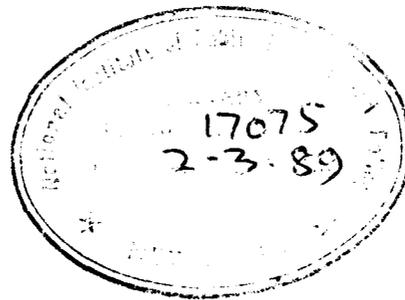


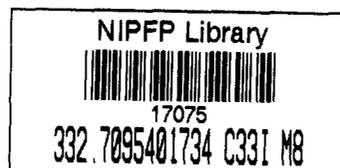


The Informal Credit Markets in Rural India



CENTRE FOR DEVELOPMENT STUDIES
Trivandrum

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P R E F A C E

The Asian Development Bank had commissioned a comparative study of Informal Credit Markets in a few selected countries in Asia. The country study on India was jointly undertaken by the National Institute of Public Finance and Policy (New Delhi), and the Centre for Development Studies (Trivandrum). The former took up the study of the urban informal credit markets, and we, at this Centre, covered the rural sector. The present volume incorporates the findings of our investigation of the informal credit markets in rural India.

The over all coordination of the work on the project was entrusted to a study team comprising Professors T.N. Krishnan, I.S. Gulati, P.G.K. Panikar (Principal Coordinator), Chiranjib Sen and Mr. D. Narayana. Drafting of the report was done by the following : P.G.K. Panikar (Chapters 1, 2, 4, 5, 6, 8, 9 and 10), Chiranjib Sen (Chapter 3 and 7) and D. Narayana (Appendix to Chapter 2).

We take this opportunity to express our thanks to the ADB for sponsoring this study and liberal financial assistance. We also wish to express our appreciation of the spirit of cooperation and understanding on the part of the NIPFP. The unrelenting and hard work of the project staff, especially of Messers Jayaraj, Jose Jacob and Namboodiri are appreciated. The support and assistance from our colleagues at the Centre, the members of the library and administrative staff in particular are gratefully acknowledged. Special mention may be made of Mrs. Girija who attended to the demanding job of typing the draft of the report.

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CHAPTER 1

INTRODUCTION

1.1 The Context

The informal credit markets (ICMs) have been dominating the credit transactions in the developing countries, especially in their rural areas. At the beginning of the fifties, the informal credit agencies, professional and non-professional moneylenders, accounted for over 90 percent of the total debt outstanding against all rural households in India. It is true that since then the volume of credit from the formal sector - government, cooperatives and commercial banks - has multiplied several fold, thereby reducing the share of the informal sector. However, thanks to a high degree of inequity in the distribution of credit from the formal sector, large sections of the rural households continue to lean heavily on the informal credit agencies. Easy access, minimum procedural formalities, prompt disbursement, flexibility in the terms and conditions like security and repayment, personalised nature of credit transactions, etc. are some of the reasons cited by the rural households for approaching the local informal credit agencies. On the other hand, the cost of such credit is widely acknowledged to be unduly high: high rate of interest, often leading to debt bondage or forfeiture of collaterals, and other forms of exploitation where credit is linked with other transactions. Given the crucial role of credit in agricultural transformation and rural economic growth, and the continued

dependence of a large proportion of rural households on the informal credit agencies, despite the entry of formal credit institutions into rural areas and introduction of several government sponsored rural credit programmes, an indepth study of the ICMs assumes added significance.

1.2 Objectives of the Study

Despite gigantic efforts in the collection of data on different dimensions of rural credit through several rounds of All India Debt and Investment Surveys conducted by the Reserve Bank of India, information on several aspects of the ICMs is not readily available. There are wide data gaps; nor have all available data been subjected to meaningful analysis with the relevant perspectives. As a result, some crucial aspects of the ICMs continue to remain in the dark. The objectives of the present study are; (i) To assess the share of the informal lenders in the total credit flows to rural households; (ii) to analyse the structure of the informal sector; (iii) to examine the level of interest rates, and the factors underlying its formulation and to decompose its components; (iv) to assess the role of ICMs in other areas than loan transactions such as domestic resource mobilisation, their allocation, equity impact, etc; and (v) to fill the data gaps on the salient features of the ICMs, gain sufficient insights into their strengths and weaknesses and, thereby, help in evolving a proper policy and legislative framework for redressing the imbalances in rural credit.

1.3 Scope of the Study

The ICMs have many dimensions such as size, composition, structure, segmentation, inter-linkage with other markets, viz., land, labour and

commodity markets, etc. The trends in size and structure of ICMs over time will have to be examined to assess the impact of the credit policies introduced in the recent period. The working of the ICMs, the terms and conditions involved like interest rates, purposes and duration of loans, security, etc. are aspects that need to be examined in depth. Apart from disbursing credit what other functions do they perform? Do they contribute to domestic resource mobilisation? Are the resources mobilised allocated to optimum productive uses? To what extent the ICMs have met credit needs of the low income, underprivileged, segments of the rural population, thereby improve equity? Are the terms and conditions imposed by the informal lenders exploitative? Is the interest rate usurious? What are the factors underlying the formation of these interest rates? These are some of the questions on which the present study will focus its attention.

1.4 Methodology

(i) Broadly speaking, any research effort should start from a look at the state of the art in the relevant field, the present frontier of knowledge. Accordingly, each part of this study is being set out against the background of received doctrines or a review of the literature.

(ii) The problems on our agenda, listed in the previous section, will be examined with the aid of both secondary and primary data. The results of the All India Rural Credit Survey (1951-52) and three successive rounds of All-India Debt and Investment Survey, throw a lot of light on

the size and structure of the ICMs, the size, purpose and duration of loans, nature of security, etc. These are collated, retabulated, and analysed keeping in mind the main perspectives of the present study.

(iii) There are major data gaps in the published results of the above surveys, and naturally so. For, they are large scale, countrywide surveys and as such cannot be expected to capture all the variables in credit transactions. Even if they were collected, they were not tabulated and included in their reports. Hence, we had to design some micro-studies in a few selected villages from the States of Kerala and Tamil Nadu.

(iv) An intensive survey of sample households was conducted. A set of household schedules covering their demographic characteristics, occupation, assets, sources and volume of credit, the purpose of loans, duration, security, interest rates, other terms and conditions, repayments, default rate, etc. were canvassed among the sample households.

(v) In addition, a sample of informal lenders such as agriculturist moneylenders, professional moneylenders and traders were identified and a set of schedules and questionnaires were canvassed among them. The information elicited included the types of borrowers, scale of transactions, security accepted, interest charged, sources of funds, default rate, etc. Case studies of a sample of chit funds (ROSCAS) in one of the selected villages sought to collect data on the rate of participation of the community in this activity, the volume of business, their modes of operation, the motives of the participants, their role as a source of credit vis-a-vis a channel of saving, etc.

The recent years witnessed a widespread collapse of finance companies, a new version of professional moneylenders, mass rallies of protests on the part of the customers who had lost their precious savings deposited with these agencies, and a strongly articulated demand for government intervention to regulate and control their activities. Against this background, we encountered considerable reluctance, if not resistance, on the part of moneylenders, traders, and foremen of chitties to respond to our queries.

In Chapter 2 we examine the past trends and present position of the size of the ICMs in India's rural areas. An analytical "model" relating size of ICMs and the explanatory variables is developed and various hypotheses tested using all available secondary data in Chapter 3. In Chapter 4, the main features of the six villages selected for micro-studies and the basic characteristics of the sample households are presented. Chapter 5 is devoted to an analysis of the structure of ICMs in the rural areas of the country as a whole, as well as that in the selected villages. In Chapter 6, we turn to the question of interest rate formation, the factors that govern interest rates and the components of the same. In the following chapter, chapter 7, all the relevant primary data are utilised to present a quantitative analysis of the factors determining interest rate. Next we proceed to critically examine the role of ICMs in savings mobilisation depositor security, allocative efficiency, and equity impact, (Chapter 8). The various policy measures for eliminating the abuses and

distortions observed among informal lenders, the scope for linking the formal and informal credit agencies, etc. form the content of Chapter 9. In the final chapter we present the main findings and conclusions emerging there from.

CHAPTER 2-

SIZE OF INFORMAL CREDIT MARKETS

2.1 Introduction

A clearcut demarcation between formal and informal credit markets is difficult since the criteria would vary between countries. The description of the informal credit market by Chandavarkar captures all the salient features:

"...it is difficult to give a logically clearcut and comprehensive definition of the sector. In fact it is often better identified by its basic characteristics such as ease of entry and exit, freedom from official regulation, multiple interest relationships between transactions, small scale operations, and above all informality of transactions, which constitute its primary economic rationale and also confers on its comparative economic advantages over the formal financial sector". (Chandavarkar, 1986, cited in Background Discussion Paper).

One of the basic criteria is freedom from regulations. Not that there are no statutory regulations. However, the effectiveness of regulation or its enforcement would vary from one situation to another. For instance, there is statutory regulation on private moneylending in India, but admittedly it is observed more in the breach, owing to many loopholes in the legislation or weakness in the enforcement machinery. For another example, many State governments have introduced legislations to regulate chit funds but they have managed to evade many of the

provisions. Therefore, the criteria have to be applied in a relative sense. In the present study, we will group landlords, agriculturist moneylenders, professional moneylenders, traders, relatives and friends under the category of informal lenders (as against government, cooperative societies, commercial banks, life insurance and provident fund falling under the formal sector). Not that they are homogeneous groups. Evidently, there are some marked differences among them in their mode of operations, nature of links with their borrowers, and terms and conditions. However, they have some similarities, viz., the personalised nature of the creditor-debtor relationships, informality in transactions, using moral suasion and social compulsion rather than legal action to ensure payment of interest or repayment of loans.

On the question of size, there is a conceptual problem, viz., the definition of the term size. The size of the ICM may be expressed in terms of a ratio of the total volume of credit emanating from the sector to the grand total of credit from both the sectors together. The size of the ICM may be viewed as a stock concept, the ratio of credit from this sector to the total debt outstanding at any point of time; or it may be expressed as a flow concept, the ratio of credit extended by this sector over a period of time to the total flow of credit during the same period. In the following sections, we shall present our estimates of the size of the ICMs in the country's rural sector.

2.2 Size of the ICM in the rural sector

2.2.1 Debt outstanding in early seventies

As mentioned earlier, the Reserve Bank of India has been carrying out fairly comprehensive surveys on credit - All India Debt and Investment Surveys - every ten years since the early fifties. The data thrown up by these surveys provide some basis, however weak, for estimating the size of the ICM in the rural areas.

According to the results of the above survey, at the beginning of the seventies total cash dues outstanding against all rural households exceeded Rs.4000 crores.* Of this amount, the informal sector accounted for about three-fourths. Estimates of the total outstanding debt of all the Indian rural households due to various credit agencies in 1971 and 1972 are presented in Table 2.1.

Evidently, the informal sector accounts for a sizable proportion of the total cash dues outstanding against all rural households together in two consecutive years at the beginning of the last decade. For the two years, the average comes to nearly three-fourths of the total outstanding debt. As against this, the share of the formal credit institutions works out to only around one quarter of the whole. It may be noted that among the informal credit agencies, the professional moneylenders account for only about 15 percent of the total or about 20 percent of the credit from the informal sector as a whole. The rest came from non-professional moneylenders who combine lending with other activities.

* 1 crore = 10 million

Table 2.1 : Cash dues outstanding against all rural households classified according to Credit Agency

Credit Agency	Proportion of households		Aggregate cash dues outstanding as				Average for 1971 and 1972	
	1971	Percent 1972	June 30, 1971		June 30, 1972		Rs. crores	Percent
			Rs. crores	Percent	Rs. crores	Percent		
1. Government	3.41	3.39	250.44	6.67	228.17	5.34	239.30	5.97
2. Co-operative Society/ bank	7.65	7.29	652.92	20.07	695.30	16.29	724.11	18.06
3. Commercial bank	0.44	0.49	82.22	2.19	75.94	1.78	79.05	1.97
4. Insurance	0.03	-	3.10	0.08	-	-	-	-
5. Provident fund	0.11	-	5.59	0.14	-	-	-	-
Sub-total			1094.27	29.14	999.41	23.41	1042.46	26.00
6. Landlord	4.62	4.97	324.05	8.63	354.07	8.29	339.06	8.45
7. Agricultural moneylender	10.65	12.27	867.15	23.11	1040.49	24.37	958.32	23.90
8. Professional moneylender	6.49	8.20	517.16	13.78	666.71	15.62	591.35	14.75
9. Trader	4.85	7.27	325.07	8.66	403.73	9.46	364.40	9.09
10. Relative/friend	8.82	7.43	518.79	13.86	350.30	8.20	434.55	10.83
11. Others	1.43	6.88	105.51	2.81	454.76	10.65	280.14	6.98
Sub-total			2657.73	70.85	3270.06	76.59	2967.82	74.00
Total	41.32	43.97	3752.00	100	4269.46	100	4010.28	100

Source: Reserve Bank of India, All India Debt and Investment Survey, 1971-72: (1) Statistical Tables Relating to Cash Dues Outstanding Against Rural Households as on 30th June 1971, Bombay, Statement II, p.15, and Statement IV, p.87. (2) Statistical Tables Relating to Cash Borrowings and Repayments of Rural Households during July 1971 to June 1972 and Cash Dues Outstanding as on 30th June 1972, Bombay, 1978, Statement IV, p.92.

2.2.2 Borrowings during 1971-72

Debts outstanding, obviously, need not reflect the current situation regarding the sources of credit or the share of the informal lenders in total credit, as the outstanding dues would include loans taken in the past. The volume of current borrowings according to sources may, therefore, be examined.

Table 2.2 summarises the data on cash loans taken by the rural households as a whole from various credit agencies during 1971-72. It may be noted that the proportion of households reporting borrowing during the year, and the aggregate borrowings from all sources together, are lower than the corresponding numbers in respect of debt outstanding. Thus, the proportion of households reporting borrowings during the year came to 27.73 percent of all rural households, as against 41.32 percent of households reporting outstanding debt. That only a little over one quarter of the rural households have reportedly resorted to borrowing during the reference period may be a reflection on the size of the total rural credit market. The proportions of households borrowing from all categories of informal lenders similarly reflect on the size of the informal credit market in rural India. It may be noted that the informal sector accounted for a little over four-fifths of the total borrowings by all rural households together. Thus, as of the early seventies, in a relative sense, that is as a proportion of total debt outstanding or that of total borrowings, the size of the ICM in the rural areas is quite large and comparable with the situation in the other less developed countries of Asia.

Table 2.2 : Borrowings in Cash during the year ended 30th June 1972
classified by Credit Agency

Credit Agency	Proportion of households reporting:	Aggregate borrowings	
	Percent	Rs. crores	Percent
1. Government	1.34	41.88	3.11
2. Cooperative society/bank	3.36	201.01	14.94
3. Commercial bank	0.19	22.43	1.67
Sub-total		265.32	19.72
4. Lendlord	2.49	86.22	6.40
5. Agricultural moneylender	5.99	251.87	18.72
6. Professional moneylender	4.43	214.43	15.93
7. Trader	6.01	200.16	14.87
8. Relative/friend	4.75	153.90	11.43
9. Others	4.73	173.49	12.89
Sub-total		1080.07	80.28
Total	27.73	1345.39	100

Source: Reserve Bank of India, All India Debt and Investment Survey, 1971-72, Statistical Tables Relating to Cash Borrowing and Repayments of Rural Households during July 1971 to June 1972 and Cash Dues outstanding as on 30th June, 1972, op.cit., Statement II, p.20.

2.3 Trends in the size of ICMs

We shall now proceed to examine the trends in the size of the ICM in the rural sector in recent decades. According to the results of

the All India Rural Credit Survey, 1951-52, around 94 percent of the total debt outstanding against all rural households was due to the informal lenders including landlords, agriculturist moneylenders, professional moneylenders, traders, relatives and friends, etc. Of the total borrowings by the cultivator households in 1951-52, viz., Rs.750 crores, non-institutional agencies accounted for about 93 percent. The share of the informal credit agencies has steadily declined since then, thanks to the expansion of institutional credit, especially that from the cooperative societies/banks and commercial banks.

2.3.1 Debt outstanding

The estimates of the total debt outstanding against all rural households and the shares of the formal and informal agencies, in 1962, 1972 and 1982 are presented in Table 2.3.

From a little over 85 percent in 1962, the share of informal credit agencies in total outstanding debt of all rural households declined to about 77 percent in 1972, and in the next ten years it dropped to about 39 percent. It is evidently the outcome of the steep increase in credit from formal credit institutions. While the latter increased by around Rs.586 crores, i.e. by 142 percent and 268 percent respectively. True, between 1962 and 1972, aggregate volume of credit from informal agencies did increase, but the increase was of a much lower order, viz., about 38 percent. But in the course of the next decade, the aggregate debt outstanding due to this sector registered an absolute decline, viz., by Rs.940 crores or 28.7 percent.

Table 2.3 : Aggregate Cash Dues Outstanding against all rural households according to sources
All India

Credit Agency	Aggregate dues Outstanding						Increase during 1962-72		Increase during 1972-82	
	1962		1972		1982		Rs.crores	Percent	Rs.crores	Percent
	Rs.crores	Percent	Rs.crores	Percent	Rs.crores	Percent				
Formal Credit Institutions	413.44	14.80	999.41	23.41	3676.00	61.20	585.97	141.73	2676.59	267.82
Informal Credit Institutions	2375.48	85.20	3270.06	76.59	2330.21	38.80	894.53	37.66	-939.80	-28.74
Total	2788.93	100	4269.46	100	6006.23	100	1480.50	53.08	1736.79	40.68

Sources: Reserve Bank of India, All India Rural Debt and Investment Survey, 1961-62, Outstanding Loans, Borrowings and Repayments of Rural Households, Bombay, 1965, Table X, p.14.
All India Rural Debt and Investment Survey 1971-72, Statistical Tables relating to cash borrowings and Repayments of Rural households during July 1971 to June 1972 and Cash dues outstanding, as Sarvekshana,.....

2.5.2 Borrowings

There has been a moderate reduction in the proportion of total borrowings from the informal sector during the sixties. The increase in borrowings from the informal sector between 1961-62 and 1971-72 is small in both absolute and relative terms. The share of the informal sector is apt to have fallen further during the seventies, as has happened in the case of debt outstanding due to the informal agencies.*

Table 2.4 : Aggregate borrowings by all rural households according to Sources

All India

Credit Agency	Aggregate borrowings				Increase during	
	1961-62		1971-72		1962-72	
	Rs. crores	Percent	Rs. crores	Percent	Rs. crores	Percent
Formal Credit Institutions	208.47	16.80	265.31	19.72	56.85	27.27
Informal Credit Institutions	1030.09	83.20	1080.07	80.28	50.58	4.91
Total	1238.55	100	1345.39	100	106.83	8.62

Sources: The same as in Tables 2.3

* Estimates of borrowings during 1981-82 are not as yet available.

2.5.3 Household participation

The trends in the proportion of households reporting outstanding debt or borrowings also fall along the above lines. The estimates of these proportions since the early sixties are presented in Table 2.5. It may be noted that the proportions of households reporting debt outstanding due to all categories of informal lenders have almost steadily and sharply fallen during the period. As for the households reporting borrowings the proportion in 1971-72, the latest year for which estimates are available, are significantly lower than in 1961-62, except in the case of landlords and traders. Even in these two exceptional categories, the proportion in the latter year are not large. That the proportions of reporting households have fallen is a significant indicator of the trend in the size of informal credit market.

Table 2.5 : Proportion of Households reporting debt to informal credit agencies

All rural households, All India

Credit agency	Households reporting debt outstanding, Percent			Households reporting borrowings, Percent	
	1962	1972	1982	1961-62	1971-72
Landlord	0.9	4.62	1.20	0.6	2.49
Agricultural moneylender	32.0	10.65	2.56	20.6	5.99
Professional moneylender	11.1	6.49	2.03	7.4	4.43
Trader	7.0	4.85	0.98	5.5	6.01
Relative/friend	8.3	8.82	2.93	7.2	4.75
Others	15.0	1.43	1.58	15.1	4.73

In brief, the informal sector's share of the total debt outstanding against all rural households has registered a significant and steady decline between 1962 and 1982. Similar is the trend observed in respect of the aggregate borrowings from informal credit agencies. The declining trend in the proportion of households reporting outstanding debt or borrowings from these sources also seem to imply a shrinking of the size of the ICM in the Indian rural sector.

2.3.4 Trends in the overall size of the rural credit market

(i) The total outstanding dues, at current prices, has more than doubled during the last three decades. How does the trend in the aggregate volume of credit look in real terms? How adequate is the increase in credit compared with the credit needs of agriculture and rural industries in transition, presumed to involve more purchased inputs, wage labour and other working capital needs? Before we get into such aspects, let us take a look at the trends in the number of borrowers, which, after all, is an important parameter reflecting the size of the credit markets.

(Table 2.6).

Table 2.6 : Proportion of Households Reporting Cash Dues Outstanding and Borrowing : All rural households: All India

Items	Percent			
	1951-52	1961-62	1971-72	1981-82
a. Proportion of households reporting cash dues outstanding	N.A.			
All rural households	..	62.80	41.32	19.97
Cultivator "		66.70	44.36	22.34
Non-cultivator "		52.00	33.35	12.35
b. Proportion of households reporting borrowings				
All rural households	51.70	48.80	27.73	N.A.
Cultivator "	58.60	52.00	29.29	N.A.
Non-cultivator "	38.60	40.00	23.44	N.A.

Sources: Reserve Bank of India, All India Rural Credit Survey, 1951-52, Report of the Committee of Direction, The Survey Report, Vol.I, Part I, Bombay, 1956, p.3.

All India Rural Debt and Investment Survey, 1961-62, Outstanding Loans, Borrowings and Repayments against Rural Households, Bombay, 1965, Table III.

All India Debt and Investment Survey, 1971-72, Statistical Tables relating to cash Dues Outstanding against Rural Households, op.cit., Statement II.

All India Debt and Investment Survey, 1981-82, Reserve Bank of India Bulletin, 1986, op.cit., Table 5.

As shown in the above table, the incidence of indebtedness, i.e. the proportion of households with cash dues outstanding, had fallen from nearly two-thirds of all rural households in 1961-62 to less than one-fifth by 1981-82. Similarly, the proportion of households that have

reported borrowing declined from over one-half of all rural households in 1951-52 to little over a quarter by 1971-72, the latest year for which estimates are available. The trend emerging from the foregoing would seem to indicate a welcome change to the traditional image of the Indian peasant described as "born in debt, lives in debt and dies in debt". On the other hand, one would expect a larger proportion of rural households than reported in the latest round of AIDIS, especially cultivator households availing of credit, as the financial requirements of the new seed-fertiliser technology are much higher than that of traditional agriculture. In this connection, it is interesting to note that decline of a similar order since the fifties has been reported in the Philippines. But in a recent publication, the authors while reviewing the studies observed: "Whether this could be an indication that a growing number of farmers were able to self-finance their farm production was, however not clear". (Orlando J Sacay, et.al., 1985, p.5).

(ii) It is true, the aggregate loans outstanding in nominal terms rose significantly during 1951-81. But in the meantime, all prices -- especially of farm inputs and wages of labour -- have risen at a higher rate. We have deflated the estimates of aggregate cash dues outstanding, from all sources, on the basis of wholesale price index as a rough approximation, to arrive at the estimate of outstanding cash dues in real terms. (Table 2.7). The wholesale price index may not be the most appropriate deflator. However, whether index number of farm prices or index of input prices would be a better deflator is a difficult question to resolve.

Table 2.7 : Cash Loans Outstanding: All Rural Households, All India

Item	1961	1971	1981
1. Aggregate cash dues outstanding.			
a. At current prices: Rs. crores	2788.93	3652.00	6006.23
b. At 1961-62 Prices: Rs. crores	2788.93	1954.12	1220.78
c. Increase during preceding decade:			
(i) at current prices			
Rs. crores	-	963.07	2254.23
Percent	-	34.53	60.08
(ii) at 1961-62 prices			
Rs. crores	-	(-) 834.81	(-) 733.04
Percent	-	(-) 29.93	(-) 37.53
2. Average amount per household at current prices Rs.	406.30	487.05	661.00
3. Average value of all assets per household Rs.	5369.80	11311.00	36090.00
4. Ratio of cash dues outstanding to value of assets per household : Percent	7.87	4.30	1.83

- Source: (i) AIDIS, 1961-62, Outstanding Loans, Borrowings and Repayments of Rural Households, op.cit.
(ii) AIDIS, 1971-72, Statistical Tables Relating to Cash Dues Outstanding Against Rural Households, op.cit.
(iii) AIDIS, 1981-82, Reserve Bank of India Bulletin, 1986, op.cit.

The aggregate cash dues outstanding in nominal terms registered on the average, an increase of about 3.5 percent per annum during 1962-72 and 6 percent over the next decade. But in real terms the variation turned

out to be negative, at the rate of about -3 to -3.7 percent a year. According to a recent study in the United States, real farm debt grew at an annual rate of 4.4 percent during 1960-71, and 5.9 percent during 1971-80. (Deen Hughes, et.al., 1986, p.17).

Again, the debt-asset ratio in the rural households as a whole, has steadily fallen, from 7.87 percent in 1961 to 4.3 percent in 1971 and 1.83 percent by 1981. A comparison with the position of U.S. farms may be interesting. "From 1960 to 1972 the debt to asset ratio rose gradually to reach a peak of 18.9 percent, after which it stabilised in the 15.5 to 16.5 percent range throughout 1979". (Ibid., p.22). An alternate estimate places the debt-asset ratio on the U.S. farms at the beginning of the 1970's at 31.4 percent (Aaron G Nelson, et.al. 1973, p.81). Thus, the trends in the ratio of increase in debt outstanding in real terms and debt-asset ratio, seem to indicate a decline in the size of the rural credit market in recent periods.

(iii) We will next examine the trends in aggregate borrowing by the rural households as set out in Table 2.8.

The increase in total borrowings by rural households between 1961-62 and 1971-72 does not appear to be very large. Even in nominal terms, the rate of increase comes to 8.62 percent only over the decade as a whole, or less than 1 percent per year. The average amount per family had fallen even in nominal terms from Rs.180.4 to Rs.173.9. The ratio of a little over 6 percent of the rural income as of 1971-72 is even less than the requisite ratio earlier estimated by the All India Rural Credit

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Review Committee, viz., 8 percent of net value added in agriculture as the requirement of productive credit for the sector - comprising 50-70 percent of cash outlay on seeds, fertiliser and pesticides, 40 percent of cash outlays on current inputs, and the rest by way of requirements for medium and long term credit. (Reserve Bank of India, 1969, pp.81-82).

Comparable figures for Latin America and Taiwan show that even institutional credit was much more ample, around one-third of gross farm output in the 1960s, the U.S. ratio being 53 percent and comprising 70-90 percent farm credit. (Lipton, 1976, p.544).

Table 2.8 : Aggregate Cash Borrowings : All Rural Households, All India

Item	1961-62	1971-72	Increase over preceding period	
			Rs. crores	Percent
1. Aggregate cash borrowing				
At current prices:				
Rs. crores	1238.54	1345.39	106.85	8.62
At 1961-62 prices:				
Rs. crores	1238.54	699.63	-539.91	-43.59
2. Aggregate rural income at current prices:				
Rs. crores	8978.20	22194.00	13216.00	147.20
3. Ratio of borrowing to income:				
Rs. crores	13.79	6.06		

Note: Rural Income is assumed to be 1.325 times that of agricultural income (NDP at factor cost in agriculture)

Source: The same as of Table 2.6.

Whatever the yardstick used - the debt asset-ratios or borrowing-output ratios - the recent trends in outstanding debt and borrowings appear to suggest a shrinking rural credit market. True, this inference is based on only one source of data, viz., the results of the different rounds of the Debt and Investment Surveys. But, then, this is the only source of data which lend themselves to an intertemporal comparison extending over such a long period.* If, as the data imply, scale of rural credit is low and declining, why is it so? Is it due to insufficiency of credit available, the supply of credit, or the sluggishness in the demand for credit? Given the consistent and perceptible decline in the proportion of households reporting cash dues outstanding, as well as borrowings, we would venture to offer the hypothesis that it is the low demand for credit, rather than supply constraints, which underlies the low rate of availing of credit. In other words, the size of the rural credit market continues to remain stagnant, thanks to the sluggishness in demand for credit.

(iv) That leads to the question why the demand for credit is sluggish despite the advent of the HYVs and the new seed-fertilizer technology, which involve greater cash outlay? Is it because the farmers are resourceful enough to be able to bear a large part of the additional expenditure

* The representativeness of the sample is an aspect, among other things, which needs close scrutiny. If the sampling design gives greater weightage to households of the upper strata, who presumably are under less compulsion to borrow, the actual trends in the various parameters of the credit market are apt to be different from the one which we have presented above. See Appendix.

involved in HYVs? The findings of a few studies conducted by the Agro-Economic Research Centres showed that in a number of districts owned funds of farmers were the preponderant source of financing farm expenditure on HYVs, and borrowings formed a low proportion of the total input expenditure of the new varieties of crops. Admittedly, the studies covered the initial phase of the HYVs programme, and the participating farmers were purposively selected from among the relatively bigger cultivators, who had larger owned resources. But more importantly, the intensity of the use of inputs and adoption of cultural practices was much lower than prescribed. (Desai and Naik, 1971, p.460). If it were so, would the demand for production credit go up in the future if small and medium farmers take to the cultivation of HYVs and also adopt the recommended levels of input use and cultural practices? Desai and Naik are inclined to think that "the adoption of the new seed varieties, the levels of inputs use and adoption of the recommended cultural practices would persistently remain low and they, in turn, will keep the demand for credit low until each times as the green revolution stabilises itself". (Ibid.)

The demand for production credit in most parts of rural India seems to be sluggish because the majority of the cultivator households, the small and medium ones, have less credit-absorption capacity, thanks to their limited knowledge, awareness and confidence in the new seed-fertilizer technology, and the constraints they suffer from in getting access to the various inputs including new seeds, fertilisers, irrigation facility, etc. Further, they have limited access to institutional credit which has been making a dramatic expansion in

recent years. On the other hand, in Punjab and Haryana, and to a limited extent in Western Uttar Pradesh, the highly favourable experience of the early adopters - mostly large farmers - with the new seed varieties and the associated technology drew prompt and widespread response from an increasing number till all the cultivators in this subregion joined the mainstream of the green revolution. In the process, demand for production credit in Punjab and Haryana swelled significantly, as we shall see below.

The spurt in the demand for credit from the cultivators of Punjab in the wake of the spread of the green revolution is reflected in the high proportion of them availing of credit. While for the country as a whole the proportion of cultivator households borrowing fell steeply from 52.1 percent in 1961-62 to 29.29 percent in 1971-72, in Punjab, it increased from 63.7 percent to 67.92 percent. The estimates of this proportion for 1981-82 are not presently available. Similarly, the proportion of households reporting cash dues outstanding as well as amount per household are also comparatively high in Punjab. The following table presents the Statewise figures on cash dues outstanding for three years (Table 2.9).

The average cash dues outstanding per reporting household in both Punjab and Haryana during 1971 and 1981 are found to be significantly higher than the average for the other States, and that this gap has widened between the two periods. True, only a relatively low and falling proportion of cultivator households are reported to have outstanding debt.

Table 2.9 : Cash Dues Outstanding per Reporting Household : Cultivators

State	Average value of assets : Rs.	Cash dues outstanding per report- ing household : Rs.		
		1962	1971	1981
1. Punjab	62788.97	1288	3118.43	9580
2. Haryana	41824.67	-	3394.00	13048
3. Himachal Pradesh	24106.74	-	1501.17	3077
4. Gujarat	18502.19	867	2330.97	5022
5. Uttar Pradesh	16350.22	482	971.47	2752
6. Maharashtra	16232.43	700	1477.40	4241
7. Jammu & Kashmir	15938.27	391	750.87	2995
8. Bihar	15539.07	599	839.95	1744
9. Karnataka	14929.77	975	1707.28	5715
10. Rajasthan	13947.09	1026	1617.37	4932
11. Kerala	12754.5	414	1107.57	3409
12. Madhya Pradesh	12342.03	660	1055.17	3005
13. Andhra Pradesh	11973.75	912	1655.39	4055
14. Tamil Nadu	10907.29	1081	1849.70	3911
15. West Bengal	9964.59	425	623.06	1677
16. Assam	9157.46	330	757.63	1113
17. Orissa	7382.04	392	582.68	1803
All India		393	1329.77	3595

Note: The states are arranged according to the average value of assets of cultivator households in the descending order.

Source: The same as in Table 2.6.

However, the difference between the average debt outstanding per cultivator household in Punjab and Haryana on the one hand and that in the other States persist at an overall level also. (see Table 2.10).

Table 2.10 : Average Cash Dues Outstanding and Borrowing per Household:
Cultivators

State	Cash dues outstanding		Increase during 1961-71 Rs.	Borrowings during		Increase during 1961-62 - 1971-72 Rs.
	1962 Rs.	1971 Rs.		1961-62 Rs.	1971-72 Rs.	
1. Punjab	968.20	1811.75	843.55	665	1265.16	900.16
2. Haryana	-	1185.49	-	-	667.16	-
3. H.P.	-	589.66	-	-	-	-
4. Gujarat	629.10	1246.07	616.97	370	306.45	-63.55
5. U.P.	295.50	370.36	74.87	168	166.57	-1.43
6. Maharashtra	441.20	801.56	360.36	219	250.60	31.60
7. J & K	241.50	369.99	128.49	154	178.27	24.27
8. Bihar	393.50	327.80	-65.60	102	68.21	33.79
9. Karnataka	823.20	943.10	119.10	324	306.81	-16.19
10. Rajasthan	815.20	920.73	115.53	388	407.98	19.98
11. Kerala	293.60	397.00	103.40	204	143.55	-60.45
12. M.P.	907.80	445.21	37.41	166	200.80	34.81
13. A.P.	702.30	-	-	269	306.56	-62.44
14. Tamil Nadu	855.20	1119.48	264.28	298	285.98	-12.02
15. West Bengal	241.10	247.57	4.47	146	126.59	-19.41
16. Assam	139.90	199.35	59.45	36	30.91	-5.09
17. Orissa	131.00	186.55	55.55	55	60.16	5.16
All India	472.70	589.92	116.22	205	203.85	-1.15

Source: The same as Table 2.9.

It may be noted that during 1971-72, the average borrowings per cultivator household in Punjab and Haryana were several times higher than that in most other States. Between 1961-62 and 1971-72, the average increased by a little over Rs.900 in Punjab, while for all the states taken together there was actually a fall, though marginal.

2.3.5 Inter-regional variations in the size of the ICM

As observed above, the recent decades witnessed a steady and rapid decline in the shares of the informal credit agencies in the aggregate debt outstanding against or total borrowings by the rural households. Thus, the proportion of the total loans outstanding against all rural households due to the informal credit agencies declined from 85 percent period in 1962 to about 71 percent in 1972 and about 39 percent in 1982. However, there are considerable inter-regional variations in the rate of decline of the shares of these agencies, as may be noted from the following table. (Table 2.11).

It may be noted that the percentage share of the informal credit agencies in the total debt outstanding as of 1982 ranges from 13.6 in Maharashtra to 69.4 in Assam. In seven of the states, viz., Andhra Pradesh, Assam, Bihar, Jammu & Kashmir, Rajasthan, Tamil Nadu and Uttar Pradesh, the share of these agencies exceeded the All-India average. That the same States had shared the feature in 1971 implies that they have some characteristics which sustain the hold of private lenders and resist the expansion of credit from the formal sector. To the factors underlying the inter-regional variations in the size of the ICM we will return in due course.

Table 2.11 : Percentage shares of the informal credit agencies in the aggregate cash debt outstanding

All rural households

States	1962	1972	1982
1. Andhra Pradesh	90.5	86.3	59.1
2. Assam	76.2	65.3	69.4
3. Bihar	94.9	89.3	52.8
4. Gujarat	76.3	53.1	30.0
5. Haryana	-	73.6	24.2
6. Himachal Pradesh	-	76.1	25.5
7. Jammu & Kashmir	90.4	79.6	56.5
8. Karnataka	83.9	70.3	21.8
9. Kerala	82.5	55.6	21.4
10. Madhya Pradesh	84.3	68.4	33.7
11. Maharashtra	53.6	32.6	13.6
12. Orissa	73.6	70.0	18.1
13. Punjab	89.3	64.0	25.8
14. Rajasthan	95.4	90.6	59.1
15. Tamil Nadu	86.5	77.9	55.7
16. Uttar Pradesh	89.1	76.6	44.9
17. West Bengal	76.7	69.4	34.5
All India	85.2	70.8	38.8

Source: Data for 1962 and 1972 the same as of Table 2.3; that for 1982 from Sarvekshana, Vol.XI, No.1, 1987, Table XII, p.13.

Note: The boundaries and names of states underwent some changes between 1962 and 1972. For example, Mysore reorganised as Karnataka, and Madras as Tamil Nadu.

To sum up: In the early seventies, about three-fourths of the total outstanding debt against rural households and a little over four-fifths of the borrowings by rural households was from the informal credit agencies. Since then, the share of these agencies registered a sharp decline, to less than two-fifths of the aggregate cash loans outstanding as of 1982. In fact, between 1972 and 1982, the aggregate debt outstanding due to the informal lenders fell even in absolute terms. The fall in the share of these agencies is but a continuation of the trend which set in from the early fifties which accelerated from the sixties, thanks to the expansion of credit from the formal sector. Apparently, not only the relative size of the informal sector but the rural credit market as a whole appears to have shrunk in size.

APPENDIX 1

A Note on the Reliability and Comparability of the various rounds of AIRCIS and AIDIS

The decennial Rural Debt and Investment Surveys are the only source of information on debt, borrowings, capital formation, etc. in the rural household sector. These surveys are statistically designed to yield comparable and reliable estimates of the above items for all-India and individual States. The reliability and comparability of the estimates is the subject matter of this note. The note is organised in four sections : Section I provides a brief account of the method of approach and plan of enquiry of the surveys of 1961-62, 1971-72 and 1981-82. In section II the implications of the shift in the selection of households within village to the reliability of the estimates of various items is gone into. Section III discusses the question of under-estimation. Section IV discusses the behaviour of the sampling variance over the three rounds assuming that the sampling technique followed for the selection of households within the villages to be the same in all the three rounds.

Section I: Changes in the Sampling Strategy over 1961-62, 1971-72 and 1981-82

For the 1961-62 survey the sample of villages from each State was selected after stratifying the State into a number of ultimate strata

which are roughly of equal size, being measured in terms of the 1961 rural population, and homogeneous with regard to general agricultural conditions. The sample of villages within each State was allocated among the strata in proportion to the population size and were selected at random with probability proportional to size, i.e. population. In each selected village, a sample of 40 households was selected at random for investigation.

For the two rounds of 1971-72 and 1981-82 two-stage stratified random sampling procedure, with villages as first stage units and households as second stage units, was adopted. The rural area of the country was divided into 66 agro-climatic zones taking into account population density, altitude and communication facilities. The all-India sample of villages were allocated among different States on a joint consideration of their rural population, area under cereal crops and available investigator strength. The allocation of villages was further modified to ensure a minimum of 180 villages in each State except in the smaller States and Union Territories. In 1971-72 from each stratum two independent subsamples of 12 villages (with few exceptions) were selected circular systematically with equal probability. In 1981-82 the sample villages were selected with probability proportional to number of house-listing and with replacement.

In each selected village the households were divided into four sub-strata, by their area of land possessed. Households possessing less than 0.05 acres formed sub-stratum 1 called non-cultivators. The remaining households were ranked by their area of land possessed and then

divided into three sub-strata, viz., small cultivators, medium cultivators, and large cultivators, in such a way that the total area owned by each category of households were the same. Three and two households respectively were selected from each sub-stratum in 1971-72 and 1981-82. In both the years circular systematic sampling with a random start was followed. Thus, from each village 12 households in 1971-72 and 8 in 1981-82 were selected to form a sample of 149,424 households in 1971-72 and 61,744 households in 1981-82.

The distribution of villages for all the three rounds is provided in Table 1.

On the whole there seems to have taken place a definite shift in the sampling strategy from smaller number of villages with larger number of households per village to larger number of villages with smaller number of households per village. The number of villages increased four-fold between 1961-62 and 1971-72, and the number remained almost the same between 1971-72 and 1981-82. The number of households per village decreased from 40 in 1961-62 to 12 in 1971-72, and to 8 in 1981-82. The sample size, i.e. the total number of households surveyed for the country as a whole, showed only a marginal increase between 1961-62 and 1971-72 and a marginal decrease between 1971-72 and 1981-82.

Table 1 : Distribution of Sample Villages Among Different States

State	Number of Sample Villages					
	1961-62		1971-72		1981-82	
	Central	State	Central	State	Central	State
Andhra Pradesh	152	-	336	336	287	293
Assam	75	24	180	180	160	167
Bihar	216	-	384	448	344	348
Gujarat	80	60	180	180	149	149
Haryana	-	-	180	60	58	174
Himachal Pradesh	6	-	96	-	70	81
Jammu & Kashmir	84	-	180	180	143	148
Karnataka	88	-	180	180	171	164
Kerala	72	-	180	180	156	156
Madhya Pradesh	136	-	360	360	255	301
Maharashtra	144	-	312	312	290	290
Manipur	3	-	96	96	59	60
Meghalaya	-	-	96	-	47	58
Orissa	82	42	180	180	148	147
Punjab	80	20	180	90	148	152
Rajasthan	80	22	180	180	159	155
Tamilnadu	128*	-	312	312	228	225
Tripura	5	-	96	96	65	71
Uttar Pradesh	320	-	528	528	454	441
West Bengal	136	-	276	-	222	219
Arunachal Pradesh, Chandigarh, Delhi etc.	2	-	36	12	142	164
All India	1889	168 (2057)	4548	3910 (8458)**	3755	3963 (7718)

Notes: Figures within brackets are total for the various rounds.

* includes Pondicherry

** In addition to the central and state samples there was a category called additional sample consisting of 3994 villages.

As the purpose of the survey is to yield reliable estimates of debt, borrowings, capital formation, etc. the presumption underlying the shift in the sampling strategy seems to be that the variation in debt, borrowings, etc. across villages within homogeneous agro-climatic zones and across households within villages is considerable and that the between-village variation is sought to be captured by increasing the number of households.

Thus, the main aspects of the shift in the sampling strategy are:

- (i) smaller number of villages and larger number of households per village in 1961 to large number of villages and smaller number of households per village in 1971 and 1981;
- (ii) simple random sample of 40 households per village in 1961 to stratified systematic sample of 12 households and 8 households per village in 1971 and 1981 respectively.

The implications of these shifts to the reliability of the estimates are discussed in the next two sections.

Section II : Implications of the Shift in the Selection of Households within the village to the Reliability of Estimates

A meaningful investigation of the implications of the shift in the sampling strategy to the reliability of the estimates can only be carried out with a proper understanding of the nature of the variables involved. By and large, the variables appearing in the AIDIS are of two

types: incidence and (quantity or) amount per household reporting incidence, the two together providing estimates for the total of the various groups. As an illustration, let us take the case of debt outstanding per rural household which is the product of the proportion of rural households indebted and the average amount of debt outstanding per indebted household (reporting household in the terminology of AIDIS). The efficiency of any sampling strategy rests in generating reliable estimates of the product of two variables, viz., the incidence and the quantity per reporting household, which is the efficiency with which the incidence and quantity per reporting household are estimated.

First let us take the question of the estimation of quantity or amount of debt, borrowings, asset.... etc., per reporting household. In 1961 these were estimated by selecting households within villages using stratified systematic sampling. In as much as these variables bear a linear relationship with the variable used for stratification, viz., land owned, the stratified systematic sampling followed in 1971 and 1981 should be able to throw up more accurate estimates compared to the 1961 estimates. But the real problem is with the estimates of incidence.

It may be noted at the very outset that the proportion of households reporting debt, borrowings, or particular types of assetsetc. need not be and are, in many cases, not related to the variable used for stratification. There is no reason to believe that the proportion of households indebted would be higher among higher size classes of landholders or vice versa (see Table 2). As is evident, the pattern is quite the contrary with

Table 2 : Incidence of Debt of Rural Household in Selected States (1981-82)

Household Asset Holding (Rs.)	Percentage of Households Reporting Cash Dues										
	Assam	Bihar	Gujarat	Haryana	J & K	Karnataka	Kerala	Punjab	Rajasthan	TN	UP
Upto 1000	1.12	13.93	0.49	0	-	9.65	2.17	0	7.52	15.58	5.1
1000 - 5000	3.20	10.68	5.15	15.25	10.28	15.87	19.37	13.77	18.94	22.20	16.4
5000 - 10000	4.27	14.38	9.01	3.94	8.86	21.49	17.70	20.40	18.53	26.60	17.3
10000 -- 20000	5.00	12.22	23.80	10.38	11.24	27.14	21.87	18.73	27.46	30.25	17.8
20000 - 50000	4.82	11.85	22.77	9.92	8.25	24.17	33.61	19.96	28.20	41.23	19.6
50000 -100000	3.03	10.95	22.06	8.03	9.39	31.26	32.48	13.64	23.87	41.83	14.1
100000 -500000	12.85	13.78	22.40	12.89	8.24	39.68	26.13	20.92	16.71	49.67	17.6
500000 +	0	15.61	20.56	27.20	12.20	51.13	27.96	35.10	23.29	38.88	22.8
All groups	4.28	12.18	17.39	10.48	8.91	23.84	28.22	18.92	24.24	28.53	17.0

Source: Sarvekshana Vol. X, No.1, 1986.

only some of the states showing a marginal increase in incidence with size and most of the states showing no variation with size at all.

In the absence of a linear relationship between landowned and incidence systematic sampling is no more efficient than simple random sampling because in such cases even with systematisation it amounts to arranging the households at random and,

"If all the units in the population are arranged at random, then systematic sampling is equivalent to simple random sampling without replacement," (p.156, M.N. Murthy).

Thus, not only that the gains of systematisation disappear but also certain other biases may creep into the estimates of certain variables (we turn to these biases later).

The stratification is not carried out with the purpose of generating reliable estimates of incidence, rather their specific aim seems to be the generation of reliable estimates of the amount per reporting household. The stratification leads to a situation where the lower two strata, viz., non-cultivators and the cultivators owning the lowest one-third of the area would account for over 80 percent of the households in almost all the states (see Table 3). Consequently, 50 percent of the sample units are chosen from two of the lower strata accounting for over 80 percent of the rural households and the rest 50 percent of the sample households from two of the upper strata accounting for less than 20 percent of the rural households.

Table 3: Distribution of Rural Households - 1971

State	Percentage of non-cultivators	Percentage of households owning top 30 pc. of land	Percentage of households owning the next 30 pc. of land
Andhra Pradesh	38	3	10
Assam	18	6	10
Bihar	20	4	9
Gujarat	36	5	9
Haryana	40	4	11
Himachal Pradesh	8	6	15
Jammu & Kashmir	6	12	29
Karnataka	31	5	15
Kerala	10	4	7
Madhya Pradesh	18	5	17
Maharashtra	31	5	9
Orissa	23	4	11
Punjab	57	4	8
Rajasthan	13	3	12
Tamil Nadu	45	3	7
Uttar Pradesh	22	5	11
West Bengal	34	4	13

Source: NSS, Land Holding Survey, 1971-72.

This considerably reduces the gains due to stratification because it turns out to be a case of large deviations mentioned by Murthy,

"When the allocation deviates much from the above three allocations, there may be a few situations where the first term on the right hand side of (7.35)^{1/} not only becomes negative but also exceeds the other term in absolute value thereby giving rise to a loss in efficiency due to stratification". (p.249)

This may be shown by a few numerical examples based on tables 2 and 3 (see table 4). As is evident in every case $V(\hat{Y}_{us}) - V(\hat{Y}_{st})$ is negative.

Table 4 : Loss in Efficiency Due to Stratification for various values of W_s and P_s

s	W_s	P_s	W_s	P_s	W_s	P_s	W_s	P_s
1	.18	.03	.20	.14	.36	.05	.10	.20
2	.66	.04	.67	.12	.50	.24	.79	.30
3	.10	.05	.09	.12	.09	.22	.07	.25
4	.06	.13	.04	.15	.05	.22	.04	.25
Loss	-.0342		-.1036		-.0963		-.3325	

$$1/ (7.35) : V(\hat{Y}_{us}) - V(\hat{Y}_{st}) = \frac{1}{n} \sum_{s=1}^K (1 - \frac{n}{n_s} W_s) W_s \sigma_s^2 + \frac{1}{n} \sum_{s=1}^K W_s (\bar{Y}_s - \bar{Y})^2$$

Thus, there does not seem to be any gain due to stratification and systematisation. In other words, though the sampling designs of 1971-72 and 1981-82 are apparently different, in effect they are no better than arswor.

