rs. in bank refinance and have 75 million Rs. of Deposits)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(2) Gujarati Bankers</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Pure Bankers (all over India)</td>
<td>2000</td>
<td>7460</td>
</tr>
<tr>
<td>Bankers and Commission Agents</td>
<td></td>
<td></td>
</tr>
<tr>
<td>at least 2500 firms</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Average Rates</td>
<td></td>
<td></td>
</tr>
<tr>
<td>* Krishnan estimates slightly less than half this level.</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(Multanis receive 30-60 million Rs. in bank refinance and have 75 million Rs. of Deposits)
Table XV: (continued)

Gujerati Hundi turnover in Bombay in millions of Rs. per annum

<p>| | |</p>
<table>
<thead>
<tr>
<th></th>
<th></th>
</tr>
</thead>
<tbody>
<tr>
<td>Pure Bankers</td>
<td>10,000 (Aiyar Survey)</td>
</tr>
<tr>
<td>Banker-Commission Agents</td>
<td>6,000 (Aiyar Survey)</td>
</tr>
</tbody>
</table>

(3) Chettiars do secured lending — There are 25,000 pawnbrokers, 25% of whose lending is for commercial purposes and dispose of a total credit of 12,500 million Rs. and 2,500 bankers who extend 3,800 million Rs. of credit and hold perhaps 2,500 million Rs. deposits. The bankers, inter alia, refinance pawnbroker lending. Normal lending rates are 18-30%, per annum; deposits for over 1 year get 15% per annum and less than a year get 12%.

<table>
<thead>
<tr>
<th>Number of Firms</th>
<th>Credit Extended in Millions of Rs.</th>
<th>Rates of Interest in % per Annum</th>
</tr>
</thead>
<tbody>
<tr>
<td>Chettiar Bankers</td>
<td>25,000</td>
<td>3,800</td>
</tr>
<tr>
<td>Chettiar Pawnbrokers</td>
<td>40,000</td>
<td>12,500</td>
</tr>
<tr>
<td>(4) Rastogi Bankers</td>
<td>500</td>
<td>1000</td>
</tr>
</tbody>
</table>

(They have roughly 550 million Rs. in deposits on which they pay 12-15% in Lucknow and 14-20% in Benares. They lend on a secured basis at 18-24%, and on an unsecured basis at higher rates. Effective rate on hire purchase finance is 36% per annum.)
Table XVI: FINANCE COMPANIES AND BROKERS FOR INTERMARKET CREDIT AND THEIR RATES (1978-79, AIYAR & TIMBERG)

(1) Intra-market and Intermarket Lending.  
| Lending to Cloth Commission Agents in Amritsar   | 9-18%                           |
| Lending to Cloth Commission Agents in Delhi     | 15%                             |
| Lending to Cloth Commission Agents in Kanpur    | 13-16%                          |
| Yarn Traders Advances to Powerlooms, Kanpur     | 18%                             |
| Yarn Traders Advances to Powerlooms, Amritsar   | 14-22%                          |

BOMBAY

| Lending to Bombay Rice and Dal (gram) Traders   | 15%                             |
| Lending to Bombay Dried Fruit Traders          | 18%                             |
| Lending to Bombay Jute Traders                 | 18%                             |
| Lending to Bombay Iron and Steel Trader's      | 18%                             |
| Lending to Bombay Share Trading ("Badla")      | 15-16%                          |

CALCUTTA

| Lending to Cloth Commission Agents             | 16.2%                           |
| Lending to Yarn Traders                        | 15%                             |
| Lending to Grain Traders                       | 15.2%                           |
| Lending to Oil Seeds Dealers                   | 15-18%                          |
| Lending to Gunny Dealers                       | 18%                             |
| Deposits with Small Pharmaceuticals Firms      | 14.5-15%                        |

(2) Finance "Companies"

There are 60 in Trichy, 40 in Kothamangalam, and 100 in Karur. Twenty firms in Trichy had assets of 440 million Rs. They pay 7-15% on deposits and charge 21-24%.
Table XVII: COMPARATIVE DATA ON COMMERCIAL BANKS AND PRICES

<table>
<thead>
<tr>
<th></th>
<th>Gross Bank Credit Outstanding Normal Rates in % Gross Bank Credit Outstanding Normal Rates in %</th>
<th>Normal Interest Rates in % per Year</th>
</tr>
</thead>
<tbody>
<tr>
<td>A. June 1978*</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Total</td>
<td>160,000</td>
<td>14-16%</td>
</tr>
<tr>
<td>Wholesale Trade</td>
<td>10,000</td>
<td></td>
</tr>
<tr>
<td>(excluding three large</td>
<td></td>
<td></td>
</tr>
<tr>
<td>public sector</td>
<td></td>
<td></td>
</tr>
<tr>
<td>corporations)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>B. Advances to Small</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Industry by State by</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Commercial Banks in</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Billion Rs.</td>
<td></td>
<td></td>
</tr>
<tr>
<td>State</td>
<td>1976</td>
<td>1977</td>
</tr>
<tr>
<td>All India</td>
<td>14.2</td>
<td>17.02</td>
</tr>
<tr>
<td>Maharashtra (including</td>
<td>2.9</td>
<td>3.3</td>
</tr>
<tr>
<td>Bombay)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gujerat</td>
<td>1.3</td>
<td>1.5</td>
</tr>
<tr>
<td>Uttar Pradesh</td>
<td>1.07</td>
<td>1.4</td>
</tr>
<tr>
<td>Tamil Nadu</td>
<td>1.5</td>
<td>1.8</td>
</tr>
<tr>
<td>C. Outstanding Credit</td>
<td></td>
<td></td>
</tr>
<tr>
<td>of Scheduled Commercial</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Banks***</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(As on the last Friday</td>
<td></td>
<td></td>
</tr>
<tr>
<td>of December 1977)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>(Amount in million</td>
<td></td>
<td></td>
</tr>
<tr>
<td>rupees)</td>
<td></td>
<td></td>
</tr>
<tr>
<td>District</td>
<td>Total Credit</td>
<td>Of Which for Trade</td>
</tr>
<tr>
<td>Bombay</td>
<td>21,297.7</td>
<td>5,360.8</td>
</tr>
<tr>
<td>Kaira</td>
<td>485.7</td>
<td>34.9</td>
</tr>
<tr>
<td>Kanpur</td>
<td>1,071.3</td>
<td>123.2</td>
</tr>
<tr>
<td>Amritsar</td>
<td>662.3</td>
<td>79.2</td>
</tr>
</tbody>
</table>
Table XVII (continued)

D. Rate of Increase in Wholesale Price Index in India Averaged 10.6% per Year from 1970-71 to 1978-79.**


** Statistical Tables, pp. 36-37.

*** Communication from the Credit Planning Cell, RBI, Bombay, April 15, 1980.

**** RBIB XXXVII (August 1979), p. 5418.
Volume and Terms of Credit and Deposits (all rates are per annum equivalents)

Rough estimates of the volume and rates charged for credit in various ICMs are found in Tables XV and XVI. In general, brokers and indigenous bankers provide money at an annual equivalent of 18-24% to larger established traders, with 18% the norm—and to smaller artisans and traders in a range sometimes as high as 24-36%. Checks and bills are discounted at 18-24%. Call money loans in urban areas are sometimes provided at rates as low as 12%. Black money also is normally available at slightly cheaper rates—12-15% in Bombay and 24% in Madras. In general, South India has higher informal rates, and a wider variety of recently started informal institutions (nidhis, finance companies, and chit funds)—possibly reflecting a greater capital stringency there. Shikarpuri bankers' rates also seem high—though more so in Bombay and Madras where they are readjusting to a decline in bank refinance.

For purposes of comparison normal bank lending rates are between 13% and 16% per annum—and most ICM clients might well have to pay the higher rates if they could get accommodation. The modal informal rate is thus only 2-8% higher than the bank rate—and probably even less if we look at the actual transactions costs to the borrower involved. The All-India Debt and Investment Survey, 1971-72 says that 75% of households (accounting for 85% of lending) in rural areas borrowed at rates under 25%. Of course, the relevant bank rate here is 11%.\footnote{Indebtedness of Rural Households and Availability of Institutional Finance, RBI, 1977, p. 146.} If the modal rate was 18%, the difference between bank and informal rates would be the same as in urban areas.