Table 5 : Variation of Survey Estimates of Cooperative debt over outstanding reported by PACs and PLDBs as on June 30, 1971

State	Percentage variation
Andhra Pradesh	-67.2
Assam	-45.6
Bihar	-45.1
Gujarat	+38.2
Haryana	-52.4
Himachal Pradesh	-43.4
Jammu & Kashmir	-50.2
Karnataka	-47.0
Kerala	-43.7
Madhya Pradesh	-41.8
Maharashtra	-32.2
Orissa	-64.6
Punjab	-56.6
Rajasthan	-60.7
Tamil Nadu	-50.8
Uttar Pradesh	-27.6
West Bengal	-29.7
All India	-38.9

Source: RBI, Statistical tables Relating to Cash Dues Outstanding Against Rural Households as on 30th June, 1971, Bombay 1976.

Section III : The Question of Under Estimation

In addition to the arguments put forth in Section II there seem to exist other empirical evidence, pointing to the unreliability and non-comparability of the estimates, some of which have a theoretical base.

It was reported that there was considerable under-estimation of debt owed to the co-operatives by rural households in the AIRCs of 1961-62 and AIDIS of 1971-72. In 1961-62 the under-estimation was of the order of 17 percent at the all India level. By 1971-72, however, the magnitude of underestimation had increased to 30 percent (table 5). One of the reasons attributed to the under-estimation is the under-reporting of the debt owed to the co-operatives. For instance, the under-reporting in Maharashtra was between 3 to 37 percent in 1971-72.^{2/} It is, however, not clear whether the under-estimation could entirely be attributed to the under-reporting as the under-reporting ranges between 3 to 37 percent (for Maharashtra) with the average being much lower than 37 percent. Further, why should the degree of under-reporting increase between 1961 and 1971? Thus, even if we attribute part of the under-estimation to under-reporting a significant part of the under-estimation remains to be explained and it could be attributed to the shift in the sampling strategy as we argue below.

^{2/} Reserve Bank of India, Statistical Tables Relating to Cash Dues Outstanding Against Rural Households as on 30th June 1971, Bombay, 1976, pp. 6 and 7.

Let us assume that Y_{isk} is the reported value of the variable whereas Y_{isk}^* is the true value and U_{isk} is the under-reported amount, all for the k^{th} household in the s^{th} strata of the i^{th} village. Let M_{is} and m_{is} , respectively, be the total and sampled number of households in the i^{th} sampled village. Further, let \hat{Y}_A be the estimate using stratification and \hat{Y}_B be the estimate that would have been obtained had there been no stratification. The estimates, then, for the 1971 scheme, are

$$\begin{aligned} \hat{Y}_A &= \sum_{i=1}^N \sum_{s=1}^4 \frac{M_{is}}{m_{is}} \sum_{k=1}^{m_{is}} Y_{isk} \\ &= \sum_{i=1}^N \sum_{s=1}^4 \frac{M_{is}}{m_{is}} \sum_{k=1}^{m_{is}} Y_{isk}^* + \sum_{i=1}^N \sum_{s=1}^4 \frac{M_{is}}{m_{is}} \sum_{k=1}^{m_{is}} U_{isk} \\ \hat{Y}_B &= \sum_{i=1}^N \sum_{j=1}^M Y_{ij} \\ &= \sum_{i=1}^N \sum_{j=1}^M Y_{ij}^* + \sum_{i=1}^N \sum_{j=1}^M U_{ij} \end{aligned}$$

Now note the interesting fact that the term $\frac{M_{is}}{m_{is}}$ is large for small cultivators, owing to large M_{is} and same m_{is} . If it is assumed that U has to do with stratification then

$$\begin{aligned} \sum_{i=1}^N \sum_{s=1}^4 \frac{M_{is}}{m_{is}} \sum_{k=1}^{m_{is}} U_{isk} &\text{ is going to be significantly different from} \\ \sum_{i=1}^N \sum_{j=1}^M U_{ij} &\text{ on the average. In other words, the same} \\ \text{amount of under-reporting may cause substantial difference in under-} \end{aligned}$$

estimation. To get the full implications of the shift between 1961 and 1971 to under-estimation the significant reduction in the number of second stage units in 1971 need also be kept in mind.

The second piece of empirical evidence is the systematic behaviour of the coefficient of variation of the estimates of various items in 1981-82 for which data is readily available. The coefficient of variation of the estimate of the proportion of households reporting cash dues payable is higher than the co-efficient of variation (CV) of households reporting land owned and buildings (see Table 6). The CV of the former is 1.98 whereas the latter are 0.37 and 0.27 respectively. These results seem to suggest that the variables linearly related to land owned are efficiently estimated whereas the others are not. The point is further supported by the fact that the CV for non-cultivator households for all items are higher than for cultivator households. The CV of proportion of non-cultivator households reporting liabilities is higher than that for cultivator households by nearly 125 percent; the CV for value of poultry and livestock owned by non-cultivator households is 12 times higher than that for cultivator households. The percentage difference is even higher for variables such as non-farm equipments, average value of financial assets....etc. Thus, the behaviour of CVs seem to support the contention that the sampling design is conducive for arriving at reliable estimates of physical assets, land-owned....etc. which are related to the land owned by the household but not for estimating other variables which do not bear such a relationship with the land owned.

Table 6 : Coefficient of Variation of All-India Estimates of Some Selected Items :
NSS 37th Round (Rural)

Category of households	Coefficient of variation (%) of estimates of												
	Items	1	2	3	4	5	6	7	8	9	10	11	12
all households		1.98	4.41	1.02	1.22	1.25	1.27	2.38	7.76	3.74	1.41	5.73	5.20
Households in asset holding classes (Rs.)													
Upto 1000		11.82	19.53	2.18	6.09	4.97	8.85	5.71	14.36	19.99	5.28	47.12	34.47
1,000 - 5,000		4.77	7.22	0.72	2.10	1.48	3.54	3.40	8.00	7.91	2.27	18.88	12.04
5,000 - 10,000		4.56	6.43	0.39	1.56	1.57	2.47	5.14	10.29	5.68	2.29	15.15	10.70
10,000 - 20,000		4.06	6.88	0.34	1.08	1.42	1.99	5.93	8.23	4.89	1.92	14.81	9.46
20,000 - 50,000		2.78	4.39	0.33	.74	1.30	1.39	3.06	14.66	2.88	1.79	10.45	11.10
50,000 - 1 lakh		3.04	4.83	0.31	.70	1.57	1.64	3.31	18.09	3.38	2.06	7.28	7.31
1 lakh - 2 lakhs		2.99	4.98	0.64	.94	1.92	1.62	2.98	12.19	7.58	2.14	11.55	9.88
5 lakhs - 10 lakhs		4.63	13.88	1.87	1.90	6.49	26.91	6.39	23.64	13.18	5.49	13.18	13.38
10 lakhs - 20 lakhs		12.12	64.45	2.70	9.36	8.76	18.75	12.43	60.26	26.75	21.20	24.13	32.03
20 lakhs and above		0.00	39.08	4.44	5.66	16.99	26.55	26.23	91.32	34.57	21.56	31.43	50.28
Household type:													
Cultivators		2.04	4.67	1.08	1.26	1.30	1.05	2.40	8.98	3.74	1.49	5.91	4.85
non-cultivators		4.58	7.23	3.20	5.35	3.58	12.32	9.57	15.57	17.08	3.48	19.92	13.34

<u>Item Nos.</u>	<u>Items</u>
1	Proportion of households reporting cash dues payable
2	Value of cash dues payable per household
3	average value of total assets per household
4	average value of land owned per household
5	average value of residential building per household
6	average value of livestock and poultry per household
7	average value of agricultural implements per household
8	average value of non farm equipments per household
9	average value of transport equipments per household
10	average value of durable assets per household
11	average value of all shares per household
12	average value of other financial assets per household

Source: Sarvekshana Vol.X, No.1, July 1986.

Section IV : Behaviour of the Sampling Variance over the Three Rounds

Ignoring the question of the shift from simple random sampling to stratified systematic sampling in the selection of households within villages for the reasons given in Section II and III this section focusses attention on the behaviour of sampling variance over the three rounds. The expression for the sampling variance of the estimator Y (total of some item) based on a two stage sampled with error at both the stages following Murthy (1967) may be written as:

$$V(Y) = N^2 M^2 (1-f) \frac{b}{n} + \frac{N}{n} \sum_{i=1}^N M_i^2 (1-f_i) \frac{w_i}{m_i}$$

$$\text{where } \sigma_b^2 = \frac{1}{N-1} \sum_{i=1}^N \left(\frac{M_i}{M} \bar{Y}_i - \bar{Y} \right)^2, \quad \sigma_{w_i}^2 = \frac{1}{M_i-1} \sum_{j=1}^{M_i} (Y_{ij} - \bar{Y}_i)^2$$

$$f = n/N, \quad f_i = m_i/M_i \quad \text{and} \quad M = \sum_{i=1}^N M_i/N$$

N = the number of villages, M_i = the number of households in the i th village

Assuming that values of σ_b^2 , $\sigma_{w_i}^2$, M_i and N are the same for the three rounds of the survey we may write,

$$V(\hat{Y})_{1961} = \left(\frac{1}{2057} - \frac{1}{N} \right) N^2 M^2 \sigma_b^2 + \frac{N}{2057} \sum_{i=1}^N M_i^2 \left(1 - \frac{40}{M_i} \right) \frac{w_i}{40}$$

$$V(\hat{Y})_{1971} = \left(\frac{1}{8458} - \frac{1}{N} \right) N^2 M^2 \sigma_b^2 + \frac{N}{8458} \sum_{i=1}^N M_i^2 \left(1 - \frac{12}{M_i} \right) \frac{w_i}{12}$$

$$V(\hat{Y})_{1981} = \left(\frac{1}{7718} - \frac{1}{N} \right) N^2 M^2 \sigma_b^2 + \frac{N}{7718} \sum_{i=1}^N M_i^2 \left(1 - \frac{8}{M_i} \right) \frac{w_i}{8}$$

As N is very large the first term on the right hand side (between variance) would decrease by approximately 76 percent between 1961 and 1971, by 73 percent between 1961 and 1981, and would increase by about 10 percent between 1971 and 1981.

The second term on the right hand side (within variance) would decrease or increase depending upon the value of M_i 's. Assuming all the M_i 's to be equal to M and giving numerical values to M it may be seen that for large M the within variance decreases in 1971 compared to 1961 and for small values of M within variance increases (Table 7).^{3/}

Table 7 : Behaviour of the within Variance (1961 to 1981)

$M_i = M$	Within variance as a percentage of the base year value		
	1971/1961	1981/1971	1981/1961
500	86	166	143
200	95	168	160
150	102	169	172
100	119	172	204

Combining the results regarding the behaviour of between variance and within variance it may be concluded that the sampling variance for 1981 would be considerably higher than that for 1971 for all values of M_i .

^{3/} The average values of M_i are below 200 in 1971 for all the states except Andhra Pradesh, Kerala and Tamil Nadu.

As regards the comparison between 1971 and 1961, it would depend on the ratio between between variance and within variance and the values of M_i .

As is evident from Table 8, for larger values of M_i and larger share of within variance in the total the sampling variance comes down between 1961 and 1971. But for values of M_i around 150 the reduction in sample variance is negligible (between 3.2 to 4.5 percent). At the same time for the same ratios the sampling variance in 1981 is considerably higher (over 25 percent at the least) than the sampling variance in 1961 (for M_i greater than 500 also).

When the share of between variance in the total dominates, the sampling variance comes down rather sharply between 1961 and 1971. However, even in such cases the reduction is related to the values of M_i , in the sense that for larger values of M_i the reduction is sharper and for smaller values of M_i the reduction is smaller.

Thus, the behaviour of sampling variance crucially depends on the value of M_i and the ratio of between variance to within variance. As the value of M_i is around 150 in most of the states the reduction in the number of sample households does not bring down the within variance over the various rounds of the survey but raises it mildly between 1961 and 1971 and rather sharply between 1971 and 1981. Coming to the ratio of between variance to within variance, although $\frac{\sigma_b^2}{\sigma_w^2}$ may be smaller compared to $\frac{\sigma_b^2}{\sigma_w^2}$ with the presence of N^2 in the first term of the expression for sampling variance would boost the share of the between variance in the total.

Table 8 : Behaviour of the Sampling Variance (1961 to 1981)

M1 = M	Sampling Variance as a Percentage of the base year value							
	Ratio between and within variance,							
	1:4		1:3		3:1		4:1	
	1971/1961	1981/1961	1971/1961	1981/1961	1981/1961	1981/1961	1971/1961	1981/1961
500	84	129	83.5	125.5	39.5	56.0	36.4	47.8
200	91.2	142.6	90.25	138.25	41.75	60.25	38.2	51.2
150	96.8	152.2	95.5	147.25	43.5	63.25	39.6	53.6
100	110.4	177.8	108.25	171.25	47.75	71.25	43.0	60.0

Hence, any sharp increase in the number of first stage units (here, villages) would bring down the sampling variance considerably.

However, because of the arguments provided in Section II above it is evident that the sampling variance could be higher in the stratified case and hence in actuality the reduction may not be high.

Conclusions

On the whole, though the shift in sampling strategy between 1961 and 1971 is able to generate reliable estimates of one component of the variable, viz., the amount or quantity per reporting household, the estimates of the other component, viz., incidence or proportion of households reporting, seem to be less reliable. Other empirical evidence also seem to suggest that the estimates are not all that reliable.

CHAPTER 3

INTERREGIONAL VARIATIONS IN THE SIZE OF FORMAL AND INFORMAL CREDIT MARKETS

In order to investigate the factors underlying variations across regions in the size of the formal and informal credit markets in India, we carried out a regression analysis using cross section data from the early 1970's. These data pertain to 59 regions into which the country has been classified by the National Sample Survey (NSS). These NSS regions are subregions of each State where groups of contiguous districts have been combined. Each region consists of groups of districts which have similarities with respect to population density and cropping pattern. On average, each NSS region comprises 4 or 5 districts. A fairly large amount of data exists, particularly for the early 1970's, at the NSS region level on several aspects, such as demographic characteristics, institutional and economic variables. The Reserve Bank of India's All-India Debt and Investment Survey which is carried out in collaboration with the NSS organisation also presents information by NSS regions. It has therefore been possible to carry out a cross section interregional analysis. Fortunately, data on a large number of variables for NSS regions had been compiled by P. Bardhan (1983), and we have been able to draw upon this rather rich data base in our analysis.

We have used a simple measure of the size of the formal and informal credit market, which is the average amount of cash dues outstanding from formal and informal credit agencies per sample household. Formal sector credit agencies comprise: Government, Cooperative Banks, Commercial Banks, Insurance and Provident Fund. Cash dues outstanding from these agencies have been clubbed together. Similarly, for the informal sector, we have added the amount outstanding due to landlords, agriculturist moneylenders, professional moneylenders, traders, relative/friends and others. Explanatory variables are of four types: measures of economic dynamism, agrarian structure variables, agroecological conditions and finance-related variables. The variables used in the analysis are the following:

1. Dependent Variables (Size of Credit Market)

CLFS = Cash dues outstanding per household from formal sector

CLIS = Cash dues outstanding per household from informal sector

2. Explanatory Variables

(a) Measures of Economic Dynamism

GROWTH = Average Exponential annual growth rates of output of 19 major crops in a region over the period 1962-65 to 1970-73. Source of data is Bhalla and Alagh (1979)

OPH = Output per Hectare; Value (in rupees) of output per hectare of 19 major crops averaged for 1970-71 to 1972-73. Source: Bhalla and Alagh.

WELLIRR = Proportion of area irrigated by wells and tubewells in total area irrigated.
Source: Season and Crop Reports.

FHA = Value (in rupees) of fertiliser input per hectare in 19 major crops. Source: Fertiliser Statistics, Bhalla and Alagh.

GEMHA = Gross Capital Expenditure (Rs.) on agricultural implements, machinery and transport equipment per hectare of 19 major crops.
Source: All India Debt and Investment Survey, 1971-72 (AIDIS)

(b) Agrarian Structure Variables

LFARMP = Proportion of total rural households operating land above 7.5 acres.
Source: AIDIS, 1971-72.

WMPROP = Proportion of Farm Wage labourers in rural labour force by usual status for males age 15-59, NSS 27th Round (1972-73)

POVP = Percentage of Rural Population in 1972-73 below poverty line defined as Rs.15 per capita per month in 1960/61 prices

LSPROP = Percentage of leased-in area to total area operated; NSS 26th Round (1971-72) Land Holdings Survey.

URR = Percentage Rural Unemployment rate on basis of daily time disposition data from NSS 27th Round (1972-73)

ASTPOOR = Proportion of Rural Households possessing Rs.1,000 or less as on June 30, 1971, AIDIS 1971-72.

(c) Agroecological Conditions

IRRP = Percentage of Owned land which is irrigated as on June 30, 1971 AIDIS, 1971-72.

SOIL = Index of soil rating in region, RBI Bulletin Oct. 1969.

(d) Finance-Related Variables

COPROP = Proportion of Households Reporting Borrowing from Cooperative Banks, AIDIS 1971-72.

HHEPROP = Proportion of Households reporting household expenditure as purpose of cash dues outstanding, AIDIS 1971-72.

- CAFPROP = Proportion of Households reporting Capital expenditure on farm business as purpose of cash dues outstanding, AIDIS 1971-72.
- CUFPROP = Proportion of Households reporting current expenditure on farm business as purpose of cash dues outstanding, AIDIS 1971-72.
- CANFPROP = Proportion of Households reporting Capital expenditure on non-farm business as purpose of cash dues outstanding, AIDIS 1971-72.
- CUNFPROP = Proportion of Households reporting current expenditure on non-farm business as purpose of cash dues outstanding, AIDIS 1971-72.

Results of Regression Analysis

We have attempted a simple ordinary least squares regression analysis to unravel the possible underlying factors which determine variations in the size of the formal and informal sector credit markets in a comparative perspective. The logic of our investigation was to systematically examine the impact of four sets of variables on the size of the credit market. It appeared reasonable to expect that the degree of economic dynamism exhibited by a region would have an important bearing on the extent of credit market in the region. Accordingly we selected some alternative measures of economic dynamism, as listed above. These included growth rates in output recently experienced in the region, the level of gross output per hectare, the quality of irrigation in the region, the degree of fertilizer use, and the gross capital expenditure on agricultural implements and machinery and transport equipment. The expected relationship between agrarian dynamism and the size of the formal credit market was generally positive. A priori, however, it was not possible

to indicate which way the relationship would go in the case of the informal sector.

Similarly we have explored the association between the size of the formal and informal credit market and variables reflecting the agro-ecological characteristics of the region (irrigation base and soil type), and characteristics of the agrarian structure (such as proportion of large farmers, the proportion of farm wage labourers in the rural labour force, the percentage of rural population below the poverty line, the extent of tenancy, the unemployment rate in rural areas, and the proportion of households who are asset-poor. We would expect that the size of the credit market would be positively associated with the proportion of large farmers and negatively with poverty measures. It was of course difficult a priori to judge which particular measures would be most closely associated with size of credit market. This could only be settled empirically.

We have also tried to investigate the statistical impact of certain aspects of credit use, such as the proportion of households reporting outstanding dues by purpose of borrowing, whether for household expenditure, or for expenditure on farm and non farm business under current and capital items. We also wanted to examine whether the formal and informal credit markets had a competitive relationship by including the proportion of households reporting borrowing from Cooperative banks which is an important formal sector credit agency in the rural areas.

The plan of analysis is as follows. At first separate set of regressions were done using variables for each type, viz., economic dynamism,

agrarian structure, agroecological conditions, and finance-related variables. Finally, a "combined regression" was done using selected variables from each set. In this manner we have sought to identify the explanatory power of different categories of variables, as well as to identify the impact of specific variables of each type on the size of formal and credit markets. For purposes of comparison we have retained the same specification of equations for both formal and informal sectors. The regressions have been carried out separately for four separate groups of borrowers: viz. all households, cultivators, agricultural labourers and all non-cultivators. The R^2 is reported and adjusted for degrees of freedom.

The results are reported below: Figures in parentheses are t-ratios.

I. All Households

Ist set (Economic Dynamism Variables)

$$\begin{aligned}
 \text{I (1) CLFS} &= 37.86 + 12.26 \text{ GROWTH} + 3.41 \text{ GEMHA} + \\
 &\quad (.94) \quad (4.77)^* \quad (2.41)^* \\
 &\quad 1.11 \text{ WELLIRR} + 531.19 \text{ FHA} - 0.03 \text{ OPH} \\
 &\quad (2.13) \quad (.58) \quad (.74) \\
 \bar{R}^2 &= 0.51
 \end{aligned}$$

$$\begin{aligned}
 \text{I (2) CLIS} &= 243.73 + 46.68 \text{ GROWTH} + 0.84 \text{ GEMHA} + \\
 &\quad (3.19) \quad (4.82)^* \quad (.03) \\
 &\quad 2.73 \text{ WELLIRR} + 4160.73 \text{ FHA} - 0.14 \text{ OPH} \\
 &\quad (2.76)^* \quad (2.39)^* \quad (1.82) \\
 \bar{R}^2 &= 0.38
 \end{aligned}$$

Figures with * are significant

2nd set (Agrarian Structure Variables)

$$\begin{aligned}
 \text{I (3) CLFS} &= 218.82 - 1.19 \text{ ASTPOOR} - 0.60 \text{ LSROP} + \\
 &\quad (3.36) \quad (1.42) \quad (.30) \\
 & 2.79 \text{ LFARMP} - 3.80 \text{ POVP} - 2.83 \text{ URR} + \\
 &\quad (2.17)^* \quad (3.64)^* \quad (.72) \\
 & 4.36 \text{ WMPROP} \\
 &\quad (1.36)
 \end{aligned}$$

$$\bar{R}^2 = 0.23$$

$$\begin{aligned}
 \text{I (4) CLIS} &= 522.26 + 2.53 \text{ ASTPOOR} - 0.60 \text{ LSROP} + \\
 &\quad (4.97) \quad (0.55) \quad (0.19) \\
 & 6.08 \text{ LFARMP} - 6.31 \text{ POVP} - 0.40 \text{ URR} + \\
 &\quad (2.94)^* \quad (3.75)^* \quad (0.06) \\
 & 1.47 \text{ WMPROP} \\
 &\quad (0.29)
 \end{aligned}$$

$$\bar{R}^2 = 0.30$$

3rd set (Agroecological Variables)

$$\begin{aligned}
 \text{I (5) CLFS} &= 101.02 + 0.12 \text{ SOIL} + 2.32 \text{ IRRP} \\
 &\quad (1.70) \quad (0.17) \quad (1.57)
 \end{aligned}$$

$$\bar{R}^2 = 0.01$$

$$\begin{aligned}
 \text{I (6) CLIS} &= 185.93 + 1.04 \text{ SOIL} + 7.23 \text{ IRRP} \\
 &\quad (2.00) \quad (.62) \quad (3.13)^*
 \end{aligned}$$

$$\bar{R}^2 = 0.15$$

4th Set (Finance-Related Variables)

$$\begin{aligned}
 \text{I (7) CLFS} &= 8.63 - 3.25 \text{ HHEPROP} - 6.65 \text{ CUFPROP} + \\
 &\quad (0.25) \quad (2.56) \quad (2.41)^* \\
 & 18.14 \text{ COPROP} + 15.89 \text{ CAFPROP} \\
 &\quad (7.98)^* \quad (4.06)^*
 \end{aligned}$$

$$\bar{R}^2 = 0.66$$

$$\begin{aligned}
 \text{I (8) CLIS} &= -85.29 + 11.62 \text{ HHEPROP} - 19.75 \text{ CUFPROP} + \\
 &\quad (1.30) \quad (4.88)^* \quad (3.80)^* \\
 &\quad 0.76 \text{ COPROP} + 31.99 \text{ CAFPROP} \\
 &\quad (1.18) \quad (4.34)^* \\
 \bar{R}^2 &= 0.58
 \end{aligned}$$

Combined Regression

$$\begin{aligned}
 \text{I (9) CLFS} &= 81.21 - 3.84 \text{ HHEPROP} + 1.78 \text{ (E-03) OPH} - \\
 &\quad (1.71) \quad (3.36)^* \quad (.05) \\
 &\quad 2.86 \text{ POVP} + 14.05 \text{ COPROP} - 1.32 \text{ IRRP} + \\
 &\quad (4.66)^* \quad (5.89)^* \quad (1.46) \\
 &\quad 0.68 \text{ WELLIRR} + 2.69 \text{ WMPROP} + 9.71 \text{ CAFPROP} + \\
 &\quad (1.52) \quad (2.28)^* \quad (2.65)^* \\
 &\quad 10.40 \text{ GROWTH} + 434.69 \text{ FHA} + 68 \text{ GEMHA} + \\
 &\quad (2.00)^* \quad (.64) \quad (1.11) \\
 &\quad 0.24 \text{ LFARMP} \\
 &\quad (.22) \\
 \bar{R}^2 &= 0.79
 \end{aligned}$$

$$\begin{aligned}
 \text{I (10) CLIS} &= -2.93 + 10.89 \text{ HHEPROP} + 8.53 \text{ (E-03)} \\
 &\quad (.03) \quad (4.57) \quad (0.12) \\
 &\quad \text{OPH} - 3.82 \text{ POVP} - 2.35 \text{ COPROP} + 2.57 \text{ IRRP} - \\
 &\quad \quad (2.98)^* \quad (.47) \quad (1.38) \\
 &\quad 0.34 \text{ WELLIRR} + 0.52 \text{ WMPROP} + 10.40 \text{ CAFPROP} + \\
 &\quad (.37) \quad (.71) \quad (1.36) \\
 &\quad 12.13 \text{ GROWTH} + 1118.62 \text{ FHA} - 0.47 \text{ GEMHA} + 4.75 \text{ LFARMP} \\
 &\quad (1.11) \quad (.79) \quad (.37) \quad (2.03)^* \\
 \bar{R}^2 &= 0.68
 \end{aligned}$$

II. Cultivators

1st Set (Economic Dynamism Variables)

$$\begin{aligned}
 \text{II (1) CLFS} &= 78.17 - 5.13 \text{ GROWTH} + 4.21 \text{ GEMHA} + \\
 &\quad (1.13) \quad (.59) \quad (3.44)^* \\
 &\quad 3.15 \text{ WELLIRR} + 2524.5 \text{ FHA} - .06 \text{ OPH} \\
 &\quad (3.53)^* \quad (1.60) \quad (.95) \\
 \bar{R}^2 &= 0.51
 \end{aligned}$$

$$\begin{aligned}
 \text{II (2) CLIS} &= 213.42 + 45.40 \text{ GROWTH} - 0.12 \text{ GEMHA} + \\
 &\quad (2.27) \quad (3.81) \quad (.07) \\
 &\quad 3.91 \text{ WELLIRR} + 6397.9 \text{ FHA} - 0.11 \text{ OPH} \\
 &\quad (3.20)^* \quad (2.98)^* \quad (1.15) \\
 \bar{R}^2 &= 0.40
 \end{aligned}$$

2nd Set (Agrarian Structure Variables)

$$\begin{aligned}
 \text{II (3) CLFS} &= 198.04 - 0.42 \text{ ASTPOOR} - 0.88 \text{ LSPROP} + \\
 &\quad (1.90) \quad (.09) \quad (.27) \\
 &\quad 7.91 \text{ LFARMP} - 6.10 \text{ POVP} - 1.81 \text{ URR} + \\
 &\quad (3.86)^* \quad (3.66)^* \quad (.29) \\
 &\quad 10.06 \text{ WMPROP} \\
 &\quad (1.97) \\
 \bar{R}^2 &= 0.33
 \end{aligned}$$

$$\begin{aligned}
 \text{II (4) CLIS} &= 562.77 + 7.91 \text{ ASTPOOR} + 0.10 \text{ LSPROP} + \\
 &\quad (4.44) \quad (1.42) \quad (.03) \\
 &\quad 8.22 \text{ LFARMP} - 9.28 \text{ POVP} + 0.31 \text{ URR} - \\
 &\quad (3.29)^* \quad (4.57)^* \quad (.04) \\
 &\quad 0.21 \text{ WMPROP} \\
 &\quad (.03) \\
 \bar{R}^2 &= 0.34
 \end{aligned}$$

3rd Set (Agroecological Variable)

$$\begin{aligned}
 \text{II (5) CLFS} &= 145.15 + .83 \text{ SOIL} + 3.61 \text{ IRRP} \\
 &\quad (1.42) \quad (.46) \quad (1.42) \\
 \bar{R}^2 &= .02
 \end{aligned}$$

$$\begin{aligned}
 \text{II (6) CLIS} &= 161.98 + 2.20 \text{ SOIL} + 9.88 \text{ IRRP} \\
 &\quad (1.45) \quad (1.01) \quad (3.55)^* \\
 \bar{R}^2 &= 0.22
 \end{aligned}$$

4th Set (Finance Related Variables)

$$\begin{aligned}
 \text{II (7) CLFS} &= -33.59 - 3.23 \text{ HHEPROP} + 18.57 \text{ COPROP} + \\
 &\quad (.89) \quad (1.98)^* \quad (5.50)^* \\
 &\quad 15.79 \text{ CAFPROP} - 6.15 \text{ WFPROP} \\
 &\quad (3.64)^* \quad (1.87)^* \\
 \bar{R}^2 &= 0.75
 \end{aligned}$$

$$\text{II (8) CLIS} = 140.88 + 3.82 \text{ HHEPROP} - 5.45 \text{ COPROP} +$$

$$(1.86) \quad (1.17) \quad (0.80)$$

$$33.70 \text{ CAFPROP} - 10.60 \text{ CUFPROP}$$

$$(3.87)^* \quad (1.60)$$

$$\bar{R}^2 = 0.32$$

$$\text{II (9) CLFS} = 46.27 - 3.36 \text{ HHEPROP} + 13.79 \text{ COPROP} -$$

$$(0.80) \quad (3.17)^* \quad (5.91)^*$$

$$0.02 \text{ OPH} - 4.00 \text{ POVP} + 5.13 \text{ WMPROP} +$$

$$(0.40) \quad (4.67) \quad (3.19)^*$$

$$0.16 \text{ IRRP} + 0.74 \text{ LFARMP} + 1.35 \text{ GEMHA} +$$

$$(0.14) \quad (0.51) \quad (1.82)^*$$

$$1.53 \text{ WELLIRR} + 220.50 \text{ FHA} + 8.79 \text{ GROWTH} +$$

$$(2.43)^* \quad (0.25) \quad (1.16)$$

$$6.93 \text{ CAFPROP}$$

$$(1.92)^*$$

$$\bar{R}^2 = 0.86$$

$$\text{II (10) CLIS} = 236.70 + 4.84 \text{ HHEPROP} - 12.50 \text{ COPROP} +$$

$$(2.38) \quad (2.65)^* \quad (3.13)^*$$

$$0.06 \text{ OPH} - 7.32 \text{ POVP} + 2.07 \text{ WMPROP} +$$

$$(0.74) \quad (4.99)^* \quad (0.82)$$

$$0.51 \text{ IRRP} + 9.72 \text{ LFARMP} - 0.15 \text{ GEMHA} +$$

$$(0.25) \quad (3.90)^* \quad (0.12)$$

$$0.28 \text{ WELLIRR} + 4751.64 \text{ FHA} + 2.98 \text{ GROWTH} +$$

$$(0.26) \quad (3.08)^* \quad (0.23)$$

$$16.23 \text{ CAFPROP}$$

$$(2.63)^*$$

$$\bar{R}^2 = 0.73$$

Agricultural Labourers1st Set (Economic Dynamism Variables)

$$\begin{aligned}
 \text{III (1) CLFS} &= 8.43 + 1.68 \text{ GROWTH} + 0.07 \text{ GEMHA} + \\
 &\quad (1.99) \quad (3.13)^* \quad (0.9) \\
 &\quad 0.10 \text{ WELLIRR} + 255.35 \text{ FHA} - 0.01 \text{ OPH} \\
 &\quad (1.81)^* \quad (2.65)^* \quad (3.07)^* \\
 \bar{R}^2 &= 0.30
 \end{aligned}$$

$$\begin{aligned}
 \text{III (2) CLIS} &= 202.46 + 34.55 \text{ GROWTH} + 0.70 \text{ GEMHA} + \\
 &\quad (3.76) \quad (5.06)^* \quad (.73) \\
 &\quad 1.19 \text{ WELLIRR} + 2512.14 \text{ FHA} - 0.18 \text{ OPH} \\
 &\quad (1.71) \quad (2.04)^* \quad (3.46)^* \\
 \bar{R}^2 &= 0.37
 \end{aligned}$$

2nd Set (Agrarian Structure Variables)

$$\begin{aligned}
 \text{III (3) CLFS} &= 17.61 - 0.54 \text{ ASTPOOR} + 0.13 \text{ LSPROP} + \\
 &\quad (3.20) \quad (2.22)^* \quad (.77) \\
 &\quad 0.15 \text{ LFARMP} - 0.32 \text{ POVP} + 0.13 \text{ URR} + \\
 &\quad (1.40) \quad (3.65)^* \quad (.39) \\
 &\quad 0.50 \text{ WMPROP} \\
 &\quad (1.85)^* \\
 \bar{R}^2 &= 0.29
 \end{aligned}$$

$$\begin{aligned}
 \text{III (4) CLIS} &= 342.17 - 3.74 \text{ ASTPOOR} + 1.09 \text{ LSPROP} + \\
 &\quad (5.34) \quad (1.33) \quad (.55) \\
 &\quad 3.68 \text{ LFARMP} - 4.18 \text{ POVP} - 5.92 \text{ URR} + \\
 &\quad (2.91)^* \quad (4.08)^* \quad (1.53) \\
 &\quad 2.19 \text{ WMPROP} \\
 &\quad (.70) \\
 \bar{R}^2 &= 0.47
 \end{aligned}$$

3rd Set (Agroecological Variables)

$$\text{III (5) CLFS} = 5.98 - 0.05 \text{ SOIL} + 0.29 \text{ IRRP}$$

$$(1.17) \quad (.51) \quad (2.29)^*$$

$$\bar{R}^2 = .05$$

$$\text{III (6) CLIS} = 107.33 - 0.24 \text{ SOIL} + 5.10 \text{ IRRP}$$

$$(1.62) \quad (.21) \quad (3.10)^*$$

$$\bar{R}^2 = 0.12$$

4th Set (Finance Related Variables)

$$\text{III (7) CLFS} = 1.63 + 0.03 \text{ HHEPROP} + 0.53 \text{ CUFPROP} +$$

$$(.72) \quad (.46) \quad (.27)$$

$$4.15 \text{ COPROP} + 0.22 \text{ CAFPROP}$$

$$(9.20)^* \quad (.10)$$

$$\bar{R}^2 = 0.60$$

$$\text{III (8) CLIS} = 7.52 + 3.15 \text{ HHEPROP} + 30.57 \text{ CUFPROP} +$$

$$(.20) \quad (2.51)^* \quad (.89)$$

$$30.73 \text{ COPROP} + 68.43 \text{ CAFPROP}$$

$$(4.12)^* \quad (1.83)^*$$

$$\bar{R}^2 = 0.40$$

Combined Regression

$$\text{III (9) CLFS} = 8.29 - 0.07 \text{ HHEPROP} - 0.13 \text{ POVP} - 5.07$$

$$(1.87) \quad (.89) \quad (2.03)^* \quad (1.45)$$

$$(E-03) \text{ OPH} - 0.09 \text{ CAFPROP} + 3.75 \text{ COPROP} +$$

$$(.05) \quad (8.20)^*$$

$$0.16 \text{ WELLIRR} + 0.12 \text{ WMPROP} - 0.02 \text{ IRRP} -$$

$$(3.26)^* \quad (.99) \quad (.21)$$

$$0.09 \text{ GEMHA} + 0.72 \text{ GROWTH} - 0.07 \text{ LFARMP} + \\ (1.7) \quad (1.38) \quad (.66)$$

$$77.91 \text{ FHA} \\ (1.13)$$

$$\bar{R}^2 = 0.72$$

$$\text{III(10) CLIS} = 172.99 + 2.87 \text{ HHEPROP} - 3.07 \text{ POVP} - \\ (2.53) \quad (2.41)^* \quad (3.07)^*$$

$$0.03 \text{ OPH} + 41.17 \text{ CAFPROP} + 20.71 \text{ COPROP} - \\ (0.54) \quad (1.27) \quad (2.94)^*$$

$$0.59 \text{ WELLIRR} - 1.28 \text{ WMPROP} + 1.84 \text{ IRRP} + \\ (.80) \quad (.70) \quad (1.33)$$

$$0.72 \text{ GEMHA} + 1.82 \text{ GROWTH} + 3.83 \text{ LFARMP} + \\ (.88) \quad (.23) \quad (2.47)^*$$

$$148.72 \text{ FHA} \\ (.14)$$

$$\bar{R}^2 = 0.63$$

IV. All Non-Cultivators

1st Set (Economic Dynamism Variables)

$$\text{IV (1) CLFS} = 20.41 + 1.40 \text{ GROWTH} + 0.19 \text{ GEMHA} + 0.31 \text{ WELLIRR} - \\ (1.86) \quad (1.01) \quad (0.98) \quad (2.21)^*$$

$$11.33 \text{ FHA} - 6.84 \text{ (E-03) OPH} \\ (.05) \quad (.63)$$

$$\bar{R}^2 = 0.11$$

$$\text{IV (2) CLIS} = 183.47 + 36.19 \text{ GROWTH} + 0.66 \text{ GEMHA} + \\ (3.55) \quad (5.53)^* \quad (0.73)$$

$$1.75 \text{ WELLIRR} + 1494.9 \text{ FHA} - 0.13 \text{ OPH} \\ (2.61)^* \quad (1.27) \quad (2.56)^*$$

$$\bar{R}^2 = 0.41$$

2nd Set (Agrarian Structure Variables)

$$\begin{aligned}
 \text{IV (3) CLFS} &= 51.32 + 0.62 \text{ ASTPOOR} + 0.37 \text{ LSPROP} + \\
 &\quad (3.83) \quad (1.05) \quad (.89) \\
 &\quad 0.42 \text{ LFARMP} - 0.59 \text{ POVP} - 0.40 \text{ URR} - \\
 &\quad (1.56) \quad (2.75)^* \quad (.49) \\
 &\quad 0.74 \text{ WMPROP} \\
 &\quad (1.22) \\
 \bar{R}^2 &= 0.21
 \end{aligned}$$

$$\begin{aligned}
 \text{IV (4) CLFS} &= 385.29 - 0.08 \text{ ASTPOOR} - 0.09 \text{ LSPROP} + \\
 &\quad (5.58) \quad (.03) \quad (.04) \\
 &\quad 3.26 \text{ LFARMP} - 2.57 \text{ POVP} - 3.16 \text{ URR} - \\
 &\quad (2.39)^* \quad (2.33)^* \quad (.76) \\
 &\quad 4.49 \text{ WMPROP} \\
 &\quad (1.33) \\
 \bar{R}^2 &= 0.36
 \end{aligned}$$

3rd Set (Agroecological Conditions)

$$\begin{aligned}
 \text{IV (5) CLFS} &= 35.25 - 0.15 \text{ SOIL} + 0.21 \text{ IRRP} \\
 &\quad (2.87) \quad (.70) \quad (.69) \\
 \bar{R}^2 &= -0.02
 \end{aligned}$$

$$\begin{aligned}
 \text{IV (6) CLIS} &= 155.34 - 0.54 \text{ SOIL} + 5.40 \text{ IRRP} \\
 &\quad (2.41) \quad (.47) \quad (3.37)^* \\
 \bar{R}^2 &= 0.14
 \end{aligned}$$

4th Set (Finance Related Variables)

$$\begin{aligned}
 \text{IV (7) CLFS} &= 12.25 + .17 \text{ HHEPROP} - 1.46 \text{ CUNFPROP} + \\
 &\quad (1.22) \quad (.43) \quad (.52) \\
 &\quad 5.89 \text{ COPROP} + 2.23 \text{ CANFPROP} \\
 &\quad (3.2)^* \quad (0.91) \\
 \bar{R}^2 &= 0.17
 \end{aligned}$$

$$\begin{aligned}
 \text{IV (8) CLIS} &= -85.94 + 8.80 \text{ HHEPROP} + 13.83 \text{ CUNFPROP} + \\
 &\quad (1.83) \quad (4.84)^* \quad (1.05) \\
 &\quad 11.14 \text{ COPROP} + 20.79 \text{ CANFPROP} \\
 &\quad (1.30) \quad (1.81)^* \\
 \bar{R}^2 &= 0.45
 \end{aligned}$$

Combined Regression

$$\begin{aligned}
 \text{IV (9) CLFS} &= 43.58 + 0.12 \text{ HHEPROP} + 1.63 \text{ CANFPROP} + \\
 &\quad (2.43) \quad (.27) \quad (.82) \\
 &\quad .01 \text{ OPH} - 0.77 \text{ POVP} - 0.10 \text{ GEMHA} - \\
 &\quad (1.03) \quad (3.45)^* \quad (.55) \\
 &\quad 0.34 \text{ IRRP} + 4.94 \text{ COPROP} + 0.19 \text{ WELLIRR} - \\
 &\quad (1.07) \quad (2.36)^* \quad (1.10) \\
 &\quad 0.14 \text{ WMPROP} - 2.63 \text{ GROWTH} - 183.35 \text{ FHA} + \\
 &\quad (.31) \quad (1.40) \quad (.75) \\
 &\quad 0.17 \text{ LFARMP} \\
 &\quad (.46) \\
 \bar{R}^2 &= .31
 \end{aligned}$$

$$\begin{aligned}
 \text{IV(10) CLIS} &= 83.54 + 6.55 \text{ HHEPROP} + 18.18 \text{ CANFPROP} - \\
 &\quad (1.06) \quad (8.49)^* \quad (2.10)^* \\
 &\quad 0.04 \text{ OPH} - 1.14 \text{ POVP} + 0.21 \text{ GEMHA} + \\
 &\quad (.75) \quad (1.15) \quad (1.25)
 \end{aligned}$$

2.06 IRRP - 0.53 COPROP - 0.21 WELLIRR -
 (1.50) (.06) (.28)

3.52 WMPROP + 5.66 GROWTH + 431.32 FHA +
 (1.77)* (.69) (.40)

2.73 LFARMP
 (1.67)*

$$\bar{R}^2 = 0.60.$$

The main findings of this exercise are the following:

(a) By and large, the explanatory variables give a reasonable clear picture of the factors associated with interregional variations in the size of the formal and informal credit markets. As a group, the economic dynamism subset and the finance related subset of variables explain a considerable proportion of the variation, as reflected in the R^{-2} (R^2 adjusted for degree of freedom). This is the case for all households and cultivators. In the case of case of agricultural labourers and all non-cultivator categories, the agrarian structure subset and the finance-related subset of variables appear to be have relatively greater explanatory power. Agroecological Variables are uniformly unimportant.

(b) Comparing the results for the formal and informal credit markets, we notice that overall, for all households, the economic dynamism subset explains a higher proportion of the variation with respect to the formal credit market, whereas the agrarian structure variables are more important for the informal credit market. The finance related variables seem slightly better able to explain variations with respect to the formal

sector, though they are important also in the case of the informal sector. The agroecological variables appear unimportant. Nevertheless IRRP is an important variable in the case of informal sector credit. In the Combined regression, we are able to explain 80% of the variation in the case of formal sector credit and 68% of the variation in informal sector credit in the case of all households.

In the case of cultivators, the results are similar to all households. However, there is a notable difference with respect to the finance-related variables, which are able to explain a much lower proportion of variation in informal credit size in case of cultivators as compared with all households. On the other hand, these variables are more important in the case of formal sector credit for cultivators, as compared with all households.

For agricultural labourers, it is noteworthy that agrarian structure variables play a remarkable role in explaining variations in informal credit, whereas finance related variables are relatively more important in explaining formal sectors credit.

In case of all non-cultivators, it is interesting to note the relatively high explanatory power of economic dynamism (of agriculture) and agrarian structure variables in regressions pertaining to the informal sector. Finance related variables are also more powerful in explaining informal sector credit, which contrast with the findings for agricultural labourers, eventhough the latter form a component of non-cultivators.

The other important component category is artisans. In the combined regression, the selected variables explain a much higher proportion of the variation in case of the informal sector compared with the formal sector for non cultivators.

Examining the particular independent variables and the parameter estimates, the following conclusions emerge.

- (c) In the regression equations with economic dynamism, GROWTH, GEMHA and WELLIRR are positive and highly significant in the case of all households for formal credit, whereas for informal credit, it seems strongly associated positively with growth rate, WELLIRR and also FHA. It is worth noticing that OPH, which measures the level of output per hectare, is not important. For cultivators, the important variables showing positive association with formal credit are GEMHA and WELLIRR, which is as expected, but neither GROWTH nor OPH seem to matter. For informal credit, GROWTH is positively associated with cash dues outstanding per household, and so are FHA (which is interesting) and WELLIRR.

In the case of agricultural labourers, a rather intriguing finding is that while GROWTH is positively and significantly associated with both formal and informal credit, there is a negative and significant association with the level of output per hac. OPH, a variable closely related with the cropping pattern. Also significant and positive is FHA for both formal and informal credit. For all non-cultivators, the results are broadly similar, particularly for informal credit.

- (d) For the regression equations using agrarian structure variables, the general picture which emerges from all regressions is that there is a strong, positive association between both formal and informal credit and LFARMP (the proportion of large farmers in rural population) and a strong, negative association with POVP (the percentage of population below the poverty line). This pattern holds for all Households and Cultivators. In the case of Agricultural Labourers, the proportion of asset poor (ASTPOOR) is important for formal credit, along with POVP, both being negatively and significantly associated. This underscores the strong negative association between formal sector credit and economic status. For non-cultivators, only POVP is significant. Otherwise the picture is consistent with that for all households and cultivators. It is also interesting that for cultivators, formal credit is also associated significantly with the WMPROP (Proportion of farm wage labour in male labour force), suggesting perhaps the importance of modern capitalist farmers in access to formal credit.
- (e) With regard to the agroecological variables, the only feature which is striking is that IRRP which measures the irrigation base of a region is positively and significantly associated with informal credit for all categories of borrowers, viz., all households, cultivators, agricultural labourers and all non-cultivators. However, for formal credit, it does not make much difference. This probably reflects the fact that the existence of formal sector credit institutions in regions reflect government's policy decisions whereas informal credit is more closely dependent on demand factors which are likely to be affected by the irrigation base.
- (f) In the regression equations using finance related variables, the picture is mixed. For formal sector credit, all the specified variables are significant in the case of all households and for

cultivators. However, for agricultural labourers and all non-cultivators, there is not the case. This suggests that for the latter categories, purpose of borrowing is not statistically significant. However, the impact of Cooperative credit is important. It is worth noting that formal credit is negatively and significantly associated with proportion of households reporting expenditure on household account (HHEPROP) for all households, whereas for informal credit, the association is positive. Both formal and informal sector credit are positively related with capital expenditure and negatively with the current expenditure on farm business. A broadly similar picture holds for cultivators. The role of informal credit financing of household expenditure is, however, not significant for cultivators, which is an exception to the general picture. The other feature worth noting is that there is no indication from cross section data of the 1970's, that formal and informal credit play a mutually competitive role. This is because COPROP is nowhere negatively associated with CLIS with statistically significant parameter estimates.

- (9) In the combined regression, perhaps due to multicollinearity a number of variables no longer have significant parameter estimates. However, the broad picture is confirmed. For all households, we find formal sector credit strongly and positively related with GROWTH, CAFPROP, COPROP, and WMPROP, as expected. The negative association with POVP and HHEPROP is also significant as earlier.

The picture is very similar for cultivators, except that WELLIRR is also significant and positive. For agricultural labourers and all non-cultivators, we see once again the robust negative association with poverty for formal credit, and the role of cooperatives in channelling funds to these borrower (COPROP) is positive.

For informal credit, we notice in all cases the strong, robust positive association with HHEPROP and the negative association with POVP (except for all noncultivators), and also a strong positive association with LFARMP. With the other variables, the picture is mixed. In the combined regression for cultivators, there is a negative, significant association with COPROP, which appears to suffer a competitive relationship between formal and informal credit of cultivators, a conclusion slightly at variance with the earlier regression result. We notice, for cultivators, the confirmation of positive association between informal credit and capital expenditure as purpose of borrowing (CAFPROP) and FHA (fertilizer per hectare).

For agricultural labourers, the association between size of informal credit and household expenditure (HHEPROP) is positive, and with POVP is negative. These are robust. Of all the agrarian structure variables, LFARMP appears most important. For all noncultivators, the picture is similar, with respect to HHEPROP. But we notice also the positive association of informal credit with capital expenditure is non-farm business.