Many of these interest rates are fixed in competitive markets. In some cases, there is some price leadership or institutional fixation as by

\footnote{Indebtedness of Rural Households and Availability of Institutional Finance, RBI, 1977, p. 146.}
the cloth market committees and in others the degree of association between lenders must lead to some coordination. The rates clearly move in some sympathy with bank lending rates as charted in some recent yet unpublished work by V.V. Bhatt and T.R. Venkatachalam.\footnote{See also S. Ghatak, \textit{Rural Money Markets in India} (Delhi, MacMillan, 1976), pp. 98-101.} The differences in interest rates from city to city are substantial and reflect the largely local and even sub-local nature of the markets surveyed. Even the Gujarati bankers who move freely back and forth between Bombay and Gujerat report money a percentage point or so cheaper in Bombay. Some of this difference may reflect the greater availability of bank credit in Bombay—or the greater liquidity of Bombay as a financial center—it clearly does not reflect arbitrage costs which are less than .2%—or .3% if one assumes a need to cover double the remittance costs. The differences between Madras and Bombay Shikarpuris are equally hard to explain because the firms are related, though money is not so mobile. Perhaps the risk level is perceived higher in Madras—or the lower Bombay figure is a reflection of the inelasticity of demand in the Madras market within the ranges the Shikarpuris charge, i.e., that they could not place more of their Bombay funds in Madras at lower rates—since the demand for their funds is interest inelastic.

As to the persisting difference between the inter-market and Gujerati rates and those charged by Shikarpuris and finance companies—we must assume that the Shikarpuris and finance companies deal with people who do not have access to sufficient lower priced finance from either informal sources or the banks, and that seems largely the case. That is, the Shikarpuri and finance company market deals in instruments which are less competitive with those used in formal markets.
Normally interest is paid when the "note" is paid off—or on current account for credits from Gujerati bankers. It is collected when the account is brought into balance. Shikarpuris and some other lenders take their interest in advance, and that has been taken account of in reporting their rates on a basis comparable to the others. Penal interest is not common except among hire purchase companies—overdues are rare and usually rolled over on a negotiated basis. In some situations, interest is paid every quarter or month, independently of principal repayment. In other circumstances, particularly in South India, installment payments, usually concealing higher interest rates are becoming common. (In these cases, actual rates are sometimes hidden by quick repayment as in one case reported by A.N. Bose from Calcutta.1)

In each case there may be some incidental fees—brokerage, charity charges, "shigriti" (speed money), and stamp taxes but I have tried to consolidate these in the reported rates. These exist in different forms for bank lending and sometimes raise the cost of lending as much as 6%—and have not been consolidated in the recorded rates in Table XVII.

Normal brokerage is less than 1/2% annually of the loan principal, but Shikarpuri brokers charge, as I noted, 2%. In no case, that I know of, does the broker guarantee the loan, but his business is obviously based on his track record in finding good borrowers who repay on schedule.

As with lending rates, Tables XV and XVI include some estimates of the size of the informal submarkets we surveyed. Short of a total survey it is hard to determine what percentage of total capital employed in trade and industry is accounted for by informal lending—and what relation informal capital employed has to that provided by the commercial banks—who are the

prime other urban credit source. Urban cooperatives are relatively small and weak; development finance is available elsewhere but usually not for working capital purposes (from State Finance Corporations, Industrial Development Corporations, and Small Scale Industry Corporations).

There are several definitional problems connected with the "concept" of informal money. On the one hand, reported figures include a considerable amount of money from friends and relatives—that might well be counted in equity. On the other hand, it includes a certain amount of money which might well be considered simple trade credit and outside our terms of reference. By and large the figures contain, today, very little agricultural credit (less than 5%). The figures also could include, but this is more easily separable—deposits and call money.

(35 billion Rs. of the former and 50-100 million Rs. of the latter.)

Just as relatively accurate figures are available showing that 70% of all debt in the rural sector was owed to "non-institutional creditors" (from the RBI's Rural Credit Survey in 1971)—similar data should become available in the next two years from the RBI's Urban Household Sector Survey (which includes non-limited company enterprises) and the Economic Census. With the rapid increase in commercial bank credit to agriculture since bank nationalization, this figure should have declined yet further. Nonetheless one has reasons to be apprehensive about the accuracy of the returns that will be made on financial matters to these two surveys.

Table XV also deals with the volume of deposits with indigenous bankers and the rates paid on them. One source estimated that Gujarati bankers may have as much as 8 billion Rs. of deposits.
Although their loan/deposits ratios are lower, Rastogis and Chettiar
covered in C.V. Aiyar's survey work reported considerable deposits; Shikarpuris
had very little in the way of deposits and most of that from family and close
associates. Finance "companies" were entirely dependent on deposits, mostly
for three year terms, at 15% per annum.
Instruments

The instruments for borrowing in the informal market vary. One of the most common is the demand note, often "informally" endorsed for a term and rate on the back. As a demand bill the instrument avoids the stamp tax on term bills such as those traditionally used by the Shikarpuris. The Shikarpuris clearly feel that even with the added cost the stamp gives their notes greater authority and it makes possible their discount with the bank. As discount has become less possible they have largely abandoned this term note—or muddati or multani hundi. In the smaller centers in the South where bank refinance is unavailable, the bulk of Shikarpuri advances are done on demand notes. Shikarpuris have in any case been moving from 90 days promissory notes to installment credit—and such credit now accounts for about half of their advances in the South. The installment notes, especially in the South, are commonly supported by post-dated checks, one for each installment payment.

Thirty to forty percent of Gujerati banker finance is done by direct cash advance and 60-70% through the issue of hundis. The Chettiars do obtain both promissory notes and security from their clients, or hire purchase agreements when appropriate. Intermarket lending is most usually done on promissory notes. Finance companies often loan on a term bill.

Deposits are often given on a simple receipt now universal because of income tax; traditional receipts, however, (called variously "ruka" or "chilka" [peels]) simply bore an amount and occasionally a name and date. Such receipts often in code are still common in black money markets.
Organization and Regulation

One characteristic of some of these informal credit markets worthy of note is their organization for self-regulation. About half the Shikarpuri financiers belong to local associations which serve both as social centers and enable their members to be eligible for bank refinance. These usually do not have explicit disciplinary functions, though they may exercise informal control. The percentage of Gujerati bankers and market finance brokers of other communities who belong to such associations is often lower, but these associations often serve key disciplinary functions such as certifying the dishonor of a hundi, and often setting maximum interest rates—especially for transactions among members. These regulatory functions are especially pronounced in the organizations that run traditional markets like the wholesale cloth markets. The Hindustan Chamber of Commerce in Bombay, the Merchants Chamber of Commerce in Calcutta, the Delhi Mercantile Chamber, and the Kanpur Cloth Committee all serve these functions. In these respects, these associations inherit the traditions of the commercial panchayats who have run such markets in India from time immemorial.

Newer markets—those in shares and futures for example—which are populated by those from traditional trading backgrounds often preserve the old governing forms as well. On the other hand, markets where a great deal of change of personnel has occurred, such as the wholesale markets of Delhi, are often characterized by looser control.

The Bombay Shroff's Association—the organization of the city's Gujerati bankers—has tried to create a national federation of these local bankers' associations—the All Indian Shroffs Association—to represent the
indigenous banking community in political matters and has achieved a modicum of success, at least within the Gujerati community.

**Transactions Costs I: The Costs of Administration**

Transactions costs in those markets (not covered in Table XIX) where brokers predominate as intermediaries may be as little as 1.2% on an annual basis though they do go as high as 1.2% of turnover or notionally 4.8% of capital employed. Shikarpuri brokers charge 2% per annum on each transaction, usually a three-month loan. Indigenous bankers and commercial financiers typically have higher costs.

The Bombay Gujerati bankers' expenses were probably lower than the small town banker, because they had fewer clients. Forty-five percent of the total administrative costs went toward wages and salaries.