Conclusion

In conclusion, we may observe that the cross section regressions using data by NSS regions shed some interesting light on the factors associated with regional variations in formal and informal credit markets, as measured by cash dues outstanding per household. Certain broad patterns

emerge, as well as differences in the impact of broad categories of explanatory variables, with respect to broad class of borrower households. By and large, economic dynamism is positively related with credit, and poverty is negatively associated. Co-operative Credit is very important for agricultural labourers and non-cultivators. There are differences in the purposes of borrowing through formal and informal credit, with respect to household expenditure, but capital expenditure is an important purpose of borrowing also for informal credit. There is only a slight indication that formal and informal sector credit are mutually competitive, only in the case of cultivators. In general, this does not seem to be the case in the cross section evidence.

CHAPTER 4

THE STUDY AREAS

4.1 Introduction

As noted earlier, there are major data gaps on certain crucial aspects of the informal credit markets (ICMs) which form focus of the present study. The Reserve Bank of India has collected voluminous data on various aspects of rural credit through the successive rounds of the All India Debt and Investment Survey (AIDIS). However, published reports of the AIDIS do not include data on some important questions such as terms and conditions of informal credit transactions including interest rate, security, duration of loans, modes of loans disbursement and repayment, etc. linkage with the formal sector, inter-linkage of credit with transactions in other markets, resource mobilisation, allocative efficiency and equity impact, etc. all of which have a great bearing on the role and functioning of the ICM. Other sources of secondary data are generally deficient. Therefore, scholars in the past in their pursuit of an understanding of the various dimensions of the ICM had to take recourse to in-depth micro-studies. In the present study also we have conducted some micro-studies in an attempt to gather data of the requisite type and detail. Due to certain constraints of time and cost, primary data collection had to be limited to a few selected villages in Kerala and Tamil Nadu. While local conditions vary from State to State, the

rural scene of Kerala has some distinguishing features: (i) Kerala has a comparatively more commercialised agriculture. (ii) The commercial banks had made their entry into rural areas of the State from comparatively early times. (iii) The vast majority of the villages here have a functioning cooperative society, which in recent years have been conducting deposit mobilisation campaigns. (iv) Recent years have witnessed migration of large number of Keralites to Gulf States, bringing in a sizeable flow of remittances. (v) Finance Companies have mushroomed during last few years extending their operations into rural areas. Four villages from Kerala were covered under this study. For comparative purposes, we have also included two villages from the neighbouring State, Tamil Nadu, the rural areas of which differ so much from a typical Kerala village. Though the limitation of the geographical coverage would not warrant any generalisation, the data from these diverse settings would, we hope, shed some fresh light on the issue of our concern.

4.2 Selection of the Study Areas

The study areas were selected keeping in view the various parameters under consideration such as size and structure of ICM, interest rate and other terms and conditions of the loan transactions, etc. While the agricultural sector as a whole claims a large proportion of credit, both formal and informal, the demand for credit would vary according to the cropping pattern, the level of commercialisation and modernization of agriculture. There are significant interregional variations in these aspects. Certain socio-economic traditions like landlord-tenant,

employer-employee relations or inter-linkage of credit with non-credit transactions also differ from one region to another. The role of informal lenders in resource mobilisation depends on (a) the availability of savings and (b) alternative channels for the disposition of savings including organised credit institutions and their terms. In this connection, the flow of remittance from Gulf migrants, referred to earlier, and the impressive rise in the volume bank deposits in certain parts of Kerala should be one useful criteria for the selection of study areas. Thus, in terms of rate of increase in commercial bank deposits, Malappuram, Trichur, and Trivandrum are ahead of the other districts in Kerala, growth of deposits during the period 1975-80 exceeding 100 percent; Alleppey, Cannanore, Kozhikode and Quilon with a medium growth of deposits ranging from 80 to 100 percent; and the remaining districts viz., Palghat, Kottayam, Idukki and Ernakulam with a growth rate of deposits below 80 percent. At the first stage of sampling, therefore, we have selected Malappuram and Trichur from the first group, Quilon from the second group and Kottayam from the third group. In terms of cropping pattern, Malappuram and Trichur have a comparatively high proportion of the area under rice, viz., 31.88 and 51.59 percent respectively, as against, 18.32 and 15.52 in Kottayam and Quilon. and the State average of 28.74 percent in 1977-78. Non-food crops cover a large proportion, 48 percent, of the total cropped area in Kottayam, of which rubber alone accounts for 23.32 percent. Quilon falls between the above two extreme cases Trichur and Kottayam, with about 41 percent of the cropped area under non-food crops. It may also be noted that these selected districts are distributed among the three topographical divisions of the State, viz., lowland, midland and highland.

At the stage two of a sampling, one taluk was selected from each district, taking into consideration the major crops grown, the proportion of cultivators in total workers, and also rate of increase in commercial bank deposits. Accordingly, the taluks of Tirur (Malappuram) Chawakkad (Trichur), Kanjirappally (Kottayam) and Quilon (Quilon) were identified as the most eligible candidates according to the norms we had in mind. Keeping the same considerations in mind, we selected the sample villages from each taluk. They are Thirunavaya, Thalikulam, Anikkad and Ezhukone from Malappuram, Trichur, Kottayam and Quilon district respectively.

In the selection of the two villages from the State of Tamil Nadu it was not possible to capture fully the diversity of its regional patterns. The cropping pattern of the State is very diverse, combining rice, coarse cereals, oilseeds, fruits and vegetables, sugar cane, cotton, etc. Of these, cereals covered 59 percent of the total cropped area in the State, and oil seeds 17 percent, and the remaining crops shared the rest of the area. Initially two districts, whose cropping pattern broadly corresponded with the overall State pattern, were identified, viz., Madurai and Thirunelveli. In both the districts, rice and coarse cereals together accounted for 50 to 60 percent of the total cropped area as against a little over 61 percent for Tamil Nadu as a whole. All cereals together covered around three-fourths of the cropped area in the two districts. The rest of the area is distributed among oil seeds, pulses, chillies, banana, cotton, etc. In terms of growth rate of agriculture, Madurai belongs to the medium growth districts (1.5 - 4.5 percent) and Thirunelveli to the group of low growth districts (0 - 1.5 percent), according to the estimates by Bhalla and Alagh.

The work-participation rates (1981), the proportion of workers - main workers and marginal workers - to total population in the selected districts from Kerala was in the range of 25 to 30 percent, while that in the two Tamil Nadu districts came to about 43 percent. These rates more or less correspond to the State average, except in the case of Malappuram which is significantly lower than the Kerala State average.

4.3 The Study Areas : An Overview

(i) Thirunavaya, the sample village from the northern district Malappuram, is located about 15 KM from Tirur, the taluk headquarters. Muslims constitute the majority of the population. Agriculture seems to be the main source of livelihood, judged in terms of the proportion of workers engaged in agriculture as cultivators and agricultural labourers. Rice, coconut, and arecanut are the principal crops. Although tenancy has been formally abolished in the State, a few cases of it have been observed in this village. In recent years, this village has witnessed a high rate of emigration of labour, mainly unskilled labour, to the Gulf states. Approximately, one fifth of the households in the village have a member or two working in the Gulf states and have been receiving remittances to supplement their incomes. A high proportion of the landholdings is small, below 25 cents, which keeps down the income from agriculture.

(ii) Thalikulam village is located about 23 KM from Trichur, the district headquarters. Topographically, the village falls in the low-land region, nearer the Arabian sea. Hindus, (mainly Ezhavas) constitute

the majority of the population, followed by Muslims, the ratio between the two being around 2:1, Christians form a small proportion. Agriculture, household industry, fishing, and trade constitute the major occupations of the households. Rice and coconuts are the principal crops. The average size of holdings is small. The village has had a long tradition of sending out labour to other parts of India like Bombay, and also other countries. Members of the Ezhava community used to migrate to Sri Lanka from early times, while the majority of Muslim emigrants ended up in the Middle East countries. Thus, remittances from the emigrants became one of the principal sources of income for the local community. The housing conditions, furnishing, household equipments, the quality of dress worn by local people, etc. which are obvious during a casual visit to the village, give one the impression of a moderately high standard of living. This is one side of the coin. The other side comprises the coastal belt where the dominant population group consists of Muslims, and among these households, except the lucky ones who have one or two members working in the Gulf countries, fishing is the main occupation. Their dwellings, domestic facilities, etc. present a sharp contrast.

(iii) Anikad in Kottayam taluk is located around 35 IM from the headquarters of Kottayam district. The village is situated in the high-land region. A high proportion of the population here are the Christians. Agriculture is the principal occupation. The average size of holdings is comparatively large. About 60 percent of the cultivated area is under rubber, and the rest under miscellaneous crops including pepper, coconut, arecanut, tapioca (cassava), etc. The dominance of cash crops

reflects a comparatively high degree of commercialisation of agriculture. The cropping pattern and the intensity of cultivation operations lead to a relatively high level of employment and wage rates for agricultural labourers.

(iv) The fourth sample village from Kerala is Ezhukone in Quilon taluk of Quilon district. It is situated in the midland region of southern Kerala. Agriculture, industry and construction are the major occupations. Rice, coconut, and tapioca are the leading crops of the village. Being dominated by food crops, the degree of commercialisation is rather low. The average size of holdings is smaller than in Anikad, but compares favourably with that in the two other villages. There are a few industrial establishments in and around this area which provide regular employment opportunities to the local labour. One or two female members from every household would be employed in the cashew factories. The Kallada Project, an irrigation scheme currently under implementation, also provide employment to local workers. The combined effect of the above has made a favourable impact on household income.

(v) Mookuperi village is in Tiruchendur Taluk in Tirunelveli district of Tamil Nadu. It is located 24 KM away from Tiruchendur town, the taluk headquarters. It is well connected by bus services with the major towns in the district. Being in close proximity with Nazerath, a leading commercial centre, the village is influenced by the urban life style. Majority of the households belong to Nadar (Christian) community, a dominant business class in the district. Conversion to Christianity from early times had made a positive impact on the socio-economic conditions

of the people in this village. For instance, the literacy rate, including that of females, is about twice the State average. Agriculture used to be the dominant occupation, and paddy (rice) the principal crop, grams (pulses) being grown on the dry land as a subsidiary crop. Due to frequent failure of monsoon and the resultant crop failures, the cultivation of gram has been neglected. The available irrigation facilities are inadequate; the tanks and canals are fast drying up. In sum, there has been a steady decline in agriculture, and more and more households have been shifting to non-agricultural occupations. At present, practically no household is getting a steady income from agriculture. Very few households cultivate rice and that too only during one season. Hence, neither cultivators nor agricultural labourers can depend solely on agriculture for their livelihood. Some of them have set up business enterprises outside, in some district headquarters like Tirunelveli, Madurai and Coimbatore and major cities like Madras, Bangalore, Hyderabad, etc. These trends are reflected in the outmigration of people from Mookuperi.

(vi) Vilpatti, the other sample village from Tamil Nadu is 6 KM away from the Taluk headquarters, Kodaikanal. It is a typical traditional village with the caste system still very strongly entrenched. The village comprises six clusters of households of different caste denominations. The Brahmins are at the top of the social hierarchy. The Reddiars, Pillai and Mudaliars in that order constitute the dominant economic groups. Earlier there used to be certain caste-specific division of labour, with Pillais who owned a greater proportion of land engaged in cultivation, and Mudaliars specialising in various business activities, particularly trade. Of late, the latter's monopoly of trade has been eroded. Agriculture

remains the major occupation in this village. In the early sixties, foodgrains, such as rice and vegetables like potato, cabbage, carrot and beans formed the crop mix, and ten years later the crop mix changed in favour of coffee and banana. Later still, when pests and diseases affected these two crops, vegetables have staged a come back. However, the decimation of more profitable crops like coffee has caused considerable damage to the village economy.

4.4 Household Characteristics

(i) The selected villages from Kerala are larger in size than those from Tamil Nadu, both in terms of area and population. The average area of the two Tamil Nadu villages comes to 6.01 KM², as against 14.94 KM² for the four Kerala villages. The average population as of 1971 for the former came to about one third of the latter group of villages, i.e. 5454 and 15116 respectively. The average size of households is also smaller in the case of the former group. (See Table 4.1).

(ii) The literacy and educational levels in the selected villages broadly correspond to the averages for the two States. Thus, in three out of the four Kerala sample villages, the proportion of literate and educated persons falls in the range of 64 to 72 percent, as per the 1971 Census data, the State average being a little above 60 percent. One of the Kerala samples deviating from this pattern is Thirunavaya, the village with a predominantly Muslim population. At the time of the field survey conducted by us, it was noted that only 50 percent of the children of the school-going age were attending schools, the rest staying back and attending to household duties or other work. Similarly, the

Table 4.1 : Demographic Characteristics of Selected Villages (1971)

Particulars	Kerala				Kerala	Tamil Nadu		Tamil-Nadu
	Anikad	Ezhukone	Thirunavaya	Thalikulam		Vilpatti	Mookuperi	
Area KM ²	22.18	15.77	10.93	10.89	..	7.15	4.87	
<u>Population</u>								
Persons	11877	18661	13376	16751		7535	3373	
Male	6051	9337	6436	7763		3898	1436	
Female	5826	9324	6940	8988		3637	1937	
Sex ratio	963	999	1078	1158	1076	933	1349	978
Number of Households	2026	3959	2021	2622		1663	629	
Average size of Households	5.9	6.1	6.6	6.4	6.0	4.5	4.1	5.3
Density per KM ²	535	1183	1224	1538	549	1054	692.61	317

Source: District Census Hand Books (1971) Part X - B

Note: Data for 1981 not readily available.

proportion of literate and educated persons in Vilpatti, one of the sample villages from Tamil Nadu, was 38.91 percent, pretty close to the State average for 1971, viz., 39.46 percent. But, the corresponding proportion for the other village, Mookuperi, was much higher, viz., 65.05 percent even by 1961. Further, unlike in the rest of Tamil Nadu or other parts of rural India (except Kerala) there is no male-female difference in the level of literacy in Mookuperi. It may be noted that while literacy rate among females in Vilpatti was less than one half that of males, in Mookuperi female literacy rate exceeds male literacy rate in the former (Table 4.2), notwithstanding the fact that the data for the latter village is one of the earlier census. The proximity of the village to Nazerath, a major commercial centre and exposure to urban life style and motivation, and availability of educational institutions within the village including a high school, may have contributed to this differential achievement.

Table 4.2 : Proportion of Literature and Educated Persons (1971)
Percent

Particulars	Kerala				Kerala	Tamil Nadu		Tamil Nadu
	Anikad	Ezhukone	Thiru- navaya	Thali- kulam		Vil- patti	Mooku- peri 1961	
Persons	71.91	69.20	46.93	64.17	60.42	38.91	65.05	39.46
Male	64.73	74.93	54.76	76.55	-	53.41	65.18	-
Female	69.09	63.47	38.67	53.47	-	23.3	64.95	-

(iii) The work participation rate in the sample villages from Kerala, 27.02 percent in 1971, is fairly close to the overall State average of 29.12 percent. While in one of the Tamil Nadu sample villages, Vilpatti, the ratio came to 39.3 percent, about four percentage points above that State's average, in the second village, Mookuperi, the ratio falls more than ten percentage points below the State average. (Table 4.3).

Table 4.3 : Work participation Rate in the Selected Villages, 1971

Particulars	Anikad	Ezhukone	Thirunavaya	Thalikulam	Kerala	Vilpatti	Mookuperi	Tamil Nadu
Total population	11877	18661	13376	16751		7535	3373	
Workers	3180	5441	3519	4326	29.12	2964	857	35.7
Percent of workers	26.8	29.2	26.3	25.8		39.3	25.4	
Non workers	8697	13220	9857	12425		4571	2516	

Source: District Census Hand Book (1971) Part XB

(iv) As for the occupational pattern of the workers, we notice considerable inter-regional variation. Agriculture constituted the leading occupation in all the selected villages. The proportion of workers in this activity, cultivators and agricultural labourers, fell in the range of 29 to 68 percent of total workers. Forestry and fishing together

accommodated a significant proportion of total workers in Thalikulam and Vilpatti, viz., 19 and 44 percent respectively. Thus, the primary sector accounted for more than 50 percent of the total workers in three of the Kerala and one of the Tamil Nadu villages. Manufacturing, including repairs and servicing, accounts for around one quarter of the workers in two of the Kerala and one of the Tamil Nadu villages (Table 4.4).

In brief: Thirunavaya and Thalikulam used to have a comparatively low work-participation rates. Among the workers in the early seventies, more than two thirds were engaged in agriculture in the former village, while agricultural labour, fishing and trade constituted the main avenues of employment in the latter. One thing in common between these two villages is that the opening of an outlet in the Middle East in recent years provided some relief, however partial and temporary, to some households whose members could find employment there. The inflow of remittances steadily increased which attracted credit institutions, both formal and informal, into these two villages. Whether this newfound affluence from Gulf migration has made any favourable and durable impact on the village economies is doubtful. However, the fact that the majority of the households stayed outside the new stream affected their aspirations and generated greater demand for credit to meet the incidental expenses connected with Gulf migration such as securing passport, Visa, NOC and other documents and commissions to the agents. Anikad is comparatively more developed. A distinct characteristic of Anikad is the dominance of commercial crops such as rubber, tea and coffee. The average size of holdings is larger than that of the other selected villages. Hired labour and

Table 4.4 : Occupational Pattern of Selected Villages (1971)

Occupation	Anikad	Ezhukone	Thirunavaya	Thalikulam	Vilpatti	Mookuperi (1961)
1. Cultivation	1255(39.4)	2047(37.6)	819(23.3)	255(5.9)	820(27.6)	262(30.6)
2. Agricultural labour	914(28.7)	685(12.6)	1487(42.3)	1015(23.5)	545(18.4)	10(1.2)
3. Livestock, forestry, fishing	224(7.0)	104(1.9)	79(2.2)	826(19.1)	1298(43.7)	21(2.4)
4. Manufacturing, process- ing, repairs, servicing	206(6.5)	1414(26.0)	351(10.0)	1022(23.6)	127(4.3)	260(30.3)
a. Household industry	65	94	84	375	94	191
b. Other than household industry	41	1322	267	647	33	69
5. Construction	14(0.4)	52(1.0)	25(0.7)	56(1.3)	68(2.3)	23(2.7)
6. Trade & Commerce	132(5.8)	230(4.2)	236(6.7)	663(15.3)	59(2.0)	129(15.0)
7. Transport, storage and communication	48(2.1)	128(2.4)	109(3.1)	126(2.9)	26(0.9)	10(1.2)
8. Other services	387(12.1)	779(14.3)	413(11.7)	363(8.4)	87(2.9)	142(16.6)
Total workers	3180(100)	5441(100)	3519(100)	4326(100)	2964(100)	857(100)

Source: Same as in Tables 1 and 2

Figures in brackets stand for percentages

purchased inputs in their production raise their costs of cultivation. Employment opportunities and wage rates are also naturally higher. The cropping pattern raises the need for credit all of which is not met by formal credit institutions, and informal agencies come to play not an insignificant role here. Ezhukone falls midway between Anikad at one end and Thirunavaya and Thalikulam at the other. With higher literacy level, proximity to major industrial towns, greater employment opportunities outside agriculture, unionisation of labour and higher wages, the level of income is higher. The role of informal lenders appears to be less dominant. Both the Tamil Nadu villages are predominantly agricultural areas; foodgrains, vegetables, fruits etc. cover the major portion of the total cropped area. Lack of adequate irrigation and continuous failure of rainfall for a few years have adversely affected the major crops. The shifting of area from cereals to other crops like vegetables and fruits in one of the villages, instead of saving the situation, has made the cultivators increasingly dependent on external market and middlemen for their marketing. With the setback suffered by agriculture and decline in employment opportunities and incomes of both cultivators and agricultural labourers, the majority of the households have been experiencing great financial strain. And the villagers have come to lean heavily on informal sources of credit, even for meeting essential consumption expenditure.

4.5 Profile of the Credit Markets in the Study Areas

As in other rural areas, there is a felt-need for credit in our study areas also. Agriculture being the principal occupation in the majority

of the selected villages, and given its seasonal nature, the need for credit on the part of the concerned households is obvious. This is particularly so in the case of small holders who constitute the majority and who don't have adequate resources to self-finance their cultivation operations and household consumption expenditure. Agricultural and other categories of wage labour add up to a significant proportion of total workers whose dependence on credit for consumption purposes should also be rather heavy. In almost all the selected villages, there is a network of formal credit institutions including commercial banks and cooperative societies. Against this backdrop we shall examine the supply of credit and their main sources in our study areas.

(i) In Thirunavaya village, branches of two scheduled commercial banks - South Malabar Grameen Bank and South Indian Bank - are located, besides one Service Cooperative Society and office of the Urban Cooperative Bank. Out of the 68 sample households, 24, over 35 percent, have reported having credit transactions with commercial banks, mostly from South Malabar Grameen Bank. Some of the respondents mentioned too much of formalities and delay in the sanctioning of loans on the part of commercial banks as the reasons for not approaching them. However, most of our respondents were favourably impressed with the performance of the South Malabar Grameen Bank, their prompt disbursal of loans and their liberal terms. The Service Cooperative Society is reported to be currently facing bankruptcy, mainly caused by high default rate. The Urban Cooperative Bank advances long term loans on the basis of security such as landed property, but the small holders, not to speak of agricultural and other labourers, have little

access to this source of credit. They, therefore, approach friends and relatives, traders and moneylenders. Friends and relatives are a major source of credit, most of which is interest free. Kinship relations, religious beliefs, and inflow of remittances from the Gulf are the factors underlying this. There are a few resident professional moneylenders who advance loans usually on sound security. Seventeen of the sample households have borrowed from them. Usually, the loans are small in size, and repayment made in instalments. However, interest rate is high. For example, a loan of Rs.200 is taken, and is to be repaid in 10 weekly instalments at the rate of Rs.25, Rs.50 being the interest for 10 weeks. For another, the loan amount is Rs.100, repayment Rs.125, and duration just 2½ months. There is another category of moneylenders, Tamilians operating in this villages. They advance loans to cultivators and small traders, and the size of loans is generally small, ranging from Rs.50 to Rs.200. They don't insist on any security other than personal surety. The rates of interest charged by them are also high. For instance, when a loan of Rs.100 is granted, Rs.3 is deducted towards the charge on credit card, and the borrower has to pay Rs.12.50 every week for ten weeks, or a total of Rs.125; i.e. Rs.25 as interest for less than three months.

(ii) In Thalikulam, besides the State Bank of India, the branches of four scheduled commercial banks, viz., Catholic Bank, Lord Krishna Bank, Canara Bank and Nedungadi Bank, are functioning. Out of the 83 sample households, 18 have borrowed from the Commercial banks. The State Bank of India is the main conduit through which loans under the Intensive Rural Development Programme (IRDP) are disbursed. Though a few of the households are reported to have availed of loans for self-employment

- major component of IRDP - many of our respondents were not happy with the functioning of this office, particularly the attitude and behaviour of its employees. A few cases of corruption and malpractices have also been reported. For instance, one lady availed of a loan under IRDP, and the last instalment paid to a village official was not credited to her account. She went from pillar to post and finally she drew a blank. In the case of the other commercial banks, loans are mainly based on the pledge of gold ornaments, and such transactions are confined to one or two days a week. Further, the formalities associated with these institutions are also felt to be too rigid. For instance, to get a loan on gold pledge, the borrower has to be introduced to the branch manager by an employee in the branch, which obviously erects a barrier to the poor peasants or fishermen in the village. One respondent reported that he had to pay a bribe of Rs.400 to the field officer of a scheduled commercial bank to obtain a loan. The erstwhile Thalikulam Service Society, a multi-purpose cooperative society, was converted into a cooperative bank in 1968. Majority of the households in Thalikulam were said to be members. The volume of its transactions is impressive. According to the Secretary, outstanding loans at present (early September 1987) came to Rs.19 lakhs;* the annual loan disbursements came to about Rs.12 lakhs; and default rate works out to 25 percent. It is also worth mentioning that this cooperative bank has been successful in attracting deposits; as of 1987 it came to Rs.25 lakhs. However, there is a feeling that the credit needs of the villagers, especially the comparatively weaker segments like fishermen,

* 1 lakh = 100000

are not adequately met. Naturally, the credit needs of such disadvantaged groups are met by informal lenders. The low income groups like fishermen and agricultural labourers have to depend on the informal lenders, because the formal credit institutions are inaccessible to them. The commercial banks, for instance, will have downed their shutters by the time the fishermen return from the sea in the afternoon. Moreover, the informal lenders are more easily accessible and more flexible in the procedures. There are quite a few professional moneylenders, more than ten of them, in and around Thalikulam village. It is the unprecedented inflow of remittances which has led to the emergence of this group of moneylenders, the so-called finance companies. They are either individual enterprises or partnerships. The moneylenders attract deposits by offering higher interest rates than the commercial banks. However, the actual rate of interest paid on the deposits was not easy to ascertain. Ofcourse, they also charge high interest on the loans given. For instance, one respondent reported his availing of a loan from one of these finance companies. The nominal value of the loan was Rs.5000, of which only Rs.4500 was disbursed and the balance of Rs.500 was accounted as interest on the loans to be repaid in 100 instalments within 100 days. Most of them also charge compound interest after the duration of the loans, usually, three months. In some cases, the moneylenders receive a bond, a promisory note, on a blank paper, and subsequently inflate the principal. Besides professional moneylenders, there are also some trader-cum-moneylenders here. For example, a group of fishing boat owners among fishermen community in the coastal areas of this village advance loans to fishermen who in turn

commit their labour services to the former till the loan is fully repaid. This is a type of labour-tieing arrangement observed also in other fishing villages of Kerala. (See Plateau, Muricken, et.al). There are also a few fish merchants or wholesale dealers in fish who advance loans to owners of fishing boats on the understanding that the catch is sold to the former at a price unilaterally fixed by him, often lower than the price prevailing in the market at the time of sale. Landlords/agriculturist moneylenders constitute another source of credit to households belonging to the lower income groups like agricultural labour. The borrowers hypothecate the yields from their coconut trees which the lenders collect till the loan is repaid; by fixing the price of coconuts at a lower rate than the going market price, the lenders realise a high rate of interest going up to 25 percent. Some Tamilians have migrated to this village, mainly the coastal area; they locally known as "Annachi", lend money to the housewives, who are presumed to be more trustworthy. The loan amounts are small, duration short, say, two months, repayment in weekly instalments, but interest rate pretty high. One respondent informed that he had to pay Rs.25 towards interest on a loan of Rs.100 of two months' duration.

(iii) In Anikad also, the offices of some commercial banks are functioning. The State Bank of Travancore disburses loans under the IRDP and also loans for agricultural purposes on the security of landed property as well as gold. Though the nominal rate of interest is low, the real cost is high because the borrower has to produce the necessary title deeds duly certified by the village office. Sanctioning of a loan

also involves considerable delay. The amount of loan will be limited to a comparatively low proportion of the value of the land as officially assessed. A few scheduled banks like the Central Bank, and South Indian Bank, have their branches in the vicinity of Anikad. Apparently, very few villagers approach these institutions, as they are less easily accessible. The Land Mortgage Bank at Kottayam is a major source of credit to rubber cultivators of this village. Anikad Regional Farmers' Co-operative Society is the most important formal credit institution here providing both short term and long term loans to agriculturists. The Society enjoys refinance facility from National Bank for Agricultural and Rural Development (NABARD) and the District Co-operative Bank. Currently, the Society's loan transactions amount to Rs.17 lakhs a year. In addition to productive credit for agriculture, the Society also disburses loans for house construction, education, marriage and other household expenditures. Notwithstanding this network of formal credit institutions, there is a large chunk of unmet demand for credit which is being met by informal credit agencies such as professional moneylenders, agriculturist moneylenders and traders. We gather that at present only one professional moneylender is active in the village. Started in 1982 with an initial capital of Rs.1 lakh, its growth is quite impressive; currently, its working capital and total deposits exceed Rs.18 lakhs each, while the annual loan transactions exceed Rs.15 lakhs. The loans are mostly on security of gold, for short duration, viz., 3 months, and interest rate 36 percent after 3 months compound interest is levied. The agriculturist moneylenders give loans on gold or personal security, and charge different rates of interest from different customers. Their business is restricted

to borrowers in whom they have full trust and confidence. Rubber traders constitute another important source of credit available to rubber cultivators. There are a dozen in Anikad village. They lend money to rubber growers on the condition that the latter sell the produce to them within one month the loan is advanced. It is reported that the loan is settled at the time of delivery of rubber valued at the prevailing price and that no interest is charged. Apparently, the trader is keen to secure the produce even at a cost. There are also a few other moneylenders whose clientele are mainly petty traders. The loans are small and are repaid in daily instalments collected by the lenders' agents who go round. The interest rates are so high that these lenders are locally known as "double edged swords", more usurious than the so-called "blade companies". Most of the respondents interviewed had serious reservations about the various informal lenders.

(iv) Ezhukone has an office of the Indian Overseas Bank, a public sector bank. However, the bank is of limited accessibility to the majority in the village. Whereas gold is the only acceptable security in the possession of the common folks, loans on gold security are not transacted on all working days. Further, our respondents had reservations about the attitude and behaviour of the bank employees. The Ezhukone Service Co-operative Bank, on the other hand, transacts a large volume and range of business. It disburses loans for agricultural and other business purposes. Agricultural loans are short term loans, one year, and carry an interest of 13 percent of this one-half is subsidised if the loan is repaid in one year, but failing which full interest and penalty of

3 percent will have to be borne by the borrower. Educational loans are also granted to the members of the cooperative, the rate of interest being 18 percent. The loan amount is differentiated according to the level of schooling of the intended beneficiaries. Loans are also sanctioned for the purposes of house construction, medical expenses, marriage ceremony, etc. Besides, credit transactions, the cooperative runs a stationary shop where clothing and various household articles are sold on credit to the members. The duration of such credit purchases is 3 months, and involves an interest of 18 percent. Ezhukone Service Cooperative Bank apparently is meeting the credit needs of a large section of the local community by the scale and diversity of its operations. A branch of the District Cooperative Bank is also functioning here; its main function is extending finance to other cooperative societies in this village. Informal credit agencies like professional moneylenders, agriculturist and other non-professional moneylenders, are also operating in the village and its neighbourhood. There is one professional moneylender in Ezhukone village. It is a partnership firm and designated as a 'bank'. It is of very recent origin (1983) with an initial capital of Rs.1.5 lakhs. This bank attracts deposits on a large scale from all groups including larger farmers, households with their members working in the Middle East, retired government employees, etc. By now, the deposits have reached Rs.10 lakhs. The bank offers an attractive interest rate, say 24 percent, to its depositors. The bank claims to have lent Rs.28 lakhs during the last two years, loans for other than agricultural purposes, carry an interest of 30 percent; on agricultural loans they charge a lower interest. The bank has adopted

a differential interest rate scheme, discriminating between different clients, apparently on the principle of each according to his ability! The poor are given interest-free loans, cultivators lower interest, less than 30 percent, while a few contractors are charged 46 percent. There are a few professional moneylenders in the adjacent villages, Arumurikada and Kundara, whom residents of Ezhukone approach in times of need. These moneylenders extend loans on gold security. However, they do not receive deposits.

(v) Vilpatti, one of the sample villages from Tamil Nadu, is served by six branches of commercial banks under the public sector, located in the adjacent places and two cooperative agricultural credit societies located within the village. A comparatively high proportion of households, 34 out of 76, reported loan transactions with the above formal credit institutions. The commercial banks, advanced loans for productive purposes such as purchase of milch animals, reclamation of land, cultivation operation, etc. However, as noted earlier, agriculture in this village suffered a major set back in recent years, with the result that the default of loans from these institutional sources mounted. The banks, reluctant to take effective recovery measures, have almost suspended the grant of fresh loans. Under the Group Loan Scheme, each one of the borrowers stands as guarantee for the other members' debt and could not receive a fresh loan unless all the members of the group have cleared their debts. There has been some relaxation of this rule in recent years so that if one member has repaid his loan, he can get a fresh loan. Certain instances of corruption, malpractices and favouritism have been brought to our notice.

For example, in the case of less influential households, the services of an agent are necessary to get a loan, a part of which has to be shared with the agent. The cooperative societies have come to play a leading role in meeting the credit needs of the local community. The informal lenders like professional moneylenders, agriculturist moneylenders, traders and commission agents fill the gap. There is only one resident professional moneylender, but the households approach five others residing outside. Three of these are registered moneylenders; they are partnership firms under the category of finance companies. However, they do not accept deposits. They follow three patterns of lending, (1) daily kandu,* (2) weekly kandu, and (3) monthly kandu. In all the three systems, the duration of loans is the same, viz., 2½ months. Loans are given for different purposes, and mode of repayment also varies. In the case of loans given to traders, repayment is made through daily collections. In the case of labourers, the system followed is weekly kandus, and to farmers loans under weekly and monthly kandus are advanced. The loans are given on the basis of recommendations by some influential persons in the locality, and no security is insisted upon. The rate of interest varies from 36 to 120 percent per annum. Vegetable wholesale dealers located at Madurai and Kodaikanal advance loans on condition that the borrower sells his crop to the merchant creditor at the price decided by the latter. A typical instance is that of a farmer who took a loan from a vegetable merchant hypothecating his crop, viz., banana. When it was ready for sale, he delivered the first consignment of 100 bananas and the trader adjusted

* Kandu means mode of payment

its value to the loan at Rs.130 when the going market price was Rs.300. There is only one agriculturist moneylender here. He lends mostly to small farmers, agricultural labourers, and traders. He resorts to certain questionable practices like overstating the amounts lent, paying lower wages to labourers who have borrowed from him, overpricing the fertilizer sold to the farmers who purchase it on credit basis, etc. However, labour-tieing arrangement is not common here. Cultivators do make wage advances to agricultural labourers usually for less than one month, depending on the requirement of labour. The wage advance is adjusted to the weekly wage bill.

Incidentally, thanks to frequent failure of monsoon in recent years, agriculture has ceased to be a profitable or viable activity. Some of the erstwhile cultivators have moved over to professional money-lending. Infact, most of the moneylenders serving this village started this activity only recently, say from 1986.

(vi) For Mookuperi, the Urban Cooperative Bank is one formal credit institution located within the village. There is also an agricultural credit society. They together do not meet a very significant proportion of the credit needs of this village. Infact, only a little over 10 percent of the sample households have had borrowings from them. Inaccessibility, too rigid formalities, favouritism, and delay in sanctioning of loans are frequent complaints about the above credit institutions. A distinctive feature of this village is the comparatively high proportion of credit met from friends and relatives. Thanks to the inflow

of remittances from migrants well settled elsewhere, there are at any time a few households with surplus funds to lend to their relatives and friends. Availability of interest-free loans from this source is its principal attraction. Hence, rather than taking loans from formal and informal credit agencies, a good proportion of the householders approach their relatives and friends who have cash to spare. The system works as a kind of mutual aid arrangement. There are no professional moneylenders here; however, there are some 10 registered moneylenders at Nazerath, an adjacent town from whom the households in this village borrow. The moneylenders lend to all occupational groups; they lend only on the pledging of gold jewellery. The size of loan varied from Rs.100 to Rs.1000, depending on the value of security. The interest rate is in the range of 30 to 120 percent. There is one resident agriculturist moneylender who lends on the pledge of household articles like cycles, utensils, etc.

To sum up: The selected villages, by and large, share the salient features of a typical village in their respective States. Agriculture is the main source of livelihood in the majority of them. All the study areas are served by formal credit institutions, viz., cooperative societies and/or commercial banks. The performance of the former in two of the villages is exemplary in terms of disbursement of credit and deposit mobilization. Side by side, ICMs are functioning in the villages catering to the unmet credit needs of the households.

APPENDIX 2

Methodology

1. Sampling design : Selection of Villages

Four villages in Kerala and two villages in Tamil Nadu were covered under the micro-studies.

For selecting the villages in Kerala the growth of deposits with commercial banks between 1975 and 1980 was used as a major criterion. The districts were grouped on the basis of growth rates in bank deposits as follows:

High growth	Above 100 percent	Malappuram, Trichur and Trivandrum
Medium growth	80 to 100 percent	Alleppey, Cannanore, Kozhikode and Quilon
Low growth	Below 80 percent	Palghat, Kottayam, Idukki and Ernakulam.

Malappuram and Trichur districts from the first group, Quilon from the second group and Kottayam from the third group were selected. One village from each of the districts was selected for in-depth survey.

In selecting the village, the main considerations were the dominant crops cultivated, and occupational pattern of the villagers. From Malappuram district, Thirunavaya village (in Tirur taluk) was

selected which was found to have about 18 percent of the main workers engaged in cultivation,^{1/} one of the highest in the taluk, with about 53 percent falling in the category of other workers.

In Trichur district, Thalikulam (in Chawakkad taluk) was surveyed for the 1961 census monograph. It is a coastal village with a large number of migrants to the Gulf countries and a certain proportion of households engaged in fishing. So it was thought appropriate to select the village.

Coming to Kottayam district, a high proportion of workers in Kottayam taluk are cultivators, and rubber is a major crop. A village from this taluk, viz., Anikad which is close to Kanjirapally, a leading commercial centre, was selected for the survey.

From Quilon district, we opted for a village which had a different occupational profile, with a higher proportion of workers being engaged in non-agricultural activities like industry, fishing, construction, trade and other tertiary activities. Ezhukone appeared to be the most eligible candidate from the district.

Thus, the villages selected from Kerala are characterised by different growth rates in bank deposits. The selected villages also cover the three leading crops of the state, viz., paddy, coconut and

^{1/} As per the census (1981) definition cultivator is one engaged either as employer, single worker or family worker in cultivation of land owned or held, wherein growing the following crops is considered: cereals and millets, pulses, fibre crops, oilseeds and sugarcane. Hence all those engaged in growing tea, coffee, rubber, tobacco, coconut, areca etc. are considered as other workers.

rubber. Regional spread is ensured by including villages from Malappuram, Trichur, Kottayam and Quilon. Also geographical spread is ensured by selecting villages from the low land, midland, and high land regions.

In the selection of the two villages from Tamil Nadu it was not possible to do full justice to the diverse regional patterns. However, an attempt was made to capture the essential features of Tamil Nadu agriculture. Keeping State level cropping pattern in mind, two districts, Madurai and Tirunelveli, were selected, both of which present equally diverse cropping pattern. In both the districts, rice and coarse cereals accounted for by oilseeds, cotton, pulses, chillies, banana, etc. Further, Madurai belongs to the medium (agricultural output) growth district (e.g. rate between 1.5 to 4.5 percent) and Tirunelveli to the group of low growth districts (growth rate of 0 to 1.5 percent) both having income levels above Rs.1300 per hectare (Bhalla & Alagh).

For the selection of villages, the distribution of workers as per the 1981 census could not be used as the data were not readily available. Hence, the 1971 census tables were used. In Kodaikanal taluk, most of the villages had a very high proportion of workers engaged in plantation, orchard and livestock activities. From this taluk, one of the villages, viz., Vilpatti, was found to have a sizable proportion of the area under paddy, potato and vegetables. Accordingly, Vilpatti from Madurai district was selected for the survey.

In Tirunelveli district, at the second stage, we identified Tiruchendur taluk which had a comparatively high proportion of workers

as cultivators. One of the villages, Mookuperi, growing dry crops with some land under tank irrigation was chosen. Mookuperi was found to be well served by a commercial bank and a cooperative credit society.

2. Selection of Sample Households

1. Kerala

List of households with the household characteristics such as (1) number of family members (2) number of earning members (3) occupation of earning members (4) monthly income of the household and (5) area owned by the households for the selected villages were collected from the various taluk supply offices. The households were grouped into two major categories: (1) households cultivating paddy and (2) households not cultivating paddy. The households in each category were divided into three sub-groups based on the source of income (as recorded in the Taluk Supply Offices registers) viz., (a) households deriving their incomes only from agriculture (b) those with income only from non-agricultural activities. The households in each of the above three categories were further subdivided into five groups based on the monthly income of the households as households earning (1) upto Rs.150 (2) Rs.150-300, (3) Rs.300-450, (4) Rs.450-600 and (5) above Rs.600. From each group, 3% of the households were selected at random for the two villages (1) Thirunavaya and (2) Anikad. For the third villages, Ezhukone, only 2½% of the households from each group were selected at this village has considerably larger

number of households. The time available was also a factor in limiting the sample size.

For Thalikulam, we used the listing schedule canvassed by Centre for Science and Technology for Rural Development (COSTFORD) among 1600 households of the village. Approximately 5% of the total number of households have been selected through stratified random sampling procedure, for the purpose of our study. Due to lack of data on cropping pattern, occupation, etc. we had to use some proxies for the stratification of the households. The criteria used are the structure and facilities in the residence. Accordingly, all the households were broadly classified into three groups, as households having (1) thatched houses (2) tiled houses and (3) terraced houses. Each of these three groups was divided into two groups as households (1) having electric connection and (2) those not having electric connection. Each of these was further sub-divided on the basis of the size of land holding, as households owning (1) less than or equal to 5 cents (2) 6-50 cents (3) 51-100 cents (4) 101-200 cents and (5) above 200 cents. In such cases where the number of households was too small, we clubbed them with the appropriate group.

2. Tamil Nadu

Basic data on the characteristics of the households such as size of family, number of earning members, occupations of earning members, land owned, land cultivated, etc. were collected by our Investigators by census enumeration method. The households were classified into two broad

categories, viz., (1) households with land and (2) households without land. These two categories of households were further divided into sub-groups based on the sources of income of the household., viz., households getting income (a) only from agriculture (b) only from non-agricultural pursuits. Finally, households who own land were further sub-divided into 5 groups based on the size of land holding, viz., (1) below 1.00 acre, (2) 1.00-2.00 acres (3) 2.00 - 3.00 acres (4) 3.00 - 5.00 acres and (5) above 5.00 acres. It is not possible to select a uniform fraction of households from each of the categories in the two villages of Tamil Nadu, as the composition of households and the size of the villages were different. Hence, 20% of the households who own land and 7% of the households who do not own any land were selected from Mookuperi village, while 15% of the households who own land and 10% of the households who do not own any land were selected from Vilpatti village. The households were selected using random number of table from each of the ultimate stratum, with equal probability of households in each size-group being selected. Since data on monthly income of the households were not available, size of land holding was taken as criterion for stratifying the households.

The sample households from each of the selected villages classified according to the occupation of their heads is given in the following statement.

Sample households classified according to the occupation of the heads
of households

	Thiru- navaya	Thali- kulam	Anikad	Ezhu- kone	Vil- patti	Mooku- pori
1. Cultivators	17	14	29	31	21	11
2. Other self-employed (household industry, craft, trade, etc.)	8	21	8	17	6	34
3. Salary earners	1	9	6	16	1	13
4. Agricultural and other casual labour	26	19	29	26	43	5
5. Skilled labour	6	1	2	1	4	2
6. Others	10	19	3	4	1	14
Total	68	83	77	95	76	79

3. Field Survey

The Investigators were given intensive training for a period of 15 days and were sent to the nearby villages of Trivandrum for pretesting of the schedules and questionnaires. In the light of this experience the schedules and questionnaires were modified.

Five household schedules were designed. Household Schedule I covered the general characteristics of the households such as demographic features, education, occupation, etc. Schedule II covered the particulars of all loans outstanding as on 1.4.1986. Household Schedule III was designed to elicit information regarding all borrowals during the reference period, namely, 1.4.1986 to 31.3.1987. Schedules II and III were divided into two parts so as to capture the transactions of cash and commodity loans separately. These two schedules include items like interest rate, duration, security offered, other conditions attached, etc. with regard to each of the loans outstanding as well as borrowed during the reference period.

Schedule IV included the details on the disposition of financial savings by households. To ascertain the net financial savings by the households during the reference period, the value of financial assets like shares and deposits at the beginning and end of the reference period was gathered. Two items, cash in hand and direct investments made during the reference period were not included.

The field survey was started in the first week of April 1987, and was completed in two months. Data collection proceeded in two stages. In the first stage household schedules were canvassed among the sample households. Needless to say, the task of eliciting accurate information from the respondents was quite arduous, though a good proportion of them were cooperative. In the second stage of the survey, we approached a few informal lenders whom we could identify in the selected villages.

The informal lenders were identified with the help of our own sample households and some other knowledgeable persons in the locality. We had prepared separate questionnaires for different categories of lenders such as professional moneylenders, agriculturist moneylenders and traders. Information regarding their lending practices to different types of borrowers was collected through these questionnaires. The questionnaires covered interest rates charged to different categories of borrowers, security accepted, percentage of defaults, etc. Further, in order to study the linkage between formal and informal lenders and between the informal lenders themselves, information was sought from these groups.

CHAPTER 5

STRUCTURE OF INFORMAL CREDIT MARKETS

5.1 Introduction

The informal credit markets in the rural areas of developing countries are heterogeneous in the sense that credit flow from diverse categories of lenders who differ so widely in their clientele, sources of funds, purpose of loans, procedures, interest rates, and other terms and conditions. A salient feature of the ICMs, as implied in its adjective, is the informality in all the aspects of credit transactions; they, by and large, function outside statutory regulations. Therefore, it follows that for the smooth functioning of the system, it is necessary that the lender has easy access to all relevant information regarding the borrower, as well as his being able to keep a close watch over the borrower's activities and to exert economic and non-economic pressure on the latter for ensuring the fulfilment of the terms and conditions of the loan. All these combine to make the ICM transactions highly personalised in character. It is inevitable, therefore, that the credit market gets segmented into several sub-markets.

5.2 Dimensions of Segmentation

The ICM comprises different sub-markets, most of them functioning within the confines of one village. The physical proximity of the borrower provides the lender detailed information about, as well as the

ability to exercise effective control over, the former, thereby ensuring payment of interest and repayment of the principal. The rationale underlying the spatial limitation of the credit market has been spelled out by Roth thus: In the case of the cultivator-borrower, a relatively high proportion of credit arrangements are underwritten by legal title to his land, and the creditor is invariably inclined to seize the land of the debtor.

"Since the cultivation of the land is almost always transferred to the creditor himself, granting a loan underwritten by the property title can be transacted only when the land given as collateral is near the habitation of the creditor.... What holds for the seizure of the land of the debtor by the creditor is equally true for the labour of the debtor. The creditor's claim of the labour of the debtor and its use as a collateral for the loan is only guaranteed when the debtor lives in the region with in the control of the creditor; that is an area within which the social and economic jurisdiction of the creditor and their attendant control - mechanisms are in full sway".
(Roth, 1983, p.31).

That is about the lender's - supply side - approach. Looking from the borrower's end, his access is, by and large, limited to the circumference of the local credit market, that is, within the confines of his own village and its immediate surroundings.

"The cost to the borrower going to a potentially competitive lending agent outside his district is likely to be considerable. The moneylender who knows him will be suspicious until the former establishes a satisfactory repayment record. Initially, it is unlikely that he will be offered a competitive rate of interest, if indeed he gets a loan at all".
(A.Bottomley, 1964, pp.432-433, Emphasis as in the original).

In fact, operationally, the circle may get narrower; the ICMs are further fragmented into credit transactions between particular groups of lenders and borrowers. The former comprises, as mentioned above, professional moneylenders, agriculturist moneylenders, landlords, traders and commission agents, friends and relatives, etc. The latter includes broadly cultivators - both owner-operators and tenant farmers - and non-cultivator households such as artisans, salaried employees, agricultural and other casual labour households. The classification of the different elements in the ICMs formulated by Holst seems to be a neat typology. According to this scheme, the transactions in the ICMs are of two broad types, viz., professional (commercial) arrangements and non-professional (non-commercial) arrangements. The latter is mainly among relatives, friends and neighbours, based on kinship relations and presumably involves no interest payment. The loan transactions under the commercial category are grouped into (a) land-based, (b) commodity-based and (c) money-based arrangements. Under the first category, the lenders comprise landlords and agriculturist moneylenders, and the customers comprise tenants. Commodity-based transactions involve shop keepers and merchant moneylenders while small farmers and small business households come under customers. The last category of transactions is between full-time moneylenders on the one hand and small farmers and small business households on the other. Whereas all the above are exclusively engaged in credit transactions, there are also some which fall under saving and/or saving-cum-credit arrangements like ROSCAS. (Holst, "The role of informal financial institutions in the mobilisation of savings", quoted in Martin-van-Nieuwkoop, 1986, p.34). Thus, even within the confines of one village,

there can be several sub-markets. There are different groups of borrowers of more or less homogeneous types like cultivators, agricultural and other casual labourers, artisans, etc. All of them are not strictly homogeneous though. For example, cultivators may be owner cultivators or tenant farmers, differing in size of holdings, crops grown, etc. And each of these groups may have credit transactions with particular lender type.

The rationale underlying the typology of segmentation is mutual interests of the parties involved. Thus, with landlords are the most easily accessible source of credit to tenants, the former is able to influence the decisions on the production process on their land as well as to ensure repayment of the loans. Ensuring the services of able and healthy workers during peak agricultural seasons is the motivation behind advancing loans by cultivators to agricultural labourers. The same logic is behind labour-tied loans in the fisheries sector in Kerala (Platteau, et.al. 1985). Similarly, commodity-tied loans from trader to farmers presumably serve mutual interest; the trader is ensured of the supply of the commodity-foodgrains in Punjab or rubber or fish in Kerala - while the producer is able to smoothen out seasonal variations in his cash-flow mechanism.

Needless to say, the degree of segmentation prevalent in the ICMEs would depend on the options before the prospective borrowers on the one hand and the socio-economic conditions in a given locality on the other. With the expansion of institutional credit and greater equity in its distribution, and the weakening of the traditional lender - borrower

(landlord-tenant, employer-employee) relations, the forces underlying segmentation would get eroded. A certain degree of segmentation may still continue to prevail, but its survival may be a reflection of the personal relations between borrowers and lenders rather than the conventional economic rationale presumed to underlie the phenomenon of segmentation.

5.3 Extent of segmentation in the ICM : an overview

In the rural ICMs in India, no particular group appears to any more to depend exclusively on one category of lenders, nor does one category of lenders limit their lendings to one specific type of clientele. Thus, according to the results of the All India Debt and Investment Survey (1971-72), households belonging to different occupational groups like cultivators, agricultural labourers, artisans, and other non-cultivators had reported cash loans outstanding due to all the informal credit agencies, viz., landlords, agriculturist moneylenders, traders, friends and relatives, and others. Similarly, each of the lender types had advanced loans to all the occupational groups. (see Table 5.1).

The difference between different occupational groups in the degree of dependance on different informal credit agencies do not fall into a systematic pattern. True, in the case of cultivator households, the proportion of cash dues outstanding owed to agriculturist moneylenders is significantly higher than to other agencies. This is understandable.

Table 5.1 : Cash Dues outstanding as on 30th June 1972, classified according to Credit Agency and Occupational Group : Percent

All-India

Occupation	Credit Agency Col. percent	Row percent	Govt.	Co-op: Societies	Comm: banks	Sub total	Land lords	Agrl. money-lenders	Prof. money-lenders	Traders	Friends and relatives	Others	Sub total	Total All Sources
All households		P	5.34	16.29	1.78	23.41	8.08	24.37	15.62	9.46	8.20	10.65	76.59	100
Cultivators		P	5.83	18.03	1.94	25.81	7.55	24.62	15.00	9.17	7.58	10.27	74.19	100
		S	95.45	96.81	95.11	96.37	79.61	88.32	83.85	84.73	80.75	84.32	84.68	100
Agricultural labourers		P	0.78	2.37	0.25	3.40	21.41	28.25	16.46	9.38	10.95	10.15	96.60	100
		S	0.73	0.74	0.72	0.73	13.08	5.88	5.34	5.03	6.76	4.83	6.39	
Artisans		P	2.96	1.88	0.23	5.07	7.55	24.86	21.25	15.18	10.77	15.32	94.93	100
		S	0.72	0.15	0.17	0.21	1.19	1.33	1.77	2.09	1.71	1.89	1.62	
Other non-cultivators		P	2.67	6.04	1.14	9.86	8.16	17.54	22.45	17.40	14.23	15.37	90.14	100
		S	3.10	2.30	3.99	2.62	6.11	4.47	8.94	8.15	10.78	8.97	7.31	
All Households			100	100	100	100	100	100	100	100	100	100	100	100

Source: Reserve Bank of India, All-India Debt and Investment Survey, Statistical Tables Relating to Cash Borrowings and Repayments of Rural Households during July 1971 to June 1972 and Cash Dues Outstanding as on 30th June, 1972, Bombay, 1978, Statement IV, pp.92-127.

P = Proportion of households reporting;

S = Percentage Share of different occupational groups in total credit from each category

For, a certain proportion of the cultivator-borrowers may be tenants of the latter. An equally high proportion of debt outstanding against agricultural labourers is also owed to agriculturist moneylenders. This may also be rationalised on the ground that the lenders are also presumably employers of the borrowers. But the heavy dependence of other occupational groups on this lender type cannot be explained by the above logic.

Coming to borrowings during the year ended 30 June, 1972, the same picture emerges. Certain proportions of all rural households had borrowed from all the informal lenders ranging from 2.49 percent in the case of landlords to 6.01 percent from traders (Table 5.2). It is true that larger proportions of cultivators and agricultural labourers had borrowed from landlords and agriculturist moneylenders than from other informal credit agencies. This may be attributed to non-credit relationship between the borrowers and lenders. But, varying proportions of households from other occupational groups had reported borrowing during 1971-72 from all informal credit agencies. The proportions of the borrowals by different occupational categories according to sources are presented in Table 5.3.

Table 5.2 : Proportion (%) of households reporting borrowings in Cash during the year ended 30th June 1972 classified according to credit Agency

All-India

Occupation	Credit Agency	Total	Govt.	Co-op: Society	Comm: Banks	Land lord	Agri. money-lender	Prof. money-lender	Trader	Friends and relatives	Others
All households		27.73	1.34	3.36	0.19	2.49	5.99	4.43	6.01	4.75	4.73
Cultivators		29.29	1.64	4.32	0.24	2.39	6.42	4.60	6.39	7.73	4.85
Agri labourers		23.75	0.30	1.34	0.13	10.67	14.66	10.78	10.11	11.29	8.40
Artisans		25.57	0.44	0.52	0.04	1.57	5.65	5.67	6.38	6.12	5.81
Other non-cultivators		21.96	0.82	1.11	0.14	1.56	3.60	4.16	4.83	4.52	4.61

Source: AIDIS, 1971-72, Statistical Tables Relating to Cash Borrowings and Repayments of Rural Households During July 1971 to June 1972 and Cash Dues Outstanding as on 30th June 1972, statement II, pp. 20-55.

Table 5.3 : Borrowings in Cash During the year ended 30th June 1972, classified by Credit Agency and Occupational Groups : Proportions of Aggregate Borrowings : Percent

All-India

Occupation	Credit Agency	Row per-cent	Govt.	Co-op: Society	Comm: Bank	Sub- total	Land- lord	Agrl. money lenders	Prof. money-lenders	Trader	Rela- tives and friends	Others	Sub total	Total
Cultivators	P		3.14	16.66	1.90	21.70	5.83	19.06	15.64	14.47	10.72	12.56	78.28	100
	S	85.87	86.76	95.77	97.76		78.18	87.42	84.26	83.54	80.51	83.66		
Agricultural labourers	P		9.48	1.98	0.19	2.65	15.76	21.65	15.93	14.93	16.68	12.41	97.36	100
	S	0.88	0.88	0.75	0.64		13.84	6.51	5.63	5.63	8.21	5.42		
Artisans	P		1.76	0.87	0.90	3.53	5.80	20.24	19.09	16.69	18.98	16.46	97.26	100
	S	1.52	0.87	0.09	0.08		1.38	1.64	1.82	1.70	2.82	1.94		
Other non-cultivators	P		5.13	7.26	0.36	12.75	6.06	11.88	18.94	19.40	14.36	16.60	87.24	100
	S	6.98	11.50	3.39	1.52		6.60	4.43	8.30	9.10	8.77	8.99	87	
Total		100	100	100	100	100	100	100	100	100	100	100	100	

Source: Same as of Table 5.2

P : Percentage share of different credit agencies in total loans

S : Percentage share of different occupational groups in total loans from each credit agency

Much water has flowed under the bridge since the AIDIS 1971-72. The results of the next round of the AIDIS a decade after have brought out a dramatic change in the shares of the institutional and non-institutional credit sectors. According to the latest round of the AIDIS (1981-82), the proportion of outstanding debt of all rural households as a whole owed to institutional agencies such as government, cooperative society, commercial bank, etc. came to 61.2 percent in 1982, as against 29.2 percent in 1971. As a result, the shares of non-institutional or informal agencies in the total debt owed by all rural households registered a sharp decline, from 70.8 to 38.8 percent. This significant, if not qualitative, change is noted across both cultivator and non-cultivator households, as well as across all the informal credit agencies.

The structure of the rural ICM itself has undergone a sea change in recent decades. The combined shares of the so-called commercial viz., agriculturist and professional moneylenders, landlords in the total credit from the informal sector came down from 62.3 percent in 1962 to 62.3 percent in 1972. During 1972-82 the total credit to rural households to the above agencies declined not only in terms but also in absolute terms. On the other hand, the credit from relatives and friends registered a significant development. (see

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The structure of the rural ICM itself has undergone a sex-change in recent decades. The combined shares of the so-called commercial lenders, viz., agriculturist and professional moneylenders, landlords and traders, in the total credit from the informal sector came down from 81.5 percent in 1962 to 62.3 percent in 1972. During 1972-82 the total debt of all rural households to the above agencies declined not only in relative terms but also in absolute terms. On the other hand, cash dues outstanding to the credit of relatives and friends registered a steady increase since 1962, a significant development. (see Table 5.4).

Table 5.4 : Trends in informal credit according to Credit agencies

Credit Agency	1962		1972		1982		Increase during 1972-82	
	Amount Rs. crores	Percent	Amount Rs. crores	Percent	Amount Rs. crores	Percent	Amount Rs. crores	Percent
Landlord	25.05	1.07	324.05	12.20	242.59	10.23	(-) 81.46	(-) 25.13
Agri. moneylender	1281.03	53.92	867.15	32.62	523.07	22.07	(-) 344.08	(-) 39.67
Prof. moneylender	415.90	17.50	517.16	19.95	504.13	21.27	(-) 13.03	(-) 2.51
Trader	213.98	9.00	325.07	12.23	207.15	8.74	(-) 117.92	(-) 36.27
Relatives/Friends	190.02	7.99	518.80	19.52	553.62	23.36	(+) 34.82	(+) 6.71
Other sources	248.87	10.47	105.52	3.97	338.53	14.28	(+) 233.01	(+) 220.82
Total	2374.45		2657.74		2369.09		(-) 288.65	

Large scale pumping of institutional credit, especially through commercial banks, into the rural sector during the seventies may lead to a widening of the rural credit market or undermining of its segmentation. Since the conduct of the latest round of the survey (1981-82), more public funds have been pumped into the rural sector under various schemes like Integrated Rural Development Programme (IRDP), Rural Labour Employment Generation Programme (RLEGP) etc. all of which might contribute to widening the options before those segments of the rural households which used to lean too heavily on particular informal lenders.

In brief, the findings of the AIDIS do not seem to reflect dependence of any particular group of rural borrowers exclusively on any particular lender type. The All India estimates in the process of aggregation may have perhaps erased the degree of segmentation prevailing at the micro level. Therefore, to get a true picture on the ground we will have to observe the situation at the village level.

4.4 The Structure of ICM in the Selected Villages

Before we turn to the ICMs in our selected villages, let us take a look at the structure of the overall credit markets. The structure of the credit markets in the selected villages under the present study seems to broadly conform to the countrywide pattern observed earlier. In five out of the six selected villages the share of informal credit agencies in the total debt outstanding and in the total borrowing is significantly smaller than that of the formal credit institutions. (Table 5.5).

Table 5.5 : Outstanding Loans : No. of Reporting Households and Amount

Village	No. of sample households	Formal Credit Agencies				Informal Credit Agencies				Total			
		No. of reporting households	% of reporting households	Amount outstanding		No. of reporting households	% of reporting households	Amount outstanding		No. of reporting households	% of reporting households	Amount outstanding	
				Total Rs.	per household Rs.			Total Rs.	per household Rs.			Total Rs.	per household Rs.
Thirunavaya	68	13	19.12	24200 (14.37)	355.88	22	32.35	144250 (85.63)	2121.32	35	51.47	168450 (100)	2477.21
Thalikulam	83	46	44.58	198782 (74.67)	2394.96	12	14.46	67419 (25.32)	812.27	58	39.04	266201 (100)	3207.24
Anikad	77	39	46.05	258198 (79.60)	3353.22	18	23.38	66187 (20.40)	859.57	57	69.44	324385 (100)	4212.79
Ezhukone	95	43	41.05	673762 (78.12)	1829.07	10	10.53	48652 (21.87)	512.13	53	51.58	222414 (100)	2341.20
Vilpatti	76	44	53.95	314079 (89.68)	4132.62	12	15.79	36130 (10.32)	475.39	88	69.74	350209 (100)	4608.01
Hookuperi	79	9	11.39	71813 (74.33)	909.02	4	5.06	24800 (25.67)	313.92	13	16.45	96613 (100)	1222.94

Note: Figures in brackets denote percentages

The proportion of households reporting outstanding debt due to formal credit institutions is significantly larger than that for the informal credit agencies in all the selected villages except in Thirunavaya. In five of the villages, the ratios of the number of households reporting outstanding loans from formal and informal sources respectively are in the range of 1.42 to 4.33, while in the exceptional case it is 0.5. As for the distribution of the outstanding loan amounts between the two sectors, again except Thirunavaya, the shares of formal credit institutions are around three-fourths or more of the total. In Thirunavaya, the share of informal credit agencies exceeds four-fifths of the total amount outstanding. Thus, in terms of either the proportion of households reporting or share in the total volume of outstanding loans, the credit market in the majority of the selected villages is dominated by the formal sector, the one exception being Thirunavaya. It is significant to note that the proportion of outstanding debt saved to formal credit institutions by the non-cultivator households is also quite high: in two of the villages, it is higher than the corresponding proportion for cultivator households. (Table 5.6).

The distribution of borrowings according to credit agencies during 1986-87 conforms to the same pattern as that of outstanding loans presented above. In terms of the proportion of households reporting borrowing as well as amounts involved, the formal sector has a significant lead over the informal sector. In four out of the six villages, the proportion of households reporting borrowings only from the formal sector is greater than those who have borrowed from informal sources. (Table 5.7).

Table 5.6 : Debt Outstanding classified according to occupational Groups and Credit Agencies

Village	Cultivator Households						Non-cultivator Households					
	Formal Agencies			Informal Agencies			Formal Agencies			Informal Agencies		
	No. of reporting households	Amount per reporting household	Amount per sample household	No. of reporting households	Amount per reporting household	Amount per sample household	No. of reporting households	Amount per reporting household	Amount per sample household	No. of reporting households	Amount per reporting household	Amount per sample household
	Rs.	Rs.		Rs.	Rs.		Rs.	Rs.		Rs.	Rs.	
Thirunavaya	3	1333.33	235.29	7	7742.86	3188.24	10	2020.00	396.08	15	6003.33	1765.69
Percent			6.87			93.13			18.32			81.68
Thalikulam	5	8319.80	3466.58	1	575.00	43.75	40	3929.57	2213.85	11	6081.27	942.17
Percent			98.75			1.25			70.15			29.85
Anikad	15	4255.13	2279.54	10	4395.20	1569.71	24	8098.79	3966.73	8	2779.38	453.78
Percent			59.22			40.78			89.73			10.27
Ezhukone	11	3404.50	1170.19	1	7500.00	199.05	30	4549.87	2163.75	9	4572.44	653.21
Percent			90.77			9.23			76.81			23.19
Vilpatti	12	7477.76	4273.01	1	4000.00	190.48	23	6828.13	2855.40	11	2920.91	584.18
Percent			95.73			4.27			83.01			16.98
Mookuperi	3	12917.00	3522.62	1	8000.00	727.27	6	5510.33	486.21	3	5616.67	247.79
Percent			82.89			17.11			66.24			33.75

Table 5.7 : Borrowings during the reference period : number of reporting households and amount borrowed

All households

Village	Formal Credit institutions (only)					Informal Credit Agencies (only)				From both sources				Average borrowings per household from all sources (Col.5, 9, and 12)
	No. of sample households	No. of reporting households	Current borrowings			No. of R.H.	Current borrowings			No. of R.H.	Current borrowings			
			Total Rs.	per R.H. Rs.	per S.H. Rs.		Total Rs.	per R.H. Rs.	per S.H. Rs.		Total Rs.	per R.H. Rs.	per S.H. Rs.	
1	2	3	4	5	6	7	8	9	10	11	12	13	14	
Thirunavaya	68	10 (14.71)	49940	4994	734.41	34 (50.00)	49045	1442.50	721.25	14	76349.98	5453.57	1122.79	2578.45
Thalikulam	83	19 (22.89)	101545	5344.47	1223.43	15 (18.07)	50350	3356.67	606.63	2	13975.00	6987.50	168.37	1978.43
Aniked	77	33 (42.86)	141670	4293.03	1839.87	6 (7.79)	8150	1388.33	105.84	12	81792.00	6816.00	1062.23	3007.74
Eshukone	95	22 (23.16)	81250	3693.18	855.26	11 (11.58)	20950	1904.55	220.53	5	23200.00	4640.00	244.21	1320.00
Vilpatti	76	13 (17.11)	59370	4566.92	781.18	18 (23.68)	20440	1135.56	268.95	11	129844.99	11804.09	1708.49	2758.62
Mookuperi	79	18 (22.78)	82200	4566.67	1040.51	17 (21.52)	32705	413.99	413.99	3	3400.01	11466.67	435.44	1889.94

Notes : R.H. = Reporting Households; S.H. = Sample Households
 figures in brackets denote the percentage of households.

The average size of loans from the formal sector is found to be larger than that from the informal sector. The ratio of average debt per household in the two groups of borrowings, i.e. borrowers from either formal or informal sources only, ranges from 1.01 in Thirunavaya to 17.38 in Anikad. However, there are a few households in each village who have borrowed from both the source. Naturally, the amount borrowed per reporting household of this group is higher than the average per reporting household for the other two groups of households. The reason is far to seek. Those households which have access to both sources of credit would be able to get higher amounts from both.

The borrowings by cultivator and non-cultivator households according to sources of credit are summarised in Table 5.8. It may be noted that the cultivator households obtained a much larger proportion of the loans from formal credit institutions except in Thirunavaya where the share of the informal credit agencies is about 64 percent of their total borrowings. It is interesting to note that the non-cultivator households have had almost equal access to the formal credit sector. The average size of loans from the formal credit institutions in their case is higher than that of the cultivator households in the majority of villages. In all the villages, except Thirunavaya the borrowings by non-cultivator households from informal agencies, account for less than one-half of their total borrowings during the reference period. Further, the proportion of loans from informal agencies to non-cultivator households is less than that in the case of cultivator households in three of the villages. Among the different categories of non-cultivator households,

Table 5.8 : Borrowings classified according to Occupation of Credit Agencies

(Rs. per household)

Village	Cultivator Households					Non-cultivator Households				
	Formal		Informal		Total	Formal		Informal		Total
	Rs.	Percent	Rs.	Percent		Rs.	Percent	Rs.	Percent	
Thirunavaya	652.79	36.19	1151.25	63.81	1804.04	1256.62	48.55	1331.76	51.45	2588.38
Thalikulam	569.87	73.56	204.81	26.44	774.69	2171.08	51.96	2007.28	48.04	4178.37
Anikad	2190.90	74.73	740.90	25.27	2931.81	3339.41	86.15	536.71	13.85	3876.12
Ezhukone	906.31	82.04	198.42	17.96	1104.73	1672.63	71.84	655.78	28.16	2328.42
Vilpatti	2308.17	68.36	1068.42	31.64	3376.59	2027.15	75.09	672.50	24.91	2699.65
Mookuperi	855.71	83.87	164.56	16.13	1020.27	1344.94	68.94	620.32	31.56	1965.25

those engaged in household industry, crafts, etc. the self-employed, have met a relatively high proportion of their credit needs from the formal sector. Even in the case of agricultural and other casual labour households, the proportion of loans from the formal sector ranged from two-thirds to three-fourths of the total in three villages. (Table 5.9).

Coming to the informal sector, friends and relatives constitute the leading credit agency in all the six villages. They are the one source from whom the largest proportion of households are reported to have loans outstanding. They also account for the highest proportion of the amounts outstanding in all the villages, ranging from 56.73 percent in Anikad and 100 percent in Mookuperi. (Table 5.10). Next to friends and relatives, professional moneylenders lead the rest in terms of the proportion of reporting households and total amount outstanding to their credit, though this category is not reported in two of the villages. Agriculturist moneylenders come next in order in terms of coverage as well as amounts involved. But outstanding loans are reported only in three of the selected villages, and the total number of loans among them add up to only six. Outstanding loans due to traders are reported in only two villages, and the number of reporting households was merely one each. As a source of credit landlords are accompanied by their absence in all the villages.

No systematic pattern seems to emerge from the analysis of outstanding debts among different occupational groups vis-a-vis different categories of informal lenders. The informal agency to which any occupational group owes loans outstanding varies from village to village.

Table 5.9 : Borrowings by sample households classified according to credit agency

Village	Percent									
	Cultivators		Household industry, crafts etc.		Salary earner		Agrl. & other casual labourers		All non-cultivators	
	Formal	Informal	Formal	Informal	Formal	Informal	Formal	Informal	Formal	Informal
Thirunavaya 68	36.19	63.81	52.73	47.27	0.00	100.00	30.87	69.13	48.55	51.45
Thalikulam 63	73.56	26.44	49.70	50.30	62.73	37.27	39.85	60.15	51.96	48.84
Anikad 77	74.73	25.27	61.02	38.98	98.71	1.29	68.77	31.23	86.16	13.85
Ezhukone 45	82.04	17.96	79.21	20.79	87.55	12.45	75.61	24.39	71.84	28.16
Vilpatti 76	68.36	31.64	56.04	43.97	Nil	Nil	76.89	23.11	75.09	24.91
Mookuperi 79	83.87	16.13	67.96	32.04	45.92	54.08	0.00	100.00	69.44	31.56

Table 5.10 : Cash loans outstanding to all informal credit-agencies

(total for all reporting households)

Village	Agri. moneylenders		Prof. moneylenders		Traders		Relatives & Friends		Total
	Rs.	%	Rs.	%	Rs.	%	Rs.	%	Rs.
Thirunavaya	-	-	-	-	1200	0.83	143050	99.17	144250
Thalikulam	-	-	9919	14.71	-	-	57500	85.29	67419
Anikad	13415	20.27	14547	21.98	675	1.02	37550	56.73	66187
Ezhukone	900	1.85	11752	24.16	-	-	36000	73.99	48652
Vilpatti	740	2.05	9390	25.99	-	-	26000	71.96	36130
Mookuperi	-	-	-	-	-	-	24800	100	24800

In the case of cultivator households, friends and relatives are the leading informal creditors in the majority of the study areas. Professional and agriculturist moneylenders are a source of credit to cultivators in only two villages. Traders are not reported among creditors of this occupational group except in Thirunavaya, but there too they have only a marginal role. For other sub-groups there is hardly any evidence to suggest a particular group leaning too heavily on one particular category of informal lenders. On the other hand, one type of creditor may have lent to most of the occupational groups, as for example, professional moneylenders, or friends and relatives in some of the villages. Agriculturist moneylenders and traders, on the other hand, appear as the least prominent categories in most of the study areas vis-a-vis different occupational groups.

As noted above, among the informal lenders, relatives and friends lead the rest by a substantial majority. From the six villages, 53 households have reported outstanding loans due to their relatives and friends. Obviously, loan transactions in this sub-market are non-commercial and are based on kinship relations. In the nature of things, this sub-market is likely to be highly segmented, both spatially and socially.

The number of households reporting outstanding debt to professional moneylenders in four villages added up to only 19; in Thirunavaya and Mookuperi no household reported outstanding debt to this agency. In the four villages where a few households have reported outstanding debt due to this agency, they are distributed among different occupational groups. That is to say, there is no systematic bias in the distribution of credit from professional moneylenders in favour of a particular group

of borrowers. Notwithstanding this, there is apt to be segmentation of the sub-markets the boundary being determined by locality. In the case of agriculturist moneylenders and traders, as observed earlier, the number of households reporting outstanding debt is too small to bring out any pattern as regards the direction of its flow. However, these sub-markets are apt to be segmented since the lenders would rather prefer to extend loans to those parties who are from their own home village, known to them well and over whom they have some hold. But, then, the number of households reporting outstanding debt owed to particular categories of informal lenders in each village is too small to bring out any inherent systematic pattern of lender-borrower relationship.

Coming to the borrowings from the informal sector during 1986-87, again relatives and friends account for the largest proportion of loans in the majority of the selected villages. (Table 5.11). The share of relatives and friends in the total borrowings from the informal sector ranged from around 63 percent in Anikad 79 percent in Thirunavaya. The average size of the loans from relatives and friends is also, by and large, comparatively large. Naturally, the loans from relatives and friends are distributed among all occupational groups.

In terms of the volume and proportion of loans, the professional moneylenders come next in order of importance. The number of loans extended by them varies from one in Mookuperi to 28 in Vilpatti. Their share in the total amount of loans from the informal sector ranges from 8.23 percent in Thirunavaya to 30.31 percent in Thalikulam. The distribution of these

Table 5.11 : Borrowings classified according to Credit Agencies

(total for all household)

Village	Agricultural moneylenders		Professional moneylenders		Traders		Relatives/friends		Total Rs.
	Rs.	Percent	Rs.	Percent	Rs.	Percent	Rs.	Percent	
Thirunavaya	200	0.11	13750	8.23	21245	12.72	131850	78.93	167045
Thalikulam	-	-	35875	30.31	-	-	82500	69.69	118375
Aniked	17650	19.39	15200	16.70	500	0.55	57650	63.35	91000
Ezhukone	6700	8.80	17400	22.85	-	-	52050	68.35	76150
Vilpatti	3500	2.57	14200	10.42	21000	15.41	97600	71.60	136310
Mookuperi	-	-	12000	19.35	5255	8.48	44750	72.17	62005

loans according to the occupation of borrowers is shown in Table 5.12. Cultivator households and other self-employed, i.e. those engaged in household industry, crafts, etc. together account for more than two-thirds of the total loans from professional moneylenders in all the villages together. In two of the villages, cultivator households account for more than three-fourths of the total loans from this source, while in two other villages those engaged in household industries and crafts claim more than one-half of the loans. The number of loans taken by the wage labour households as a whole exceeded that by other occupational groups; but the average size of loans to this group is small. Their share in the total amount lent by professional moneylenders falls in the range of 5.4 to 37.09 percent. In the nature of things, this sub-market is apt to get segmented spatially, for no professional moneylender would be inclined to lend to labour households or even cultivator households outside his home village.

Agriculturist moneylenders and traders are less prominent. In two of the villages, no loans from agriculturist moneylenders were reported, and in the remaining four the number of loans varied from 1 (Thirunavaya) to 6 (Anikad). For all the four villages together, the total number of loans comes to only 12. Of these 4 go to cultivators and 4 to wage earners. Apparently these loans do not fall into the conventional type where the borrower is a tenant or employee of the lender, and where other considerations are involved. As for traders, they as a source of credit are conspicuous by their absence in two villages, and in one of them just a single loan is reported.

In the other three places, the number of loans varied from 7 to 30. Of the total 46 loans from traders, cultivators and labour households received 15 loans each, and the rest is distributed among the other occupational groups. These creditors are mostly owners of grocery shops located in the same village as in Thirunavaya or itinerant merchants selling cloth and domestic utensils as in Vilpatti and Mookuperi. Traders belonging to the conventional typology who advance loans to cultivators on the condition that the latter sell their crop to the former have been reported in Anikad and Vilpatti. But the majority of traders observed in our study areas sell goods on credit and do not extend cash loans.

In brief, the rural credit market in general has been undergoing a structural transformation in recent years with the expansion of the formal credit sector undermining the role of informal lenders. With all sections of rural households getting a share of the expanded formal sector credit, informal lenders of the commercial type like professional money-lenders, traders, etc. suffered a set back. Certain changes in the socio-economic conditions further weakened the hold of informal lenders over their debtors and placing restraints on their exploitative tactics. The net outcome is a change in the structure of the ICM itself which is no more dominated by lenders of the commercial type.

5.5 Other characteristics of the ICM

(a) Size of loans

The average size of loans from the informal sector is comparatively small, smaller than those from the formal credit institutions. A larger

proportion of the borrowers from these agencies may belong to the low income groups. The bulk of their borrowings may be for the purpose of meeting necessary consumption expenditures. They are also comparatively less creditworthy, with less valuable collateral security to offer. On the other hand, the loanable funds at the disposal of informal lenders may also be limited. Thus, factors on both the demand for and the supply of credit from the informal sector tend to lower the size of loans.

In our study areas, the average size of outstanding loans ranges about Rs. 1984 at Vilpatti to Rs.4000 at Thalikulam. As for the borrowings during the reference year, the size of loans falls in the range of a little over Rs.927 at Thirunavaya to Rs.2894 at Thalikulam. A good proportion of the borrowings, from one quarter at Thalikulam to two-thirds at Thirunavaya, is below Rs.500. (see Table 5.13). It may also be noted that the average size of loans from the informal sector is smaller than that from the formal sector.

The small size of loans has some cost implications. Obviously, for a given amount of loanable fund, the smaller the average size of loans, greater the number of loans. The real cost of administration - the time and energy involved in the disbursement of these loans and their recovery, maintenance of accounts, etc. for loans of small size - would be high. Naturally, formal credit institutions develop no allergy to small-sized loans.

Table 5.13 A: Number of Loans outstanding classified by size of loans from Informal Credit Agencies

Size of loans Rs.	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
1. 500	5	20.00	7	46.67	2	10.00	2	15.38	4	26.67	3	50.00
2. 501 - 1500	4	16.00	2	13.33	9	45.00	6	46.15	4	26.67	1	16.67
3. 1501 - 2500	7	28.00	-	-	1	5.00	-	-	3	20.00	-	-
4. 2501 - 5000	7	28.00	1	6.67	5	25.00	4	30.76	3	20.00	-	-
5. 5000 -10000	1	4.00	2	13.33	3	15.00	-	-	1	26.67	1	16.67
6. Above 10000	1	4.00	3	20.00	-	-	1	7.69	1	-	1	16.67
Total	25	100	15	100	20	100	13	100	15	100	6	100

5.13 B: Number of Loans borrowings classified by Size loans from Informal Credit Agencies

Size of loans Rs.	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
1. 500	48	66.67	4	25.00	13	48.15	5	27.78	22	56.41	9	40.91
2. 501 - 1500	15	20.83	1	6.25	8	29.53	6	33.33	6	15.38	8	36.36
3. 1500 - 2500	3	4.17	3	18.75	4	14.81	4	22.22	-	-	1	4.55
4. 2501 - 5000	3	4.17	6	37.50	2	7.41	2	11.11	7	17.95	3	13.64
5. 5000 - 10000	3	4.17	2	12.50	-	-	1	5.56	1	2.56	-	-
6. Above 10000	-	-	-	-	-	-	-	-	3	7.69	1	4.55
Total	72	100	16	100	27	100	18	100	39	100	22	100

(b) Security

The non-cultivator households account for the majority of the number of outstanding loans and borrowings from the informal sector in all but one of the selected villages. The singular exception is that of Ezhukone where the proportion of borrowings by non-cultivator households is slightly less than one-half; but even here, the proportion of outstanding loans of the group is above three-fourths. The non-cultivator group of households which include agricultural and other casual labourers, artisans, etc. are comparatively poor. Agricultural and other casual labourers account for a sizable proportion of the total number of loans - both outstanding and borrowings - in the selected villages. The share of the above category of households in the total number of outstanding loans of all non-cultivator households falls in the range of 25 to 82 percent; the corresponding proportions of the number of borrowings ranges from 15 to 72 percent. Apparently, the non-cultivator households are less creditworthy in terms of the value of assets they can offer as collateral against loans. Therefore, a comparatively higher proportion of their loans, is against personal security.

For the sample households as a whole, the proportion of outstanding loans against personal security ranges from 20 percent in Vilpatti to 95 percent in Thirunavaya. (Table 5.14). In three of the six villages, loans against personal security outnumber those against other forms of security. The proportion of borrowings against personal security ranges from 30 to 79 percent being above 50 percent of the loans in half of the villages. Gold, land and buildings are three tangible assets offered as collateral, though in a far fewer cases of either outstanding loans or borrowings.

Table 5.14 A : Number of Outstanding Loans from informal credit agencies classified according to Security

Security	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal security	36	94.74	30	46.15	25	36.23	17	26.98	15	20.00	10	58.82
Gold	2	5.26	21	32.31	21	30.43	8	12.70	2	2.51	3	17.65
Land/building	-	-	11	16.92	19	27.54	30	47.62	61	76.25	2	11.76
Others	-	-	3	4.61	4	5.78	8	12.70	1	1.25	2	11.76
Total	38	100	65	100	69	100	63	100	80	100	17	100

5.14 B : Number of Borrowings from informal credit agencies classified according to security

Security	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
Personal security	77	78.57	12	30.77	37	37.96	17	30.36	35	52.24	27	51.92
Gold	18	18.37	24	61.54	42	42.86	16	28.57	8	11.94	21	40.38
Land/building	3	3.06	3	7.69	18	18.39	20	35.71	21	31.34	2	3.85
Others	-	-	-	-	1	1.02	3	5.36	3	4.48	2	3.85
Total	98	100	39	100	98	100	56	100	67	100	52	100

Obviously, the type of security would vary between different groups of households. For instance, the proportion of the loans against land or buildings as the security in the case of cultivator households should be greater than that of other occupational groups. However, be it noted that even in the case of cultivators, land or building is not the security for the majority of loans. For the 'other self-employed' group, i.e. those engaged in household industry, crafts, trade, restaurants, etc. personal security and gold together account for a substantial proportion. The largest proportion of loans to agricultural and other labour households is against personal security. As between different lender types, we do not observe any marked differences in the security accepted against loans.

The implications of a high proportion of the outstanding debt and borrowings against personal security are obvious. The lenders have to have a strong hold over their clientele. This leads to segmentation of the ICMs.

(c) Duration of loans

Given the type of lenders in the ICM, the sources and quantum of loanable funds and nature of the credit transactions, the duration of loans in this market should be short. As is well documented, the informal lenders in the rural areas in India and other third world countries generally do not receive deposits, but lend out of their own resources. In the nature of things, funds at the disposal of an informal lender will be

limited. At the same time, too many potential borrowers may be approaching him. Therefore, the lenders would not like to lock their funds in long term or medium term loans. As noted earlier, in our study areas, the largest proportion of informal credit - loans outstanding and borrowings - is from friends and relatives. The funds at their disposal to repeat, are limited, and further, their status changes from day to day; that is, today's lenders will be tomorrow's borrowers. If so, these households, while able to spare some cash now will anticipate shortfall in their income in the future sooner or later. They, therefore, are compelled to restrict the duration of their loans to any party, however close the relationship. Financial constraints and pressure of demand may compel the other informal credit agencies also to restrict the duration of their loans.

In the majority of the selected villages, the largest proportion of loans outstanding and of borrowings are of less than one year duration (Table 5.15A). In half of the villages, more than four-fifths of the outstanding loans due to informal agencies have a duration of one year or less. Anikad with the highest proportion of outstanding loans, 85 percent for 5 years or over, is at the other end of duration scale. Coming to the borrowings during the last one year (1986-87), the pattern across the villages is more or less the same as in the case of outstanding loans (Table 5.15 B). In three of these villages, loans with duration of one year or less exceed 90 percent in two villages, loans of the above duration add up to more than 60 percent. And in the remaining village, viz., Anikad, they come to about 30 percent where as loans with longest duration, five years and above, constitute over 70 percent. It may be

Table 5.15 A : Number of Loans Outstanding due to Informal Credit Agencies
According to Duration

Duration (months)	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
1 - 6	12	48.00	14	93.33	2	10.00	3	23.08	2	13.33	4	66.67
6 - 12	12	48.00	-	-	1	5.00	3	23.08	2	13.33	1	16.67
12 - 24	1	4.00	-	-	-	-	-	-	-	-	-	-
24 - 36	-	-	-	-	-	-	-	-	6	40.00	-	-
36 - 60	-	-	1	6.67	-	-	-	-	2	13.33	-	-
60	-	-	-	-	17	85.00	7	53.85	3	20.00	1	16.67
Total	25	100	15	100	20	100	13	100	15	100	6	100

5.15 B : Number of Borrowings from Informal Credit Agencies according
to Duration

Duration (months)	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	No.	%	No.	%	No.	%	No.	%	No.	%	No.	%
1 - 6	65	90.28	15	93.75	7	25.93	5	27.78	26	66.67	19	86.36
6 - 12	6	8.33	-	-	1	3.70	6	33.33	2	5.13	3	13.64
12 - 24	1	1.39	-	-	-	-	-	-	-	-	-	-
24 - 36	-	-	-	-	-	-	-	-	5	12.82	-	-
36 - 60	-	-	-	-	-	-	-	-	1	2.56	-	-
60	-	-	1	6.25	19	70.37	7	38.89	5	12.82	-	-
Total	72	100	16	100	27	100	18	100	39	100	22	100

recalled that Anikad has highly commercialised agriculture demanding heavy investment with a comparatively long gestation period. Given the direction of the flow of credit, its duration turns out to be long.

In an earlier section we examined the size of loans. Is there any relationship between the size and duration of loans? On the one hand, there are strong reasons for this type of lenders to restrict both the size and duration of loans. On the other hand, credit used for certain purposes like investment as mentioned above in the case of Anikad, tends to be both large in volume and long in duration. Therefore, the association cannot be unidirectional. The analysis of correlation between size of loans - outstanding and borrowings - and their duration has yielded the following results.

Correlation coefficients of loan size and duration

	<u>Outstanding loans</u>	<u>Borrowings</u>
Thirunavaya	0.270	0.500*
Thalikulam	0.110	0.554*
Anikad	-0.060	0.357
Ezhukone	0.314	0.034
Vilpatti	-0.013	0.395*
Mookuperi	0.824*	0.108

* Indicates that the Coefficients is significant at 5% level.

Thus, the correlation between size of outstanding loans and their duration, as agreed upon at the time the loans were taken, is positive

in three out of the four Kerala villages; and in one of the villages from Tamil Nadu it is not only positive but significant 5 percent level. The correlation coefficient is negative in one each of the villages from the two States. As for the association between the size of borrowings during the reference period and duration of loans, the coefficient of correlation is positive in all the six villages. It may be noted that the coefficients are significant at 5 percent level in three instances. Thus, apparently, the results of the above analysis seems to suggest that for our sample households the association between size of loans and duration is generally positive. However, no generalisation can be drawn from these results, given the limitation of the data such as small number of observations and heterogeneity of the borrowers and lenders.

4.6 Inter linkage of Credit, Land, Labour and Community Market

One of the characteristics of the ICM which leads to its segmentation is the interlinkage between credit and transactions in land, labour and commodity markets. Given the social structure, power relations, limited access to formal credit sources and highly personalised nature of informal credit transactions, the options before a good proportion of borrowers are limited to parties with whom they have other ties: their landlords if they are wage earners, village merchants or their agents trading in food-grains or other crops or farm inputs if they are cultivators. The lenders under each category presumably have strong reasons for preferring their respective clientele, and also on the part of borrowers for approaching particular sources of credit. While such associations facilitate credit transactions, the latter tends to reinforce the former.

The rationale underlying the interlinkage of credit and other markets, and the extent of its prevalence have attracted a great deal of research efforts in recent years. It has been argued that the conjoint exploitation in interlinked markets by a dominant party like the landlord enhances his power more than he otherwise would have enjoyed had he been operating in only one market. (Bharadwaj, 1980, p.). Interlinked, personalised, transactions also act as a formidable barrier to entry for a new potential competitor from outside, and is thus a source of additional monopoly power for the dominant partner in such transactions (Bardhan, 1980,). It is further argued that

"Interlinking of transactions in different markets is also a very effective way for the dominant party to avoid social or legal controls on charging high prices in some markets and to select criteria for rationing scarce resources". (Ibid., p.94).

Bardhan observes that the link between credit contracts and labour-tieing arrangements is one of the most important aspects of production relations in a poor agrarian economy. Thanks to certain distinct characteristics of agricultural production in these economies such as the weather factor, unpredictability of the timing of different operations, the time constraint, etc.

"the employer is usually keen on entering into some implicit or explicit contract with workers about a dependable supply of labour at the right time..... Since the employer puts a high premium on quick and ready availability of labour, he is usually prepared to provide their tied or committed workers with wage advances long before the crop is harvested, and with other kinds of consumption credit, some times at interest rates below what the professional village moneylenders would charge for such credit". (Ibid., p.93).

During the course of a survey of selected villages in Eastern India it was found that in 68 percent of the cases in West Bengal and 33 percent in Bihar the casual labourer takes advances from his employer against future commitment of labour; and in such cases he works at lower than market wage rate at the time of employment. The payment of interest thus takes the forms of wage cut. (Bardhan and Rudra, 1978, p.379). Reporting on the results of another survey on the terms and conditions of labour contracts in West Bengal, Bardhan and Rudra observed that in 86 out of the 110 sample villages, the system of loans against labour existed. Under this system, known as Dadan, a labourer takes cash or grain loan in the lean season from a potential employer against commitment of future labour when the latter needs it.

"In 58 of these villages the number of labour days in which the loan is repaid by the labourer is calculated at an imputed wage rate which is below the market wage prevailing at the time of repayment. The imputed wage rate is sometimes prefixed at a given level which is below the market wage rate by a fixed differential. The difference between the ruling wage rate and the imputed or accounting wage is the implicit cost of the loan". (Bardhan and Rudra, 1981, p.93; See also Bardhan and Rudra, 1979, p.1483).

In a recent study on credit market in Sambalpur district, Kailas Sarap (1986) has made a detailed analysis of interlinkage of credit, and land, labour and commodity transactions among small and marginal farmers, tenants and agricultural labour households in the region. The study has brought out the presence of a variety of linked credit transactions involving land, labour, inputs and output, while

credit is central in all types of linkage. However, tying of credit with output and labour are the two most important forms of linkage. The lenders with whom labour-tying arrangements are entered into were generally big cultivators. The labourers take consumption loans, in cash or grain, during the lean period with the understanding that they would work for the lender-employer at the time of his need; this type of linking consumption credit with labour was observed in about one-third of the households. The commitment of future labour services is often at a predetermined wage which is lower than the market wage prevailing at the time of the execution of work. Thanks to the diffusion of the HYV technology, the success of which depends on the timely performance of different cultivation operations, and uncertainty about the supply of wage labour at crucial periods in the crop growing season, cultivators place a high premium on the quick and ready availability of labour. They, therefore, prefer to offer credit against committed labour services.

Linking of land lease and credit markets used to be another major type of interlinkage. It has been argued that in the context of imperfect capital markets, linking is mutually convenient:

"a tenant lacking suitable collateral may find in his landlord the only source of credit, while the landlord may be willing to provide credit to his tenant because he is better informed about his tenant's loan repayment capacity, and also because he can accept collaterals which are not acceptable to other sources of credit". (Pant, 1980, p.243).

As noted in the case of other types, interlinkage, of credit and landless markets also enhance the power of the creditor, i.e. the landlord-cum-moneylender.

"Where regulations prevent the exercise of monopoly power in one of the markets, then, by linking transactions in this market with those in which the landlord has unrestricted monopoly power, the landlord neutralises the adverse impact of the control". (Ibid., p.244).

Linking of tenancy and credit is viewed as a convenient screening device for the selection of borrowers. (Braverman and Guasbh, 1984, p.360). As for the extent of its prevalence, according to the results of a sample survey of eastern India in the late seventies, landlords emerged as an important source of credit for tenant farmers: 51 percent of the tenants in West Bengal, 50 percent in Bihar and 55 percent in Uttar Pradesh reported taking consumption loans from landlords, all repayable in grains from the harvest shares of the tenants. Landlords sharing of the costs of cultivation, as well as advancing production loans also worked out to more or less of the above order.

"Production loans as well as cost-sharing obviously indicate a strong interest on the part of the landlord in productive investment on the tenant farms... All this is a far cry from the usurious landlords uninterested in productive investment". (Bardhan and Rudra, 1978, p.377; See also Rudra, 1975, p.1050-1051).

Of the total cash dues outstanding against all rural households at the end of June, 1978, the proportion owed to traders and commission agents were estimated at 8.7 percent, their share of the total due to all informal credit sources came to 12.2 percent. The bulk of the credit from traders and commission agents, viz., 84.4 percent was taken away by cultivators. (See Tables 4.2 and 4.3 in the earlier sections). Presumably, a sizable proportion of such credit is linked, input or output linked,

because

"petty merchants and shop keepers in the rural areas selling to or buying from, farmers obviously have substantial advantages in that their contacts with farmers is intimate. They too can well assess the credit worthiness of individual farmers, administer loans at low cost and maintain the continuous surveillance of individual families which is so often needed in poor rural localities".
(Ghosal, 1973, p.26).

According to the study on credit in Sambalpur district referred to earlier, credit and input/output linkage was observed in the case of a good proportion of the small farmers. (Sarap, op.cit., Table 3.2, p.32. See also Kurup, 1976).

Needless to say, in a vast country of India's size, there are bound to be considerable inter-regional variations in the structure and functioning of the rural informal credit market. The role of the different categories of lenders, the extent to which different groups of rural households depend on them, the prevalence and modes of inter-linkage, the degree of exploitation, etc. will naturally vary from region to region.

Interlinkage of credit and landlease is not observed in any of our study areas. In none of the selected villages, loans from landlords have been reported. In Kerala tenancy had been abolished in the early seventies. Though tenancy continues to prevail in Tamil Nadu, the landlord's hold over tenants has apparently weakened, presumably they have no longer any incentive to extend loans to their tenants. The fact that in our selected villages the cultivator households have been able to obtain

loans from the formal credit institutions has also eroded the hold of the landlords as a source of credit on exploitative terms and conditions.

Commodity-tied loans have been observed in some of the villages. For instance, at Anikad rubber cultivators have been taking short term, one to two weeks' duration, loans from rubber dealers on the condition that they sell their produce to their creditors. However, it may be noted that the rubber growers have easy access to formal credit institutions. Moreover, being educated and resourceful they are not at the receiving end. On the other hand, it would appear as though the traders are more keen on extending the loans to the growers in order to get hold of the produce than the latter in getting the loan. There is a high degree of competition among the traders and the cultivators are aware of it. The latter also keep their eyes and ears open to the daily price trends of rubber at different marketing centres which are reported in the local newspapers and by the All India Radio. The traders do not charge any interest on such commodity-tied loans. Nor are they able to levy an implicit interest by underpricing the produce. In Vilpatti vegetable cultivators are reported to take loans from traders from the wholesale markets. The cultivators are committed to dispose of their produce through their creditors at a pre-determined price. The loan is repaid through the delivery of crop which is valued at a price lower than the going price. Thus, there is some implicit interest involved in the transactions. At Thalikulam, linked credit transactions are reported in the fishing industry. The boat owners, majority of whom do not belong to this village, depend on the local middlemen

for marketing their ^{fish} catch and obtaining short term credit. The middlemen auction the catch on the beach. The fish venders generally are not able to pay the price on the spot, but require some time. But in the meantime, the boat owners need cash to meet the expense such as cost of operations, maintenance of the boat, payment of wages, etc. They, therefore, seek credit from the middlemen on the condition that the catch will be sold through them at a price arbitrarily fixed by the middlemen. Though the loans are avowedly interest free, there is apt to be a concealed interest in the price fixation.

The fishermen of Thalikulam who belong to the lowest strata of society lead a hand to mouth existence. Employment is seasonal and even during the fishing season their earnings are subject to large variations. Their access to institutional credit is limited and their employers, the boat owners, are the only source of credit. Whenever they are in financial stress, they take loans from boat owners, committing their services to the letter. The contract is usually for one year. The loan is adjusted from their wages. Apparently no interest is charged on the loans, as the boat owners are keen on ensuring the services of experienced and hard working fishermen during the peak season.

To sum up: The rural credit markets in the developing countries are generally dominated by informal credit agencies. The ICMs in these areas are characterised by personalised transactions and therefore segmented. Interlinkage of credit with land, labour and commodity markets is also observed. However, with expansion of formal credit and weakening of the traditional institutions like tenancy and bonded labour, the structure of the ICMs would undergo some transformation. The competition of formal credit institutions which lend at subsidised, interest rates would make moneylending by informal lenders like professional moneylenders increasingly non-lucrative and unattractive. The pressure would be felt also by landlords, agriculturist moneylenders and traders. The outcome would be a steady decline in the quantum of credit from the above agencies. Given the inequitable distribution of institutional credit, the households who are denied access to it would have to rely on informal credit sources. Even in their case, the non-professional, non-commercial, credit agencies, namely, relatives, friends or neighbours would emerge as the principal sources of credit. In the process, interlinkage of credit with land, labour and commodity markets would also get gradually eroded. The findings of our field studies seem to exemplify the above inferences on the structural transformation of the ICMs in the wake of a steady expansion of formal credit and changes in the social and institutional set up in the rural areas of the country.