Table XVIII: A. Expense Ratios of Different Informal Credit Market Agencies

(Aiyar, 1979)

<table>
<thead>
<tr>
<th>Type of Banker</th>
<th>% Wages and Salaries to Total Expenses</th>
<th>% Rental to Total Expenses</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shikarpuris</td>
<td>25</td>
<td>20</td>
</tr>
<tr>
<td>Gujeratis (Bombay)</td>
<td>45</td>
<td>20</td>
</tr>
<tr>
<td>Chettiars</td>
<td>55</td>
<td>15</td>
</tr>
<tr>
<td>Rastogis</td>
<td>35</td>
<td>25</td>
</tr>
</tbody>
</table>
B. Spreads Between Borrowers and Lenders

(Aiyar, 1979)

<table>
<thead>
<tr>
<th>Agency</th>
<th>Deposit Cost Used</th>
<th>Cost of Lendable Funds in % per annum (as percentage of working funds)</th>
<th>Charge to Borrower in % per annum</th>
<th>Margin</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shikarpuris</td>
<td>15%</td>
<td>20/20.5</td>
<td>31.5</td>
<td>11.5</td>
</tr>
<tr>
<td>Gujeratis</td>
<td>8%</td>
<td>11</td>
<td>20</td>
<td>9</td>
</tr>
<tr>
<td>Chettiars</td>
<td>9%</td>
<td>14</td>
<td>24.5</td>
<td>10.5</td>
</tr>
<tr>
<td>Rastogi</td>
<td>9%</td>
<td>14</td>
<td>20.5</td>
<td>6.5</td>
</tr>
<tr>
<td>Finance Companies</td>
<td>10%</td>
<td>15</td>
<td>26.5</td>
<td>11.5</td>
</tr>
</tbody>
</table>

Comment—For the markets I observed, the deposit rates are on the low side by 2-3% for the Gujeratis, and the charges to borrower slightly high even including brokerage again by 1-2%. (Timberg).

Table XIX: Transactions Costs of Commercial Banks

(As percentage of outstanding loans and advances, 1975)

<table>
<thead>
<tr>
<th></th>
<th>Administration</th>
<th>Default loss</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Syndicate Bank</td>
<td>2.24</td>
<td>.52</td>
<td>2.76</td>
</tr>
<tr>
<td>Other Small Enterprise (non-industrial, small business loans)</td>
<td>2.75</td>
<td>1.00</td>
<td>3.75</td>
</tr>
<tr>
<td>Large Metropolitan Bank 1/</td>
<td>1.70</td>
<td>.70</td>
<td>2.40</td>
</tr>
<tr>
<td>Mampilly Estimate 2/</td>
<td>3.00</td>
<td>1.00</td>
<td>4.00</td>
</tr>
</tbody>
</table>

1/ Bhatt and Roe, p. 42.

2/ Paul Mampilly, Innovations in Banking: The Indian Experience, Part II, IBRD (1979), pp. 36, 41-42, 148, 185, 195-196. This is an average figure. For certain categories of small loans the cost is much higher. Mampilly estimates that the commercial banks lose 34.99% on a full cost basis on cash credit loans under 10,000 Rs. They break even at 45,506 Rs. The modal loan at least for Gujerati, Chettiar and Rastogi bankers is well under this loan amount.
Table XIX (cont'd): Transactions Costs as Percentage of Working Funds of Informal Credit Systems

(Aiyar, 1979)

<table>
<thead>
<tr>
<th>Type</th>
<th>Administration</th>
<th>Default Loss</th>
<th>Total</th>
</tr>
</thead>
<tbody>
<tr>
<td>Shikarpuri</td>
<td>4.5</td>
<td>1.0</td>
<td>5.5</td>
</tr>
<tr>
<td>Gujerati</td>
<td>2.5</td>
<td>.5</td>
<td>3.0</td>
</tr>
<tr>
<td>Chettiar</td>
<td>3.1</td>
<td>1.5</td>
<td>4.6</td>
</tr>
<tr>
<td>Rastogi</td>
<td>3.5</td>
<td>1.5</td>
<td>5.0</td>
</tr>
</tbody>
</table>
The employees, if any, of informal credit agencies are typically less well paid (and educated), the establishment less elaborate, and the paper work less complex than in commercial banks. Operations are smaller and typically under the personal supervision of the owner, so numerous crosschecks against fraud are not needed. Not surprisingly, costs are usually somewhat lower than those reported by the Indian commercial banks--on their relatively high cost small scale lending operations. (See Table XIX).

The brokers in the informal market have a limited span of lenders and borrowers. The largest surveyed in Kanpur and Amritsar dealt with 15-30 firms each, on both the lending and borrowing side. The Shikarpuri brokers in Bombay deal with clientele that changes but may be no larger at any given time. Shikarpuri market borrowers are usually expected to deal with only one broker, but lenders may deal with many and thus they constitute the market. Indigenous style bankers rarely have more than 200 clients in a single branch.

By contrast, commercial banks deal with larger and more rapidly changing clienteles—and clienteles who are far more varied in terms of the markets in which they deal. While this gives them a flexibility in adjusting to market fluctuations they lose in the detailed knowledge of their clients, and thus have increased "information" costs.

Transactions Costs II: Bad Debts and Reserves

Beside administrative costs a major transaction cost is typically occasioned by bad debts. See Table XIX Bad debt figures, as reported, are particularly questionable because of the obvious opportunities to use non-paid bills to "whiten" otherwise unaccounted money. The five to ten percent of profits reported as bad debt may thus be an underestimate, since it is understood that income tax authorities will rarely allow more.

1/ One Bombay Shikarpuri found that 10% of his profits are accounted for by arrearage, of which half is eventually recovered. This Shikarpuri found that he went into court twice during the previous year to secure payment on his credits. A Madras Shikarpuri reported that 5% of his profits went to cover bad debts. This 5% seems to be the big city norm, though small town Shikarpuris report as high as 7-10% of profits accounted for by bad debts.
One Kanpur broker has about one failure a year among his 20-30 clients (meaning an arrearage not a loss), another two. A Rastogi banker in Kanpur reports bad debts equal to 10-15% of profits—though he could not tell how much was on commercial accounts. The figure was echoed by other Rastogi bankers.
Informal intermediaries avoid legal proceedings. They find them too costly and the resulting judgments often hard to collect. For some, the fact that non-prosecuted bad debts can be marked as paid and used to "whiten", legalize, "black" money on which income tax has not been paid, is also an incentive not to pursue debts through the courts. In any case, bad debts are usually compromised or re-scheduled.

Whatever the precise figures, it is clear bad debts are few and relatively easy to allow for. In fact, they are roughly comparable or slightly higher than those reported for small enterprise lending by the commercial banks, but the commercial banks are widely granted to seriously understate their losses on these small enterprise loans.

One cost advantage of the informal agencies is their exemption from the large idle reserve requirements imposed on the organized sector—over 30% of total deposits. The larger proportion of their own capital they use, however, achieves a somewhat similar anti-inflationary effect to compulsory reserves (deposits in the Reserve Bank and holdings of low interest government securities). Few of the Gujerati firms surveyed in Anand and Bombay had as high a deposit-capital ratio as ten or twelve to one. Three to one and two to one were more common, and many firms used little outside money.

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1/ One large Gujerati banker kept 12.5% of his money as reserves—2.5% in cash and 5% each in a bank fixed deposit (against which a large overdraft could be taken) and with other indigenous bankers. He never loaned out more than 80% of his funds in peak periods. Two large Bombay Gujerati bankers keep 10% of their resources in cash and 20% in fixed deposit. The Anand indigenous bankers had 5-15% of their resources in readily cashable form and that seems a norm for small towns—Bombay bankers kept up to 30% because they did a considerable business cashing and discounting for cash hundis, checks and other commercial instruments.
Modus Operandi

The borrowers in the informal market are "known" parties--under continuous surveillance in the closely packed lanes of the urban wholesale markets. Each bale of cloth that comes in and out is observed by neighbors, the finance brokers among them; an expensive night on the town is reported and judged the next morning in market gossip. In contrast to the relatively anonymous world of Western businessmen, even in the larger metropolitan centers, Indian businessmen live their lives in a narrow social ambit. Most of the brokers interviewed seemed incredulous that they would have to ask formal questions of borrowers in whose shops they visited each day, and with whose business confreres they were in continual contact. Still, one Shikarpuri in Bombay said he asked to see income tax returns in about 10 percent of his transactions and one in Madras indicated that he, too, occasionally asked for income and wealth tax forms. These requirements are common, and some Shikarpuris in Bombay and Salem will only lend to income tax assessees. But the Shikarpuris deal with a more diffuse clientele than the typical informal market lender--a fact reflected as well in their higher than average interest rates.