APPENDIX 3

Informal lenders : a few case studies

To identify sources of informal credit like professional moneylenders, agriculturist moneylenders, etc. and to elicit accurate information on their sources of funds, business turnover, the terms and conditions of loan transactions are admittedly difficult even during normal times. Certain recent developments in Kerala have made the task more difficult. Since the first quarter of 1987 there has been a growing manifestation of the erosion of the soundness and credibility of the finance companies or the so-called "blade companies", as reflected in the massive runs on these institutions by depositors in different parts of the State. A large number of finance companies downed their shutters and their proprietors decamped, leaving a large number of persons from all walks of life who, attracted by the high rates of interest, left most of their savings with these agencies. Naturally, this evoked strong protests from the public and demands for penal action against the culprits and stringent regulation to prevent their recurrence. In the wake of these developments, the State Government initiated steps to issue an ordinance, closing the various loopholes in the Kerala Moneylenders' Act. And these developments had made the private moneylenders more inaccessible and reticent when we launched our field surveys. We faced serious difficulties in eliciting the relevant information from moneylenders in the

two Tamil Nadu villages also. In the case of Mookuperi, the villagers borrow from moneylenders located at Nazerath. When our Investigator approached one of them in his office he was so rude that canvassing of the questionnaire had to be given up. A new class of moneylenders belonging to Devar caste is emerging here of late. They are equally unapproachable. An official of the same caste advised our field staff not to approach the newly emerging group of lenders lest it affect completion of other facets of our study, if not personal risks. In Vilpatti, the moneylenders were less rude, but equally reluctant in parting with the requisite information. For that matter, even borrowers were reluctant to give any details relating to the activities of the professional moneylenders. The case studies presented below may be considered against this background.

A questionnaire was canvassed among such of these informal lenders in the selected villages as we could identify and who could be persuaded to respond to our queries. The queries included their sources of funds, the types of their clientele, amount lent, security accepted, rate of interest charged, average duration of loans, mode of repayment, default rate, etc. Besides friends and relatives, professional moneylenders, agriculturist moneylenders and traders were the main sources of informal credit among the sample households surveyed in the course of this study. We have canvassed our questionnaire only among moneylenders and traders. Needless to say, against the particular background referred to earlier, the respondents especially those from Kerala were more suspicious about the objectives of the study and reluctant to reveal all the facts.

(i) In Thirunavaya we could identify five moneylenders, carrying on credit transactions on a commercial basis. Only one of them is a fulltime moneylender. ✓ He is a Tamilian residing in the village in a rented building. He has been lending mostly to small farmers, agricultural labourers and small traders. The loan amounts are small, Rs.300 being the maximum. Loans are advanced against personal security. Repayments are in weekly instalments which he himself collects by going from house to house. Duration of the loan is 10 weeks. He does not accept deposits, but when he feels lack of liquidity he borrows from his friends or other moneylenders in Tamil Nadu. Last year he gave loans to 105 persons, a sum of about Rs.14000. Of these 75 borrowers were small cultivators, and 15 each agricultural labourers and other households. The rate of interest charged is high. For example, loan of Rs.100 is repaid in 10 weeks at the rate of Rs.12.8 per week, Rs.28 being the rate of interest for 2½ months. The remaining four combine moneylending with other activities. Two of them, with medium size land holdings, 3.25 and 10.9 acres each, and income from agriculture at Rs.15000 and Rs.50000 respectively during 1986, may be designated as agriculturist moneylenders, though one of them, besides cultivation, carries on arecanut trade. He advances loans to arecanut cultivators on condition that the nuts when ripe be sold to him. His clients are small and medium cultivators, size of loans small and duration 5 to 6 months. During 1986 he advanced loans to 8 such clients, and a total sum of Rs.7400. Interest is exacted by under-pricing the commodity by 10 to 20% of the going price when delivered as repayment of loans. Thus, the rate of interest would work out to

about 50% per year. He did not report any default. He sells the nuts so procured to a wholesaler who is a source of credit when he is in need of cash. The second one under this category had inherited a large holding and agriculture has been his main occupation. He started moneylending activity wayback in 1940. During the initial period he gave loans in kind, rice including seed, and later switched over to cash loans. His clients were cultivators, large and medium. Owing to increasing default rate, the difficulties he faced in litigation and also his advancing age (he is now over 70 years), he has been reducing his loan transactions. During the last two years he gave only 13 loans, a total sum of Rs.2 lakhs. The loan size ranged from Rs.500 to Rs.35000. The rate of interest reported to be levied is 20 percent. There is one case of a moneylender for whom the main occupation is said to be agriculture, but the area under cultivation during last year was a bare 20 cents yielding an income of Rs.2000. Infact, he is a retired Civil servant, and his wife a retired teacher. They have invested their past savings and retirement benefits such as gratuity and provident fund in credit transactions. They are having financial transactions with a few people, mostly medium and small farmers. Security depended on the size of the loan: small loans on personal security, and for larger loans, above Rs.5000, landed property. During 1986, 15 loans were given, most of them to cultivators, and they added upto Rs.32000. Mode of loan repayment was flexible, both lumpsum and instalment systems were allowed. According to the lender, the rate of interest charged varied, but the average would be 30 percent.

(ii) At Thalikulam we could contact four professional moneylenders, three of them being individual enterprises, and one a partnership firm. As different from traditional professional moneylenders, these agencies receive deposits, a common designation used by them is 'trusts'. The oldest among these (Janata Trust) is an individual enterprise, set up in 1964 with an initial investment of Rs.1000. The proprietor depended on deposits from his friends and relatives as the source of loanable funds. The office of the trust is located in his own building, and there are six employees involving a monthly salary bill of Rs.3590. Though an individual enterprise, the scale of transactions is quite impressive. During the last two years, deposits to the tune of Rs.4 lakhs have been received, and the annual turn over of loan transactions is claimed to be Rs.25 lakhs on the average ! According to the proprietor, interest is paid on deposits at the rate of 12 to 14%. Small farmers, agricultural labour and fishermen households comprise the major groups of borrowers. Loans are extended against gold and personal security. Duration of the loans varies from 60 to 100 days. The rate of interest charged was reported to be 24%. During last year only 4% of the borrowers or 16% of the outstanding loan amount was defaulted. The second enterprise (Kallara farm) was started in 1970 with an initial investment of Rs.8000. He has also been receiving deposits. The office of the enterprise is located in a rented building. There are two paid employees and their monthly salary will add up to Rs.650. Total deposits received during the last two years came to Rs.22000. On deposits, interest is paid at the rate of 10 to 13%, as reported by the proprietor. Total loan transactions during the last two years added up to Rs.4.5 lakhs. The size of loans is small, in the range of Rs.50 to Rs.1000. Low income groups of households including fishermen and agricultural labourers are

his principal borrowers. The rate of interest charged on the loan was stated to be 24% on the average. The default rate is not too high, 5% of the borrowers, and 20% of the loan amount, given the fact that the majority of his clientele belong to the low income groups. Another individual proprietorship (Sukumar Trust) started in the mid-sixties, and with an initial investment of Rs.7000 has made an impressive growth. The enterprise has grown apparently on the basis of deposits from friends and relatives, involving a nominal interest of 12% only. He has housed his office in a rented building, and is assisted by a staff of 3 members. The annual turn over of loan transactions increased from Rs.22.6 lakhs in 1985 to Rs.26 lakhs in 1986. The rate of interest on loans was reported to be 24%. The default rate, both in terms of the number of borrowers and loan amount was insignificant, viz., just 1%. The fourth is a partnership firm (Idassiar Trust) with 15 partners started recently (1984). The initial investment of Rs.3 lakhs was contributed by the partners. It accepts deposits, the total deposits received during the last two years comes to Rs.21 lakhs, and the interest paid on deposits reported being 10 to 12.5%. It is located in a building belonging to the SNDP Trust (Sree Narayana Dharma Paripalana Sangham), an organisation representing a particular caste (Ezhava). There are four employees including the manager, the total monthly salary bill coming to Rs.1500. The main borrowers of the trust comprise small farmers and fishermen. The interest on loans was claimed to be only 18%, but according to some respondents from the village the actual rate of interest charged worked out to 30% or more. Loans are mostly short term, upto 6 months, and secured against the pledge of gold.

(iii) At Anikad, we could contact a dozen informal lenders: one professional moneylender, four agriculturist moneylenders and seven traders or dealers in rubber. The professional moneylender started his business quite recently (1983), with an initial capital of Rs.2.5 lakhs. The source of his funds included his own household income, (he is cultivator, with over 4 acres, three-fourths of which is under rubber), and contributions from his brothers. The enterprise received deposits, the total of which for the last two years was reported at about Rs.4.5 lakhs, mostly from friends and relatives. The interest paid on the deposits was reported to be 24%. The office of this enterprise is located in a rented building for which monthly rent being Rs.500. There is no salaried staff attached. The scale of transactions has been quite impressive. Total turn over came to about Rs.18 lakhs in 1985 and a little over Rs.19 lakhs next year. The loans are given mostly on the security of gold pledged with the firm. Duration of the loans ranged from 3 months to one year, and repayment either in lumpsum or instalments is allowed. Most of his clientele are small farmers, 219 of whom were recipients of loans during the last two years. The rate of interest came to 36% on the average. The four agriculturist moneylenders had medium to large holdings in the range of 3.75 to 14.75 acres. Rubber is the principal crop, accounting for more than two-thirds of the cropped area. The income from agriculture during the last one year ranged from Rs.7000 to Rs.30000. Three out of the four normally borrow from the local cooperative credit institutions, Anikad Regional Farm Cooperative Bank. Majority of their clientele comprised cultivators, followed by agricultural labourers. The loans are of short term duration,

3 to 6 months, and are issued against the security of gold, land and, to a limited extent, personal. There seems to be a uniformity in the rate of interest charged; all the four have reported 36%. One of the four in the category, the person with the largest number of households, viz., 75 of which 55 constitute cultivators. The maximum amount lent to an individual varies from Rs.500 among agricultural labourers to Rs.5000 with large cultivators. He depends solely on his own resources, and does not accept deposits or borrow from others. During the last one year he has lent a total amount of Rs.1 lakh on which he charged 36 to 60% as interest. The duration of these loans is 3 months. About 10% of the borrowers have defaulted, which constituted 5% of the loan amount. Traders form a major source of credit. We could contact eight of them in the village. All of them are dealers in rubber. By and large, their lending is financed with own resources; none of them had accepted deposits, and only half of them had to seek credit from cooperative society, commercial banks or friends and relatives. Annual turn over of loan transactions registered a significant increase between 1985 and 1986. In 1986, it ranged from Rs.5.1 lakhs to Rs.23 lakhs. Together these eight persons extended loans totalling a little over Rs.79 lakhs. They limit their loan transactions to cultivators, obviously to rubber cultivators, who are committed to sell their produce to the trader - creditors. Apart from this condition, there is no other security. There is no explicit interest charged on the loans. According to these traders, there is no underpricing of the commodity when delivered for settling the loan outstanding. The duration of the loan is short, say 1 to 4 weeks. Perhaps, the growing

competition among rubber dealers and the short duration of the loans may be the factors underlying interest-free loans, if true.

(iv) At Ezhukone, we could contact five informal lenders, four of whom were professional moneylenders and one an agriculturist moneylenders. All of these enterprises were of recent origin, started during the present decade. Given their comparatively short life and initial investment, their rate of growth is impressive. For example, one enterprise started in 1985 with an initial capital of Rs.30000 had a turn over of loans to the tune of Rs.5 lakhs; another started in 1983 with an initial investment of Rs.1.5 lakhs reported its total loan transaction of Rs.19 lakhs in 1986. Of the four, only one, the oldest among them has received deposits so far; the other three are of more recent origin, since 1985, and they are yet to establish their credibility. Two of them have augmented own resources by borrowing from friends and relatives on which they pay an interest of 12 to 15%. Two of them are functioning with an office in a rented building. The annual turn over of loan transactions varied from Rs.1.5 lakhs to Rs.19 lakhs. Gold, landed property or personal security is the basis on which loans are extended. Interest charged from 30 to 36%. The default rate is generally low. Of the four, the oldest is a partnership of four members. Set up in 1983, it (Kumar Bankers) is a typical finance company. Its initial capital was Rs.1.5 lakhs, contributed by four parties. The bank is located in the proprietor's own building and has eight employees. The monthly salary bill amounts to Rs.3000. Deposits, received from friends and relatives during the last two years totalled Rs.10 lakhs on which interest paid varied from 12 to 24%. Between 1985 and 1986, total loan transactions more than doubled from Rs.9 lakhs to

Rs.19 lakhs. The size of loans fall in a wide range, from Rs.20 to Rs.2 lakhs. Businessmen, Gulf migrants, and farmers were the main categories of borrowers. Duration of loans varied from 6 months to 3 years. The rate of interest charged came to 30% on the average. On loans for agricultural purposes, the bank charges a lower interest. The bank has adopted a differential interest scheme, discriminating between different group of clients, apparently on the principle of each according to his ability. The poor are given interest-free loans; cultivators lower interest at less than 30%, while a few contractors are charged 46%. The agriculturist moneylender has 4 acres of land of his own, one fourth of which is under paddy and the rest under coconut and tapioca. Income from this source during last year came to Rs.20000. He uses his own funds for his lending activities, though occasionally he borrows from his kith and kin. The amount borrowed during last year was Rs.10000. During that period, he extended loans to 145 persons, 85 of whom were cultivators, 10 agricultural labourers and 50 businessmen. The size of loans ranged from Rs.50 (agricultural labour) to Rs.2000 (businessmen). The average duration of loan was reported to be 3 months and interest rate 36%. Only 4% of the borrowers seem to have defaulted who accounted for about 10% of the total loan amount.

(v) In Mookuperi, one of the professional moneylenders, operating from Nazareth, owns 5 acres of land. His cultivation activities have declined as a result of persistent drought conditions. His father had entered the field of moneylending as early as 1945. At present,

his investment in the business comes to Rs.1.75 lakhs. He does not accept deposits. He occasionally used to borrow from other moneylenders to whom he paid an interest of 24%; but during the last two years he has not resorted to borrowing. The annual turnover of loan transactions in 1986 was reported to be Rs.2.4 lakhs. The only security acceptable to him is gold. The normal duration of loan is six months. The rate of interest charged by him is 30%. He lends to all occupational groups; however, for reasons of risk of default, cultivators have lower priority than salaried classes and business people. Borrowings by the last group are at a peak during festival seasons like Divali, Pongal and Christmas. Such loans are of short duration, 15-20 days, and he charges 7 to 10% interest for this short period. The default rate was reported to be Rs.10000 to Rs.15000 per year, which is not too high given the scale of turnover during 1986. The agriculturist moneylender in the village owns a little over 5 acres, of which 2 acres are irrigated. He combines agriculture with moneylending; for the latter he depends on his own resources. He lends mostly to petty traders and labourers, the size of loans varying from Rs.50 to Rs.2000. If gold is not available, articles like cycles, utensils, etc. are accepted as security. Interest charged comes to 60% per year.

(vi) For Vilpatti, one party which cooperated with us most is a finance company which has the earliest start of lending in this village. This is a registered firm with an office located at Kodaikanal. Every Friday, the proprietor or his agent visits Vilpatti for carrying on the credit transactions. This firm was started in 1962 by a Muslim Moneylender

settled down in Kodaikanal. The present owner of the firms was an employee with the firm till 1972 when its proprietor transferred the entire assets, i.e. loans due to him as a gift. The present owner started afresh, as it were, with an initial capital of Rs.50000 part of which was from collection of outstanding loan amounts due to the present company, and the rest his own savings. He neither accepts deposits nor borrows for the conduct of the business. His clientele include cultivators, traders and agricultural labourers. The rates of interest vary from 24% in the case of big farmers to 90% for traders. The second case is difficult to classify; he is neither a professional moneylender, nor agriculturist moneylender. He owns 15 acres of land of which only one-third is cultivated. Besides cultivation, he carries on trade in seeds, fertilizer, etc. Moneylending he started very recently (1985), with an initial capital of Rs.50,000. He lends to small and marginal farmers, agricultural labourers, shop keepers, etc. Agricultural labourers who are granted loans are committed to work for the creditor when he needs their services. The loans are on the basis of the daily Kandur system, and adjusted to the daily wage bill. The wages are reckoned at Rs.2 per day below the going rate, and this deduction forms the interest on the loan. The loan amount varies from Rs.50 to Rs.200. To cultivators the loans are in kind, viz., fertilizers (and seeds). He takes fertilizers from wholesale traders on credit and distributes the same to farmers also on credit. On the credit purchases from wholesalers he has to pay an interest of 18% while on credit sales to his outcomers he charges from 24% to 36% interest. His business turnover on this account during 1984-85 was reported as 33 tonnes of fertilizer worth Rs.15000; during 1985-86 the turnover had sharply

declined to 4 tonnes, valued at Rs.4000. On his transactions in seeds, no information was forthcoming. On the loans to the shop keepers, interest is deducted in advance. For instance, only Rs.800 is disbursed for a loan of Rs.1000 the duration of which is 100 days. We shall now present the case of a vegetable trader. He is himself a small cultivator, but his main occupation is vegetable trade. He lends to small and medium farmers, in the range of Rs.500 to Rs.1000. Loans are given on the condition that the borrowers sell their vegetables to him. The price of vegetables so delivered is fixed at Rs.4 less per bag than the going price prevailing in the apex market at Madurai. In case the borrower hypothecates the crop in advance, the deduction on the price is even higher, because of the longer waiting period on the part of the trader-lender in procuring the crop, and the risk of loss inherent in price fluctuations. The trader disposes of the crops through commission 'Mandi' owners at Madurai, who give credit to the farmers and traders of vegetables. They only act as middlemen. It is estimated that the annual turnover of trade on vegetables at these mandies comes to Rs.2 lakhs. The mandie owners have advanced Rs.15000 to 20 small farmers, Rs.22000 to medium and Rs.5000 large farmers at Vilpatti. The growing crop is the security for the loans. The commissions in vogue at present are Rs.4 per bag of potatoes, Rs.2 per bag of turnip and sonai, and 10 paise per rupee worth of beans. Thus, in Vilpatti credit and marketing are interlinked to a great extent thanks to the prevailing cropping pattern.

CHAPTER 6

INTEREST RATE FORMATION IN THE RURAL ICMs

6.1 Introduction

It is generally held that the interest rates in the rural ICMs of developing countries are exorbitant. The usurious interest rate has many implications. It inhibits the use of credit for productive purposes and diverts credit into socially unproductive channels like conspicuous consumption, hoarding, and speculation. The high cost of credit from informal sources, on which households from the lower income and asset classes depend heavily, accentuates inequalities in the credit market. As has been argued (Bhaduri, 1975), high interest rates charged by informal lenders lead to default of loan and eventual forfeiture of land and other assets offered as collateral by the borrower. High interest rates may perpetuate indebtedness on the part of some borrowers who are compelled to keep on borrowing to repay past debts, thereby cementing inter-linkages of credit with land, labour, and commodity markets. No wonder that this phenomenon has attracted so much attention of academicians and policy makers alike. The level of interest rates in the ICMs, nominal and real rates, explicit and implicit interest, the factors underlying the high rates, the relative shares of the different explanatory variables, the wide range of interest rates prevailing in the ICM of the same locality, inter-group and intra-group differences in interest rates are the major issues on which recent research efforts have been focussed.

5.2 Level of interest rates in the rural ICMS

As pointed out by Sarap,

"Calculation of in the informal credit market presents some difficulties. For instance, a portion of such loans is made in kind and the kind rate of interest involves valuation of commodities advanced as loan and refund liabilities. In some cases such as kind to cash loans, the interest rates attached to the loans are subsumed because while the loan liabilities in terms of quantity of grain remains constant, the value of the same quantity of grain at the time of loan repayment differs from the time of loan offer. Some times, creditors overvalue the commodities advanced as loan and undervalue the repayable commodities".
(Sarap, 1986, pp. 115-116).

The above situation arises in the loan transactions of a linked type, the focus of sarap's analysis. Implicit or concealed interest in inter-linked credit transactions, which escapes the estimates based on data of macro studies, has also been brought out by a number of other researchers. Apart from this, there are other constraints in the estimation of effective interest rates on informal credit. For instance, it is a common practice to deduct interest from the principal at the time of loan disbursement. For another, interest at an annual rate is levied even when the duration of the loans is only a few months. Last, but most important, it is difficult to obtain the necessary information either from the borrower, who is seldom willing to divulge the information for obvious reasons. The information on the interest rates charged on loans from informal lenders to cultivator households was collected by the All India Rural Credit Survey during 1951-52, and included in one of the reports.

According to the findings of this survey, the proportion of cultivator households paying an interest rate of 25 percent and above ranged from 27 percent in Bihar to about 70 percent in Orissa. (Reserve Bank of India, 1955, p.67). Apart from this crude approximation of the proportion of cultivator households paying an interest above a certain rate, the report does not contain any information on this question. However, the reports of the two rounds of the All India Debt and Investment Survey, 1961-62 and 1971-72, conducted by the Reserve Bank of India, did not contain even this bit of information. That agency-wise data on the rates of interest are not available has been noted in the reports. (Reserve Bank of India, 1969, p.119; Reserve Bank of India, 1977, p.143). But why such crucial data are not available is left unexplained.

In the course of our micro studies we attempted to collect information on interest charged by informal lenders such as professional moneylenders, agriculturist moneylenders, traders, and friends and relatives. As brought out in other studies, we observed considerable information gap on the part of the respondents regarding the actual or effective rate of interest due on their loans. For instance, a certain annual rate of interest is charged even when the loans are of shorter duration. Advance deduction of interest at the time of disbursement of loans is not uncommon; where a trader advances loans to a grower vegetables, interest is concealed in the undervaluation of the crop which the latter is under obligation to sell to the former at a predetermined price, significantly lower than the going price. These limitations must be kept in mind when examining the data presented below. The average (weighted) rates of interest cash loans

taken by the sample households in the selected villages are set out in Table 6.1.

Table 6.1 : Average rate of interest on loans from Informal Credit Agencies
(Percent per annum)

Village \ Credit Agency	Professional moneylenders		Agriculturist moneylenders		Traders		Friends & Relatives
	Average	C.V. %	Average	C.V. %	Average	C.V. %	Average
Thirunavaya	54	127	--	--	nil	--	Nil
Thalikulam	53	10	--	--	--	--	Nil
Anikad	41	104	29	54	60 ^{a/}	--	Nil
Ezhukone	30	17	34	10	--	--	Nil
Vilpatti	60	86	24	0	13	161	Nil
Mookuperi	24 ^{a/}	--	--	--	Nil	--	43.03 ^{b/}

a/ Only one observation

b/ Out of 15 borrowings from friends and relatives, 11 are interest free.

(a) Professional moneylenders

Thus, the average rates of interest on borrowings from professional moneylenders is seen to range from 30 percent in Ezhukone to 60 percent in Vilpatti. There is considerable variation among households in the same villages in the rates of interest charged by this group of lenders, as reflected in the high coefficient of variation in three out of five villages where borrowings are reported from this source. It is significant that the majority of the loans borrowed bear high interest, above 24 percent a year.

The following table (Table 6.2) shows the distribution of loans according to interest rate.

Table 6.2 : Number of borrowings from professional moneylenders classified according to rate of interest

Rate of Interest Percent	Village						
	Thirunavaya	Thalikulam	Anikad	Ezhukone	Vilpatti	Mookuperi	All
0	-	1	-	-	-	-	1
1 - 6	-	1	-	-	-	-	1
6 - 12	-	-	-	-	-	-	-
12 - 24	-	3	-	1	2	1	7
24 - 36	2	17	4	9	1	-	33
36 - 60	-	-	1	-	2	-	3
Above 60	16	1	4	-	22	-	43
All	18	23	9	10	28	1	88

It may be noted that more than one-half of the total loans carry an interest rate above 36 percent; further, the interest rate on nearly one-half of the total number of loans is above 60 percent. It may also be noted that they are mostly distributed between two villages, viz., Thirunavaya and Vilpatti. In fact, of the total 18 loans reported from Thirunavaya, the interest rate on 15 of them is 120 percent; in Vilpatti, 14 and of the 22 in the above-60 percent interest loans carry a uniform rate of 12 percent. Apparently, in the other four villages, such high-interest loans are absent.

(b) Agriculturist Moneylenders

Before coming to the rate of interest charged by agriculturist moneylenders, we have to note the comparatively minor role of this agency as a source of credit. In all the villages together, only 12 loans are reported from the source. (Table 6.3). In two of them, Thalikulam and Mookuperi, they are apparently absent. In Thirunavaya only a solitary loan has been reported and that is avowedly interest-free. In Vilpatti, Ezhukone and Anikad, the number of loans came to 2, 3 and 6 respectively. Of these, in Vilpatti and Ezhukone the range is within 24 to 36 percent, while in Anikad it falls in the range of 18-60 percent. Thus, the range of variation of interest rates reported in the case of this category of creditors seems to be significantly less than that for professional moneylenders.

Table 6: Number of Loans from Agriculturist Moneylenders classified according to rate of interest

Rate of Interest Percent	Village	Thirunavaya	Thalikulam	Anikad	Ezhukone	Vilpatti	Mookuperi	All
0		-	-	-	-	-	-	-
1 - 6		-	-	-	-	-	-	-
6 - 12		-	-	-	-	-	-	-
12 - 18		-	-	-	-	-	-	-
18 - 24		-	-	2	-	-	-	2
24 - 36		-	-	3	3	2	-	8
36 - 60		-	-	1	-	-	-	1
60 & above		-	-	-	-	-	-	-
All		1	Nil	6	3	2	Nil	11

(c) Traders

In two of the selected villages, viz., Thalikulam and Ezhukone, traders are not reported as a source of credit. They are most prominent in Thirunavaya where 27 loans have been reported from this source, and in Mookuperi where the number came to 8. However, the loans are avowedly interest-free. Only in Vilpatti, interest is reported on loans from this source, at rates ranging from 10 to 60 percent, the weighted average being 13.33 percent.

The 27 cases reported in Thirunavaya are not actually cash loans, but seller's credit, i.e., consumer goods purchased from local merchants on credit. A good proportion of the concerned households belong to lower income strata like headload workers and other casual labourers, and the purpose being obviously consumption, the elasticity of demand is bound to be low. The volume of transactions is also comparatively low, the average coming to less than Rs.450. In Mookuperi also, loans reported are actually credit purchases, mostly utensils and clothes from itinerant merchants. No explicit interest is charged on the goods sold on credit in these two villages. However, we have to take note of the fact that these traders meet urgent, comparatively inelastic, demand of the participating households who have very limited options. Being short of liquid assets, the other option before the concerned households would be to borrow from local money-lenders at a high cost. Therefore, they should be prepared to recompense the traders who provide them goods on credit. As for the traders, on the other hand, though maintaining good relations with their customers is

essential for the smooth running of their business, being small merchants with limited resources, the opportunity cost of extending credit sales is bound to be high. They also command some monopolistic or oligopolistic powers over their customers. Under these circumstances, overpricing of goods sold on credit to elicit some interest is not an unlikely proposition. The practice of cultivator households in Vilpatti taking loans from vegetable merchants in the wholesale markets of Kodaikanal and Madurai we have already referred to. In the case of such loans, the cultivator-borrower hypothecates his crop which has to be sold to the creditor at a pre-determined price. The trader-cum-lender gets a wide margin, which includes also a high rate of interest. Compared to other borrowers, those who avail of credit from traders, whether as cash loans or commodity loans, are more vulnerable to usury, the extent of which they may not be aware themselves. Nor are we in a position to estimate the implicit or concealed interest in such credit transactions.

(d) Friends and Relatives

As noted before, friends and relatives constitute the leading source of informal credit in our selected villages - both in terms of the number of loans and volume of credit. Almost all these loans are reported to be interest-free, except in Vilpatti and Mookuperi. In the former, of the 13 loans from friends and relatives, 9 are interest free. On the remaining 4 loans, interest is charged ranging from 16 to 120 percent. In Mookuperi, the total number of loans from this source comes to at, out of which two-thirds are without interest; the interest rate on the remaining five ranges

from 24 to 120 percent. However, the average (weighted) rate of interest on all loans from this source even in these two villages will be much lower than the interest rates on loans from formal credit institutions. Overall, loans from friends and relatives are interest-free, and being extended for non-pecuniary considerations, they are non-commercial. The distribution of loans from all informal credit agencies, except friends and relatives, in the selected villages, classified according to the average rates of interest is presented in Table 6.4

Table 6.4 : Distribution of loans from Informal Credit Agencies classified according to average rate of interest

Rate of Interest Percent	Village						
	Thirunavaya	Thalikulam	Anikad	Eshukone	Vilpatti	Mookuperi	All
0	31 (63.3)	1 (4.3)	-	-	2 (5.4)	8 (88.9)	42 (28.96)
0 - 6	-	1 (4.3)	-	-	-	-	
6 - 12	-	-	-	-	2	-	2 (1.37)
12 - 24	-	3 (13.0)	2 (12.5)	1 (7.7)	6 (16.2)	1 (11.0)	13 (8.27)
24 - 36	2 (4.1)	17 (73.9)	7 (43.8)	12 (92.3)	2 (5.4)	-	40 (27.58)
36 - 60	-	-	2 (12.5)	-	3 (8.1)	-	5 (3.44)
60 & above	16 (32.7)	1 (4.3)	5 (31.3)	-	22 (59.5)	-	44 (30.34)
All	49 (100)	23 (100)	16 (100)	13 (100)	37 (100)	9 (100)	147 (100)

Note: Figures in brackets denote percentages.

It may be noted that, notwithstanding quite a few interest-free loans, the largest number of loans are those with an interest rate of 60 percent and above. However, this group of loans are concentrated in two villages, Thirunavaya and Vilpatti, which together account for more than four-fifths of these high interest loans.

5.3 Factors underlying interest rates

A major thrust of the research efforts on interest rates in the ICMEs of developing countries has been directed at identifying the explanatory variables underlying it. One set of studies attempted to decompose the components of the interest rates. In this context, Bottomley (see for instance: Bottomley, 1963, 1965, 1975) had identified four components of interest rates, viz., (a) the opportunity cost of money involved, (b) the premium for administering the loan, (c) the premium for risk, and (d) monopoly profit. Of these, "administration charges, together with the premium for risk are probably the major determinants of the high level of interests which obtain throughout the underdeveloped world". (Bottomley, 1963, p.646). Commenting on the above, Chandavarkar (1965) has argued that "the degree of monopoly power of the lender may well be the most important single determinant of interest rates". Millard Long (1968) and Charles Nisbet seem more or less to agree with this position. Bhaduri examines the formation of usurious interest rates in backward agriculture against the background of the peculiarities of agrarian credit market such as its isolation, its highly personalised nature, the exceptional economic power of the lender, the kinds of collaterals accepted by private lenders - though unmarketable in the organised money market - the lender's

ability arbitrarily to value such collaterals and to set the interest rate. In this situation, there is no risk of default; in the event of default, the value of transferred collaterals would exceed the value of defaulted risk, thanks to the undervaluation of the collaterals.

"Lender's risk is then reduced to an irrelevant concept... With lender's risk reduced to an irrelevant concept, usurious extraction can be seen to form the very basis of interest rates in unorganised money markets. Since default on a loan taken against undervalued collaterals works to the economic advantage of the lender, he will quite naturally have an incentive to raise the interest rate to a level which induces default of both principal and interest on a large scale". (Bhaduri, 1977, p.351).

The formation of usurious interest rates in the informal credit markets of developing countries may be examined from the demand and supply sides. Looking from the demand side, the purpose for which the loan is used - the degree of elasticity of demand for the goods on which the loan amount is spent which in turn is reflected on the elasticity of demand for funds - the borrower's access to alternative sources of credit, the borrower's income and asset levels, etc. have a bearing on the interest rate. Looking from the supply side, the degree of monopoly power of the lender, his hold on the borrower in the form of non-credit links, his position in the rural power structure and ability to enforce the terms and conditions of loans, etc. influence the rate of interest. Bandyopadhyay (1981) has analysed the factors underlying inter-farm variations in interest rates in West Bengal. The factors which have been identified to be relevant are (a) nature of security, (b) purpose of borrowing, (c) duration of loan (d) size of holding, and (e) size of loans. Of these, the purpose of loan,

whether for consumption or production, is a factor which determines the degree of elasticity of demand for credit and the size of holding, a proxy for the resource position and bargaining strength of the borrowers. The nature of security, duration of the loan, size of loans, and size of holding are variables which influence the lender's assessment of the credit worthiness of the borrower, and costs of administering the loans. The data yielded by the study showed correlation between interest rates, and the variables listed above, and the signs are along the expected lines: positive in the case of unsecured, consumption purpose, short duration, and small sized loans and negative in the case of size of holding. (Bandyopadhyay, pp. 103-110).

Sarap (1986) examines the differential rates of interest on loans from informal lenders in Sambalpur district, Orissa state, and brings out the influence of the purpose of loans, the size of loans, cash deficit/surplus position of households, etc. The findings of the field survey brings out that interest rates are higher on linked credit transactions, on loans for medical purposes, loans of small size, and those taken by households with cash-deficit position.

"Our findings show that in the inter-linked credit transactions the borrowers have to pay higher rates of interest compared to non-linked credit transactions, that as much as 25% of the total effective interest was hidden in such transactions, that even within the inter-linked credit market interest rates varied for different borrowers depending upon the inelasticity of demand for loans, which, in turn, is influenced by the purpose of loan". (Sarap, p.123).

Karkal (1967) proffers a longer list of the factors affecting interest rates in the unorganised credit market. They are: (1) element of risk involved in lending, (2) credit worthiness of the borrower, (3) liquidity of security, (4) monopolistic or monosonistic situation of the trader - moneylender, (5) extent of urgency, i.e. elasticity of demand for funds coupled with inelastic or limited supply of funds with the lender, (6) availability of owned and borrowed funds with the lender, (7) adequate security behind the loan, (8) size and period of loan, and (9) other socio-economic factors. (Karkal, p.83).

In brief, the purpose of loan or elasticity of demand for credit, size of loans, its duration, nature of security, asset size or credit worthiness of the borrower, and degree of monopoly control on the part of the lender are the factors underlying interest rates in the ICMs. However, in the final analysis, they all seem to boil down to the resource position of the borrower, asset size, or cash deficit/surplus position. The elasticity of demand for credit, size and duration of loan, security and credit worthiness of the borrower vary positively with size of assets. The borrowers at the bottom rung generally have more urgent or inelastic demand, take loans of smaller size for shorter duration, are perceived to have less credit worthiness, and less collateral security to offer; further they have limited options other than informal sources such as professional moneylenders. So other things being the same, the rate of interest on loans from informal credit agencies should vary inversely with the size of borrowers' assets.

Returning to our selected villages, as noted earlier, loans from friends and relatives are interest-free. Borrowings from agriculturist moneylenders are not reported in half of the selected villages. Loans from traders are reported in four of the villages, but in two of them they are apparently interest free. On the other hand, professional moneylenders have wider presence and larger scale of transactions than agriculturist moneylenders and traders. Therefore, we shall focus our attention on the loan transactions of professional moneylenders in the selected villages.

(i) Purpose of the loan

It is generally presumed that loans put to consumption purposes carry higher interest rates, because the demand for consumption loans is more inelastic. In our study areas also, the average rate of interest on 'consumption loans' in its wider connotation (including loans used for building houses, marriage, etc.) is higher than that on loans used for production or other purposes. (see Table 6.5).

It may be noted that out of the total 88 loans from the professional moneylenders in all the villages together, loans for consumption per se add up to 47 or over one-half. Of these 47 loans, 45 carry an interest rate of 75 percent or above.

Table 6.5 : Average rate of interest (percent) on loans from professional moneylenders classified according to purpose

Purpose	Village Thirunavaya	Thalikulam	Anikad	Ezhukone	Vilpatti	Mookuperi	All
1. Production	40.0 (6)	13.0 (2)	36.0 (1)	-	75.0 (7)	24.0 (1)	(27)
2. Consumption	125.0 (8)	105.0 (13)	76.0 (4)	30.0 (2)	75.0 (20)	-	(47)
3. Construction and repairs of house	-	16.0 (3)	-	31.0 (2)	-	-	(8)
4. Marriage	125.0 (1)	30.0 (2)	50.0 (2)	17.0 (1)	-	-	(6)
5. Education	-	-	-	36.0 (1)	-	-	(1)
6. Others	124.0 (3)	28.0 (3)	48.0 (2)	30.0 (1)	-	-	(9)
All	(18)	(23)	(9)	(10)	(27)	(1)	88

Note : Figures in brackets denote the number of loans.

(ii) Occupation of borrowers

Among different occupational groups, agricultural and other casual labourers account for more than one-half of the number of loans from the professional moneylenders in three of the selected villages, though their share of the total amount of credit from this source is comparatively small. Belonging to the lowest income and asset class, a larger proportion of their loans would be used for consumption purpose. Thus, thanks

to their low income level, the demand for essential consumption goods, and, therefore, the resulting demand for credit to meet it, turns out to be more inelastic than credit for other purposes. That is, it is not the purpose of the loan which determine the interest rate, but rather the resource position of the borrowing groups. The average rates of interest on loans from professional moneylenders to agricultural and other casual labourers in juxtaposition with those to cultivators and salary earners are presented in Table 6.6.

Table 6.6 : Average Rates of Interest on loans from professional moneylenders according to occupational groups

Village \ Occupation	Cultivators	Salary earners	Wage earners
Thirunavaya	35.00	-	125.00
Thalikulam	30.00	30.00	28.00
Anikad	39.00	-	67.00
Ezhukone	21.00	30.00	36.00
Vilpatti	40.00	-	34.00
Mookuperi	-	-	-

Thus, in three out of the five villages, loans taken by agricultural and other casual labourers bear significantly higher interest rates. Only in two villages interest on consumption loans borrowed by cultivator households are higher, but in one of them the difference is marginal.

(iii) Size of loans

Another variable which is cited to affect the interest rate in the ICMs is size of the loan. It is presumed that the interest rates on loans from informal agencies vary inversely with the size of loans. The avowed reason for the inverse relationship is the higher administrative costs on smaller loans. The average rates of interest on loans from professional moneylenders in our study areas classified according to size of loans, are given in the following table.

Table 6.7 : Average rates of interest of loans from professional moneylenders according to size of loans

Size of loans Rs. \ Village	Thirunavaya	Thalikulam	Anikad	Ezhukone	Vilpatti	Mookuperi
Upto 500	125 (16)	29 (11)	82 (5)	30 (2)	84 (20)	-
500 - 1500	-	30 (3)	45 (3)	30 (2)	53 (4)	-
1500 - 2500	-	28 (3)	-	28 (3)	90 (2)	-
2500 - 5000	35 (1)	67 (6)	-	32 (3)	Nil (1)	-
5000 - 10000	35 (1)	-	36 (1)	-	-	-
Above 10000	-	-	-	-	-	24 (1)
All (No. of loans)	18	23	9	10	27	1

The rates of interest do not seem to fall steadily as the size of loan increases in all the selected villages. However, the average rates of interest in the case of loans of the smallest size are significantly higher in some of the villages. In two of the selected villages, viz., Thirunavaya and Vilpatti, the correlation between the two variables is highly significant, viz., -0.9940 and -0.6778 ; in Anikad, the coefficient is not significant, viz., -0.4221 . On the other hand, in two of the villages, Thalikulam and Ezhukone, the correlation is positive, though not significant, viz., 0.3749 and 0.9623 . In Mookuperi, it may be recalled, there has been only one observation.

6.4 Components of interest rates

(i) Administrative Costs

Even if the correlation between the size of loan and interest rate were negative and significantly high in all the villages, it could as well be a spurious relationship, a mere statistical coincidence. Higher interest rates on small sized loans need not necessarily be due to the higher administrative costs. As Plateau, et.al have observed;

"For the theory of administrative costs to be valid, two basic conditions must be met: (a) administrative costs must be perceived as such by the lenders and (b) they must be assessed in monetary terms... neither of these conditions can be taken for granted. For one thing, lenders do not usually keep detailed accounts of their money transactions and supervision costs are likely to be low in overcrowded areas where social control is easy. For another thing, the time and energy which they have to spend in order to collect the interest payments and to recover the principal of the loans are not necessarily considered by them as having a money equivalent and as forming a cost-component liable to enter into economic calculation pertaining to their moneylending business". (Plateau, et.al, op.cit., p.320).

With the entry of the new generation of professional moneylenders, the finance companies, the transaction costs might increase. The new moneylenders' scale of transactions is larger. They mobilise savings. For canvassing deposits, collection of interest and recovery of principles, keeping accounts, etc. they have to employ paid staff and maintain an office. Therefore, some costs are involved, which would increase with the volume of transactions. The administrative costs incurred by a sample of professional moneylenders in the selected villages are shown in Table 6.8.

Table 6.8 : Costs of Administering Loans for Professional moneylenders in the selected villages 1986

Village	Lender Series	Annual turn over Rs.	Administrative cost Rs.			Ratio of col.6 to col.3 %	Interest rate reported by	
			Rent	Salary	Total		The lender	The borrower
1	2	3	4	5	6	7	8	9
Thirunavaya	1	3422400	3600	12000	15600	0.45	24.0	54
Thalikulam	1	2600000	6000	54600	60600	2.33	24.0	
	2	250000	600	7800	8400	3.36	24.0	
	3	300000	N.R.	18000	18000 x	6.00	30.0	53
	4	2600000	600	4000	40600	1.56 (3.31)	24.0 (25.5)	
Anikad	1	1916250	6000	12000@	18000	0.93	36.0	41
Ezhukone	1	500000	1200	Nil	1200	0.24	36.0	
	2	150000	2400	14200	15600	10.40	36.0	
	3	1900000	NR	36000	36000 x	1.89	30.0	30 ^x
	4	500000	NR	1200	1200 x	0.24 (3.19)	36.0	
Vilpatti	1	100000	NR	NR	NR x	0.00	NR	60
Mookuperi	1	100000	2100	-	2100	2.10	30.0	
	2	125000	-	-	-	0.00	30.36	24 ^x

It is seen that administrative costs in the Kerala villages vary, on the average, from 0.45 percent of annual turn over in Thirunavaya to 3.31 percent in Thalikulam. As against this, no administrative costs are reported in Vilpatti, and it works out to 2.10 percent in Mookuperi. Incidentally, Millard Long had "conservatively" assumed the average administrative cost of rural credit as 3 percent. (Long, op.cit., p.282). It is significant to note that the interest rates charges by different moneylenders as reported by themselves, do not show a consistent relationship to their transaction costs. In other words, interest rates do not vary *pari pasu* with administrative costs. In the same village, for example, Thalikulam or Ezhukone professional moneylenders with different administrative costs charge the same rate of interest. Whether these administrative costs are high and whether they can explain the high interest rates prevailing in the study areas, the answer appears to be negative. For, the average administrative costs in most of the villages do not seem to constitute a high proportion of the actual interests paid by the borrowers. (Compare columns 7 and 9 in the table).

In the light of the foregoing it seems that the higher interest rates on small size loans can not be explained by the premium on administering such loans. The explanation probably lies in the socio-economic characteristics of the borrowers. Other things being the same, the average size of loans should vary directly with the size of assets. Needless to say, it does not imply that all small loans are taken by households of the lower strata. The average size of loans taken from the professional moneylenders by our sample households belonging to different asset classes is set out in Table 6.9.

Table 6.9 : Average Size of loans from professional moneylenders classified according to asset classes

Asset classes Rs.	Village	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi		All	
		No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.	No.	Amount Rs.
1. Upto 500		-	-	1	-	-	-	-	-	15	919.83	-	-	16	799.84
2. 5000 - 10000		-	-	-	-	1	200.00	-	-	5	100.00	-	-	6	116.67
3. 10000 - 15000		-	-	-	-	2	700.00	-	-	1	300.00	-	-	3	633.37
4. 15000 - 20000		3	200.00	3	300.00	-	-	1	500.00	-	-	-	-	7	285.91
5. 20000 - 30000		3	133.33	3	2066.67	4	525.00	-	-	5	264.00	-	-	15	668.00
6. 30000 - 50000		3	133.33	3	275.00	-	-	2	2100.00	2	550.00	-	-	10	652.50
7. 50000 - 100000		4	187.50	7	1728.57	1	1500.00	2	1500.00	-	-	-	-	14	1267.83
8. 100000 & above		5	2300.00	6	2308.33	1	10000.00	5	1940.00	-	-	1	12000	18	4075.00
All		18	763.89	23	1559.78	23	1688.88	10	1740.00	28	507.50	1	12000	89	

It is true that the average size of loans does not steadily increase with the size of household assets. However, by and large, average size of loans in the lower strata is smaller than that in the top asset classes. The correlation between the value of assets and loan size is found to be positive in four out of the five villages, and highly significant in Anikad and Thirunavaya, viz., 0.9374 and 0.7806, but not significant at Ezhukone, 0.4593 and Thalikulam, 0.2695. Vilpatti is an exception where the correlation is highly significant, but negative.

In brief, smaller size of assets of the borrowers, lower their credit worthiness, smaller the size of loans and higher the rate of interest. Thus, the interest rates and size of assets may be inversely related, as shown in Table 6.10.

Table 6.10 : Average rate of interest on loans from professional moneylenders according to asset class

Asset Class Rs.	Village					
	Thirunavaya	Thalikulam	Anikad	Ezhukone	Vilpatti	Mookuperi
Upto					120(1)	
500 - 1000					120(1)	
1000 - 2500					20(7)	
2500 - 5000		30(1)			84(4)	
5000 - 10000			120(1)		120(5)	
10000 - 15000			34(2)		36(1)	
15000 - 20000	125(3)	30(3)	-	30(1)	-	
20000 - 30000	124(3)	207(3)	62(4)		63(5)	
30000 - 50000	125(3)	27(3)		30(2)	32(2)	
50000 - 100000	125(4)	9(7)	60(1)	21(2)	-	
100000 & above	40(5)	27(6)	36(1)	33(5)	-	24(1)

Note: Figures in brackets stand for the number of loans.

Although interest rate does not steadily fall with increase in the value of assets, there seems to be an inverse relationship, however weak. The coefficient of correlation between the two variables is negative in all the five villages for which sufficient number of observations are available except Ezhukone. However, it is significant only for Thirunavaya, viz., -0.7699 .

(ii) Risk premium

We have briefly referred earlier in this chapter to the views on premium for risk as a determinant of interest rates in the ICMs. It may be recalled that while Bottomley includes premium for risk as one of the important determinants, Bhaduri concludes that risk of default is to the advantage of the lender and is, therefore, irrelevant in the determination of interest rate. Basu (1984) seems more or less to agree with Bhaduri's position that "lenders risk is indeed non-existent and one of the motives in raising i [interest rate] could be to encourage default". (p.154). Mohan Rao (1980), on the other hand, questions the theoretical adequacy Bhaduri's model for the conclusion he draws from it.

"A comparison of the risk premium theory and Bhaduri's model shows that they are to some extent based on opposite set of assumptions: while the risk premium theory is based on free competition, involuntary default, and exogenously caused default, Bhaduri's model assumes monopoly power, voluntary default and default induced by interest rate. The problem is situated in non-competitive pre-capitalist context where the lender's freedom to set the interest rate is relatively unchecked by market forces; for the credit relations that are the subject of the theory

originate and assume wide economic significance only in historically identifiable, pre-capitalist mode of production. The nature and context of such credit relations require further elaboration..."

(Rao, 1980, p.164).

Raj has taken a more balanced position. While default risk is not ruled out, he has set a limit to the mark-ups on interest rates.

"In practice the extent of the lender's risk would tend to be reflected not so much in actual mark-ups on the pure rate of interest but in the degree of credit rationing imposed by the lenders on the borrowers. For while higher interest rates could act as a deterrent to larger borrowing the problem is not solved from the lenders' point of view if their own risk-rating is higher than of the borrowers. In fact, higher interest rates would have a significant deterrent effect only if the borrowers concerned have assets that to lose in the even of default. But it is when the assets that could have been taken over by the lender in the event of default are not large - either because the borrowers have few assets or because there are obstacles to acquiring them - that the risks are greater for the lender, and it is precisely in these circumstances that the borrower might be tempted to place a lower rating on the risks involved. Moreover, it is only within a narrow range that interest rates can be effectively raised to cover anticipated risks of default without such higher interest rates themselves becoming a factor increasing the probability of default".

(Raj, 1979, p.113).

In essence, Raj has argued that "the higher rates of interest prevalent in these economies cannot be wholly (or perhaps even largely) explained simply in terms of risk premia to compensate for expected default of loans". (Ibid., p.114. Emphasis added).

The collateral or security offered has obviously a bearing on risk. Borrowers with no security or low value collateral would have a greater propensity to default. Their own rating of the value of the collateral may be low, lower than the volume of loans. In such situation they may be considered high risk clients and charged higher interest. In our study areas the rate of interest charged on unsecured loans (mostly on personal security) are higher than on loans against gold, the collateral preferred by the professional moneylenders in the selected villages (see Table 6.11).

Table 6.11 : Distribution of borrowings according to interest rate and security

Village Security	Anikad	Ezhukone	Thirunavaya	Thali- kulam	Vil- patti	Mooku- peri
Gold	36 (1)	30 (10)	35 (2)	28 (20)	-	-
Land or house	-	-	-	-	0.0 (1)	-
Personal security	62 (7)	-	124 (16)	93 (3)	65 (26)	24 (1)
No durables	36 (1)	-	-	-	-	-
Total	9	10	18	23	27	1

Note: Figures in brackets show the number of loans.

(iii) Opportunity cost of money

Bottomley's identification of the opportunity cost of the money involved as one of the components of rural interest is generally accepted. The opportunity cost of money is defined as the returns on alternative risk-free investments. As Bottomley (1964) put it:

"Let us suppose that a particular village moneylender has more cash than he needs. What can he do with the excess? He can invest in real estate, fixed interest securities, and so forth. If generally competitive conditions obtain, apart from moneylending investments should be forced down to equality with the rate of return on investments without either risk or administrative costs, such as government bonds. The opportunity cost of moneylender's cash would therefore equal the rate of return on such securities and it is probably appropriate for us to consider it as such".
(Bottomley, 1964, p.).

Raj has questioned the above presumption limiting the options before the rural lenders, and hypothesised that holding commodity stocks will yield, better returns than government bonds, and that

"if the main agencies involved in lending are agricultural moneylenders and traders, and both have the alternative of holding commodity stocks to lending (i.e. to holding promissory notes), the rate of returns realizable on commodity stocks is likely to have a significant influence on the rate of interest charged on loans". (Raj, op.cit., p.125).

The lender's opportunity cost is invariably viewed as the earnings foregone from possible alternative investments. The underlying assumption is that the lender, whether professional or non-professional

moneylenders, lends out of his own savings.

"In agrarian economies there are few agencies engaged simultaneously in both borrowing and lending, and so not only are there no institutional arrangements for intermediation between savers and investors but such lending as is done is almost wholly out of the own-wealth of the individuals or households concerned". (Ibid., p.111).

This may be true of a static agrarian economy, when both the demand for funds can be envisaged with dynamic changes in agriculture, as for example, with the new high yielding seed varieties and greater use of fertilizers, agricultural machinery, etc. as in Punjab and Haryana, or mechanisation of fishing in Kerala or higher consumption expenditure by way of house construction, purchase of consumer durables, or for purpose of financing emigration to the Gulf as in Kerala. Given the constraints on supply of funds from formal credit institutions, a good proportion of rural households may turn to informal credit agencies. The supply of loanable funds may also increase as a result of the increase in savings, generated by the aforementioned factors like dynamic changes in agriculture, mechanisation of fishing or flow of remittances, and these are attracted by the professional moneylenders, thanks to the lower interest rates offered by the formal credit institutions.

In the light of the foregoing, professional moneylenders no more limit their lending activities to their own funds, but attract deposits or borrow from those households with savings. Thus, the interest they have to pay on such deposits or loans would be the minimum cost of the money they lend to others. In most of our selected villages, the

professional moneylenders are seen to have taken deposit and/or loans from the households of the respective villages. (Table 6.12).

Table 6.12 : Loan transactions of a sample of professional moneylenders in the selected villages

Village	Money-lender Serial No.	Total amount lent Rs.	Interest charged %	Deposits/loans received Rs.	Interest paid %	Source
Thirunavaya	1	3422400	24	200000	19.5	Friends and relatives
Thalikulam	1	2600000	24	400000	12.0	-do-
	2	500000	24	22000	10-13	-do-
	3	500000	30	200000	10-12	-do-
	4	2500000	24	N.R.	12	-do-
Anikad	1	1916250	36	447000	24	-do-
Ezhukone	1	15000	36	-	-	-
	2	2800000	30	1000000	12-24	-do-
	3	500000	36	-	-	-
Vilpatti	1	52150	24-36	-	-	-
	2	15000	-	-	-	-
Mookupori	1	N.R.	30-36	-	-	-
	2	N.R.	30-36	-	-	-

That the majority of the sample professional moneylenders from Kerala villages have been depending on external funds to support their lending activities is clear from the foregoing table. (Table 6.12).

The interest they had to pay on deposits received even from friends and relatives ranged from 10 to 24 percent is not negligible either.

That gives an indication of the opportunity cost of the money involved. As against this, the professional moneylenders in the two Tamil Nadu villages have not reported receiving any deposits or borrowings. Presumably, this may be due to the smaller scale of their loan transactions.

Monopoly Profit

Chandavarkar contends that Bottomley "overlooks that the elements of monopoly and oligopoly in the lending business may be even more important as an explanation of high rate of interest in these economies than the risk premium and administration charges". He attempts to prove that the "degree of monopoly power of the lender may well be the most important determinant of interest rates". (Chandavarkar, 1965, p.323). The basis of his assertion is that

"the available evidence atleast for India suggests that the 'density' of moneylenders as a professional class is very low and as such highly conducive to monopoly in the business both within and outside the village. While the figures below show that pure monopoly could be said to exist in only 11.5 percent of Indian villages, i.e. those with one resident moneylender, their number and concentration in the other village in the sample are also more indicative of oligopoly than competition. It is significant that the category with four or more resident moneylenders, which may be regarded as nearest to competitive amongst all the five groups, accounts for only 10.3 percent". (Loc.cit).

Long has argued that Chandavarkar's use of the number of moneylenders in a village as a measure of competition is misleading.

"In 64 percent of all villages in the sample cited by Chandavarkar, there was not a single reported lender! If one lender in a village implies monopoly, what does the absence of lenders imply. I suggest that it does not mean there is no borrowing, for the figure cited are only for lenders who responded to the inquiry and many creditors presumably did not consider themselves moneylenders or for some other reasons failed to reply". (Long, 1968, p.277).

The figures cited by Chandavarkar are from the report of the All India Rural Credit Survey, 1951-52. Since then the structure of the rural credit market has undergone major changes. As we have observed earlier, the share of formal credit institutions in the total borrowings by rural households has increased nearly ten fold, from around 6 to over 61 percent between 1951-52 and 1981-82. Consequently, whatever monopoly power the professional moneylenders had previously would have been greatly eroded.

Most of our study areas, it may be recalled, are served by formal credit institutions like cooperative societies and/or commercial banks. Friends and relatives are a major source of credit. Naturally, professional moneylenders are lenders of the last resort. In some of the selected villages, there is more than one professional moneylender. Under these circumstances, the degree of monopoly power for any one of the moneylenders is apt to be weak. And, therefore, monopoly profit cannot explain the high rate of interest charged by them.

Which of the four components of interest rates discussed above -- the opportunity cost of the money involved, administrative cost, risk premium and monopoly profit -- is the most important, it is difficult to say. To generalise that "administration charges, together with the

premium for risk are probably the major determinants of the high level of interests which obtain throughout the underdeveloped world" (Bottomley), or "the degree of monopoly power of the lender may well be the most important single determinant of interest rates" (Chandavarkar) is too sweeping. Obviously, given the great diversity of the socio-economic conditions in any country, to to speak of between countries, the relative role of the factors or shares of the components would vary from region to region. This diversity was brought out by the inter-village differences in the different parameters involved. In fact, we observed differences in the administrative costs or default rate between professional money-lenders from the same village.

To sum up, the average rate of interest on loans from professional moneylenders, the principal commercial informal credit agency in our selected villages, was seen to vary from 24 to 60 percent. Wide variations in interest rates charged by professional moneylenders within the same village were also observed. The loan propose, size and security emerge as the principal factors underlying the intra-village variations in interest rates. Loans used for consumption purpose, loans of small size and those with no collateral security were seen to bear higher interest rate. Borrowings from low income non-cultivator households generally share the above characteristics.

Data from our field studies also seem to imply that risk premium and monopoly profit are not important elements in the interest rate charged by professional moneylenders. Risk of default is apt to be taken care of

by credit rationing rather than by mark-ups of interest rates. With the emergence of alternative sources of credit, monopoly profit has ceased to be relevant for a good proportion of the rural households. On the other hand, opportunity cost of money, i.e. interest on deposits or borrowals, is an eligible candidate for consideration. Under the emerging system of finance companies, administrative costs may also assume importance.

CHAPTER 7

FACTORS UNDERLYING INTEREST RATES VARIATION IN THE SAMPLE VILLAGES

The findings of our survey of selected sample villages reflect the existence of wide variations in the rates of interest (calculated on an annual basis) on loans both from formal as well as informal agencies. This has ofcourse been observed in other studies also. Under conditions of imperfect markets as well as fragmented markets, one would expect to observe a wide spectrum of rates rather than a tendency for the rates to converge. In the theoretical and empirical literature reviewed earlier, the following factors have been identified as having an important bearing on the rate of interest: the size and duration of loans, the purpose of borrowing (which reflects the ^{differing} underlying elasticity of demand for credit) the nature of the security offered, the credit worthiness or bargaining power of the borrower as reflected in the size of land holding or the value of total assets.

In this chapter, we have put the survey data to closer scrutiny with a view to identifying the relative importance of these determining factors in explaining variations in interest rates. The analysis is carried out on the basis of loan wise data, i.e. each loan is treated as an observation. We have confined the analysis to each loan, since the calculation of the relevant interest rate is much easier in that case;

The main explanatory variables used in this analysis are:

LAND : Cultivated Area (in Cents)
 DUR : Duration of Loan (in months)
 TOASST : Total value of Assets
 EDU : Education level of the Head of Household which has borrowed.
 SIZE : Size of the loan.

In addition, there are the following qualitative variables.

OCCU : Occupation of the head of the borrowing household. This is coded as follows: 1 = Cultivator; 2 = Agricultural or Casual Non-agricultural labour; 3 = Non cultivator.
 AGENCY : The agency from which the loan has been taken. This is coded as follows: 1 = Formal sector; 2 = Agricultural Moneylender; 3 = Professional Moneylender; 4 = Traders; 5 = Friends and Relatives.
 SECU : Security offered coded as follows: 1 = Gold, other durables; 2 = Land, Buildings; 3 = Personal Security; 4 = Deposit.
 PURPOSE : Purpose of loan coded as: 1 = Production; 2 = Consumption; 3 = Family Expenses (marriage, education etc.); 4 = Others.
 REASON : Reason given for agency preference. Coded as : 1 = Low Interest Rate, Subsidy etc.; 2 = Urgency of Requirement; 3 = Easy Terms (such as repayment schedules, easy access).
 VILCO : Village Code. This is coded as follows: 1 = Mookuperi; 2 = Vilpatti; 3 = Anikad; 4 = Ezhukone; 5 = Thirunavaya; 6 = Thalikulam.

The plan of the analysis is as follows. In the first phase, we subjected the data for all the villages pooled together, to two types of analysis. We first carried out a series of one way analysis of variance for formal and informal sector loan separately with respect to the following groupings: VILCO; OCCU; AGENCY (Formal and Informal sector loans

combined) SECU and PURPOSE. The results are given below. These show very starkly that in no case was the F ratio on the ANOVA significant. Thus for none of the above mentioned qualitative variables is there much homogeneity in the data. The only variable where the F - ratio is relatively high is VILCO, suggesting that a disaggregated analysis separately for each village might be worthwhile. In a way, this rather negative finding is very interesting in its own right, because it suggests that a great deal of heterogeneity and variability exist in the interest rate.

COMBINED ANOVA for all Villages Together

1. Formal

Variable IRATE
By Variable VILCO

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	5	10350.7730	2070.1546	1.1948	.3107
Within Groups	451	781419.1964	1732.6368		
Total	456	791769.9694			

Informal

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	5	1275671.007	255134.2015	1.7537	.1225
Within Groups	282	41025507.44	145480.5228		
Total	287	42301178.44	14		

2. Formal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	3750.4188	1875.2094	1.0804	.3403
Within Groups	454	788019.5506	1735.7259		
Total	456	791769.9694			

Informal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	258399.2682	129199.6341	.8758	.4176
Within Groups	285	42042779.18	147518.5234		
Total	287	42301178.44			

3. Variable IRATE
By Variable AGENCY

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	4	365304.6974	91326.1744	1.5737	.1794
Within Groups	740	42944263.04	58032.7879		
Total	744	43309567.74			

4. Formal

Variable IRATE
By Variable SECU

Analysis of Variance

Sources	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	5803.3078	1934.4359	1.1149	.3426
Within Groups	453	78966.6616	1735.0257		
Total	456	791769.9694			

Informal

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	67184.3370	33592.1685	.2267	.7973
Within Groups	285	42233994.11	148189.4530		
Total	287	42301178.44			

5. Formal

Variable IRATE
By Variance PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	21.2973	7.0991	.0041	.9996
Within Groups	453	791748.6721	1747.7896		
Total	456	791769.9694			

Informal

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.E.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	181242.4169	60414.1390	.4074	.7478
Within Groups	284	42119936.03	148309.6339		.
Total	287	42301178.44			

In the next phase of the analysis, we attempted a regression exercise, again for all the village combined. In these regression we regressed the Rate of Interest (on informal credit) on LAND, DUR, SIZE, TOASST and EDU, along with separate sets of dummy variables, to allow for different level (in the constant term). The dummy variables; which we tried in separate regression equations were: VILCO, OCCU, AGENCY, SECU, PURPOSE and REASON. The result of this regression exercise are reported below. Once again, the findings are striking, though negative. All the regression equations do extremely poorly, and have hardly any explanatory power. Hardly any of the formulated economic variables are significant, and of the dummy variables only VILCO shows some statistical significance. Thus we conclude that the data do not beyond to a population with uniform characteristics, and it was thought best to carry out the analysis separately for villages. In a sense, this is not surprising because the villages have been selected with particular attention to their representing different types of situations with respect to a large number of characteristics.

Combined Regressions: (Figures in parentheses are t-values, and R squares are adjusted for degree of freedom)

$$\begin{aligned}
 1. \text{ IRATE} &= 288.28 - 215.47 \text{ VILCO5} - 2.10 \text{ DUR} - 0.02 \text{ LAND} \\
 &\quad (3.73) \quad (-2.64) \quad (-0.747) \quad (0.208) \\
 &\quad - 185.35 \text{ VILCO1} + 0.0048 \text{ SIZE} - 171.68 \text{ VILCO4} \\
 &\quad \quad (-1.79) \quad (-0.82) \quad (-1.68) \\
 &\quad - 0.00015 \text{ TOASST} - 48.03 \text{ EDU} - 191.12 \text{ VILCO3} \\
 &\quad \quad (-0.76) \quad (-1.38) \quad (-2.10) \\
 &\quad - (167.77) \text{ VILCO2} \\
 &\quad \quad (-1.84)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.0091$$

$$\begin{aligned}
 2. \text{ IRATE} &= 180.01 - 89.38 \text{ OCCU2} - 1.92 \text{ DUR} + 0.0028 \text{ LAND} \\
 &\quad (3.11) \quad (-1.59) \quad (-0.738) \quad (0.038) \\
 &\quad + 0.0068 \text{ SIZE} - 60.35 \text{ EDU} - 0.00024 \text{ TOASST} \\
 &\quad \quad (1.15) \quad (-1.92) \quad (-1.203) \\
 &\quad - 65.63 \text{ OCCU1} \\
 &\quad \quad (-1.05)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.0039$$

$$\begin{aligned}
 3. \text{ IRATE} &= 127.47 - 56.34 \text{ AGENCY4} - 0.00023 \text{ TOASST} \\
 &\quad (2.30) \quad (-0.834) \quad (-1.19) \\
 &\quad - 12.65 \text{ AGENCY2} - 2.55 \text{ DUR} + 0.0041 \text{ LAND} \\
 &\quad \quad (-0.019) \quad (-0.964) \quad (0.056) \\
 &\quad - 46.62 \text{ EDU} + 0.0069 \text{ SIZE} + 2.27 \text{ AGENCY3} \\
 &\quad \quad (-1.53) \quad (1.165) \quad (0.041)
 \end{aligned}$$

$$\bar{R} \text{ Square} = -0.0067$$

$$\begin{aligned}
 4. \text{ IRATE} &= 86.94 + (25.40) \text{ SECU3} - 44.68 \text{ EDU} + 0.0075 \text{ SIZE} \\
 &\quad (1.22) \quad (0.397) \quad (-1.48) \quad (1.27) \\
 &+ 0.0096 \text{ LAND} - 0.00025 \text{ TOASST} + 0.05 \text{ DUR} \\
 &\quad (0.13) \quad (-1.31) \quad (0.001) \\
 &- 91.67 \text{ SECU2} \\
 &\quad (-0.538)
 \end{aligned}$$

$$\bar{R} \text{ Square} = -0.0041$$

$$\begin{aligned}
 5. \text{ IRATE} &= 112.42 + 61.77 \text{ PURPOSE3} + 0.0086 \text{ LAND} - 2.50 \text{ DUR} \\
 &\quad (1.50) \quad (0.840) \quad (0.117) \quad (-0.952) \\
 &- 50.06 \text{ EDU} - 0.00026 \text{ TOASST} - 10.41 \text{ PURPOSE1} \\
 &\quad (-1.64) \quad (-1.38) \quad (-0.129) \\
 &+ 0.0059 \text{ SIZE} - 4.18 \text{ PURPOSE2} \\
 &\quad (0.974) \quad (-0.058)
 \end{aligned}$$

$$\bar{R} \text{ Square} = -0.0037$$

$$\begin{aligned}
 6. \text{ IRATE} &= 104.3 + 22.32 \text{ REASON2} - 0.00024 \text{ TOASST} - 2.41 \text{ DUR} \\
 &\quad (2.11) \quad (0.241) \quad (-1.272) \quad (-0.911) \\
 &- 0.0079 \text{ LAND} - 0.0073 \text{ SIZE} + 22.98 \text{ REASON1} \\
 &\quad (0.107) \quad (1.231) \quad (0.460) \\
 &- 48.34 \text{ REASON1} \\
 &\quad (-1.563)
 \end{aligned}$$

$$\bar{R} \text{ Square} = -0.0053$$

The next phase of the analysis, we carried out ANOVA (one way) with respect to same variables as earlier, for both formal and informal sector loan separately, for each village. These results are reported below:

In summary, the results show the following patterns:

(a) Village : Anikad

The F ratio is highly significant with respect to AGENCY. Also, SECU and PURPOSE are significant for formal sector loans. OCCU is insignificant. For the informal sector loans, however, none of the variables, viz., OCCU, SECU and PURPOSE are significant in the ANOVA. This shows a lack of homogeneity with respect to these groupings in the data.

(b) Village : Ezhukone

Here again, the F ratio with respect to AGENCY is highly significant. For formal sector credit OCCU, SECU and PURPOSE are highly significant.

In case of informal sector credit, SECU only is highly significant.

(c) Village : Thirunavaya

Once again, the F ratio with respect to agency is highly significant. For formal sector loan, once again OCCU, SECU and PURPOSE show significant discrimination.

(d) Village : Thalikulam

AGENCY again yields a high F ratio. For formal sector credit, none of the groupings appear to show a high discriminating power. OCCU is only weakly significant. For informal credit, none of the variables yield a statistically significant F-ratio.

(e) Village : Vilpatti

Here again AGENCY is highly significant. For the formal sector credit, we find OCCU, SECU and PURPOSE to be statistically significant. In the case of informal sector credit, in this village, SECU, PURPOSE and OCCU are also highly significant.

(f) Village : Mookuperi

In this village also, AGENCY is significant. For formal credit PURPOSE is highly significant, and OCCU is very weakly significant. For informal credit, PURPOSE is highly significant.

Village wise ANOVAAnikadFormal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squeres	Mean Squares	F ratio	F Prob.
Between Groups	2	2.9997	1.4998	.1106	.8954
Within Groups	118	1600.8350	13.5664		
Total	120	1603.8347			

Anikad (Contd,)

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	4	36911.2512	9227.8128	81.9233	.0000
Within Groups	163	18360.2666	112.6397		
Total	167	55271.5179			

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	375.3200	125.1067	11.9148	.000
Within Groups	117	1228.5147	10.5001		
Total	120	1603.8347			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	255.7638	85.2546	7.399	.0001
Within Groups	117	1348.0709	11.5220		
Total	120	1603.8347			

Anikad (Contd.)Informal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	2170.3798	1085.1899	.9563	.3922
Within Groups	44	49930.9393	1134.7941		
Total	46	52101.3191			

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	1	806.2858	806.2858	.7073	.4048
Within Groups	45	51295.0333	1139.8896		
Total	46	52101.3191			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	5769.7501	1923.2500	1.7850	.1643
Within Groups	43	46331.5691	1077.4784		
Total	46	52101.3191			

EzhukoneFormal

Variable IRATE

By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	100.5008	50.2504	3.1265	.0489
Within Groups	86	1382.2183	16.0723		
Total	88	1482.7191			

Variable IRATE

By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	245.1688	122.5844	8.5187	.0004
Within Groups	86	1237.5503	14.3901		
Total	88	1482.7191			

Variable IRATE

By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	569.222	189.7407	17.6552	.0000
Within Groups	85	913.4969	10.7470		
Total	88	1482.7191			

Ezhukone (Contd.)Informal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	588.2996	279.1498	1.1709	.3248
Within Groups	28	6675.4423	238.4087		
Total	30	7233.7419			

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	4124.8008	2062.4004	18.5746	.0000
Within Groups	28	3108.9412	111.0336		
Total	30	7233.7419			

Variable IRATE
By Variable AGENCY

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	877.1419	292.3806	1.2419	.3139
Within Groups	27	6356.6000	235.4296		
Total	30	7233.7419			

Ezhukone (Contd.)

Variable IRATE
By Variable AGENCY

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	5739.7031	1913.2344	64.7514	.0000
Within Groups	116	3427.4969	29.5474		
Total	119	9167.2000			

Thirunavaya

Variable IRATE
By Variable AGENCY

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	4	194666.8353	48666.7088	435.9788	0.0
Within Groups	131	14623.0470	111.6263		
Total	135	209289.8824			

Formal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	52.6541	26.3270	3.8495	.0308
Within Groups	36	246.7818	6.8551		
Total	38	299.4359			

Thirunavaya (Contd.)

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	94.9609	47.4804	8.3594	.0000
Within Groups	36	204.4750	5.6799		
Total	38	299.4359			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	59.7216	19.9072	2.9006	.0483
Within Groups	35	239.7143	6.8490		
Total	38	299.4359			

Informal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	792.6567	3986.3284	1.8802	.1582
Within Groups	94	199297.26	2120.1198		
Total	96	207263.9175			

Thirunavaya (Contd.)

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	1	59.8853	59.8853	.0275	.8683
Within Groups	95	207204.0323	2181.0951		
Total	96	207263.9175			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	12221.2241	4073.7414	1.9424	.1281
Within Groups	93	195042.6934	2097.2333		
Total	96	207263.9175			

Thalikulam

Variable IRATE
By Variable AGENCY

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	4549625.352	2274812.676	6.0789	.0032
Within Groups	101	37795894.76	374216.7798		
Total	103	42345520.12			

Thalikulam (Contd.)

Formal

Variable IRATE

By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	42113.4990	21056.7495	2.0034	.1425
Within Groups	70	735740.8298	10510.5833		
Total	72	777854.3288			

Variable IRATE

By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	10975.1667	3658.3889	.3292	.8043
Within Groups	69	766879.1621	11114.1908		
Total	72	777854.3288			

Variable IRATE

By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	7344.5678	2448.1193	.2192	.8827
Within Groups	69	770509.7610	11166.8081		
Total	72	777854.3288			

Thalikulam (Contd.)Informal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	480564.7484	240282.3742	.1677	.8464
Within Groups	28	40113884.80	1432638.743		
Total	30	40594449.55			

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	1	2426354.112	2426354.112	1.8435	.1850
Within Groups	29	38168095.44	1316141.222		
Total	30	40594449.55			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	3762454.151	1254151.384	.9194	.4447
Within Groups	27	36831995.40	1364147.978		
Total	30	40594449.55			

Vilpatti

Variable IRATE
By Variable AGENCY

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	4	160823.0327	40205.7582	100.6841	.00
Within Groups	142	56704.2462	399.3257		
Total	146	217527.2789			

Formal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	4.8044	2.4	2.4111	.0955
Within Groups	90	89.6687	.9963		
Total	92	94.4731			

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	12.4190	6.2095	6.8108	.0018
Within Groups	90	82.0541	.9117		
Total	92	94.4731			

Vilpatti (Contd.)

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	12.4190	6.2095	6.8108	.0018
Within Groups	90	82.0541	.9117		
Total	92	94.4731			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	4.8595	2.4297	2.4402	.0929
Within Groups	90	89.6136	.9957		
Total	92	94.4731			

Informal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	15663.0332	7831.5166	3.1184	.0528
Within Groups	51	129080.4483	2511.3813		
Total	53	143743.4815			

Vilpatti (Contd.)

Variable IRATE

By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	67652.5481	33826.2741	22.6721	.0000
Within Groups	51	76090.9333	1491.9791		
Total	53	143743.4815			

Variable IRATE

By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	65833.0648	21944.3549	14.0831	.0000
Within Groups	50	77910.4167	1558.2083		
Total	53	143743.4815			

Mookuperi

Variable IRATE

By Variable AGENCY

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	1958.1328	652.7109	2.2780	.0877
Within Groups	66	18910.5100	286.5229		
Total	69	20868.6429			

Mookuperi (Contd.)

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	7.3017	3.6509	1.8467	.1713
Within Groups	39	77.1030	1.9770		
Total	41	84.4048			

Variable IRATE
By Variable SECU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	2.7964	.9321	.4340	.7299
Within Groups	38	81.6083	2.1476		
Total	41	84.4048			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	36.6453	12.2151	9.7190	.0001
Within Groups	38	47.7595	1.2568		
Total	41	84.4048			

Mookuperi (Contd.)Informal

Variable IRATE
By Variable OCCU

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	2	609.4286	304.7143	.3789	.6885
Within Groups	25	20106.0000	804.2400		
Total	27	20715.4286			

Variable IRATE
By Variable PURPOSE

Analysis of Variance

Source	D.F.	Sum of Squares	Mean Squares	F Ratio	F Prob.
Between Groups	3	8623.0286	2874.3429	5.7048	.0043
Within Groups	24	12092.4000	503.8500		
Total	27	20715.4286			

It is thus very clear that when the data for different villages are analysed separately, the results are much more meaningful. However, the relative heterogeneity of informal sector interest rates, as compared with the formal sector is clearly brought out.

Finally, we have attempted a set of regression analyses of IRATE with attractive specifications of explanatory variables for each village separately. This has been done only for informal sector loans. We have maintained a set of explanatory variables, as earlier, and have varied the dummy specification. Because of relatively few degree of freedom, we have not tried to the use more than one type of dummy variable in a single equation. The results for these village wise regressions are given below.

I. Anikad

$$\begin{aligned}
 1. \text{ IRATE} &= 59.23 - 24.25 \text{ PURPOSE3} - 16.34 \text{ EDU} + 4.99 \text{ DUR} \\
 &\quad (2.72) \quad (-1.272) \quad (-2.097)^* \quad (2.54)^* \\
 &- 47.34 \text{ PURPOSE1} + 0.142 \text{ LAND} - 0.00102 \text{ SIZE} \\
 &\quad (-2.33) \quad (0.69) \quad (0.389) \\
 &- 16.91 \text{ PURPOSE2} - 0.00013 \text{ TOASST} \\
 &\quad (-0.946) \quad (-0.696)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.246$$

$$\begin{aligned}
 2. \text{ IRATE} &= 56.46 - 37.66 \text{ REASON2} - 0.0024 \text{ SIZE} + 1.45 \text{ DUR} \\
 &\quad (6.45) \quad (-2.131)^* \quad (-1.351) \quad (-0.104) \\
 &- 0.60 \text{ EDU} + 0.029 \text{ LAND} - 47.79 \text{ REASON1} \\
 &\quad (0.186) \quad (-5.672)^* \quad (0.276) \\
 &- 0.000039 \text{ TOASST} \\
 &\quad (6.45)^*
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.531$$

Anikad (Contd.)

$$\begin{aligned}
 3. \text{ IRATE} &= 30.14 + 2.63 \text{ OCCU2} + 5.59 \text{ DUR} - 10.23 \text{ EDU} \\
 &\quad (1.79) \quad (0.191) \quad (2.94)^* \quad (-1.29) \\
 &- 0.0014 \text{ SIZE} + 0.058 \text{ LAND} - 3.30 \text{ OCCU1} \\
 &\quad (-0.561) \quad (0.28) \quad (-0.23) \\
 &- 0.000045 \text{ TOASST} \\
 &\quad (-0.24)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.140$$

$$\begin{aligned}
 4. \text{ IRATE} &= 11.74 + 65.19 \text{ AGENCY4} - 6.03 \text{ EDU} + 36.21 \text{ AGENCY2} \\
 &\quad (1.72) \quad (2.95)^* \quad (-1.29) \quad (4.05)^* \\
 &- 75.37 \text{ AGENCY3} - 0.00080 \text{ SIZE} - 0.11 \text{ LAND} \\
 &\quad (7.40)^* \quad (-0.53) \quad (0.89) \\
 &- 1.79 \text{ DUR} - 0.000093 \text{ TOASST} \\
 &\quad (-1.20) \quad (0.781)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.668$$

II. Ezhukone

$$\begin{aligned}
 1. \text{ IRATE} &= 29.90 - 4.50 \text{ OCCU2} - 7.26 \text{ EDU} + 1.24 \text{ DUR} \\
 &\quad (2.10) \quad (-0.54) \quad (-1.4) \quad (2.27)^* \\
 &- 0.00063 \text{ SIZE} - 0.052 \text{ LAND} - 0.000035 \text{ TOASST} \\
 &\quad (-0.941) \quad (-1.02) \quad (0.757) \\
 &- 12.51 \text{ OCCU1} \\
 &\quad (-1.401)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.250$$

$$\begin{aligned}
 2. \text{ IRATE} &= 6.23 + 20.85 \text{ AGENCY3} - 0.90 \text{ EDU} + 0.000023 \text{ TOASST} \\
 &\quad (1.27) \quad (5.11)^* \quad (-0.39) \quad (0.79) \\
 &+ 26.54 \text{ AGENCY2} - 0.00025 \text{ SIZE} + 0.606 \text{ DUR} - 0.036 \text{ LAND} \\
 &\quad (5.04)^* \quad (-0.641) \quad (1.69) \quad (-1.16)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.712$$

Ezhukone (Contd.)

$$\begin{aligned}
 3. \text{ IRATE} &= 6.77 + 7.235 \text{ PURPOSE3} - 0.058 \text{ LAND} + 1.82 \text{ DUR} \\
 &\quad (0.75) \quad (1.11) \quad \quad \quad (-1.26) \quad \quad \quad (3.23)^* \\
 &+ 0.93 \text{ EDU} - 0.00043 \text{ SIZE} - 15.21 \text{ PURPOSE1} \\
 &\quad (0.24) \quad \quad \quad (-0.72) \quad \quad \quad (-1.65) \\
 &+ 2.496 \text{ PURPOSE1} - 0.000238 \text{ TOASST} \\
 &\quad (0.302) \quad \quad \quad (0.518)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.346$$

$$\begin{aligned}
 4. \text{ IRATE} &= 15.43 + 5.05 \text{ REASON2} - 1.31 \text{ EDU} - 0.06 \text{ LAND} \\
 &\quad (1.61) \quad (0.658) \quad \quad \quad (-0.383) \quad \quad \quad (-1.212) \\
 &- 0.0000067 \text{ SIZE} + 1.10 \text{ DUR} - 8.08 \text{ REASON1} \\
 &\quad (0.011) \quad \quad \quad (2.141)^* \quad \quad \quad (-1.05) \\
 &- 0.000025 \text{ TOASST} \\
 &\quad (0.579)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.336$$

III. Thirunavaya

$$\begin{aligned}
 1. \text{ IRATE} &= 43.90 - 4.87 \text{ OCCU2} - 1.13 \text{ DUR} - 4.88 \text{ EDU} \\
 &\quad (3.61) \quad (-0.358) \quad \quad \quad (-1.03) \quad \quad \quad (-0.626) \\
 &+ 0.044 \text{ LAND} - 0.00045 \text{ SIZE} - 9.60 \text{ OCCU1} \\
 &\quad (2.206) \quad \quad \quad (-0.349) \quad \quad \quad (-0.597) \\
 &- 0.000080 \text{ TOASST} \\
 &\quad (-1.08)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.021$$

$$\begin{aligned}
 2. \text{ IRATE} &= 9.38 - 4.98 \text{ AGENCY4} - 0.0000013 \text{ TOASST} - 0.748 \text{ AGENCY2} \\
 &\quad (2.89) \quad (-1.53) \quad \quad \quad (-0.08) \quad \quad \quad (-0.06) \\
 &- 0.00075 \text{ SIZE} - 1.94 \text{ EDU} + 110.63 \text{ AGENCY3} \\
 &\quad (-0.46) \quad \quad \quad (-0.96) \quad \quad \quad (31.59)^* \\
 &- 0.856 \text{ DUR} - 0.003 \text{ LAND} \\
 &\quad (-2.68)^* \quad \quad \quad (-0.65)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.934$$

Thirunavaya (Contd.)

$$\begin{aligned}
 3. \text{ IRATE} &= 40.02 - 12.15 \text{ PURPOSE3} + 0.03 \text{ LAND} + 16.49 \text{ PURPOSE1} \\
 &\quad (2.84) \quad (0.866) \quad (-0.158) \quad (1.01) \\
 &- 0.00054 \text{ SIZE} - 1.83 \text{ EDU} - 0.80 \text{ DUR} \\
 &\quad (-0.43) \quad (-0.24) \quad (-0.68) \\
 &- 1.72 \text{ PURPOSE2} - 0.0000896 \text{ TOASST} \\
 &\quad (-0.125) \quad (-1.25)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.045$$

$$\begin{aligned}
 4. \text{ IRATE} &= 68.75 - 39.85 \text{ REASON2} + 0.0000045 \text{ SIZE} \\
 &\quad (7.89) \quad (-1.39) \quad (0.004) \\
 &+ 0.000034 \text{ TOASST} - 10.55 \text{ EDU} + 53.83 \text{ REASON1} \\
 &\quad (0.54) \quad (-1.62) \quad (-6.22)* \\
 &- 1.94 \text{ DUR} - 0.14 \text{ LAND} \\
 &\quad (-2.1)* \quad (0.798)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.316$$

IV. Thalikulam

$$\begin{aligned}
 1. \text{ IRATE} &= 650.99 - 654.93 \text{ OCCU2} + 20.25 \text{ DUR} + 8.88 \text{ OCCU1} \\
 &\quad (0.80) \quad (-0.952) \quad (0.167) \quad (0.011) \\
 &- 0.09 \text{ LAND} + 0.074 \text{ SIZE} - 0.0025 \text{ TOASST} - 491.63 \text{ EDU} \\
 &\quad (-0.334) \quad (1.256) \quad (-0.97) \quad (-1.53)
 \end{aligned}$$

$$\bar{R} \text{ Square} = -0.095$$

$$\begin{aligned}
 2. \text{ IRATE} &= 2531.86 - 2360.80 \text{ AGENCY3} + 0.128 \text{ LAND} + 94.51 \text{ DUR} \\
 &\quad (2.50) \quad (-2.83)* \quad (0.504) \quad (0.892) \\
 &- 0.0025 \text{ TOASST} - 472.41 \text{ EDU} - 0.098 \text{ SIZE} \\
 &\quad (-1.18) \quad (-1.78) \quad (-1.23)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.181$$

Thalikulam (Contd.)

$$\begin{aligned}
 3. \text{ IRATE} &= 465.57 + 628.81 \text{ PURPOSE1} - 393.23 \text{ EDU} \\
 &\quad (0.51) \quad (0.909) \quad (-1.17) \\
 &+ 0.0081 \text{ LAND} - 0.0013 \text{ TOASST} - 18.64 \text{ DUR} \\
 &\quad (0.02) \quad (-0.49) \quad (-0.14) \\
 &- 11.98 \text{ PURPOSE2} + 0.053 \text{ SIZE} - 224.21 \text{ PURPOSE3} \\
 &\quad (-0.019) \quad (0.761) \quad (-0.201)
 \end{aligned}$$

$$\bar{R} \text{ Square} = -0.128$$

$$\begin{aligned}
 4. \text{ IRATE} &= 1562.98 - 351.25 \text{ REASON2} - 0.04 \text{ LAND} - 0.0043 \text{ TOASST} \\
 &\quad (2.04) \quad (-0.434) \quad (-0.126) \quad (-1.934)* \\
 &- 152.18 \text{ DUR} + 0.062 \text{ SIZE} - 460.74 \text{ EDU} \\
 &\quad (-1.223) \quad (-0.897) \quad (-1.704) \\
 &+ 2327.85 \text{ REASON1} \\
 &\quad (2.913)*
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.177$$

V. Vilpatti

$$\begin{aligned}
 1. \text{ IRATE} &= 82.33 - 15.39 \text{ PURPOSE3} + 9.27 \text{ EDU} - 0.05 \text{ LAND} \\
 &\quad (3.12) \quad (-0.657) \quad (0.958) \quad (-1.006) \\
 &- 1.571 \text{ DUR} - 24.11 \text{ PURPOSE1} + 0.000006 \text{ SIZE} \\
 &\quad (-4.576)* \quad (-1.006) \quad (0.004) \\
 &- 0.0031 \text{ TOASST} + 24.01 \text{ PURPOSE2} \\
 &\quad (-0.682) \quad (1.028)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.631$$

$$\begin{aligned}
 2. \text{ IRATE} &= 124.95 - 45.25 \text{ REASON2} - 3.07 \text{ EDU} - 0.00033 \text{ SIZE} \\
 &\quad (7.6) \quad (-1.41) \quad (-0.30) \quad (-0.19) \\
 &- 0.027 \text{ LAND} - 28.28 \text{ REASON1} - 1.54 \text{ DUR} \\
 &\quad (-0.43) \quad (-1.64) \quad (-4.42)* \\
 &- 0.00066 \text{ TOASST} \\
 &\quad (-1.21)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.52$$

Vilpatti (Contd.)

$$\begin{aligned}
 3. \text{ IRATE} &= 111.04 - 7.24 \text{ OCCU2} - 1.66 \text{ DUR} - 10.004 \text{ EDU} \\
 &\quad (6.53) \quad (-0.51) \quad (-4.83)^* \quad (-0.894) \\
 &- 0.04 \text{ LAND} - 0.00065 \text{ SIZE} - 3.26 \text{ OCCU1} \\
 &\quad (-0.680) \quad (-0.382) \quad (-0.179) \\
 &- 0.00049 \text{ TOASST} \\
 &\quad (-0.827)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.490$$

$$\begin{aligned}
 4. \text{ IRATE} &= 66.91 - 21.71 \text{ AGENCY4} - 0.00061 \text{ SIZE} - 16.69 \text{ AGENCY2} \\
 &\quad (4.74) \quad (-1.37) \quad (-0.462) \quad (0.729) \\
 &- 6.69 \text{ EDU} - 0.018 \text{ LAND} - 1.32 \text{ DUR} + 44.18 \text{ AGENCY3} \\
 &\quad (-0.826) \quad (0.378) \quad (-4.11)^* \quad (3.42)^* \\
 &- 0.000061 \text{ TOASST} \\
 &\quad (-0.144)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.692$$

VI. Mookuperi

$$\begin{aligned}
 1. \text{ IRATE} &= 30.47 + 5.66 \text{ OCCU2} - 6.70 \text{ OCCU1} + 3.45 \text{ DUR} \\
 &\quad (1.35) \quad (0.21) \quad (-0.42) \quad (2.04)^* \\
 &- 0.00010 \text{ TOASST} - 0.00032 \text{ SIZE} - 20.87 \text{ EDU} \\
 &\quad (1.45) \quad (0.211) \quad (-1.80) \\
 &+ 0.042 \text{ LAND} \\
 &\quad (1.71)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.155$$

$$\begin{aligned}
 2. \text{ IRATE} &= 34.59 - 24.79 \text{ AGENCY4} - 18.66 \text{ EDU} - 0.57 \text{ AGENCY3} \\
 &\quad (1.77) \quad (-2.45)^* \quad (-1.85) \quad (-0.021) \\
 &+ 3.92 \text{ DUR} - 0.000108 \text{ TOASST} - 0.00046 \text{ SIZE} \\
 &\quad (2.537)^* \quad (-1.736) \quad (-0.296) \\
 &+ 0.036 \text{ LAND} \\
 &\quad (1.689)
 \end{aligned}$$

$$\bar{R} \text{ Square} = 0.343$$

Mookuperi (Contd.)

$$\begin{aligned}
 3. \text{ IRATE} &= -1.98 - 4.28 \text{ PURPOSE3} - 0.00014 \text{ TOASST} \\
 &\quad (-0.09) \quad (-0.28) \quad (-3.52)* \\
 &+ 2.61 \text{ DUR} - 0.0026 \text{ SIZE} - 1.57 \text{ PURPOSE2} \\
 &\quad (2.7)* \quad (-2.767)* \quad (-0.09) \\
 &+ 1.10 \text{ EDU} + 0.024 \text{ LAND} + 55.53 \text{ PURPOSE1} \\
 &\quad (0.129) \quad (1.696) \quad (2.96)* \\
 \bar{R} \text{ Square} &= 0.741
 \end{aligned}$$

$$\begin{aligned}
 4. \text{ IRATE} &= 14.537 + 13.21 \text{ REASON1} - 0.000097 \text{ TOASST} \\
 &\quad (0.57) \quad (1.154) \quad (-1.431) \\
 &+ 0.00046 \text{ SIZE} + 4.08 \text{ DUR} - 19.34 \text{ EDU} \\
 &\quad (0.32) \quad (2.39)* \quad (-1.77) \\
 &+ 0.04 \text{ LAND} \\
 &\quad (1.65) \\
 \bar{R} \text{ Square} &= 0.235
 \end{aligned}$$

As can be seen, these estimates show a great deal of improvement over the combined regressions reported earlier, where all the village data had been combined. However, the fits are still not full satisfactory in most cases, and this calls for further research. Nevertheless the findings are interesting. As before, we have maintained a set of explanatory variables in all the equations. These are EDU, DUR, LAND, SIZE and TOASST, as before. The alternative dummy specifications are for PURPOSE, REASON, OCCU and AGENCY. For reasons of brevity, we have reported the findings in a "raw" form, and not separately written out the equations for each value of the dummy variable. Our main purpose here is to obtain an idea of the ^{types of dummy} variables which matter.

The main findings are as follows:

(a) Village : Anikad

Among all the equations, the overall explanatory power of the equation with AGENCY dummy variable is the highest, followed by the equation with REASON. This suggests that a large part of variation in IRATE is accounted for by these two (qualitative) variables. Among the other variables the results are not constant, and variables appear to change in statistical significance as the dummies are varied. However, one notices a significant positive association between IRATE and DUR in two of the equations. One way to view these results is to recognise the **alternative** dummy specifications are a way of sorting the data according to different criteria. In this perspective, we note that when the data are "sorted" by PURPOSE, IRATE varies negatively with the education level of the borrower (EDU). When we sort by REASON, then the negative association between IRATE and variable reflecting land holding and asset value becomes apparent.

(b) Village : Ezhukone

In this village also, there appears to be a fairly robust positive and statistically significant relationship between IRATE and the duration of the loan (DUR). None of the other variables show high statistical significance. However, the role of AGENCY as a dummy variable is extremely significant here, and the \bar{R}^2 is quite high when this is used. Different agencies charge very different rates of interest in this village, regardless of most other factors.

(c) Village : Thirunavaya

Here, there is an extremely strong association between IRATE and AGENCY, and the \bar{R}^2 is very high. The explanatory power of all the other equations is poor, though the equation using REASON is marginally better. In this village, for both the equations using AGENCY and REASON dummy variable, we notice a strong negative association between IRATE and the duration of the loan (DUR). This is in contrast with the pattern observed for the villages Anikad and Ezhukone. None of the other variables in the regression are significant.

(d) Village : Thalikulam

The explanatory power of the regression equations is not high under any specification. Clearly there are factors here which affect the interest rate which we have not been able to capture. In the two equations that do relatively well, i.e., with AGENCY and REASON we find a weak negative association between the rate of interest and education (EDU) and the value of total assets (TOASST) of the borrower. This suggests the importance of bargaining power in the determination of the interest rate in this village.

(e) Village : Valpatti

In this village, no particular dummy variable specification is clearly superior, they all do reasonably well in terms of \bar{R}^2 , the best equation being the one with AGENCY. What stands out very sharply

in this village is the strong negative association between the rate of interest (IRATE) and loan duration (DUR).

(f) Village : Mookuperi

In this village, IRATE variation are best explained by PURPOSE of borrowing, as this equation using this as a dummy variable does the best. The role of AGENCY is not as important in this village, in contrast with most others. Here we notice a robust positive and significant association between IRATE and DUR, which holds in all the equations. We also find that in this village, the characteristics of the borrower matters more. There is the expected negative association between IRATE and TOASST in the PURPOSE equation, but the t - ratio for this variable is on the high side in other equations also. This is true also for EDU, which also indicates a negative association. Thus richer and better educated borrowers tend to pay a lower interest rate for their loans. However, there is also a counter tendency, in that there appears to be a weak, positive relationship between IRATE and the size of landholding of the borrower (LAND).

Conclusion

These regression equations estimates reflect the heterogeneity of the informal credit market in the selected villages. Relatively few generalisations can be made. However, in most villages the role of supply side characteristics such as AGENCY is important in explaining

the IRATE. Loan characteristics are important in some cases, particularly the loan duration (DUR). However, the direction of association varies from village to village. PURPOSE and REASON also play a role in some villages. By and large, the characteristics of borrowers do not play a very important role, except in one village. Of the variables that matter TOASST and EDU are worth noting. But these associations are weak in most cases, contrary to expectation about informal sector credit. This is somewhat surprising. The regression estimates are exploratory in nature, and further detailed analysis may help sharpen our knowledge about informal sector interest rate formation.

CHAPTER 8

ROLE OF INFORMAL CREDIT MARKETS : SAVINGS MOBILISATION, ALLOCATIVE EFFICIENCY AND EQUITY IMPACT

8.1 Introduction

Financial intermediaries play an important role in economic growth by way of stimulating and mobilising savings and allocating savings to more productive channels of investment. The vicious circle of low savings, low investment and low rate of growth syndrome of underdevelopment is an essential part of the received doctrines. Savings of the household sector, which dominates the economy of a developing country, remain low partly because of the low incentives for saving, thanks to the limited opportunities for investment in their own household enterprises or elsewhere. Financial intermediation may stimulate savings of rural households by providing remunerative channels for their disposition and offering attractive returns on them. The domestic resources so mobilised are placed at the disposal of enterprises short of funds, thereby help financing investment on a larger scale. How significant is the role of informal credit agencies in domestic resource mobilisation? To what extent they mobilise savings? Are they able to stimulate additive savings? Is the security of deposits with them ensured? How are the resources so mobilised allocated? Are they channelised in to such directions as to ensure allocative efficiency? What is the

impact of resource allocation on equity? These are some of the questions that are examined in the present chapter.

8.2 Role of Informal Credit Market in Domestic Resource Mobilisation

8.2.1. The Setting

The paradox of high saving and low growth rate surfacing in the Indian economy in recent years attracted wide attention. The Working Group on Savings appointed by the Government of India against this background in its report observed that while the saving rates in the public and private corporate sectors recorded only modest increase over the period 1951-52 to 1978-79, the ratio of household saving to gross domestic product more than doubled. (Reserve Bank of India, 1982, Table 5.8, p.33). The saving performance of the rural households also seems to be quite impressive. According to one estimate, gross savings of all rural households increased more than three and a half times between 1951-52 and 1978-79, while net financial savings registered a forty-fold increase. (Ashoka Mody, 1983, Tables 1 and 3). During this period, the proportion of financial savings to total savings of the rural households had also risen commensurately. Thus, not only the rural households' propensity to save has improved, but more of their savings is tending to be susceptible to financial intermediation. This period also witnessed an unprecedented expansion of formal credit institutions like cooperative societies and commercial banks, especially of the latter after the nationalisation of major banks in the late sixties. Between 1969 and 1984, number of all commercial bank offices increased from 8262 to 45332, i.e. by 548.6 percent.

The bulk of this addition was in the rural areas. Moreover, a wide range of saving media such as the National Saving Certificate, Unit Trust, Post Office Savings Bank, etc. has been introduced, thereby widening the options before the savers. However, it is worth noting that the rate of returns on these investments is comparatively low. Since the government is committed to a policy of low lending rates on loans from banks and cooperative institutions to priority sectors like agriculture, the interest on deposits is also kept low or below what may be called equilibrium rate of interest. If due allowances is made for inflation, the real rate of interest on the deposits turns out to be much lower than the nominal rate offered. The informal credit agencies offer higher interest rates; but there is an element of risk involved in entrusting the savings with these agencies.