In fact, the people in the market not only have a twenty-four hour relationship--they typically have one that extends over generations. I asked one broker how he evaluated "new borrowers"--he answered that he never took them. By this he meant to say, that all his clients were children and grandchildren of businessmen with whom he and his father and grandfather had done business.

Informal financial agencies, by and large, concern themselves with the overall credit standing of the borrowing "party"--rather than the specific enterprise or project for which credit is taken. They, thus, do not do any
close check of the specific use of their funds—but are generally content with monitoring the party’s total activity. In bankers’ jargon, they lend on "cash flow," rather than "asset protection basis".

The brokers in the informal market watch closely the level of business activity not only in their borrower’s main establishment but in any others he may have. They watch his personal expenditure. They talk with his competitors and especially his employees. They then judge what sort of margin he is operating on and how likely he is to pay them. Most especially they watch his payments record to see if he may be faltering on any of his market obligations.

Criteria for Credit

It was somewhat difficult to get informal market lenders and brokers to specify their criteria for lending. They resisted mightily being forced into any of bankers’ language or using most of their ratios. The key elements were clearly the overall prosperity, wealth, and cash position of the borrower and an evaluation of his commercial integrity. Most important seemed to be a reputation for punctiliousness in meeting debts. As one elderly cloth market finance broker answered my questions about criteria—“Payment! Payment! Payment!” In reverse, borrowers, potential and actual, felt that they had to have a reputation for the prompt meeting of market dues.

One explicit criteria for lending which seemed common was some target relationship between total borrowings and net worth. Two Shikarpuris (one each in Bombay and Madras) and the private banker in Kanpur mentioned 25% of net worth as their normal limit. A third Shikarpuri in Bombay set 33%—though he clearly had a relatively adventurous financing posture. In Amritsar, there seemed to be an informal one-third rule—one-third from banks,
one-third from the market, one-third from own capital in financing at least larger borrowers. On the other hand, an informant who audits the books of larger trading firms in Calcutta says most of them try to limit their own equity to 25% of gross employed—but much of the rest must be trade as distinguished from financial credit. The Gujerati firms in particular seemed reluctant to commit themselves to any net worth figure—perhaps because their concern is more focussed on the cash and stock position of their clientele than their net worth.

In general, urban informal intermediaries try to avoid coming under the restrictive money lending acts and do not lend in amounts less than 3,000 Rs. or to agriculturists precisely for that reason. They usually provide working capital accommodation to prosperous enterprises in well known markets. Their major risk is either of a wave which sweeps under all the firms in their market or of the male fide non-payment of their dues. They reduce risks of the latter sort by lending only to those with strong roots in the community. One is reminded of the success of recent bail reforms in the United States in substituting release on personal trust of those criminal accused with community roots—for a requirement that such accused post high money bail. As one indigenous banker said to me—"I guess they could run away, but where would they go? They would have to do business with their friends and relations and I would find them."

Many lenders also have informal limits on their maximum lending to any one party. Shikarpuris usually limit their exposure to one party to 10-25,000 Rs. Two of the larger non-Shikarpuri firms surveyed—one a Gujerati indigenous banker the other an Amritsar broker had a single debtor with a
limit of 1,500,000 at one time or another recently—representing in one case 5% of net lending. 1/ Except for the Shikarpuris, most lenders and brokers were too specialized in one or another commodity market to limit their exposure in it.

Third party guarantees are often required especially by Gujarati Shroffs, but rarely by Shikarpuris except when a limited liability company is involved. On the other hand, the standardized Shikarpuri bill does require two co-signers.

Several lenders expressed particular skepticism about borrowers who were too well off or had access to low cost credit markets (such as Joint Stock companies who could advertise for deposits). It was felt they were up to no good if they came into more costly informal markets.

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1/ One Gujarati indigenous banker arranged 10,000,000 Rs. of finance for a contractor in Bombay, recently.
Table XX: Destination of Informal Credit Market Funds in Percentage of Loans Outstanding (Aiyar)

<table>
<thead>
<tr>
<th>Source</th>
<th>Trade</th>
<th>Exports</th>
<th>Small Scale Industry</th>
<th>Large Scale Industry</th>
<th>Others</th>
</tr>
</thead>
<tbody>
<tr>
<td>Multani bankers</td>
<td>32</td>
<td>20</td>
<td>16</td>
<td>7</td>
<td>25</td>
</tr>
<tr>
<td>Gujerati bankers (pure, in Bombay)</td>
<td>60</td>
<td>10</td>
<td>5</td>
<td>10</td>
<td>15</td>
</tr>
<tr>
<td>Chettiar bankers (in Tamil Nadu)</td>
<td>45</td>
<td>10</td>
<td>5</td>
<td>10</td>
<td>70</td>
</tr>
<tr>
<td>Rastogi in Uttar Pradesh</td>
<td>55</td>
<td>12</td>
<td>--</td>
<td>--</td>
<td>23</td>
</tr>
<tr>
<td>Chettiar pawnbrokers in Tamil Nadu</td>
<td>22</td>
<td>--</td>
<td>5</td>
<td>--</td>
<td>73</td>
</tr>
<tr>
<td>Finance companies in Trichy and Karur</td>
<td>40</td>
<td>--</td>
<td>8</td>
<td>--</td>
<td>52</td>
</tr>
</tbody>
</table>

In December 1976, according to the Statistical Tables Relating to Banks in India, RBI, Bombay, 1976, Graph 7 and 10, 27% of commercial bank advances were to trade 7-8% to exporters, roughly 10% to small scale industry, 44% to large scale industry and 19% to other commercial borrowers.

The bulk of informal lending goes to finance trade and industry, mostly the former (See Table XX), "Badla" financing of stock market speculation is a large and important exception which flows through specialized channels. Essentially it involves short term lending at rates about 14% plus 1.2-2.4% brokerage on the security of shares and with no margin requirement.
Gujerati credit goes almost entirely to funding trade, especially wholesale trade in agriculture and craftwork commodities. The Shikarpuris loan to a wide variety of small, and occasionally large enterprises—as do the finance "companies". Rastogis and Chettiars finance smaller traders and artisans.

The credit provided by brokers in wholesale markets for cloth and grain is obviously solely trade credit. Brokers providing money to industrial firms in the form of deposits, call money, or promissory notes obviously serve industry. Special demands on the informal market come from exporters who need quick money, and builders and restaurateurs who have no physical security to give. Certain industries—tanneries in Madras, "zari" cloth (indigenous style cigarette) manufacturers in Surat and "biri"/tobacco merchants in Anand have needs which banks are unable to meet.

The report of the 1972 Banking Commission noted that informal finance was particularly important in chemicals and dyes. But that is the kind of fact which increased bank credit for small scale industry should have affected. Madras Shikarpuri bankers themselves mentioned building, leather tanneries, cashew nut and government and forest contractors (who log areas in national forests), hotel and restaurant owners, "biri" (indigenous style) tobacco merchants and sea-food exporters as especially numerous among their clientele. Engineering, chemicals and pharmaceuticals were mentioned (as fields in which he did a lot of lending) by one Bombay Shikarpuri. The grain and cloth traders, and powerloom owners seemed to have their own informal credit markets everywhere. The Gujerati indigenous bankers in Anand were especially involved in "biri" (indigenous style cigarette) tobacco finance,
and those in Ahmedabad and Surat in financing textile manufacture and trade. Rastogis finance traders and to some extent artisans. Chettiars financed traders except in Coimbatore where they primarily finance small scale industries. The finance companies do a lot in hire purchase finance of commercial vehicles and consumer durables in larger cities and cash crop trade finance in smaller places.