8.2.2. Scope for savings mobilisation by informal lenders

Of the informal lenders in the rural areas, except the professional moneylenders, all other categories practise moneylending as only a subsidiary or part time activity. Among these, as mentioned earlier, loan transactions by friends and relatives, who account for not too small a share, are of a non-commercial type, and they are apt to be lending out of their own savings. As for professional moneylenders, the scope for mobilisation of savings would depend on the scale of their loan transactions. Thanks to the massive expansion of the formal credit institutions in to the rural areas, and the segmentation of the ICM, the scale of an average professional moneylender's loan transactions is likely to be

curtailed, unless he extends his area of operations to other villages or urban areas. Owing to the constraints inhibiting the entry of a moneylender to unfamiliar areas, a typical moneylender limits his transactions to an area around his residence, thereby keeping down his annual turnover. If so, most of the moneylenders can meet the demand for credit from their savings and have less need for tapping other sources to supplement their own resources. Hence, unless new investment opportunities outside the traditional agriculture and household industries open up, demand for credit is likely to remain low and the role of professional moneylenders in mobilising household savings likely to be minimal. If, on the other hand, there is a growing demand for credit for purposes usually not met by formal credit agencies like consumption, house construction, purchase of consumer durables, etc. and there are potential borrowers indifferent to the cost of credit, then the moneylenders would become more active in savings mobilisation. The emergence of a new breed of professional moneylenders, the finance companies so-called, exemplifies this situation. (More about it later). In the case of non-professional moneylenders like agriculturist moneylenders and traders, they might be accepting deposits or loans from others to a limited extent, but mainly for financing their principal activities, viz., agriculture or trade as the case may be. Financing of loans to their limited clientele with borrowed funds does not seem to be a viable proposition. With these general observations, we shall now proceed to examine the actual situation on the ground.

8.2.3. Savings disposition of rural households

The composition of household assets may be taken as an indication of the disposition of household savings. A predominant share of the assets of rural households in India, and other developing countries, used to comprise physical assets. Even at the beginning of this decade, according to the results of the latest round of the All India Debt and Investment Survey (1981-82), of the total assets of all rural households, (Rs.36090 per household), the value of physical assets such as land, buildings, livestock, agricultural machinery, non-farm business equipments, durable household assets, etc. added up to Rs.35693 or 98.8 percent, while financial assets including shares, deposits, dues receivable, etc. came to just a little over 1 percent. (Reserve Bank of India, 1986, p.442). However, the proportion of savings in the form of financial assets to total household savings has increased several fold between early fifties and late seventies, as per the findings of the Working Group on Savings. Gross savings in the form of financial assets which was estimated at 0.5 percent of GDP (as against 6.1 percent in the form of physical assets and total domestic saving of 9.5 percent) in 1951-52 rose to 6.6 percent of GDP in 1978-79 (the ratio of saving in the form of physical assets and total domestic saving to GDP being 9.2 percent and 22.2 percent respectively). (RBI, 1982, op.cit., Table 5.8, p.33). It may be noted that these estimates of saving include that of all households proper, both rural and urban, as well as unincorporated enterprises. A break-up of the savings of the household sector, yields an estimate

of total net financial savings for the rural sector at Rs.930 crores as against aggregate savings of Rs.3650 crores, i.e. a little over 26 percent. (Mody, loc.cit.) This would work out to 2.34 percent of the estimated rural income for the country as a whole.

8.2.4. Asset composition and savings of the sample households

(i) In our study areas too, the portfolio of assets reflects a very high preference for physical assets. Of the total assets as on 1 April, 1987, the proportion of physical assets to total assets among our sample households ranges from 93.9 to 98.94 percent; obviously, the share of financial assets is very low falling in the range of 1.06 to 6.71 percent. It is significant to note that even in the case of the sample households from the Kerala villages, the proportion of savings in the form of financial assets is so negligible. That the proportion of financial assets is lowest in Anikad, where agriculture is highly commercialised, is indeed surprising. (Table 8.1).

Table 8.1 : Composition of Assets of Sample Households as on 1.4.1987

Village	Rs. per household				
	Physical		Financial		Total
	Rs.	%	Rs.	%	
Thirunavaya	144500.74	98.85	1866.01	1.15	146186.76
Thalikulam	253249.42	93.29	18212.18	6.71	271462.23
Anikad	183467.66	98.94	1969.58	1.06	185437.24
Ezhukone	138649.32	97.26	390.71	2.74	139040.03
Vilpatti	20960.82	97.37	565.08	2.63	21525.90
Mookuperi	96486.90	94.13	6020.45	5.87	102507.35

(ii) Coming to the savings by our sample households, it may be mentioned at the outset that our estimates are limited to savings in the form of financial assets. Since the focus of the present study is on savings mobilisation, rather than estimates of total savings, data on savings by sample households in the form of financial assets only were collected. It may also be noted that the estimates are of gross savings. Though the estimates of financial savings are net of reduction in assets like shares and deposits, they are not net of changes in liabilities by way of borrowings. The estimates, based on the balance sheet method, are presented in Table 8.2.

Thus, in all the selected villages, except Thirunavaya, financial savings have been positive, ranging from Rs.121 per household at Vilpatti to Rs.10883 at Thalikulam. The increase in financial assets exceeded 100 percent in four of the villages. Thirunavaya is an exceptional case where the average saving is negative representing a decrease of over 87 percent compared to the total at the beginning of the reference period.

(iii) The broad composition of financial savings consists of addition to shares, mostly of cooperative societies, and deposits. The latter includes deposits with formal credit institutions like cooperatives, commercial banks, and contribution of life insurance premium, as well as informal credit agencies such as subscription to chit funds, and deposits with professional moneylenders/finance companies. The shares of formal and informal credit agencies in the total deposits are set out in Table 8.3.

Table 8.2 : Financial Savings of Sample Households

(Rs. per household)

Village \ Asset type	Sources		Diffe- rence	Deposits		Diffe- rence	Total		Diffe- rence
	At the be- ginning of the year	At the end of the year		At the be- ginning of the year	At the end of the year		At the be- ginning of the year	At the end of the year	
Thirunavaya	1.70	1.55	-0.15	2727.96	1684.59	-1043.37	2729.66	1686.14	-1014.52 (-87.87)
Thalikulam	13.84	13.84	0.00	7306.02	18189.04	10883.02	7319.86	18202.88	10883.02 (148.68)
Anikad	180.52	229.55	49.03	989.91	1725.11	735.20	970.43	1954.86	984.23 (101.42)
Ezhukone	26.41	26.78	0.37	1810.42	3879.92	2069.50	1836.83	3906.70	2069.87 (118.69)
Vilpatti	336.13	345.28	9.15	105.55	217.43	111.88	441.68	562.71	121.03 (27.40)
Mookuperi	180.38	174.17	-6.21	1326.26	5846.29	4620.03	1506.64	6020.46	4513.82 (299.59)

Figures in brackets, last col., stand for percentage change over the reference period.

Table 8.3 : The shares of Formal and Informal Credit Agencies in the Savings of Sample Households

Credit Agency	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	At the beginning of the year	Change during the year	At the beginning of the year	Change during the year	At the beginning of the year	Change during the year	At the beginning of the year	Change during the year	At the beginning of the year	Change during the year	At the beginning of the year	Change during the year
Cooperatives	1126.76	43.24	740.97	9383.14	102.47	433.85	478.16	88.24	7.89	22.33	156.96	1956.37
Commercial banks	1385.76	-985.65	29.52	283.73	866.71	132.06	953.05	360.32	13.55	35.69	610.76	1931.14
Government	-	-	-	-	-	-	32.16	586.10		neg	241.37	404.93
Insurance	-	-	6024.10	1204.82	-	-	201.98	950.84	84.11	53.73	115.70	130.38
Sub-total	2512.52 (29.10)	-940.40 (90.32)	6794.58 (93.00)	10871.69 (99.90)	969.39 (97.93)	565.91 (76.97)	1672.35 (92.37)	1985.50 (95.94)	105.55 (100)	111.75 (100)	1124.99 (91.74)	4423.32 (94.74)
Chit funds	50.15	-12.41	23.49	7.71	20.52	169.29	117.28	41.58	-	-	-	12.66
Professional money-lenders/Finance Companies	165.29	-89.56	6.02	3.62	-	-	-	-	-	-	-	-
Others	-	-	481.93	0.00	-	-	20.79	42.42	-	-	101.27	184.55
Sub-total	215.44 (7.00)	-100.97 (9.68)	511.44 (7.00)	11.33 (0.10)	20.52 (2.07)	169.29 (23.03)	138.07 (7.63)	64.00 (4.06)	-	-	101.27 (8.26)	184.55 (4.11)
Total	2727.96 (100)	-1043.37 (100)	7306.02 (100)	10888.02 (100)	989.91 (100)	735.20 (100)	1810.42 (100)	2069.50 (100)	505.55 (100)	111.75 (100)	1226.24 (100)	4620.03 (100)

8.2.5. Savings Mobilisation by Informal Agencies

(1) An Overview

It may be noted that of the total deposits of the sample households on the initial date, the share of informal agencies ranges from 2.1 percent in Anikad to 8.3 percent in Mookuperi; in one of the villeges, formal credit institutions accounted for the entire deposits. Coming to the increase in financial savings in the form of deposits during the reference period, the share of informal agencies falls in the range of 0.1 percent in Thalikulam to 23.0 percent in Anikad. The two informal agencies with whom some savings are entrusted are professional moneylenders or finance companies and chit funds. However, be it noted that the former are reported in only two villeges, while the latter is represented in five out of the six villeges.

We had also collected data from a few sample informal lenders including professional moneylenders, agriculturist moneylenders and traders on the sources of funds and annual turn over of loan transactions. The sample is purposively chosen, depending on their responsiveness, and the findings need not be representative. With this due caution, we present the data in respect of professional moneylenders in the table below. (Table 8.4).

Table 8.4 : Annual Average Turnover of loans and sources of funds of professional moneylenders

Village	No. of sample lenders	Annual turnover Rs.	Borrowings/ Deposits Rs.	Col.(4) as % of Col. (3)
(1)	(2)	(3)	(4)	(5)
Thirunavaya	1	13750	1500	10.90
Thalikulam	4	788750	77750	9.85
Anikad	1	1856573	223500	12.13
Ezhukone	4	591625	146875	24.82
Vilpatti	1	95000	nil	-
Mookuperi	3	144167	3500	2.42

One thing which emerges from the foregoing table is that the professional moneylenders, by and large, carry on their loan transactions mostly with their own funds. The extent of dependance on borrowings or deposits would be less than one-tenth of the volume of their credit transactions in the majority of the selected villages. In other words, the average professional moneylender borrows or attracts deposits to supplement his own funds and deposit mobilisation is not his primary objective. However, as mentioned earlier, a new breed of moneylenders have emerged in recent years who have set their sights high and extend the frontiers of their operations.

(ii) Finance Companies

The growth and decline of this type of financial intermediaries has been dramatic and spectacular. Since the mid-seventies, finance

companies - alias financial enterprises, investment corporations, bankers, trusts, etc. - sprouted like mushrooms all over Kerala in both urban and rural areas. There has been a significant increase in the outmigration of workers from Kerala, especially to the Middle East Countries, since mid-seventies. The inflow of remittances reached unprecedented level. According to one estimate, foreign remittances to Kerala increased from Rs.1500-1875 million during 1975-77 to Rs.7340-9175 million in 1980-81; remittances as a proportion of the State Domestic Product rose from 6 - 8 percent to 22-28 percent. (Gulati and Modi, 1983, Table 14 p.70, mimeographed).

The inflow of remittances stimulated a spurt of activities like construction of residential buildings, cinema theatres and hotels, purchase of real estate, cars, scooters, trucks and various consumer durables like television and video sets, refrigerators, etc. thereby stimulating the demand for credit. Thanks to the low returns on the various saving media promoted by the government and formal credit institutions, the households with some savings were on the lookout for more lucrative channels. On the other hand, there were several constraints on obtaining credit for the above purposes from formal credit institutions, since they did not belong to the priority sectors. At the same time, there emerged a growing number of potential borrowers who were more concerned with easy and prompt disbursement of credit than its cost. Thus, financial intermediation became an attractive proposition, for a lender could make a reasonable margin of profit even after paying an interest significantly higher than the deposit rate of formal credit institutions. The above factors contributed to the rapid spread of finance companies.

There are no firm estimates of the number of finance companies transacting business in the State, the volume of deposits or their scale of loan transactions. According to the Revenue Department of the State Government, the number of firms registered and obtained licence for moneylending business came to about 4000, while the Economic Division of the Cochin office of the Reserve Bank of India has estimated the total to be over 10000. (Kerala Kaumudi, 5 August, 1986). As against this, according to the Kerala Small Financiers' Association, the total of these finance companies functioning in Kerala came to about 12000. Prakash has estimated that in Trichur town alone there were some 1500 partnership firms carrying on financial activities. (Prakash, 1984). In Kottayam town within one KM on the same road 30 finance companies conducted business, 12 of them being located under the same roof. (Kerala Kaumudi, 9 August, 1987).

Estimates of deposits are more difficult to obtain. 'Guestimates' of deposits with some particular companies were reported in the local dailies like Kerala Kaumudi, Malayala Manorama, Mathrubhumi, etc. For example, the deposits collected by the Kottayam offices of Amarias and Oriental Finance and Exchange Companies were reported to be Rs.5 million and Rs.10 million respectively. The New India Finance Company had mobilised deposits to the tune of Rs.20 million, the Labella Arsha Bharat had Rs.65 million by the middle of this year. (Kerala Kaumudi, different issues during May 1987). Estimates of total deposits of the finance companies in a few centres are, however, available. Thus, according to the results of a sample survey of 24 partnership firms in Trichur town, which is estimated to have more than 1500 such firms, the total deposits came to Rs.150.5 lakhs. The volume of

deposits among these 24 firms ranged from Rs.3 lakhs to Rs.11 lakhs or above. The total deposits of 1500 firms in Trichur town is estimated as Rs.100 crores. (Prakash, 1984, op.cit., pp.2131-32). On the above basis, the average per company would work out to Rs.0.06 crore or Rs.6 lakhs. Nayar in his survey of 114 finance corporations distributed over the four southern States, Andhra Pradesh, Karnataka, Kerala and Tamil Nadu, estimated the total volume of outstanding deposits of these sample firms at Rs.3530.46 lakhs as on 31 March, 1980, and the deposits mobilised during the preceding one year at Rs.3373.78 lakhs. (Nayar, 1982, Table 5, pp.26). The average deposits outstanding and received during the past one year would work out to Rs.30.97 lakhs and Rs.29.59 lakhs respectively. The survey covered 32 companies distributed at 7 centres in Kerala. The total deposits outstanding of these 32 firms came to a little over Rs.975 lakhs, and the average per firm would work out to about Rs.30.5 lakhs, about the same as the average for all the 114 firms together. The above figures would give an indication of the volume of total deposits mobilised by the finance companies in this State.

True, there are certain provisions in the Banking Companies Act and Kerala Moneylenders Act which impose restrictions on the number of depositors, amount of deposits, interest paid on deposits or charged on loans, etc. For instance, according to the former, the maximum number of deposits permitted is 25 if the concern is an individual proprietorship and 250 in case it is a partnership. The State legislation imposed ceilings on interest rates on deposits received and loans disbursed, viz., 15 percent and 19.5 percent respectively. The restriction on the number

of deposits was circumvented by the same proprietors floating several firms under different names, as for example: Trinity Trust, Trinity Jewellers, Trinity Financiers, Trinity Enterprises; Josecos Investments, Josecos Fashion Jewellers, Josecos Financiers; Muthuttu Financiers, Muthuttu Mini Bankers, Muthutu Chitti Fund, Muthuttu Bankers, Muthuttu Mutual Funds, Mini Muthuttu Financial Chitti Fund, Muthuttu Kuries and so on. Coming to interest rate offered on deposits collected or interest rates charged on loans, they were invariably higher than those permitted under the provisions of the prevailing law.

The boom in activities like construction, trade, etc. and the spread of finance companies mutually reinforced each other. Several of the enterprises attracted by the possibility of high and quick returns from investment in these grey areas and the ease of obtaining credit from finance companies soon started getting into the red and started defaulting repayment of loans.

"The mushroom growth [of finance companies] within a short span led to a substantial increase in supply of credit. In the beginning, loans were issued only to credit worthy business. Later due to competition between firms, loans began to be issued to all and sundry... The easy availability of credit led to large over borrowings and resulted in over trade". (Prakash, 1987, p.39).

Some of the finance companies diverted the deposits into financing their own ventures. The Labella Arshabharat Company, an alibi for Labella Financiers, cast its net wide setting up enterprises in such diverse fields cement, fertilizers, construction, paints, beverages, plantations, travels, marketing, food, textiles, distillery, film development,

and so on. The proprietor of Shalimar financiers fulfilled one of his pet dreams, viz., to act in a hero's role in a movie, by himself producing a cinema, financed of course, with the deposits collected. Oriental Finance and Exchange Company had invited its own doom by locking up the funds in real estate, film industry, etc. To cite another example, Adithya Finance Company, with 148 branches and over 180 extension centres in the State, has been running several other enterprises including a supermarket. The inevitable result of extending loans to enterprises of dubious viability or diverting the deposits to support the finance companies' other activities is the erosion of their liquidity to a slender margin, so slender a margin that the whole structure might come down the moment a few depositors get an alarm signal. The run on these finance companies and their downing the shutters, the proprietors decamping with the loot leaving hundreds of thousands of their helpless customers in utter distress were daily occurrences reported during the last one year. When the customers went to the offices of their respective concerns to take back deposits or interest on the same falling due on the stipulated dates, or repay the loan and take back the hypothecated gold, they were asked to come back later, if the office was open. More often than not, the office was closed with no member of the staff around. The proprietor's whereabouts were unknown. Majority of the company staff, who had got their job after giving sizable amounts as security had now lost their job as well as security, were themselves in utter distress. The run on the finance companies spread like wild fire and in such a situation their normal practice of coming to each other's rescue could not redeem the situation.

The closure of a few firms was being reported every day from early this year with the frustrated customers holding demonstration in front of the closed doors or 'dharnas' at the gates of the proprietors' residences. The tales of woe of the aggrieved parties who forfeited all their savings filled the pages of the local dailies.

In only two of our selected villages, viz., Thalikulam and Ezhukone, we came across some finance companies and they too are presently keeping a low profile. In the former village, there are at present four firms, majority of them being partnership firms. All of them have received deposits, the total deposits received during the last two years ranging from Rs.20,000 to Rs.2 lakhs. The reported rate of interest is 12 to 14 percent. At Ezhukone, we came across two firms. One of them, an individual proprietorship, was started only 1986, and has not been receiving deposits at the time of our survey. The second one is a partnership firm with four partners, and functions in a separate office building under the caption of a bank. The firm received deposits to the tune of Rs.10 lakhs in the course of last two years, an impressive record. It has a differential interest rate system, paying different rates of interest to different groups of depositors and ranging from 12 percent to 50 percent. The lowest rates of interest, 12 percent, are paid to Gulf emigrants' households, medium rates, 25 percent to cultivators and highest rates, 50 percent to employees. The rationale underlying this differentiation appears to be "to each according to his need". The general erosion of confidence in the finance companies in the State has naturally affected the tempo of business activities of these few surviving firms also.

The crash of the finance companies seems to be rather due to their liberal extension of credit to some enterprises or activities of obvious viability which have grown out of all proportions, than to "the steep fall in the Gulf remittances, the severe drought in 1982-83 and fall in the prices of agricultural products...." as averred in a recent report. (Prakash, 1987, op.cit., p.38). It is not that all finance companies had misallocated or mismanaged their funds. But the failure of a few companies to meet their due commitments to their customers was enough to arouse suspicion in the minds of the customers of other firms also and cause a general run on all firms. After all, even a normally stable and financially sound bank could collapse if it suddenly faces a run, as it happened on more than one occasion in the past.*

Certainly, the finance companies have been successful in mobilising the savings of rural households in Kerala. They entered the scene at a time when, thanks to certain fortuitous circumstances, a large number of households in certain pockets of the State were left with surplus funds. True, there were offices of the commercial banks and post office savings banks within easy reach, but the interest offered on deposits was not attractive enough. The new informal financial intermediaries exploited this situation and mobilised these savings, perhaps to a greater extent than formal savings media. However, whether such savings mobilised by them were put to productive use is another question. As the finance companies were charging excessively high interest on their loans, an

* The liquidation of the Travancore and National Quilon Bank, and the Palai Central Bank are well known examples.

interest rate beyond the normal returns from any productive investment, it should appear that the functional purpose of savings mobilisation is not served. Evidently, the mobilisation efforts proved to be counter-productive. Now that the vast majority of them have established their lack of credibility and concern for their clientele, their role in savings mobilisation will remain a sad memory of the past in the minds of all concerned.

(iii) Chit funds

Chit funds belong to a type of indigenous financial intermediaries which have been providing the savings and credit facilities to different communities from very early times. There has always been a felt need for an arrangement or mechanism for pooling the savings and meeting the credit requirements of a community, irrespective of the type of society or level of economic development. Before formal credit institutions entered the scene, it was the informal intermediaries who filled the gap; even after the former, has made considerable headway, the latter continues to play a major role in the developing countries, especially in their rural areas. Informal saving and credit associations are active in most of these countries, as reported in a series of recent studies. (See for example, Bouman, 1977; Miracle, et.al., 1980). Under this arrangement, the members of an association make regular contributions to a fund which is allocated to each member by lot, auction or some other mutually agreed formula.

"A member saves until he receives the fund, after which he starts to repay a loan in instalments. In other words, the fund received by members at intermediate

points in the life of the cycle includes a portion equal to the sum of their past and current contributions, plus a portion which is a loan to be repaid on their future contributions. Not only does the credit rotate, the saving positions rotate too. Therefore, I prefer the term rotating saving and credit associations - ROSCA, for short". (Bouman, op.cit., p.37).

Easy accessibility, simple procedures, flexibility, and adaptability to many purposes have been noted as the factors accounting for their popularity. (Ibid., pp.37-39; see also: Miracle, op.cit., pp.701-708).

There is considerable diversity in the organisation and functioning of chitties, the Indian version of ROSCA. They differ in their size (number of members instalments, total fund), life of the cycle, the way in which the order of rotation is determined (lot, auction, or arbitrary selection by the foreman), periodicity (daily, weekly, monthly, quarterly, etc.) distribution of discounts in auction chitties, etc. (Nayar, 1973, Chapters 2-5; see also: Radhakrishnan, 1973, Chapters 3-4).

Irrespective of the type of associations, savings constitute a core feature of the chitties. "Participants in these informal banking arrangements seem to believe that they save more than they would if, instead, they saved in a solitary fashion because of the discipline of having to regularly meet with the rest of the group and make a deposit", (Miracle, et.al, op.cit., p.707). Bouman also concurs with this view: "The foremost reason for joining a ROSCA is probably the "forced" saving element. Through the regularity of small deposits, which otherwise might be spent on trivillities, one is able to accumulate more sizable sums for a worthwhile cause". (Bouman, op.cit., p.38). Saving for a rainy day or

for meeting unforeseen contingencies has been the main motivation for many people joining chitties. In fact, during the early phase of its evolution chitties were primarily savings associations; during that phase the pooled savings or the capital, was distributed by lot. When the demand for credit enlarged, chitties became savings-cum-credit association; in the process, the lot chitties, were replaced by auction chitties, since the latter accommodated the credit needs of the subscribers according to their urgency.

"The main drawback of other forms of chitties is that they are unable to meet the credit needs of the subscribers, and, if at all they can, it is not at the appropriate time or on a proper scale. The auction chitty, on the other hand, can give away a fairly large sum of money as the prize amount when the subscriber needs it. By just subscribing one or two instalments to an auction chitty of the desired value, a subscriber will be able to raise a substantial amount. The access to a large lump sum at an investment of a small amount enables many an enterprising individual to start new business or trades or small industries or to expand the existing ones with the help of which they can easily repay the future instalments of the chitty. Personal credit of such magnitude with provision for repayments extending over a fairly long period, indeed, makes this chitty unique in the field of finance". (Nayar, op.cit., p.52).

Coming to the growth of chit funds, Kerala and Tamil Nadu accounted for a major share. According to Nayar's estimate, there were 5257 working chitties in Kerala in 1967-68, with an annual turn over of Rs.6378 lakhs; the corresponding number for Tamil Nadu were 3043 and Rs.1442.4 lakhs. (Nayar, op.cit., Tables 2-A, and 2-B, pp.165-166). As against this, Radhakrishnan estimated the number of chitties in Kerala, in 1967 at 12491, and their annual turnover at Rs.7500 lakhs. (Radhakrishnan,

op.cit., p.37). In the case of Kerala, the latter estimate is twice as high as the former, both in terms of the number and volume of turnover. For Tamil Nadu, no comparable figures for the above period are included for want of reliable data. However, Radhakrishnan has cited the information furnished by the Tamil Nadu Chit Funds Association according to which at the end of 1972 there were 557 registered chit companies, who were members of this association. If we take into account those who were not members, then the total may rise to 1000, the annual turnover of these companies would come to Rs.60 crores in 1971 and Rs.96 crores in 1972-73. Besides these registered chitties, there are also quite a few unauthorised ones, though run by registered companies. Their number was reported to be 19216 involving Rs.7.55 crores. (Ibid, p.45).

To what extent the chitties are able to stimulate and mobilise savings are the basic questions we are presently concerned with. Nayar's hypothesis is that a chitty maximises the quantum of individual savings.

"A person can be induced to join a chitty in which the amount of his periodic savings. As for instance, if his ability to save is Rs.100 a month, he can be admitted to a chitty the monthly contribution of which is, say, Rs.125 because owing to a high rate of dividend, the actual monthly contribution will be much less than the specified periodic subscription. In most of the instalments the subscription will be Rs.100 or still less". (Nayar, op.cit., pp.52-53).

The Banking Commission (1972) does not agree with this hypothesis. The Commission observed,

"the estimated return on the savings of a subscriber to a chit fund depends on a number of factors and assumptions. It depends, among other savings, on the discount

offered by subscribers, the commission of the foreman, the duration of the chit, the period for which the prize winner has to wait before he gets the prize, the interest he may save earned on his savings elsewhere, and the return that he can obtain by investing his prize amount.... In no case can all members get more than what they contribute because unlike a commercial bank, a chit fund does not get any return on capital employed, from anybody except from the members of the chit fund". (Banking Commission, p.117).

The Commission's conclusion is that "as savings institutions chit funds do not offer to all their savers schemes superior to those offered by commercial banks and other financial institutions". (Ibid., p.120). As for mobilisation of savings, in the case of chit funds, the commission pointed out that unlike other financial intermediaries, the collective savings of one group are made available to the same group by rotation. That is, financial intermediation is limited between members of the same group.

Despite the availability of alternative savings media of commercial banks and other financial institutions which supposedly offer better returns than the savings of subscribers to chit funds, why do they continue to flourish in both the rural and urban areas? Why do the chit funds attract more and more people to join them despite certain irregularities and malpractices brought out from time to time? One probable explanation is that, as mentioned earlier, there is an element of saving discipline or compulsory saving once the membership of a chitty is taken. Any way, it seems reasonable to presume that chit funds to generate more savings than would be the case in their absence. As for the mobilisation of

savings, it is true that the collection of savings of one group are shared by the same group. But does this negative mobilisation of savings and financial intermediation, one wonders. The fact that under the chit fund scheme transfer of funds from the savers to users does not involve intermediaries helps to eliminate intermediation costs. The built-in provision for credit serves as an additional incentive for saving by chit funds subscription.

Coming to our study areas, while all the selected villages from Kerala had chit funds functioning in their areas, they were not reported in one of the two villages from Tamil Nadu. Among the four Kerala villages, Ezhukone had the largest proportion of households reporting membership of chitties. Hence, we chose Ezhukone for the study of this institution. Our enquiry was limited to a sample of 12 chitty enterprises of which 11 are private firms and one a cooperative. They are conducting³³/currently running chitties distributed between them. Among the 11 private firms, one to three chitties are being run simultaneously, while the Ezhukone Service Cooperative Bank is running 6 chitties currently. All of them are auction chitties. The periodicity viz., monthly, and the number of instalments/subscribers, viz., 40, are uniform for all these chitties. The monthly subscription per member ranged from Rs.250 to Rs.1250.

It is significant to note the high degree of participation by the local community. The total number of subscribers to the 33 running chitties comes to 1320. Even allowing for the possibility of one person subscribing to more than one chitty simultaneously, the proportion of households participating in this activity appears to be comparatively large. More over,

besides the 12 firms we have surveyed, there is likely to be an equally large number of similar chit funds in Ezhukone, according to informed sources. Then, there are also chitties of other types differing in periodicity, procedures, etc. Mention may be made of daily chitties to which petty traders, wage earners, housewives, etc. subscribe. Evidently, chitty is a popular financial institution. With the right to take the total saving of the entire period even at the beginning of a chitty, and receive dividend after bidding, and the built-in provision for borrowing, auction chitties are a convenient saving media. As a source of credit also chitties are attractive. Entitlement to borrow the chitty amount in any instalment, facility of easy repayment in instalments, right to receive dividends even after taking the chitty amount, minimum procedural formalities are the reasons cited by our respondents for the attractiveness of chitties as a credit agency.

The scale of saving-cum-credit transactions is quite impressive. It may be recalled that among the chitties covered by our survey, there were 1320 subscribers with the monthly subscription ranging from Rs.250 to Rs.1250. The total gross subscription (without discount) for the 33 running chitties would come to Rs.7.7 lakhs per month or over Rs.92 lakhs per year. If the transactions in the other chitty enterprises are also included, the total turn over would swell further.

It has to be noted that the chitties are saving-cum-credit media. The subscribers are savers or investors for a certain period; but as and when they succeed in the bidding, they turn borrowers for the rest of the period. It is true that the returns on the savings by way of subscription

are low. But the implicit interest on the borrowing, i.e. the prize amount received, also seems to be comparatively low. At any rate, the margin of difference between the two rates may turn out to be less than in the case of alternative credit institutions.

We shall analyse the profile of a terminated chitty in Ezhukone. (See Annexe Table). Like the running chitties in our sample, the present one was a monthly auction chitty. It had 40 members, and the average subscription (gross) was Rs.625. In the auction the competition for bidding seems to have been rather acute in the first half of the chitty period, as reflected in the high discount. During the first twenty months, the average discount, including the foreman's commission of Rs.1250, came to Rs.6738 or about 27 percent of the Capital (Rs.25000) as against Rs.2548 or 10 percent during the later half of the chitty. The subscribers whose total net subscription exceeded the prize amount (capital less discount including the foreman's commission) may be treated as borrowers, and the others as investors. The total subscription per member, net of discount, came to Rs.21572.25. Thus, 26 out of the 40 subscribers turned out to be borrowers. The remaining 14 members, including the foreman, may be considered to be investors, since they apparently were not interested in bidding and thereby reduce the surplus of prize amount over subscription.

As a first approximation, we may treat the difference between prize amount and total net subscription as interest paid or received by a subscriber depending on his status whether as borrower or investor. The ratio of the difference to the prize amount would indicate the rate of interest (Ramamurthy, p.227). In our sample, the interest rate for

the borrower members ranged from 0.57 to 6.98 percent; on the other hand, for the investor members, the excess of the prize money over their total subscriptions carried an implicit interest in the range of 0.57 to 2.75 percent. The small margin of difference between the rates on savings and borrowings may be noted. However, this is a crude estimate. For one thing, the interest rates on loans and on investments would not be uniform. The interest rate relevant for borrower-members is the opportunity cost of credit, interest charged on similar loans by other credit agencies. On the other hand, the interest rate on subscriptions by investor-members should be the rate in deposits offered by credit institutions. Obviously, the former is higher than the latter. For another, when the life of a chitty exceeds one year, a simple interest rate would not capture the full cost or benefit of a transaction. In the light of the foregoing Nayar (1973 and 1975) has applied 12 percent interest on borrowals, the prize amount received by successful bidders, and 4 percent interest on investments, the subscriptions, both compound, in the estimation of discount rates in the case of a sample of a few terminated chitties.

Be that as it may, a significant proportion of the households at Ezhukone subscribe to the chit funds, inspite of the fact that the village is served by commercial banks and cooperative societies which offer saving and credit facilities. The fact that the Ezhukone Service Cooperative Society itself is currently running quite a few chitties is a reflection of the attractiveness of this media for mobilisation of savings.

8.3 Allocative Efficiency of ICMe

8.3.1. Criteria

As noted before, the ICMe in rural areas are segmented, thereby making the loan transactions largely personalised. The parties involved are known to each other fairly closely. Thus, the informal credit agencies are easy to approach. The transactions involve a minimum of procedural formalities, verification of documents, etc. Disbursal of the loans is prompt. Informality in procedures and promptness in the disposal of loan applications have a bearing on the allocative efficiency of the ICMe.

Another aspect in terms of which the efficiency of ICMS is assessed is the allocation of credit purpose-wise. It is presumed that the allocation of the informal sector credit is not optimal, that a larger proportion of it is used to finance unproductive outlays, or those with lower social benefits or returns like hoarding, speculation and consumption, particularly conspicuous consumption. Whether the allocation of the whole or a major part of informal credit is sub-optimal or not is a debatable question. Even if it is, the purpose-wise allocation of credit is in the hands of its users rather than with the lenders. It is the borrower who decides for what purposes the loans are to be used though they may often differ from the priorities of planners and policy makers. Therefore, to adjudge the allocative efficiency of ICMe on the basis of the purposes for which credit from informal sources is actually used vis-a-vis the priority purposes in the perspective of policy makers does not seem to be very meaningful.

8.3.2. Consumption credit vs production credit

One of the live issues in the literature on ICMs has been the direction and purpose of credit there in, and particularly the role of informal lenders in the provision of consumption credit, so-called. That the dichotomy of credit into production credit and consumption credit conceptually unsatisfactory had been pointed out by several scholars in the past. (see for examine, Mellor, 1966, Chapter 17). The fungibility of production and consumption credit has been again reiterated in a recent study:

"One of the main features of small holders' agriculture is the integration of household expenditures and expenditure related to the financing of farming activities. Therefore, it is quite difficult to identify the real purpose of a loan a farmer applies for. A loan can formally be directed to something productive but the money which should have been used to finance this investment in case there was no loan can now be used for other purposes. It has to be realised that money is fungible and that in many cases the end of a loan can not be monitored. Hence, if purposes of loans are discussed it must be kept in mind that these are just the purposes mentioned by the applicants of loans and that funds are not necessarily used for financing these purposes". (Martien van Nieukoop, op.cit., p.48).

While drawing a distinction between production credit and consumption credit, there seems to be a value judgement, implicit or explicit, that the latter is less desirable, that it presumably diverts the savings of the community to channels of low social returns or benefits such as speculation, conspicuous consumption, etc. This presumption is uncalled for. A good proportion of the so-called consumption credit

is used to meet necessary consumption. Equally unwarranted is the presumption equating consumption credit with credit from informal sources. Obviously, the fact of the matter is that the sources of credit and its purpose depend on certain characteristics of the households concerned such as their asset and income levels, access to different credit agencies, the priorities of purposes, etc. While households in the upper strata, have greater access to formal credit institutions, those at the other end of the scale have to depend more on informal credit agencies. Similarly, whereas households in the higher strata may use a greater proportion of credit for financing productive expenditure, those at the lower strata resort to borrowing for meeting consumption expenditure.

Given the inequality in the distribution of institutional credit, it is natural that households in the lower strata have to lean heavily on the the informal credit agencies. The findings of the All India Debt and Investment Survey (1971-72) bring out sharply the extreme skewness in the distribution of credit from the government, cooperative societies and commercial banks. The shares of households belonging to different asset groups in the total cash dues outstanding from the above three sources are set out in Table 8.5. It may be noted that the percentage share from each of the sources rises sharply as the size of household asset holding increases. The cooperatives and commercial banks account for a larger proportion of institutional credit than the government. Of the total credit extended by the above sources, the shares of the bottom four classes of households, which constitute more than half the number of rural households,

add up to about 12 percent of total credit from the government, 6 percent of total credit from the cooperatives and a little over 2 percent of total commercial bank credit. As against this, the corresponding shares of the households in the highest three asset classes, i.e. above Rs.30000, which constitute less than one-tenth of the total, come to 40.17 percent, 49.87 percent and 68.88 percent respectively. In fact, the shares of credit from the cooperatives and commercial banks in the case of the top asset class, constituting less than 1 percent of all rural households far exceed the corresponding shares of the bottom four asset groups.

Table 8.5 : Share of each asset group in the aggregate cash dues outstanding owed to formal credit institutions as on 30th June 1971

Asset Group	Proportion of households %	Government	Co-operative Society	Commercial Bank
1	2	3	4	5
Upto 500	11.28	0.64	0.13	0.20
500 - 1000	8.35	0.46	0.30	0.25
1000 - 2500	15.53	3.61	1.48	0.70
2500 - 5000	16.13	7.28	3.84	1.01
5000 - 10000	18.33	14.1	9.93	3.99
10000 - 15000	9.71	11.5	10.14	3.02
15000 - 20000	5.72	9.76	8.19	7.24
20000 - 30000	6.22	12.92	16.11	14.72
30000 - 50000	4.84	15.90	18.54	19.81
50000 - 100000	2.94	15.45	19.16	21.54
100000 - above	0.95	8.82	12.17	27.53
Total	100	100	100	100

Source: All India Debt and Investment Survey 1971-72, Statistical Tables Relating to Cash dues outstanding against rural households as on 30th June 1971, Reserve Bank of India, 1976, p.97.

Data on the purpose-wise distribution of credit from each of the credit agencies are not readily available. However, the distribution of total credit classified according to credit agencies, and that according to purpose for each asset group are available in the reports of the All India Debt and Investment Survey. When these are placed in juxtaposition they should give us some insight into the phenomenon we are trying to unscramble. We now proceed to examine these data. In Table 8.6 we present the data on the sources and uses of funds borrowed by the rural households to different asset groups during the year ended 30th June 1972. We observe significant differences between asset groups in the size and sources of credit on the one hand and the purposes to which they are reported to be used on the other. For instance, the average size of loans in the top asset class is about 30 times that of the lowest asset group. The proportion of loans from informal credit agencies is a little over 98 percent of the total borrowings of households in the lowest stratum; this proportion drops to about 60 percent in the case of households at the other end of the asset scale. The proportion of credit from informal agencies almost steadily falls with increase in the size of assets. Coming to the use of credit, the proportion of it put to productive use, comprising farm and non-farm business, varies directly with the size of household asset holdings, ranging from about 10 percent with households in the bottom stratum to about 64 percent among households from the top stratum. Opposite is the trend in the case of the proportion of credit used to finance household expenditure, which falls from about 78 percent to a little over 26 percent between the two extreme strata.

Table 8.6 : Borrowings in Cash according to Credit Agency and Purpose Rural Households of Different Asset Groups, 1971-72

All India : All Households

Household asset holdings Rs.	Proportion of households	Borrowings Total : Rs. per household Rs.	Source		Purpose				Others	
			Formal %	Informal %	Farm & non-farm business Rs. %		Household Expenditure Rs. %		Rs.	%
Upto 500	11.28	39.34	1.98	98.01	3.93	9.98	30.66	77.93	4.75	12.07
500 - 1000	2.35	60.36	3.72	96.28	6.54	10.83	46.54	77.10	7.29	12.07
1000 - 2500	15.53	83.54	6.64	93.35	15.17	18.15	58.66	70.21	9.70	11.61
2500 - 5000	16.13	107.90	10.40	89.60	22.53	20.88	71.65	66.40	13.71	12.70
5000 - 10000	18.33	149.14	11.57	88.42	44.99	30.16	87.32	58.54	16.82	11.27
10000 - 15000	9.71	221.12	16.32	83.67	84.09	38.02	114.73	51.88	22.30	10.08
15000 - 20000	5.72	250.42	24.82	75.17	107.14	42.78	118.71	47.40	24.56	9.80
20000 - 30000	6.22	323.97	22.67	77.33	126.43	39.02	158.14	48.81	39.40	12.16
30000 - 50000	4.84	413.24	26.31	73.68	104.62	47.09	171.93	41.60	46.69	11.69
50000 - 100000	2.94	665.17	34.83	65.16	352.92	53.05	241.05	36.23	71.21	10.70
100000 & above	0.95	1162.78	40.12	59.87	739.65	63.61	305.06	26.23	118.01	10.14
Total	100	173.89	19.71	80.27	64.29	36.97	90.15	51.84	19.46	11.19

Source : Department of Statistics, All India Debt and Investment Survey 1971-72, Statistical Tables Relating to Cash Borrowings and Repayments of Rural Households During July 1971 to June 1972 and Cash Dues Outstanding as on 30th June, 1972, Reserve Bank of India, Bombay 1978, Table 2 (p.132) and Table 3 (p.136).

The break up of cash dues outstanding as on 30th June, 1972, according to sources and uses of funds displays the same pattern. (Table 8.7). The share of informal credit agencies came to about 96 percent of total cash dues outstanding against households in the lowest asset group from which it steadily fell in the case of households of the upper strata, coming down to about 10 percent with those in the top class. The rise in the proportion of credit going into farm and non-farm business with increase in the size of assets is comparatively steep, from about 11 percent to 73 percent. As against this, the proportion of credit accounted for by household expenditure declined from about 78 percent to 16 percent.

Apparently, the seventies witnessed some significance changes in the sources and uses of funds. Thus, the share of formal credit institutions in the total cash dues outstanding against all households together, as on 30th June 1981, came to a little over 61 percent compared to about 29 percent ten years back. The proportion of total credit used in farm and non-farm business by households of all the strata together came to about 69 percent in 1981 as against 50 percent earlier. Naturally, the proportion of credit used for household expenditure declined, to nearly half the earlier figure. (See Table 8.8). However, the pattern of variation across the asset groups in respect of the sources and uses of funds continues, and naturally so. More over, it is significant to note that the degree of inequality in the distribution of institutional credit has been accentuated. The inter-group differences in the reliance on informal credit sources has widened. Thus, while the households in the bottom

Table 8.7 : Percentage Distribution of Households reporting and average amount of Households of Cash dues outstanding by asset groups credit agency purpose, as on 30.6.1971

All Households

Household asset Holding (Rs. 000)	Percentage of Households	Sources			Purpose				Others	
		Total Rs.	Formal %	Informal %	Farm & non-farm business Rs. %		Household Expenditure Rs. %		Rs.	%
Upto 500	11.28	80.06	3.92	95.85	8.47	10.58	62.25	77.75	9.35	11.68
500 - 1000	8.35	133.32	4.23	95.78	19.02	14.27	97.52	73.15	16.79	12.59
1000 - 2500	15.53	216.07	8.03	91.97	44.79	20.73	146.96	68.01	24.32	11.26
2500 - 5000	16.13	298.73	12.93	87.07	87.06	29.14	178.13	59.63	33.55	11.23
5000 - 10000	18.33	412.51	19.47	80.53	165.96	40.23	205.87	49.91	40.67	9.87
10000 - 15000	9.71	567.28	25.09	74.91	270.57	47.70	252.44	44.50	44.29	7.81
15000 - 20000	5.72	673.66	31.00	69.00	364.38	54.09	248.81	36.93	60.46	8.97
20000 - 30000	6.22	954.65	36.21	63.79	567.88	59.49	315.50	33.05	71.24	7.46
30000 - 50000	4.84	1323.43	39.67	60.33	848.97	64.15	383.93	29.01	90.52	6.84
50000 - 100000	2.94	1946.33	45.58	54.42	1373.12	70.55	420.37	21.60	152.85	7.85
100000 & above	0.95	3699.58	50.17	49.83	2690.31	72.72	576.12	15.57	433.15	11.71
Total	100	487.05	28.93	71.07	243.52	50.00	199.26	40.91	44.28	9.09

Source: All India Debt and Investment Survey, 1971-72, Statistical Tables Relating to Cash Dues Outstanding Against Rural Households on 30th June, 1977, Table 2, p.97 and 3, p.101.

Table 8.8 : Percentage Distribution of Amounts of Outstanding Cash Dues contracted from Institutional and Non-institutional Credit Agencies for Each Household Asset Holdings Group, as on 30.6.1981

All India : All Households

Household Outstanding Rs. (000)	Proportion of Households	Total Rs.	Sources		Purpose				Others	
			Formal %	Informal %	Farm & Non-farm business		Household Expenditure		Rs.	%
					Rs.	%	Rs.	%	Rs.	%
	5.75	53.22	8.92	91.08	8.11	15.23	41.94	78.80	3.17	5.95
1 - 5	18.18	159.98	28.60	71.40	46.96	29.35	94.96	59.35	18.06	11.28
5 - 10	14.58	246.94	32.55	67.45	101.80	41.22	110.95	44.92	34.19	13.84
10 - 20	18.68	394.87	45.69	54.31	212.22	53.74	136.01	34.44	46.64	11.82
20 - 50	23.77	670.48	55.06	44.94	431.05	64.28	182.05	27.15	57.33	8.55
50 - 100	11.89	1037.85	57.99	42.01	741.33	71.42	200.32	19.30	75.26	7.25
100 - 500	7.60	2365.70	76.37	23.69	1915.39	80.96	239.06	10.10	211.25	8.92
500 & above	0.35	16343.30	94.90	5.10	15793.12	96.63	263.32	1.61	287.44	1.75
Total	100	652.69	61.21	38.79	450.42	68.99	145.76	22.32	56.19	8.60

Source: Estimated from various Tables in Sarvekshana, Vol. XI, No. 1, July 1987, Ministry of Planning Government of India, New Delhi.

stratum had reported a little over 91 percent of their total outstanding credit to be due to informal agencies, it was only 5 percent in the case of the top asset group. The corresponding proportion in 1971, it may be recalled, were around 96 percent and 50 percent respectively. The changes in the purposes to which credit was directed are also more pronounced in the case of households belonging to the higher-asset classes. Since the class intervals of the asset groupings for the two periods are different, comparisons have some limitations.

Among the two broad groups of households, viz., cultivators and non-cultivators, the former, by and large, allocates a greater proportion of credit to productive purposes than the latter. According to the results of the latest round (1981-82) of the All India Debt and Investment Survey, the proportion of total cash dues outstanding allotted to production purposes, i.e. farm and non-farm business, came to 63.93 percent in the case of cultivator households as against 37.74 percent in the case of the other group. A smaller proportion of credit, a little over 20 percent, is used to finance household expenditure by the former compared to about 51 percent in respect of the latter group of households. Inter-group differences in the proportion of credit from institutional and non-institutional sources also show significant differences. Thus, the proportion of credit from formal credit institutions came to 63.2 percent in 1981 in the case of cultivator households, while the non-cultivator households had met an identical proportion of their credit needs from informal agencies. (Sarvekshana, Vol.XI, No.1, 1987, Table 8, pp. S-71).

The explanation for the above inter-group differences in the sources and purposes of credit lies to a large extent in the differences in the levels of income and assets of the two groups of households. Thus, the non-cultivator households who have on the average lower income avail of credit more for meeting consumption expenditure, and for the purpose they have greater access with informal agencies. Further, the apparent restrictions on formal credit institutions extending credit for consumption purposes are enforced more strictly against lower income households like non-cultivators.

Needless to say, among the cultivator households themselves, there are apt to be considerable differences in the sources and uses of funds. The proportion of credit used for production purposes depends, among other things, on the level of technology. The spread of high yielding varieties (HYVs) and intensity in the use of chemical fertilizers and pesticides, mechanisation, etc. may be taken as indices of the levels of technology in agriculture. Irrigation facilities to a large extent govern to success of the new agricultural technology. Punjab, Haryana and Western Uttar Pradesh stand out from the rest of India in the success of the so-called Green Revolution. The spread of HYVs in the region has been nearly total. The annual compound rate of growth of fertilizer consumption in the Northern Region - which includes Punjab and Haryana - during 1960-61 to 1980-81 has been estimated at 16.29 percent as against 9.91 percent for All-India. (Daya Krishna and S.B.Sarin, "Regional Dimensions of Agricultural Growth", in Regional Dimention of India's Economic Growth, Proceedings of Seminar Held at Nainital, 1982, Annexure Table 5, p.89). Punjab and Haryana topped the list of states in the

intensity of cropping, ratio of gross-cropped area to net sown area in the late seventies, the index working out to 159 and 151 respectively compared to the All-India average of 123. The proportion of irrigated area to net sown area as of 1978-79 came to 78.09 percent and 52.55 percent respectively in Punjab and Haryana, the highest among all the States. (Ibid. Annexure IV, p.87). The index of intensity of irrigation, i.e. ratio of gross irrigated area to net irrigated area, came to 169 and 155 respectively in Punjab and Haryana, again leading the other States. The inter-State Punjab and Haryana, again leading the other States. The inter-State differences in the purposes in which total credit was used by cultivator households broadly reflects the differences in the levels of agricultural technology and associated factors. Thus, the proportion of outstanding cash dues in mid-1981 used in farm business amounted to 78.84 percent and 76.71 percent respectively in the case of cultivators from Punjab and Haryana, the second and third highest among all the State as against the all-States average of about 64 percent. Further, in the proportion of credit used as capital expenditure in farm business, Punjab and Haryana top the list. On the other hand, the proportion of cash dues outstanding accounted for by household expenditure in these two States, 13.4 percent and 12.5 percent respectively, turned out to be among the lowest. In Table 8.9 we present the distribution of outstanding dues in different States according to purpose of use. In juxtaposition with the above we also present data on the shares of formal and informal credit agencies in the total debt outstanding. It may be noted that the share of credit from formal credit institutions in Punjab and Haryana

is significantly above that of the majority of States. It seems that, by and large, the share of formal credit varies directly with the proportion of credit used in farm business, and inversely with that of household consumption expenditure.