None of the groups we study now do much finance of agriculture—even those like the Chettiars and Rastogis who formerly did so—because restrictive legislation makes it unprofitable. Less than 5% of indigenous bank finance now goes to agriculture.

Speculative activities and even high risk ones are eschewed by normal operators in the legal informal credit market. Film finance, a high risk proposition, is normally done by a separate set of financiers—and in any case is mostly in "black money", on which income tax has not been paid. It is estimated that of 7,500 million Rs. involved in film finance, 5,000 is such "black money". There are more than 500 brokers involved in arranging film finance. They lend money at rates ranging from 36 to 60% but occasionally as high as 120%.
Informal money is, in fact, generally only available for working capital purposes, precisely because new ventures are seen as too risky. To accommodate demands for credit in risky fields—speculation and the cinema, and the needs for illegal "black" money—there exist two parallel sets of informal financial institutions—the former (high risk ones) taking much higher interest and the latter ("black" ones) taking lower interest than the legal, normal, informal market. In Bombay alone there are a number of firms which discount fictitious hundis (with an estimated annual flow of 4500 million Rs.) and provide fictitious book entries (havalas) at a rate of 2% a month. These firms enable businessmen to move a sum in and out of their white books at will. Direct lending of black money is usually done at rates of 12-15% in Bombay (24% in Madras)—with all kinds of coded receipts given in exchange. At least 200 remittance facilities for unaccounted black money at a rate of 1-1/2% exist in Bombay. A set of overlapping firms can perform the same functions for illegal foreign exchange. (Aiyar).

Though there are points where these two parallel markets overlap the normal legal market we surveyed—this report is concerned only with that legal market.

In the urban markets surveyed, observers estimated and cross-checks confirmed that perhaps 50% of the working capital employed in the wholesale cloth trade in Calcutta and 20% of the working capital in the grain trade came from the informal market. The percentages in Kanpur and Amritsar cloth market were probably lower. These are markets in which little if any bank finance is available. Small industrial units in the Amritsar powerloom industry got 5-10% of their capital in peak season from the informal market.
The Anand tobacco trade receives 15-30% of its working capital as advances from Gujerati indigenous bankers. Calcutta pharmaceutical firms were dependent for 25-30% of their working capital on public deposits.

Earlier, in a survey for the 1972 Banking Commission, it was noted that indigenous bankers provided 1/12 to 1/2 of all credit provided different sizes of industrial units. The amount advanced ranged from an average of 300 Rs. or 20% of borrowings for units of under Rs. 25,000 capitalization and increases to 35,000 Rs. or 7% of capitalization for those with over Rs. 750,000 capitalization. Much of the smaller units "borrowings" must represent trade credit.

A recent RBI study (of firms with bank credit) shows that 28% of using firms with bank credit report / non-institutional finance—and the Shikarpuri bankers report that almost every sizeable firm in Bombay comes into their market at one time or another. According to the returns to the RBI Census of Public Limited Companies, 1971-72, 56% of the debt of small companies (or 220 million Rs.) and 27% of large company debt came from "unofficial" sources.¹/

As a general pattern, much of trade on a routine basis including exports and many industrial firms on a sporadic basis go into the informal market—for flexibility and accommodation they cannot get from the commercial banks, in financing their working capital. Usually they treat the informal market as a residual—for working capital needs the banks cannot accommodate.

¹/ EPW XV, 10, March 8, 1980, p. 490.
The typical borrower in informal markets has well over 100,000 Rs. in assets but does not belong to the big business category.\(^1\)

While it is clear that the bulk of informal finance is provided directly to trading enterprises and very little is provided directly to very small units (under Rs. 100,000 capitalization). It is an error to assume that the borrowers are the ultimate beneficiaries, of the credit. The working capital needs that are financed are typically for advances to trading partners and manufacturers, large and small—who demand cash payment. The advances fund as well as the 30-90 day credit on which the smaller retail shops subsist. India's largest category of small enterprise—handlooms—are funded by master weavers who may in turn borrow on local informal markets. And the pattern is repeated for shoemakers and other smaller artisan units. Thus, indirectly the entire economy is dependent on informal sector advances.

**Advantages — And Why the Borrower Chooses**

At times, the advantage of the informal financial sector for the borrower is the rapidity with which it can provide money, or the cheapness of the money provided, though neither of these is the norm.

\(^1\) Of those lenders we studied who would give estimates, one broker in the Kanpur cloth market guessed his average client was worth from 500,000 to 1,000,000 Rs. Another Kanpur financier and an Amritsar broker said their mean client was worth 2,000,000 Rs. One of the Anand indigenous bankers said that his minimum advance was 25,000 Rs. (his maximum was 1,000,000), others would loan as little as 5,000 and one had some 100 Rs. clients, presumably small shopkeepers. Bombay Gujerati Shroffs said their modal credit was 50-100,000 Rs. Among industrial firms, the smallest capital normally encountered among borrowers in the informal market were about 100,000. One Shikarpuri banker said that his modal debtor was worth 800,000 to 1,000,000 Rs. The modal credit in the Madras Shikarpuri market is perhaps 100,000 Rs. and rising—though the amounts go up to 1.5 million Rs.
Generally, informal money is slower to arrange and more expensive for the borrower than money from the organized sector. In several markets it is even quoted in terms of a 1-3% premium on bank rates. The exceptions to this slowness and expensiveness are found especially in the larger metropolitan markets--where indigenous bankers and commercial financiers provide money far more quickly than the banks, and brokers in markets like the cloth market or the inter-corporate call money market provide finance more cheaply than the banks.

The informal money market has some other advantages from the point of view of the borrower. Informal lending is almost all unsecured. Many borrowers do not have or want to tie-up stocks as collateral. Restaurant owners and construction contractors often have to borrow on the informal market because their business does not generate acceptable collateral. Even where collateral is available the restrictions on the collateral and the procedures for checking it often prove onerous. Indian bank credit to S[e] is almost always secured--and the procedures for checking and conserving the collateral often appreciably increase the cost of the loan. On the other hand, there are forms of secured lending on the informal market--firms that buy up Bombay textile market accounts receivable fall in this category; I can also point to the "financier" I came across in Amritsar (one of a number) who did roughly the same thing but this time as an accommodation to the purchaser, rather than the mill. In other cases, guarantees were demanded.

Informal finance is generally provided without having to fill up forms, or spend much time in the intermediary's office--and is not tied-in to all sorts of formal requirements like compliance with municipal land
use regulations. In these respects, its costs to the borrower is not higher than face interest cost—in contrast to most "organized" bank lending. Small businessmen complain that they are foreclosed from loans for lack of official clearances, for example, by land use authorities. But even if eligible, they may have to spend endless hours in offices waiting for their paperwork to be processed. Again, especially in SSE where entrepreneurial time is often the scarcest resource, this waiting and time has a very high cost. In fact, in many informal credit markets the broker visits the client's place of business and does all the preparatory work for the loan as part of his service. That is, the broker does what the borrower has to do when dealing with a bank.

On the other hand, there are some negative aspects to informal sector lending from the borrowers point of view. Much informal credit is "call" money and in any case may have to be paid on some precise due date, whereas "bank" credit is seen as more flexible and easier to delay payment on. There is also a feeling that informal credit is less reputable than bank credit, and that informal market transactions are more likely to be challenged by the tax man.

Almost half the units surveyed even in markets in which informal finance is important, denied using it—often because they were either too rich or too poor to be accommodated. Some of them may simply have been reluctant to discuss the issue. On the other hand, over 90% of Kanpur and Amritsar cloth firms were reported to use some informal sector credit in the busy season.
Some Issues

1. Competition with the Banks

Despite their advantage in their lower transactions and reserve maintenance costs, many informal agencies are almost totally non-competitive with the "organized" banking sector in the giving of loans and only somewhat so in attracting deposits. There is certainly some diversion of deposits from the "organized" banking sectors—but most lenders/depositors in the informal market have higher earning possibilities than the bank interest rates available to them, if they are not tempted by the rates informal credit intermediaries offer them. This is not so much the case of those who are attracted to the elaborate savings schemes organized by some of the more aggressive finance companies—and it is in fact these schemes which have been widely copied by banks to mobilize deposits.

The informal agencies do evade some of the credit and monetary control measures which the banking system promotes. They provide an escape hatch from the losses in efficiency which too tightly controlled administrative allocation of credit might cause.

We have come across one case of the suppression of a market. Rastogi and Chettiar financiers once lent extensively to agriculturalists and now no longer do so. This is partly because of onerous reporting and other requirements under state moneylenders acts—and partly because of measures obstructing debt collection from agriculturalists, including partial and total moratoria. Though some displacement has taken place to illegal and alternative credit sources—many former borrowers are apparently sorely strapped for credit. There has been considerable distress selling of jewelry—that would formerly simply have been pawned—to get needed working funds.
2. **Money Creation**

Some of the agencies in the informal credit market create money by issuing sight drafts ("darshani hundis") or activating idle balances by brokering them. But most informal credit agencies do not create significant amounts of money in the normal sense. For each rupee they lend in one market, they borrow a rupee of active money from another market. The funds that these informal credit agencies use—in addition to a high proportion of own funds—are attracted from lenders by higher interest rates than are available elsewhere and occasionally by the assurance of access to credit in time of need and other services. The lenders often, but not always, are cash rich market traders. In several cases, they include a number of prosperous farmers—and even professional men (mentioned both in rural Gujerat and Amritsar). Thus, though the informal credit agencies include those who perform all of the banker's essential functions—its major function is as a channeler of credit from those with excess money to those who need it.

The Shikarpuri bankers are able to discount or borrow on the security of their own bills from some commercial banks—though the total amount has declined rapidly in recent years and is now a small fraction of their own lending. Other indigenous bankers of any size maintain considerable sums in term deposits and on current account with the commercial banks against which they do borrow—and many of their payments are made by check. To this extent they serve to support the commercial banks own money creation, but their relations with the banks are relatively distant, though largely complementary.
The one form of money creation of particular interest is the issuance of "darshani hundis"--sight drafts. These differ from checks in current Indian usage in that the person to whom they may be paid is usually far more constrained, at the same time that they are more transferable among the class of eligible payees. Darshani hundis can be cashed at any time of the day or night. Unlike Indian checks which rarely pass through more than one set of hands before deposit--darshani hundis are typically negotiated several times before ultimate encashment. Darshani hundis are also preferred because they often cost less and are cheaper to negotiate a settlement on if dishonored. But they are clearly a declining institution, and are largely used for remittance to areas which are not yet heavily banked. The Merchants Chamber of Commerce in Calcutta reports a sharp drop in the number of hundi cases it handles. The Hindustan Chamber in Bombay, reports the same.

But the volume of hundi transactions is still considerable. A study of 5 leading Bombay pure indigenous bankers (Gujerati) shows that their annual turnover of hundis was between 1500 million and 3600 million Rs. each. It is estimated that the total annual turnover in Gujerati hundis in Bombay is 16,000 million Rs. of which 10,000 million Rs. is accounted for by the 6 pure, non-commission agent, shroffs. Marwaris in Bombay are estimated to have a 5,000 million Rs. turnover in hundis. These or the other depending on are two way figures--though the flow is usually primarily in one direction/seasons. The bankers also discount bank checks and commercial bills, in an amount roughly equivalent to the hundis they handle. The rates charged are generally cheaper than the commercial banks--since the indigenous
bankers can remit the check or hundi back to the issuing area by cheap and rapid couriers (called "angaria") and redeem them for face value. The commission on hundi issue in Bombay is 7 to 15 Rs. for 100,000 Rs. face value. Marwari indigenous bankers also provide a large number of demand "darshani" hundis for remittance though Calcutta to traders throughout Assam and Eastern India—but there, too, despite the hundi's cheapness they report the increasing popularity of the bank check. The major advantage of bank checks is clearly their greater acceptability to income tax authorities as the records of a transaction. Other groups of indigenous bankers appear to have almost ceased using darshani hundis—except in connection with trade bills or what are called "bill-ti" hundis.

3. Segmentation

Over time there is a strong tendency for the different categories of lenders in the market to merge their forms and to some extent overlap in the markets they serve. The rigid community differentiation in which Gujeratis served only Gujeratis, and Shikarpuris worked only through Shikarpuris brokers (but never lent exclusively to Shikarpuris clienteles) breaks down. On the other hand, the market remains local—and rates differ systematically between different markets within the same town. All rates seem to move in some sense sympathetically with bank and organized sector interest rates—but the spread and particularly what seems higher rates and greater supply stringency in South India remains.

This market segmentation partially represents the cost of the advantage informal credit intermediaries have. They lend to a couple of hundred well known local parties and borrow usually from the same sort of constituency. The obligations are imperfectly subject to discount—though

\[1/\] See Lakshmi Narain, op. cit., p. 27.
discount is available to a greater extent among Gujerati and Marwari Shroffs which explains the somewhat greater uniformity of their rates. But the reasons for the lack of movement of funds among centers, particularly among the Multanis who have a national network is not clear.

The segmentation of the market means, of course, that money does not go to the most eligible use, and is relatively immobile among centers. Again, the Gujerati and Marwari networks which are especially concerned with financing long range trade are exceptions. Perhaps someone might argue that the relative allocation of funds in the first place to local market serving systems may reflect the overall relative returns in local and extra-local lending.

Further, the segmentation means that the risks of lenders are not spread and increases market risk—though for reasons dealt with earlier this seems less of an issue in the stable markets, informal credit markets serve.

One of the most difficult cases of segmentation to explain is that which has Shikarpuri bankers in Bombay charging almost double the rates that Gujeratis do. Now some of this difference connected with the greater risks: Gujeratis—and intramarket finance finances the accounts and stocks of established traders in what has traditionally been a sellers market. Much of Shikarpuri finance goes to finance export enterprise and construction which are inherently more risky. Further, the clients of the Gujerati Shroff are tied to him through a myriad of social channels—as fellow Gujerati traders; the Shikarpuris deal with a more mixed, cosmopolitan clientele. Nonetheless, the Shikarpuris bad debt experience at 10% (at
the highest) of profit (representing 1-2% of turnover) hardly justifies the difference in rates charged.

If the clientele in the Shikarpur market has remained constant and they can neither secure commercial bank accommodation nor gain admittance to other informal markets—while the relative amount of money in the market declines because of declining bank refinance, that might partially explain the higher rates. Perhaps over time, some adjustment will occur and the rates will move closer together.

Another facet of segmentation is the fact that South Indian markets are consistently so much tighter, at least higher interest rate, than North Indian ones. This is a difference noticeable in the organized sector as well—but rates are far higher in informal markets in the South.

Even more dramatic is the situation within the Gujerati Shroffs system, where funds are continuously remitted between branches and firms according to market needs. The reigning lending rates and borrowing rates are 1-1½% lower in Bombay than in the smaller Gujerati centers. Some of this does reflect arbitrage costs and the greater looseness of the Bombay markets, and some the larger average size of the Bombay clients which may increase their credit standing. Our data did not permit us to draw any conclusions about an interest differential between East and West India, to parallel that observed in the organized money market—but one could wager that one could be established.

4. Dynamic

The pattern of evolution of the informal markets seems to be driven by three factors —
1. The demands of the traditional trading groups in Gujerat and South India whom they have served for hundreds of years—and of whose trading system they are an essential ancillary.

2. The availability of surplus funds with some members of the investing public looking for higher yield returns.

3. The pressure of regulatory and repressive measures which affect the form and direction of credit—in particular, channeling it to activities and firms who cannot get lower interest bank credit.

This repression at the same time has interrupted the integration of markets that might have proceeded and was foreseen in the two Banking Commission Reports of 1929-31, and 1972—and thus increased the separation of informal and regulated markets—at the same time that there appears to be some integration of informal markets themselves as regards forms and personnel. Geographically, the markets remain largely segmented despite the presences of links and intermarket flows at least in the Multani and Gujerati case.