Table 8.9 : Purpose-wise Distribution of Credit, 1981
Cultivator Households

States	Purpose-wise distribution of dues outstanding		Share of the Credit Agencies	
	Farm business %	Household expenditure %	Formal %	Informal %
1. Karnataka	79.14	12.26	78.70	21.29
2. Punjab	78.84	13.40	76.77	23.23
3. Haryana	76.71	12.48	80.35	19.65
4. Gujarat	76.31	18.70	71.61	28.40
5. Maharashtra	74.06	9.05	87.78	12.23
6. Madhya Pradesh	73.94	15.15	67.46	32.54
7. Orissa	63.90	15.38	83.46	16.55
8. Andhra Pradesh	63.79	21.64	43.53	56.48
9. Uttar Pradesh	62.74	22.08	59.24	40.77
10. Tamil Nadu	57.27	24.12	45.27	54.73
11. West Bengal	52.55	34.52	65.55	34.65
12. Rajasthan	48.28	31.98	42.46	57.54
13. Bihar	46.68	26.12	49.07	50.91
14. Himachal Pradesh	42.51	37.91	71.42	28.58
15. Kerala	37.25	21.36	78.74	21.25
16. Assam	26.59	40.45	26.04	73.97
17. Jammu & Kashmir	21.79	30.15	45.82	54.19
All State	63.93	20.07	63.15	36.85

Source : Sarvekshana, Vol.XI, No.1, July 1987, Table 12, pp. S-99 - 101.

$$r = 0.2059699$$

$$r^2 = 0.4886$$

7.3.4 The Study Areas

Against this backdrop, we now proceed to examine the functioning of the ICM in our study areas. The purpose-wise distribution the informal sector credit among the sample households is set out in Table 8.10. The proportion of credit put to production, farm and non-farm business, purposes is comparatively low (except in Mookuperi) ranging from 6 percent to 27 percent. As against this, consumption including household expenditure, construction and repairs of houses, purchase of consumer durables, education, marriage and other ceremonies, etc. accounted for more than one half of the total borrowings from this sector in five of the villages. However, it may be noted that consumption per se claimed a comparatively low proportion, varying from about 4 per cent in Ezhukone to a little over 21 percent in Mookuperi. Among the items under the broad category of consumption, construction and repairs of residential buildings constitute the single most important one in all but one village. The share of this items falls in the range of 21 to 45 percent of the total informal sector credit. Obviously, housing conditions greatly influence health and productivity of the members of a household. Hence, expenditure on this item is atleast partly productive or may be treated as productive consumption. Another leading item under consumption is expenditure on marriage and other ceremonies, its share exceeding one-fifth in half of the villages. There may be a considerable amount of avoidable waste in this item. But, then, a typical householder does not have much of an option, thanks to social compulsion. This has become a fact of life,

Table 8.10 : Purpose-wise Distribution of Credit from Informal Agencies

Purpose of Loans	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookupari	
	Amount Rs.	Share %										
1. Production												
1.1 Cultivation	-	-	-	-	6300	-	850	-	23500	-	-	-
1.2 Non-farm business	31250	-	7500	-	18100	-	7000	-	7000	-	41200	-
Sub total	31250	18.71	7500	6.34	24400	27.14	7850	14.69	30500	22.46	41200	66.45
2. Consumption												
2.1 Household expenditure	33895	8.32	14325	12.10	8500	9.15	2100	3.93	21810	16.06	13330	21.50
2.2 Construction & repairs of houses	71000	42.50	49500	41.82	24970	27.77	11300	21.14	61500	45.28	-	-
2.3 Purchase of construction durables	400	0.24	-	-	-	-	-	-	-	-	5175	8.34
2.4 Education							9000	16.84	-	-	1800	2.90
2.5 Marriage and other ceremonies	21450	12.84	2800	2.37	27150	30.19	12200	22.63	12000	18.84	200	0.32
Sub total	106745	63.90	66625	56.28	60620	67.42	34600	64.73	95310	70.18	20515	33.07
3. Repayment of past debts	26850	16.07	11750	9.93	4900	5.45	11000	20.58	10000	7.36	300	0.48
Total	167045		118375		89920		53450		135610		62005	

and expenditure on this item is almost a 'necessary consumption', so to say. Repayment of past debts claimed not an insignificant proportion of informal credit. The assessment of the functional role of financing of this item is more problematic. For, the debt in question may have been incurred for meeting production and/or consumption expenditure. Further, given the high rate of interest on loans from informal agencies, the livelihood of households indulging in conspicuous consumption with borrowed funds is less. The average size of loans borrowed for consumption per se also appears to be small (Table 8.11). It may be noted that the bulk of the loans taken for this purpose, more than three quarter of the number of loans in five of the villages, are below Rs.1500.

Table 8.11 : Number and Size of Loans (Borrowings) used for Consumption

Village	Loan size Rs.	Upto 500	500- 1500	1500- 2500	2500- 5000	5000- 10000	>10000	Consumption Total	All purpose Total
	No. %								
Thirunavaya	No.	29	7					36	98
	%	80.56	19.44					100	
Thalikulam	No.	4	2	3	1		1	11	39
	%	36.37	18.18	27.27	9.09		9.09	100	
Anikad	No.	15	4	1	-	1		21	98
	%	71.43	19.05	4.76		4.76		100	
Ezhukone	No.	1	2					3	56
	%	33.33	66.67					100	
Vilpatti	No.	20	4		1			25	67
	%	80.00	16.00		4.00			100	
Mookuperi	No.	6	9	2	3			20	52
	%	30.00	45.00	10.00	15.00			100	

In brief, the sources of credit and its purpose vary across the asset classes of households. The proportion of credit from formal credit institutions and that put to production purposes vary with the size of household assets. On the other hand, the proportion of credit from informal agencies and that used to meet consumption expenditure vary inversely with the asset class. A high proportion of credit from informal agencies in the selected villages is used for non-production purposes. Of this necessary consumption accounts for a comparatively small share, the rest going into items like house construction, repayment of old debt, marriage and other ceremonies, etc. All consumption credit, therefore, can not be deemed to be wasteful or inproductive. Neither is all credit from the informal sector absorbed in consumption outlay, nor is all consumption expenditure met by informal credit. After all, credit is fungible.

7.4 Equity Impact

Equity aspect of credit has two elements, namely its distribution and terms. Credit from the formal sector comprising government, cooperative institutions, and commercial banks is heavily subsidised. Naturally, the formal sector credit is the most sought after. But the procedural formalities involved, the documents to be produced, not to speak of the money and real cost to be borne by the prospective borrowers are heavily weighted against the households from the lower income/asset strata. No wonder that the distribution of formal credit is unequal, more unequal than that of credit from the informal agencies (Table 8.12).

Table 8.12 : Distribution of Cash Dues Outstanding according to Sources and asset groups, 1982
All rural households, All India

Household asset holding (Rs. 000 's)	Proportion of households (Cumulative Percentages)	Share of different asset holding class	
		Formal	Informal
Upto 1	5.75	0.08	1.35
1 - 5	23.93	2.55	11.35
5 - 10	38.52	6.02	23.07
10 - 20	57.20	16.00	42.39
20 - 50	80.97	42.00	76.91
50 - 100	92.06	43.42	78.59
100 - 500	99.65	84.09	98.53
500 & above	100.00	100.00	100.00

Sources: Estimated from various tables in G.O.I. N.S.S.O.,
Sarvekshana, Vol.XI, No.1, July, 1987.

The Lorenz ratios in respect of outstanding debt against all rural households owed to the government, cooperatives and commercial banks in 1982 come to 0.4954, 0.5218 and 0.7001 respectively. For all the above sources as a whole it works out to 0.6057, as against 0.2063 for all the informal credit agencies. Evidently, the proportion of credit from the informal lenders reaching the lower income groups of households is greater than that from the formal credit sources. Thus, informal credit apparently helps to redress the inequity in the distribution of formal credit.

We shall now examine the degree of equality in the ICMs of our selected villages. In the adjoining table (Table 8.13) we set out the distribution of loans from all informal sources combined in the selected villages. The distribution of the loans from the informal sector does not appear to be very equitable. The share of the top asset class of households, which constitute less than percent in all the villages falls in the range of 45 to 74 percent, except Vilpatti where the second highest class accounts for a little over 49 percent. It is interesting to note that the degree of inequality in the distribution of informal sector credit in the selected villages is slightly higher than that of credit from the formal sectors. The Lorenz ratios of the distribution of loans from the two sectors are given in the following statement.

Table 8.13 : Distribution of loans from all informal credit agencies by asset class in the selected villages

Asset Class Rs. per household	Thirunavaya		Thalikulam		Anikad		Ezhukone		Vilpatti		Mookuperi	
	Amount Rs.	Percent										
	-	-	-	-	-	-	-	-	200	0.14	-	-
500 - 1000	-	-	-	-	2077	2.11	-	-	250	0.18	400	0.06
1000 - 2500	-	-	-	-	2400	2.44	-	-	7440	5.45	1600	2.58
2500 - 5000	-	-	8500	4.62	-	-	-	-	11500	8.43	1300	2.10
5000 - 10000	-	-	-	-	3350	3.41	-	-	3500	2.56	3258	5.29
10000 - 15000	-	-	1500	0.82	5250	5.34	-	-	4000	2.93	2000	3.23
15000 - 20000	2550	1.51	3400	1.85	4700	4.78	500	0.62	500	0.36	-	-
20000 - 30000	3910	2.31	11200	6.09	9550	9.71	-	-	21820	16.00	225	0.03
30000 - 50000	11850	7.01	11205	6.09	1500	1.52	11200	13.80	20100	14.74	8450	13.63
50000 - 100000	37100	21.95	46079	25.04	6750	6.86	9300	11.46	67000	49.15	16650	26.85
100000 & above	113635	67.22	102150	55.51	62800	63.84	60150	74.12	-	-	28100	45.32
Total	169045	100	184034	100	98377	100	81150	100	136310	100	62005	100

Table 8.14 : Distribution of the number of loans from formal and informal credit agencies

Household asset Holdings (Rs.)	Thirunavaya		Thalikulam		Anikad							
	Formal	Informal	Formal	Informal	Formal	Informal						
	No. percent											
Upto 500	-	-	-	-	-	-	-	-				
500 - 1000	-	-	-	-	-	-	3	5.88				
1000 - 2500	-	-	-	-	-	-	1	1.96				
2500 - 5000	-	-	2	3.92	2	3.77	-	-				
5000 - 10000	-	-	1	1.96	-	-	6	5.13	5	9.80		
10000 - 15000	-	-	-	-	2	3.77	10	8.55	6	11.76		
15000 - 20000	3	8.11	7	7.07	4	7.84	6	11.32	4	3.42	2	3.92
20000 - 30000	2	5.41	11	11.11	4	7.84	5	9.43	12	10.26	12	23.53
30000 - 50000	4	10.81	9	9.09	5	9.80	7	13.21	11	9.48	1	1.96
50000 - 100000	10	27.03	27	27.27	7	13.73	13	24.53	19	16.24	4	7.84
100000 & above	18	48.65	45	45.45	28	54.90	18	33.96	55	47.01	17	33.33
All group	37	100	99	100	51	100	53	100	117	100	51	100

Contd.....

Table 8.14 Contd...

Household asset holding (Rs.)	Ezhukone		Vilpatti		Mookuperi	
	Formal	Informal	Formal	Informal	Formal	Informal
	No. Percent					
Upto 500	- -	- -	- -	1 1.85	- -	- -
500 - 1000	- -	- -	- -	3 5.56	- -	1 3.57
1000 - 2500	- -	- -	3 3.23	9 16.67	- -	3 16.71
2500 - 5000	1 1.15	- -	8 8.60	7 12.96	1 2.38	2 7.14
5000 - 10000	2 2.30	- -	13 13.98	6 11.11	2 4.76	4 14.29
10000 - 15000	3 3.45	- -	10 10.75	3 5.56	4 9.52	3 10.71
15000 - 20000	3 3.45	1 3.13	7 7.53	1 1.85	- -	- -
20000 - 30000	6 6.90	- -	15 16.13	11 20.37	5 11.90	1 3.57
30000 - 50000	6 6.90	4 12.50	17 18.28	7 12.96	7 16.67	3 10.71
50000 - 100000	23 26.44	11 34.38	18 19.35	6 11.11	7 16.67	3 10.71
100000 & above	43 49.43	16 50.00	2 2.15	- -	16 38.10	8 28.57
All groups	87 100	32 100	93 100	54 100	42 100	28 100

Table 8.15 : Concentration of formal and informal sector credit in selected villages

Village	Lorenz ratio	
	Informal	Formal
Thirunavaya	0.2572	0.1767
Thalikulam	0.2696	0.1812
Anikad	0.3236	0.3070
Ezhukone	0.2131	0.1658
Vilpatti	0.5066	0.0903
Mookuperi	0.3552	0.2614

The Lorenz ratios of the distribution of informal sector credit appears to be rather low in all the villages except Vilpatti. It is true that the corresponding ratios of loans from the formal sector are lower, though only marginally. Given the small size of the sample we should not hasten to generalise from the above findings. For the rural areas in the country as a whole, there is apt to be less inequality in the distribution of credit from informal sources than that from the formal credit sector. The factor underlying the difference is their easier accessibility to the low income households rather than their concern for equity. There is no reason to presume that the informal credit agencies should be motivated by considerations of equity. The fact of the matter is that they extend more credit to the lower income

groups of households than the formal credit institutions because of personal relationships and for other considerations.

Interest rate and other terms and conditions of loans have their implications for equity. Evidently, loans from the informal credit agencies carry much higher interest rates than those from the formal credit institutions, though the latter is heavily subsidised. The other terms and conditions and malpractices associated with the informal lenders are also exploitative, especially so in the case of disadvantaged groups of households. Thus, the equity impact of more equal distribution of informal credit is more than offset by the exorbitant interest rate and extortionate terms and conditions associated with it.

One aspect cited in favour of informal credit agencies is that they provide consumption credit which is generally not available from their counterparts. It is true that without access to the informal sources, a good proportion of the rural households would find it difficult to tide over periods of financial stress. The other side of the coin is that the extremely vulnerable position of their clientele embolden the lenders to exact maximum price for the credit. After all, it is not humanitarian considerations, the desire to save the needy from starvation, which motivate the informal lenders to extend credit to them.

The distribution of informal credit does not seem to be according to the need of particular borrowers either. The lower income households do not seem to be able to meet all their credit requirements from these informal agencies. Apparently, the informal lenders practise certain

credit rationing on the basis of their assessment of the credit worthiness of the prospective borrowers and the security which the latter can provide. By and large, in our selected villages, the average size of loans in the case of the households from the lower strata is small, in both absolute and relative terms.

In brief, it is true that the informal credit agencies fill the credit gap experienced by the disadvantaged groups of rural households to some extent. By providing credit to meet essential consumption, they rescue some sections from starvation and distress. However, the cost of this credit, which generally varies inversely with the borrowers' resource position, is too high to make a favourable equity impact on those who mostly depend on this source.

To sum up : The scope for savings mobilisation by informal credit agencies in a typical Indian village used to be limited, thanks to constraints on both the demand and supply sides. Landlords, agriculturist moneylenders and traders carried on the lending business as a part time activity which they could manage with their own savings. Even professional moneylenders did not feel the need to tap other's savings mainly because the credit requirements of their customers could be met with own resources. However, with increase in demand for credit and supply of liquid funds with some households, the informal credit agencies, the professional moneylenders in particular, began to attract savings by offering higher interest rates. The new breed of professional moneylenders - finance companies - have been able to mop up considerable volume

of savings in Kerala and Tamil Nadu in recent years by offering attractive returns and other incentives. But, for the savings entrusted with these informal agencies there was hardly any security, as vividly brought out by the closure of the finance companies in Kerala in recent days. Another informal credit agency which mobilises household savings is the chit fund. The chit funds have expanded considerably in these two States. Thanks to some of their distinct characteristics such as the right to take the total savings of the entire period at the beginning of a chitty, to receive dividend after bidding, the built-in provision for borrowing, etc. the auction chitties are a convenient saving media. Though it is an informal agency, the security of the participants' savings is ensured by the community pressure.

As for allocative efficiency, the informal credit agencies are more easily accessible and have less transaction costs. True, a larger proportion of credit from these sources is allotted for consumption expenditure. But, all consumption credit is not necessarily unproductive, as for example necessary consumption. Neither is all consumption expenditure met with informal credit, nor is all informal credit used for consumption. The purpose wise distribution of informal credit would depend upon the borrowers' resources. However, informal credit may be more prone to be spent on non-essential or conspicuous consumption, hoarding and speculation, investment in non-viable enterprises, etc. The allocation of credit from the finance companies, referred to earlier, exemplifies this proposition. The diversion of the funds to unproductive uses erodes the

financial viability of such enterprises and the depletion of the savings mobilised by them, as illustrated earlier.

We have noted that the equity impact of the transactions in the ICM is negligible if not negative. After all, in the nature of things, the informal lenders motivated primarily by profit are not concerned with equity.

Annexe Table : Profile of a terminated auction chitty

Instal- ment	Prize amount Rs.	Discount Rs.	Forman's Commission Rs.	Dividend available for dis- tribution Rs.	Dividend per sub- scriber Rs.	Amount per subscriber at the instalment Rs.	Discount as % of Capital
1	2	3	4	5	6	7	
1	2500	-	-	-	-	625.00	30
2	17500	7500	1250	6250	156.25	468.75	30
3	17500	7500	1250	6250	156.25	468.75	30
4	17500	7500	1250	7250	156.25	468.75	30
5	17500	7500	1250	6250	156.25	468.75	30
6	17500	7500	1250	7250	156.25	468.75	30
7	17500	7500	1250	6250	156.25	468.75	30
8	17500	7500	1250	6250	156.25	468.75	30
9	18490	6510	1250	5260	131.50	493.50	26.04
10	17710	7290	1250	6040	151.00	174.00	29.16
11	17500	7500	1250	6250	156.25	468.75	30
12	17790	7210	1250	5960	149.00	476.00	28.84
13	17500	7500	1250	6250	156.25	468.75	30
14	17500	7500	1250	6250	156.25	468.75	30
15	17500	7500	1250	6250	156.25	468.75	30
16	18470	6530	1250	5280	132.00	493.00	26.12
17	18550	6450	1250	5200	130.00	495.00	25.8
18	18910	6090	1250	4840	121.00	504.00	24.36
19	18750	6250	1250	5000	125.00	500.00	25
20	19070	5930	1250	4680	117.00	508.00	23.72
21	20190	4810	1250	3560	89.00	536.00	19.24
22	20710	4290	1250	3040	76.00	549.00	17.16
23	20510	4490	1250	3240	81.00	544.00	17.96
24	20760	4210	1250	2960	74.00	551.00	16.84

Contd.....

1	2	3	4	5	6	7	8
25	21990	3010	1250	1760	44.00	581.00	12.04
26	20850	4250	1250	3000	75.00	550.00	17
27	21550	3450	1250	2200	55.00	570.00	13.8
28	22150	2850	1250	1600	40.00	585.00	11.4
29	22050	2950	1250	1700	42.50	582.50	11.8
30	23750	1250	1250	-	-	6250.00	5
31	23050	1950	1250	700	17.50	607.50	7.8
32	23150	1850	1250	600	15.00	610.00	7.4
33	23270	1730	1250	480	12.00	613.00	6.92
34	23250	1750	1250	500	12.50	612.50	7
35	23390	1610	1250	360	9.00	616.00	6.44
36	23610	1390	1250	140	7.00	618.00	5.56
37	23630	1370	1250	120	3.00	622.00	5.48
38	23750	1250	1250	-	-	625.00	5
39	23750	1250	1250	-	-	625.00	5
40	23750	1250	1250	-	-	625.00	5

CHAPTER 9

ALTERNATIVE APPROACHES TO INFORMAL CREDIT SECTOR

9.1 Introduction

The informal sector, notwithstanding the reduction in its relative share in total rural credit, continues to meet a significant proportion of the total credit requirements of the rural households. As is generally agreed, the informal lenders are noted for their easy accessibility, prompt disbursement of loans, minimum procedural formality, greater flexibility regarding the purpose, duration, security and repayment and other aspects of credit transactions. The default rate is also lower. There is a limit to the expansion of credit from the formal sector due to constraints of resources and organisational and administrative set up. Therefore, the informal sector will retain its role in rural credit. However, the informal lenders have earned a bad reputation for their usurious interest rates and various malpractices. What are the options before us in rectifying the shortcomings of the informal credit agencies and at the same time taking advantage of their strong points? Regulation of the functioning of private moneylenders, and provision of suitable alternatives, (Agricultural Finance Sub-Committee, p.81) promoting links between formal and informal sector, (Rural Credit Survey Report, Vol.II, pp.133-34) offering effective competition to the latter, and

transforming it into formal financial institutions are some of the suggestions (Hulst, 1985) that have come up. We shall examine these proposals below.

9.2 Regulation of moneylending activities

As is widely recognised private moneylenders have been indulging in various questionable practices.

"Moneylenders because of their strong socio-economic position in the villages and also because of comparative absence of alternative lending institutions of organised type, are in a position to resort to various objectionable practices in their financial dealings with their clients in rural areas. These are obtaining thumb-impression of borrowers (who are generally illiterate and ignorant and extremely needy and hard pressed) on blank papers, demanding or deducting advance interest, manipulating accounts, taking conditional sale deeds relating to borrowers' land or house as a sort of insurance against the possibility of failures to repay the principal, exacting free services or service in nominal payment of various sorts... from debtors, thus reducing the borrowers to the status of serf or semi-serf, non-issue of receipts on payment of interest and principal, charging high rates of interest, forcing agriculturist borrowers to sell their produce to moneylenders at pre-determined prices and so on". (Suresh Chandra Mehta, 1987, pp.68-69).

The exorbitant interest rate and various malpractices prevalent in the rural ICM had attracted wide attention of the public and the demand for remedial measures became increasingly articulated. It is in response to this that the Government of India and the State Governments introduced various measures to remedy the exploitation and aberrations in the ICM.

One set of policies were aimed at regulating activities and operations of the moneylenders. The other sought to build up an alternative by widening and strengthening organised credit institutions like cooperative societies.

Starting with the Deccan Agriculturists Relief Act in 1979, the Government of India and various State Governments enacted several laws covering this field. Some of the important provisions of the Moneylenders Acts in the Indian Union as of 1951-52, are: registration of moneylenders, licensing of moneylenders, maintenance of accounts in the prescribed forms, prohibition against showing in books of accounts or in any other document a sum larger than what has been actually lent, furnishing periodical statements of accounts to the debtors in prescribed form giving full details about each loan as and when advanced, issue of receipts to the debtor for every payment received, prohibition against taking unlawful charges for expenses, provision to entitle a debtor to deposit at any time in a court of law an amount in part or full payment of a loan to be paid to his creditor, institution of suits by debtors for taking accounts and for having dues from them determined, protection of debtors from molestation and intimidation, infringement of the provisions of the law to be made a criminal offence punishable with fine and in appropriate cases with imprisonment, etc. as brought out in a detailed Statewise table (Table 21.1) in the All India Rural Credit Survey (AIRCS) Report. (Reserve Bank of India, 1956, op.cit., pp.406-409). The enactments covers all of the foregoing provisions. (Ibid. 410-415). On the working and effects of these Acts in different States, the Committee of Direction of AIRCS conducted an enquiry by canvassing a general questionnaire among the concerned groups, like office bearers of

cooperative societies and officials of the cooperative department, cultivators, etc. Their responses indicated strong reservations. (Ibid., pp.689-691). Admittedly, there has been large scale and country-wide evasion of the law. The Committee of Direction of the RCS came to the conclusion that "the control sought to be exercised through legislation has had little effect on the moneylender or his operations beyond putting him to the necessity of devising a variety of legal comouflage for a wide range of illegality". (RCS, Survey Report, Vol.II, p.361). Questionable practices like demand for advance interest payment, taking signature or thumb impression on a blank paper with a view to insert any arbitrary amount if the debtor becomes irregular in payment, demand for conditional sale deeds, charging higher than the permissible interest rate, maintaining duplicate account books, even doing business without obtaining licence, etc. have been reported. As for the reasons why the enactments could not prevent illegal transactions, Karkal has emphasised the following: (1) the customers are attracted by the agencies by the secretive nature of their business; (2) the agencies accept inferior, unmarketable, securities; and (3) the agencies also allow larger margin, i.e. advance large amount of the value of the security. (Gopal Karkal, 1967, p.104). The limitations of legislative enactments to directly suppress usury and other forms of exploitations have been observed elsewhere in the literature. (See for e.g., Shroff, U.N., 1950, FAO, 1953, all cited by Karkal, pp. 104-105).

Several amendments to close the loopholes in the earlier enactments have been introduced subsequently. For example, the Kerala Moneylenders Act,

1958, was amended in 1963, 1986 and 1987. The Tamil Nadu Moneylenders Act, 1956, was amended upto 1987. These amendments included insistence on obtaining license for carrying on moneylending, stipulation of maximum interest rates on loans, regularly recording and maintaining account for each debtor in sufficient detail including the date of the loan, amount of the principal, rate of interest charged on the loan, issue of receipts to the debtor for every payment made by him, and a statement of account on his requisition, etc. (Government of Kerala, Kerala Moneylenders Act, 1958 as amended by Act 33 of 1963, Kerala Moneylenders (Amendment) Act, 1986, Kerala Moneylenders (Amendment) Act 1987; Government of Tamil Nadu, Tamil Nadu Moneylenders Act 1957 as amended upto February, 1987).

9.3 Development of Alternative Credit Institutions to offer effective competition

The Agricultural Finance Sub-Committee appointed by the Government of India in its report had observed:

"The vast business of the moneylender class cannot be all taken over by any other agency in a short period. But it is possible to affect the working and character of their business immediately. One means of affecting this business is, of course, that of legal regulation. An even more effective way of affecting it is, however, the provision of suitable alternatives".
(Government of India, 1945, p.31).

The Rural Credit Review Committee after making a detailed review of the trends in the demand for and the supply of credit since the time of the Rural Credit Survey (1951-52) arrived at more or less the same conclusion.

With the widening gap between demand and supply of credit, the committee, while reiterating that the cooperatives will have to be strengthened as in the past and continually treated as the principal agency of rural credit, suggested that the potentialities of commercial banks should be fully utilised. (Reserve Bank of India, 1969, p.412).

The major thrust of the rural credit policy in recent years has been institutionalisation of rural credit. Thus, in the Fourth Five Year Plan (1969-74), main reliance was placed on cooperative credit system for provision of agricultural credit.

"While, as in the past, cooperatives will have to be strengthened and treated as the principal agency for agricultural credit, the approach in the Fourth Plan will be to ensure that agricultural production is not inhibited by the weakness of the cooperatives. In areas where cooperative credit structure is weak, there will be a special effort to provide alternative institutional sources... For meeting the gap in agricultural credit, the potentialities of commercial banks have to be fully mobilised". (Planning Commission, Fourth Five Year Plan, pp.140-141).

The important role of cooperatives as the principal source of rural credit was stressed in the Fifth Plan also.

"Cooperation represents institution of the principle and impulse of mutual aid. It has the merit of combining freedom and opportunity for the small man with the benefit of large-scale management and organisation. Cooperation is, therefore, eminently suited to bring about the desired socio-economic changes in the context of the existing conditions in the country. Thus the building up of a strong and viable cooperative sector, with special emphasis on the needs of the peasants, the workers and the consumers, will be one of the major objectives of national policy in the Fifth Plan". (Planning Commission, Draft Fifth Five Year Plan, Vol.II,p.78).

However, in the meantime, the actual experiences in the field raised serious reservations about the ability of the cooperative system alone to meet the growing demand for credit. This led to the government's taking social control over the commercial banks in 1968. The measures of social control give a new direction to the credit policy of commercial banks which began to evince interest in agricultural credit. (RBI, 1969-70, p.111). About the same time, the National Credit Council gave a more specific directional lead and indicated certain minimum targets of lending to agriculture by commercial banks. The nationalisation of 14 commercial banks (1969) which came in quick succession gave a further fillip to the policy of getting the banks increasingly involved in agricultural/rural credit. The progressive liberalisation of branch licensing policy by the Reserve Bank of India in favour of rural and semi-urban areas, is another major policy measure in the same direction adopted during the Fifth Plan Period. Village adoption scheme under which some public sector banks 'adopted' some villages is an innovative programme under which the concerned banks extended credit to the disadvantaged groups on liberal terms. Other measures that were taken to assist the weaker sections included: (i) setting up of special agencies called Small Farmers Development Agencies (SFDA), and Marginal Farmers and Agricultural Labourers Development Agencies (MFAL) to help these groups, and (ii) stipulation by the Reserve Bank for setting aside a specific portion of agricultural advances made by Central Cooperative Banks to primary agricultural credit societies for economically weak farmers. The foregoing measures were intended to providing increased credit on relatively soft terms and better facilities to small and economically weak farmers with a

view to removing disparities between different categories of farmers, and reducing regional disparities in the availability of credit. (RBI, 1972-73, p.122; RBI, 1973-74, p.128). In the Sixth Five Year Plan, 1978-83, a major objective of agricultural credit policy was stated to be

"a progressive institutionalisation with a multi-agency approach and the earmarking of an increasingly larger share for the weaker sections... The main burden of providing credit would continue to be on the cooperative sector. The Commercial Banks would also be expected to assume greater responsibilities for supplementing the efforts of the cooperative credit agencies". (Planning Commission, Draft Five Year Plan, 1978-83, p.151; See also: RBI, Multi Agency Approach in Agricultural Finance).

In 1978, the Government of India appointed a Working Group to study the progress of agricultural credit from commercial banks with special reference to small and marginal farmers. As recommended by the group, the Reserve Bank advised commercial banks to ensure that at least 50 percent of their total direct agricultural advances would meet the requirements of the small and marginal farmers by the end of the Fifth Plan. (RBI, 1978-79, p.168). Ensuring a substantial increase in the flow of credit, particularly to the weaker sections of the population, continues to be the declared policy objective in the sphere of agricultural credit during the Seventh Plan. (Planning Commission, Seventh Five Year Plan, Vol.II, 1985, p.42). Two other major policy measures with an egalitarian objective introduced during the seventies, viz., (i) extending consumption loans to weaker sections upto 10 percent of their borrowings from commercial banks, and (ii) introducing the Differential Rate of Interest Scheme are worth mentioning in this connection. (RBI, 1971).

The results of these policies are reflected in the geometric increase in the number of the rural branch offices of commercial banks, and that of institutional credit especially from commercial banks in the rural areas. Thus, of the total number of bank offices opened in 1969-70, 1216 or 66 percent were in rural areas, and in 1970-71, another 1288 branches or 64 percent of the total were opened in rural areas. The total outstanding advances to agriculture by scheduled banks increased from Rs.44.58 crores as on June 30 on 1969 to Rs.188.42 crores in June 1969 and Rs.341.77 crores in June 1978. (RBI, 1969-70, 1970-71). By the end of June, 1986, according to provisional estimates, the corresponding figure had soared to Rs.8959.95 crores. (RBI, 1985-86, p.238).

True, the availability of institutional credit has registered an impressive rise. However, high level of overdues and default rate have begun to surface on an increasing scale. "The main constraint in the credit flow has been low recoveries, high level of overdues and consequent ineligibility of a large number of cooperative institutions for refinancing". (Draft Five Year Plan, 1978-83, op.cit., p.151). "The main constraint in the credit flow has been low recoveries, high level of overdues and consequent ineligibility of a large number of cooperative institutions for refinancing". (Loc.cit). "During 1982-83, the ratio of overdues to debt at the level of primary agricultural credit societies, as well as at the level of primary land development banks was reported to be 40 to 42%. The recovery position in the case of commercial banks has been even worse and the proportion of overdues to debt in this case stood at 47% in 1982-83". (Seventh Five Year Plan, op.cit., p.44; See also: Dantwala, p.31). What are the implications of these high default rates?

Would these mounting overdues and defaults lead to an eventual reduction of the flow of institutional credit and resurgence of informal agencies, as it happened in the Philippines in similar circumstances under the Masagana 99 Programme?

9.4 Promotion of links with the formal sector

A third alternative suggested (Holst, 1985) is promoting links between the formal and informal sectors. Such links presumably would widen the financial market. They would enlarge the flow of funds into the rural areas, on the one hand, and facilitate the mobilisation of household savings on the other. Another advantage claimed is that the linkage will reduce the cost of intermediation of credit.

Are the formal and informal credit sectors segmented? Are the ICMs insulated from the impact of the policies pursued by the monetary authorities? Are the two sectors substitutes or complementary to each other? These are some of the issues debated in the literature.

The formal and informal credit sectors in India had established contacts with each other for quite some time now. As pointed by Karkal, the flow of funds from the country's central bank, the Reserve Bank of India, to the commercial banks and cooperative societies reaches the informal sector, thanks to the position and influence of landlords, agriculturist moneylenders, etc. in the rural areas. The nationalisation of commercial banks in 1969 and the big push to branch expansion into the rural areas since then have helped to further strengthen the link between

the two sectors. Increasing number of professional moneylenders and traders have come to borrow from the commercial banks and cooperative societies for on-lending to their customers. However, the link between the two sectors continues to be rather weak as far as the rural areas are concerned.

The main thrust of the credit policy of recent years has been to liberalise provision of credit from the Reserve Bank and commercial banks to the priority sectors including agriculture. As a result, more and more credit at concessional rate of interest has flowed into the rural sector. As observed earlier, the share of formal credit institutions in the total cash dues outstanding against rural households multiplied several fold since the middle of this century. Obviously, the size of the ICM in rural India has shrunk, atleast for the present. In the process, the hold of private lenders over their clientele has been weakened and presumably the monopoly profit in the interest rate kept down. Thus, it would seem that the informal sector is not totally immune to the credit policies vis-a-vis agriculture, handicrafts and other priority sectors.

The formal and informal credit sectors are substitutes for each other rather than complementary. A typical households first preference is for credit from the formal sector because of its lower cost, including the cost obtaining the loan. Only when that is not accessible, it would approach an informal credit agency. True, the majority of rural households may not be able to meet all their credit requirements from the formal credit sources, and informal credit may be sought by them to supplement credit

obtained from the formal sector. But this does not alter the fact that the two sectors are substitutes for each other.

The interest rate policy is likely to affect the pattern of disposition of the household savings. Financial regression in the form of keeping down the deposit rates of commercial banks and cooperative societies in order to minimise the burden of subsidy on interest on loans to the priority sectors will affect the flow of savings to the formal sector. Informal lenders are able to compete with the commercial banks and cooperative societies/banks, and attract more deposits by offering higher interest rates. This has important implications for sustaining the tempo of credit flow from the formal sector.

A major difference between the formal and informal credit sectors underlined in the literature is that of administration costs-- the cost of processing loan application, disbursement of loans, and recovery. Hence it is argued that, if competition of formal credit is to be effective, the transaction costs of formal sector have to be lowered. To achieve this, it is suggested that the methods and practices of the informal sector may be emulated. The above reasoning does not seem to hold water. In the first place, the cost of informal credit to the borrower, notwithstanding its informality and lower transaction costs, is now low. Second, such of those borrowers who borrow from the informal lenders do so not because of their lower costs, but because the formal credit sources are less accessible to them. Third, the level of administration costs of the formal sector, especially that of government and commercial banks has a floor below which it cannot be brought down owing to the costs of procedural formalities,

staff structure, pay, etc. As the formal sector institutions handle others' funds for which they are accountable, they have to ensure the security of the funds loaned out; for this a minimum of procedural formalities is unavoidable. And last, but not least, a higher level of transactions costs of the formal sector is not a major constraint on the flow of funds to the prospective borrowers.

Promoting links with the informal sector is another approach suggested. The strategy involves coopting informal lenders including input suppliers and output purchasers by refinancing the credit involved in their transactions. It is presumed that this will facilitate the flow of funds from the formal sector to small borrowers more cheaply.

The above suggestion raises several questions. First, cannot the desired goals, namely reaching credit from the formal sector to "small borrowers", be attained without the service of the informal agents? After all, we do have at present a wide network of cooperative societies and branches of commercial banks spread over the country side. In 1982-83, there were over 94000 primary agricultural credit societies in the rural areas of the country, with a membership of 63.5 million. The cooperative societies, besides extending credit, were also engaged in various activities like marketing of agricultural produce, sale of fertilizers and consumer goods, etc. which establish direct contact with a wide range of potential borrowers. Being grassroot level organisations with statutory provisions for elected bodies and democratic functioning, the societies ensure certain degree of community participation and involvement. They are more easily approachable for the small borrowers than other sources of formal credit.

They also have a comparatively less transaction cost they are operating with smaller staff and less expensive establishment. Notwithstanding their potentialities, if the distribution of cooperative credit is inequitable, that merely reflects the inequalities in the distribution of assets and other inequities in the socio-economic order.

Admittedly, the success of the strategy of promoting links with the informal sector would require a mechanism to monitor the on-lending rates and to ensure that the informal lenders do not take advantage of access to cheaper institutional credit to make abnormal profits. However, the creation of such monitoring mechanism would entail costs, and its effective and impartial functioning under the prevailing socio-economic set up is to more easily said than done.

CHAPTER 10

SUMMARY AND CONCLUSIONS

The ICMs dominate rural credit in the developing countries thanks to their easy accessibility, minimum procedural formalities, prompt disbursement of loans and greater flexibility on their terms and conditions compared to formal credit institutions. It is presumed that ICMs, by meeting the credit needs of small farmers and other disadvantaged groups of households usually bypassed by the formal credit institutions, make an equity impact. The ICMs are also credited with lower transaction costs and allocative efficiency. On the other hand, the ICMs are featured by a high degree of segmentation into several sub-markets, each with particular categories of lenders and borrowers, and differing in the size, purpose and duration of loans, interest rates and other terms and conditions. The present study is an attempt to assess the size, structure and role of the ICMs in India's rural sector, keeping in view the various perspectives in the received doctrines.

As in other developing countries, the ICMs claimed a lion's share of total rural credit in India also till recently. In early seventies, the ICMs accounted for about three fourths of the total debt outstanding and four-fifths of the total borrowings of the Indian rural households. But, thanks to the massive infusion of loans from formal

credit institutions since then, reflecting certain important policy changes in the field of credit, the size of the ICMs was further curtailed; their share of the total cash dues outstanding came down to about 39 percent by the beginning of the present decade. The fall in the share of these informal agencies is but a continuation of the trend which set in from the early fifties and which accelerated from the sixties.

The structure of the rural ICMs is characterised by segmentation. The rural ICMs are fragmented into several sub-markets based on the lender and borrower types. The participants in each sub-market are presumed to be tied together by mutual interests based on non-credit relationships as for example, between landlords and tenants, agricultural moneylenders and farm labour households, or traders and cultivators. The strength of tenancy, agrarian production relations and other socio-economic institutions are the factors underlying segmentation. With the massive infusion of credit from the formal sector into the rural areas in recent years mentioned above, and other socio-economic changes, the structure of the rural ICMs itself has undergone some major changes. Apparently, the segmentation of the rural credit market is getting eroded. The increasing competition from the formal credit sector has made moneylending less and less lucrative and attractive for private institutions is weakening the hold of landlords and agriculturist moneylenders on their erstwhile clientele and reducing the scope for usury and other forms of exploitation. The combined effect of the above changes is a structural transformation of the ICMs, as reflected in the reduced role of the informal ^{lenders} /of the commercial type, and an increase in the proportion of informal credit emanating from relatives, friends and others.

In our study areas, the average rate of interest on loans from the professional moneylenders ranged from 24 to 60 percent. More than one-half of the number of loans carried an interest rate above 60 percent, while an equal proportion of the amount of loans bore an interest above 36 percent. In two of the selected villages interest on a high proportion of the loans was 120 percent. Taking loans from all informal credit agencies in the six villages together, the interest on nearly one-third of the total number of loans exceeded 60 percent. Evidently, the rate of interest on informal credit is high by any standard. The purpose of loans, their size, nature of security, credit worthiness of the borrower and the elasticity of demand for funds seem to have a bearing on the interest rates. In our study areas, the average rate of interest on consumption loans is higher than that on loans used for production or other purposes. The rate of interest, by and large, tends to vary inversely with the size of loans; the correlation between the two variables is found to be negative in five villages and highly significant in two of the villages which account for a larger proportion of loans from professional moneylenders. The average interest on loans taken by agricultural and other casual labourers, whose demand for credit is less elastic and whose credit worthiness is low and have nothing but personal security to offer, is higher than that charged on loans taken by other occupational groups. As for the components of interest rate, thanks to private and social pressure on the borrowers, default rate of informal sector loans is comparatively low; and therefore the premium for risk does not seem to be relevant. Monopoly profit also has ceased to be relevant as, with the exponential growth of the formal sector credit, the informal credit agencies like

professional moneylenders have lost their monopolistic or oligopolistic position. As against this, the opportunity cost of money used and administrative cost assume significance, especially when the moneylenders enlarge the scale of their transactions and come to depend on borrowed funds to supplement their own resources.

The role of ICMs is usually assessed applying such criteria as domestic resource mobilisation, allocative efficiency and equity impact. In a comparatively static situation, the scope for savings mobilisation by informal lenders is limited. In such a set up both the demand for credit and supply of savings may be limited. But with some dynamic changes in the agrarian economy or spurt of activities in other sectors like fisheries and construction, or purchase of consumers durables, etc. the demand for credit may rise beyond what can be met from the professional moneylenders' own resources. The influx of remittances from the Gulf Emigrants in Kerala has generated considerable savings. The professional moneylenders have been able to mobilise a large chunk of these savings by offering more attractive returns than the formal credit institutions. The mushrooming of the finance companies in Kerala in recent years exemplifies this trend. However, the funds so mobilised were diverted to channels of low or no returns with the result that the finance companies collapsed like a house of cards, forfeiting the depositors of all their savings. The success of the informal credit agencies in savings mobilisation is more a reflection of the unrealistically low or sub-optimal interest rate on deposits offered by the formal credit institutions than the ingenuity and capabilities of the informal credit agencies. The fact that the latter does not guarantee

depositor security more than offsets the attraction of higher interest rates offered by them. Whether the ICMs display better allocative efficiency is equally dubious. True, with the informal lenders there is minimum procedural formalities and delay, greater flexibility, etc. These characteristics help to lower the transaction costs. But these conditions do not necessarily ensure allocative efficiency. Motivated as they are apt to be by a quick buck and nothing else, the informal lenders venture into financing enterprises of poor financial viability, not to speak of any social benefit, as exemplified by the record of the finance companies in Kerala. As for the ICMs equity impact, it may be true that the socially and economically disadvantaged groups of households, who are by-passed by the formal credit institutions, are able to meet their urgent, essential consumption requirements with credit from these informal sources. But it is also true that the borrowers have to pay through their nose for the credit obtained from the sources. The low income households have easier access to the professional moneylenders; but they are charged higher interest rates than the borrowers from the upper income or asset strata.

In brief, the size of the ICMs has shrunk in recent years thanks to the expansion of the formal credit sector. The structure of the ICMs itself has undergone a transformation with the decline in the share of informal lenders of the commercial type, while relatives and friends emerging as the leading sources of informal credit. Nevertheless, the average rate of interest in the ICMs remains high. Inter-linkage of the credit market with the land, labour^{and}/commodity markets facilitate the exaction of concealed interest of a high order. As against these, the ICMs have some positive features such as easy accessibility, low informational and administrative

costs, and supply of credit to the low income households usually bypassed by the formal sector.

In the light of the above, we will consider the various policy options to tackle the shortcomings of the ICMs and the possibilities of making use of their positive aspects. One obvious remedy recognised for quite sometime is regulation of moneylending activities. Legislation controlling private moneylending had been initiated more than a century ago. Since, then considerable improvement has been made in the legal framework, widening its scope, closing of loopholes and tightening of the enforcement machinery. Still some loopholes remain. Interest rates much above the permissible limit continue to be charged, and other provisions in the enactments are evaded or circumvented. It is no wonder, since, after all, the informal lenders like landlords, agriculturist moneylenders, professional moneylenders, etc. belong to those socio-economic classes which enjoy considerable influence and power. Thus, it was realised in due course that regulation of moneylending was not enough and that alternative sources of credit have to be provided.

In the early phase of national economic planning the main thrust was placed on cooperative credit institutions. But the cooperatives did not rise upto the expectations; the quantum of credit was inadequate and its distribution inequitable. Hence from the late sixties, the government adopted a multi-agency approach, drawing the newly nationalised commercial banks into financing agriculture and other priority sectors in the rural areas. The outcome of this reorientation of the credit policy, as reflected in the enlargement of the share of the formal sector in total rural credit,

has been documented earlier. Despite the exponential growth of formal sector credit, there are some perceptible lacunae in the functioning of the formal sector such as inequities in the distribution of credit, apparently high transaction costs and low recovery rate.

Under the existing order there is no built - in mechanism to ensure larger share of formal credit to the disadvantaged small borrowers. The fact that the formal credit institutions are not able to recover a significant proportion of the loans advanced and that they are unable to mobilise the savings of rural households to the full extent have made them increasingly dependent on the Reserve Bank of India, other financial institutions like the NABARD and the government for funds to carry on their lending activities. Obviously this is not a viable arrangement.

An alternative approach suggested is that of linking the informal sector to the formal sector. The avowed rationale of this is that of taking advantage of the low informational and administrative costs of the former, thereby reaching credit to the small borrowers at cheaper rate. Given the socio-economic inequalities in the rural set up, it is doubtful whether linking of the two sectors will ensure that cheaper credit from the formal sector will reach the more needy group of small borrowers. Admittedly, the success of the strategy of promoting links between the two sectors would require a mechanism to monitor the onlending rates and to ensure that the informal lenders do not take advantage of cheaper institutional credit to make abnormal profits. However, the establishment of such a mechanism would entail costs and its effective and impartial functioning under the prevailing set up is more easily said than done.

Moreover, can not the desired goal, viz., reaching credit from the formal sector to small borrowers, be attained without the service of the informal lenders, one wonders. After all, we do have at present a wide network of cooperative societies and branches of commercial banks spread over the countryside. In 1982-83, there were over 94000 primary agricultural credit societies, with a total membership of 63.5 million. Besides these, there were several non-credit cooperatives. The cooperative societies, apart from extending credit, were also engaged in various activities like marketing of agricultural produce, sale of fertilizers and consumer goods, etc. which help to establish direct contact with a wide range of beneficiaries. Being grassroot level organisations with statutory provision for elected bodies and democratic functioning, the cooperative societies ensure a certain degree of community participation and involvement. They are more easily accessible for the small borrowers than other sources of formal credit. They also have comparatively low transaction costs as they are operating with smaller, less expensive establishments. Notwithstanding these plus points, if the distribution of cooperative credit is inequitable, that merely reflects the inequalities in the prevailing socio-economic order.

The main thrust of the current credit policy, vis-a-vis the rural sector in general and agriculture in particular, is extension of cheap credit. The interest on loans from the formal sector is heavily subsidised and kept down at a sub-optimal level. The cost to the public sector of such across-the-board subsidisation is mounting. The self-imposed low ceiling on lending rates acts as a constraint on the formal credit institutions offering reasonably high interest and attracting deposits. Further,

laxity in the recovery of loans has led to mounting defaults. Rural credit has of late become highly politicised. The recent efforts of massive injection of credit into the rural households nicknamed "loan melas" have attracted a lot of adverse comments from the public. The loan melas whet the appetite of the rural households who ask for more. The recipients of the loan take them for gifts. The propensity to default has almost become a part of their culture. The bank officers dare not take recovery measures lest they invite trouble for themselves.

The present credit policy vis-a-vis the rural sector calls for a critical evaluation. In the first place, as mentioned above, credit is heavily subsidised. Such across-the-board subsidy involving heavy drain on the exchequer is uneconomic and unwarranted. If at all some subsidy on loans from the formal sector is a must, the benefit should be limited to the deserving low income groups of households. The restoration of interest rates to an optimum level is called for, though it may be an unpopular step. After all, even the formal credit institutions must recover at least the opportunity cost of the money involved. Recovery of loans extended by the formal sector needs to be enforced more resolutely and without fear or favour. The demands for moratorium on repayment and even for writing off of the outstanding debts from certain quarters must be resisted rather than encouraged, as some politicians of the ruling and opposition parties have been doing of late. The formal credit institutions must also pursue the goal of self-reliance. The increasing dependence on the central Bank and the government for replenishing their funds is an unhealthy trend. For this purpose, as observed above, recovery measures have to be tightened.

These institutions should also intensify their deposit mobilisation efforts. They will of course have to offer higher interest on deposits. There is no point in keeping the deposit rates too low, or below a reasonable level, turning a blind eye to the more attractive channels for the savers or the inflation rate.

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