One of the hardest issues to determine in the case of the informal market is the extent to which its growth is a response to credit needs, and the extent to which it has an inherent institutional logic which may in fact form those credit needs. The empirical evidence available to us answers this question very ambiguously. On the one hand, many of the informal credit markets serve traditional markets (respond to their needs).
This applies as much to the Gujerati and Shikarpuri indigenous style bankers as to the market credit provided through brokers. Even the movements into more modern activities often simply represents the service of old clients who have entered new lines. In this sense the development seems demand-led. The rapid development of informal sources of credit to meet the demands cut off by bank selective credit controls--again shows a response to demand. On the other hand, the very dominance of certain communities in trade and industrial lines partially responds to their possession of access to an established informal credit system--a supply factor. And to that extent the existence of a credit supply enables, if it does not drive, the process of informal intermediation. In addition, at least in the case of the Shikarpuris and probably to some extent for the other traditional banking communities, their possession of excess funds searching for investment, the existence of supply, is what brought them into the banking business.

5. **Public Policy**

The history of the public policy involvement with the indigenous market has two aspects. One is sporadic efforts to regulate the market directly by trying to label some of the agents in it as "money-lenders" and controlling their rates and recourse for collection. The results of these efforts are embodied in the various Moneylenders' acts, which have been passed from time to time by Provincial and later State governments. The other aspect is an attempt to link at least indigenous bankers and perhaps shroffs as well to the formal market, subjecting them to RBI control and using their abilities to get funds to productive sectors in the economy. In a number of cases, in reverse, indigenous style bankers have reincorporated themselves as modern commercial banks.
As the Banking Committee of 1971 said, "Such Indigenous Bankers as are engaged in banking proper or are prepared to shed their business other than banking should be eligible to be placed on the approved list of the Reserve Bank in the same manner as joint stock banks." 1/

The policy concerns have led to some research and policy interest in the informal credit area. The classic study is still L.C. Jain's, Indigenous Banking in India (1929), (but a longer list is appended to this study). The two Banking Commissions (1929-30 and 1972) both studied the "indigenous" market in some detail, spoke highly of its merits and recommended a "linkage" scheme—in 1930 directly with the RBI, in 1972 through the commercial banks. On the ground, the RBI and the indigenous bankers found themselves unable to agree on a level of control that would be appropriate to such a link and the issue may be considered dead.

The RBI did have, from 1941 to 1975, a concessional remittance facility for those indigenous bankers who conformed to its standards, which put them on a par with the non-scheduled banks. This facility was withdrawn because it was not sufficiently used—though the organized indigenous bankers made some effort to have it reinstated. 2/

Since it contains the most recent public consideration perhaps a review of the 1971 Banking Commission's report is particularly in order. The Commission concluded:

1/ The Indian Central Banking Enquiry Committee, 1931, Calcutta 1931, p.499.
2/ Proceedings of the 4th All-India Shroffs Conference, October 9, 1976.
The indigenous bankers continue to play an important role in the Indian financial system, in that they look after the credit needs of numerous small industrialists and retail traders. (p. 99).

The key recommendations of the 1971 Banking Commission's Study Group on indigenous banking were for a licensing of indigenous bankers with a requirement that they submit "a summary statement of the volume and nature of business", maintain "books of account in the usual recognized manner" and have them certified by outside auditors—plus observing some constraints on overlending, (pp. 102-108). In return, the RBI would refinance commercial bank lending to indigenous bankers who would in turn charge reasonable rates, (pp. 103-104). Some licensing of financial brokers in the informal market is also recommended, (p. 109).

For the future, the Study Group saw a possibility for the indigenous bankers to evolve in the direction of private bankers in Europe, merchant bankers in the U.K., and commercial finance companies in the U.S., or broker commercial bills and function like London discount and acceptance houses.

After the Study Groups' report was largely endorsed by the whole Banking Commission—some efforts were made to carry out these recommendations. But the Banking Commission introduced several qualifications in its endorsement—which "toned-down" its effect and efforts to effect the recommendation floundered on the issue of the precise controls to be implemented and have largely been dropped—and the community of indigenous bankers have limited themselves to fending off specific regulatory inroads on their business.
Meanwhile, the one segment of the informal credit market which was linked to and supervised by the commercial banks has been declining. Despite a positive recommendation in the 1972 Banking Commission Report, the 1200 or so Shikarpuri or "Multani" bankers, have seen their links with the banking system become progressively more tenuous. With bank funds running dry, demand push has driven up their rates by 100%, but they remain an important lender for small and medium-scale enterprises in Bombay and South India. Of course, bank rates have increased almost as rapidly over the period— but the point is that the gap has widened.

It is clear that sections of the informal financial market are in decline as the organized sector expands its activities. Bias by income tax officers, moneylending acts, bank credit officers, and the expanding credit from the banks all take their toll. Darshani bundis—indigenous sight bills—are less and less used. Kanpur private bankers no longer take deposits. Shikarpuri bankers get 10% of the bank accommodation they used to; their numbers and assets in Bombay are static in the face of an inflationary expanding economy. Call money has vanished from the Amritsar market. In several cases the sons of indigenous bankers were engineers in America or had founded their own factories; in two other cases they were a restaurateur in Bombay and a tennis pro in suburban New York. In remarkably few cases were they working in their father's firm.

There is now a proposed law to limit radically the taking of deposits or of unsecured loans by non-banks. The immediate result would be to end the entire indigenous style banking category, the similar Finance

Companies, and corporate deposits. Brokered lending would be limited in scope. The results would include the wiping out of the bulk of the 20-30% of the present credit in the urban areas provided by informal agencies. Much of the money would undoubtedly then flow to the banks—though there should be significant leakage and the sectors now receiving finance are unlikely to receive the same amount from the banks. The result would be a considerable decrease in and reallocation of the working capital funds in the economy.

On the other hand, the Gujerati indigenous bankers operating in some sense competitively with the "organized" banking sector have been expanding their operations at a par with the rest of the economy. Inter- and intra-market money continues to be available to traders and at rates that compare favorably with the banks.

There should be no difficulty with the apparent contradictions. Activities like trade in cloth, grain, and "biri" are essential and related in a relatively automatic way to the overall growth of the economy. The "organized" banking sector's rejection of them has preserved a growing role for indigenous informal agents in serving them. The "organized" banking sector will not for the foreseeable future be able to fill all the pressing if not "priority" needs of the Indian economy—and an informal market will necessarily exist to do so. The excessive contraction of the informal financial markets would lead to a rigidity in the economy whose costs will be apparent in reduced economic activity, higher overheads, and lessened efficiency.
Summary

In summary, legal informal financial markets exist and provide perhaps up to 30% of all working capital in Indian urban markets (50% if such items as interest bearing corporate deposits by private investors are included). They finance half of wholesale trade in certain commodities and 10-30% of the capital needs of small scale producers like powerloom owners and pharmaceutical manufacturers. Despite the rapidly increasing bank credit for small scale industrial units, most of these units find it necessary to go into the informal market, at least during their busy season. The rates in this informal market are generally 2-4% higher than the bank lending rates—but there is enormous variance in rates, and forms of lending. Very small enterprises when served by these markets directly may pay nominal rates as much as 10% higher than normal bank rates—but they normally are financed through trade credit refinanced with the informal market and increasingly by discount facilities. In Southern Gujerat, a parallel system of indigenous-style bankers successfully serves much of the urban economy. Elsewhere informal markets are conducted by commercial financiers like the Shikarpuris, brokers, and discounters of commercial paper.

This informal market is used because it provides funds for purposes like trade which the banks do not finance, more rapidly than the banks for those who require speed like exporters, and without security for those including restaurants and contractors for whom security is a big stumbling block.

The operating margins—the transaction costs and bad debt experi-

ience of these markets is, by and large, superior to the banks and, as was indicated, their normal lending rates are 2-8% higher.

The Shikarpuri bankers of Bombay and South India might be presumed to be an exception since their margins and rates are higher than the banks by a considerable margin, but some of this is due to the limited funds in their market due to the banks cutting them off since 1970 and the resulting pressures of demand. As well one might consider that their borrowers represent relatively high risks, and perhaps increasingly so as banks accommodate their safer clients.¹/

¹/ Letter from Professor J.C. Sandesara, October 9, 1979.
CONCLUSIONS

The "Capital market...does get progressively integrated, widened and deepened with economic and financial evolution. The crucial variable in this context seems to be transactions costs (both administrative costs and default risk). Financial innovations reduce these costs and thus lower the costs of lending and borrowing (not completely represented by the interest rate) and narrow the interest rate differentials."


The above represents a schematic description of financial development as an ancillary and prerequisite of overall economic development. Roe and Bhatt deal in another part of the same working paper with the relations of Informal Credit Market to these developments (pp. 78-82).

They posit three characteristics of these markets:

(1) Lower transactions costs because of well-known clienteles entailing low information costs;

(2) Avoidance of controls on lending and borrowing rates;

(3) Avoidance of tax--in the forms of idle reserves or reserves in the form of low interest government obligations.

It is the absence of these three characteristics which often lead to a sub-optimal level of intermediation in the Organized Credit Market. To the extent that the Informal Credit Market has these characteristics, it increases the volume of intermediation--and in particular, distributes credit to the traditional sectors of the economy. The overall level of intermediation is higher and more economic activity is funded, particularly in traditional sectors.
But ICMs are typically highly localized and segmented and do not necessarily distribute funds to the best users from an overall point of view. The small markets may permit an undue amount of monopoly power to lenders and intermediaries. And society may wish to use credit channeling to favor sectors with low financial but high social returns.

Indian ICMs do have relatively low transactions costs, particularly for small loans—and their rates reflect relatively low monopoly power and relative integration—though both are certainly present in some submarkets. Indian ICMs certainly do serve traditional and other sectors who would otherwise be unserved. The volume of intermediation is certainly higher than it would be without the ICM (because of its higher lenders' rates) and the allocation of credit different. The existence of large informal markets has not kept the commercial banking system from rapidly expanding.

There is clearly a dynamic reduction in segmentation in Indian ICMs over time as traditional groups merge and overlap in their clientele and modus operandi. It is still the case, however, that rates differ systematically among markets—particularly contrast the difference in Shikarpuri and Gujerati lending rates in Bombay—and the systematic differences between capital scarce South India and better endowed North India.

In some more recent work, Bhatt proposes an alternative model in which credit is conceived of as a non-homogenous good and in which different credit markets specialize in different credit instruments which serve different needs. Informal credit markets often provide instruments that are non-competitive or complimentary to the instruments provided in formal markets, and whose terms and conditions are largely independent of those in the formal markets, as well as instruments which are competitive with those provided in formal markets. The differences in behavior between these two
different types of market (competitive and non-competitive) are marked, as was seen in the case of Korea.

This would help explain the rising rates in the Shikarpuri market. One would expect the growing separation of the formal and Shikarpuri market to be reflected in the deviation of their rates. The lower rates in the Gujerati and intra-market credit markets, on the other hand, would reflect the lesser deviations from the formal market rates required by the fact that these markets are competitive with the formal market.

Dynamically as the banks have expanded in the years since Bank Nationalization in 1969 and legal restrictions on the ICM have tightened—some segments and activities of the ICM have declined—but others have expanded to serve needs the Banks now refuse to serve. This reflects the dominant demand push aspect of the Indian ICMs. In fact, in many of these demand led markets, the needs for funds are so high that rates can go up drastically. In the Shikarpuri market, the cut in the amount of bank funds available for relending has contributed to a considerable hike in lending rates. (Unless we presume that the bankers increased their rates, in the face of existing slack, to achieve a constant income on the basis of a reduced volume). In the South Indian agricultural markets where debt payments moratoria have caused a decline in informal lending—large scale asset sales by impoverished agriculturists have occurred.

On the other hand, Rastogi and Chettiar funds, no longer employable in their traditional fields have poured into hire purchase and commercial financing. Gujerati bankers have ventured into those fields which their long-time clientele have moved into. In these supply led cases, the direction and volume of lending in different markets have been affected by government regulation, and other outside causes.
APPENDIX I

COPIES OF SELECTED INSTRUMENTS

FOR INFORMAL CREDIT
Rs. .................................................. 197 •

Received from M/s. .......................................................... Bankers the sum of Rupees

through .......................................................... on .................................................. being the amount
of .......................................................... Hundies Promote/executed by .............................. in your favour this day payable .................................................. days after
this date without grace days.

In case of non-payment of the above Hundies by you are liberty to sue at your Office or
Head Office at your discretion and we agree to submit to that jurisdiction & will raise no dispute to pay over due interest at .................................................. per month. We agree to repay the amount in equal Monthly instalments of Rs. .................................................. commencing from

Particular of charges paid

Interest Paid by me/us as under

Rs. .................................................. percent per month

Interest

Hundi's Stamp

Charity

Total Rs .................................................. Cash

Verified as correct and the relative hundies are signed by Authorised person of the party before me.

Signature of Broker ..............................

MADRAS HUNDI FORM (SHIKARPURI)
To

Dear Sirs,

We hereby declare as under:

1. Name of the party

2. Nature of Business

3. How long established and branches if any

4. Value of the property held whether encumbered

5. Capital invested in business and any other asset

6. Name of the Drawer's Banker and if aided

7. Total Borrowing at present Hundi Pronote

8. Total worth of the party

9. Whether assessed to Wealth tax Income Tax & Sale Tax

10. If we further declare that the party is not borrowing money on kant or tundal basis etc.,

11. There is no guarantee or security given to any other person in respect of this party nor this party has given guarantee or joint signature in respect of any other party.

Prop.

Name of Partners

Directors

Phone No.

Broker's Signature
DILL OF EXCHANGE

Due date
Bombay, dated,

At (90) Ninety days after date without days of grace pay at Bombay to M/s
or order the sum of Rupees

( ) for value received this day.

To,
For A.B.C. & Sons

Name of Acceptor
Signature

Address of Acceptor
Partner

Address:

Notice of dishonour waived
Signature of drawer.

BOMBAY SHIKARPURI OR MULTANI HUNDI
PROMISSORY NOTE

Rs. __________

Miti ————

Date ————

ON DEMAND, I/We ————

Date ————

Carringon Business at ————

Jointly and severally promise to pay to ———— or order at his above address ————

the sum of Rupees ————

for value received by cheque No ———— dated ————

drawn on ———— for Trade Purposes ————

with interest there on at the rate of ———— percent per

mensum from this date till the date of repayment in full

LOAN TAKEN FOR BUSINESS.

Amritsar Promissory Note, to be endorsed on back.
Calcutta Hundi form -- used by leading Marwari firm.

Hari Prasad Prayag Narain
161/1, Mahatma Gandhi Road, Calcutta-7

Note---Hundi keval 3 din tak hi baadhi rohenge. 
"Uparok Nang koi Hundi sikhara na bundur hain."

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Calcutta Hundi form -- used by leading Marwari firm.
Gujerati Hundi form -- issued in checkbook like books.
PROMISSORY NOTE

Rs._________  Mit___________

Date______

ON DEMAND, I/we__________________________
jointly and severally promise to pay to__________________________
or order at his above address
the sum of Rupees__________________________
for value received by cash/cheque No.__________________________ dated___________
drawn on__________________________
with interest thereon at the rate of__________________________ percent per
mensum from this date till the date of repayment in full.

LOAN TAKEN FOR BUSINESS

AMRITSAR PROMISSORY NOTE
RECEIPT

Rs._________  Mth _________

Date _________  

I/We _________  _______  _______  _______

confirm having received from  

___________  _______  _______  _______  _______

the sum of Rupees _________  _________  _________

___________  _______  _______  _______

by Cheque No. _________  dated _________  _______

on _________  _______  _______  _______

with interest thereon at the rate of _________ percent per mensum from this date till the date of repayment in full against which we have this day executed a Pronote on Demand in his/their favour.

AMRITSAR PROMISSORY NOTE RECEIPT.